# 2013 Annual Report

George Weston Limited

Weston

Weston

## Footnote Legend

(1) See non-GAAP financial measures beginning on page 49.

(2) For financial definitions and ratios refer to the Glossary beginning on page 134.

(3) Effective income tax rate excludes the tax impact of items excluded from adjusted basic net earnings per common share from continuing operations[(1)].

(4) To be read in conjunction with "Forward-Looking Statements" beginning on page 4.

(5) Certain 2012 figures have been restated due to the implementation of revised IAS 19, "Employee Benefits". See Section 19, "Accounting Standards Implemented in 2013 and Changes in Significant Accounting Policies" of the Company's 2013 Annual Report Management's Discussion and Analysis.

# Financial Highlights[2]

| As at or for the years ended December 31<br>($ millions except where otherwise indicated) | 2013 | 2012[5] |
|---|---|---|
| **Consolidated Operating Results** | | |
| Sales | **$ 33,582** | $ 32,742 |
| Operating income | **1,621** | 1,393 |
| Adjusted operating income[1] | **1,584** | 1,570 |
| Adjusted EBITDA[1] | **2,471** | 2,406 |
| Net interest expense and other financing charges | **497** | 441 |
| Net earnings from continuing operations | **849** | 708 |
| Discontinued operations | **58** | |
| Net earnings | **907** | 708 |
| Net earnings from continuing operations attributable to shareholders of the Company | **616** | 475 |
| **Consolidated Financial Position and Cash Flows** | | |
| Cash and cash equivalents, short term investments and security deposits | **$ 6,150** | $ 4,075 |
| Adjusted debt[1] | **7,259** | 5,584 |
| Free cash flow[1] | **529** | 490 |
| Cash flows from operating activities of continuing operations | **1,738** | 1,852 |
| Fixed asset purchases | **976** | 1,110 |
| **Consolidated per Common Share** ($) | | |
| Basic net earnings from continuing operations | **$ 4.48** | $ 3.36 |
| Basic net earnings from discontinued operations | **0.46** | |
| Basic net earnings | **4.94** | 3.36 |
| Adjusted basic net earnings from continuing operations[1] | **4.49** | 4.39 |
| **Consolidated Financial Measures and Ratios** | | |
| Sales growth | **2.6%** | 1.1% |
| Adjusted operating margin[1] | **4.7%** | 4.8% |
| Adjusted EBITDA margin[1] | **7.4%** | 7.3% |
| Adjusted debt[1] to adjusted EBITDA[1] | **2.9x** | 2.3x |
| Interest coverage[1] | **3.2x** | 3.2x |
| Return on average net assets[1] | **11.9%** | 10.7% |
| Return on average common shareholders' equity attributable to shareholders of the Company | **11.0%** | 9.1% |
| **Reportable Operating Segments** | | |
| Weston Foods | | |
| Sales | **$ 1,812** | $ 1,765 |
| Operating income | **238** | 230 |
| Adjusted operating income[1] | **267** | 275 |
| Adjusted operating margin[1] | **14.7%** | 15.6% |
| Adjusted EBITDA[1] | **330** | 334 |
| Adjusted EBITDA margin[1] | **18.2%** | 18.9% |
| Return on average net assets[1] | **23.3%** | 25.1% |
| Loblaw | | |
| Sales | **$ 32,371** | $ 31,604 |
| Operating income | **1,308** | 1,187 |
| Adjusted operating income[1] | **1,317** | 1,295 |
| Adjusted operating margin[1] | **4.1%** | 4.1% |
| Adjusted EBITDA[1] | **2,141** | 2,072 |
| Adjusted EBITDA margin[1] | **6.6%** | 6.6% |
| Return on average net assets[1] | **10.4%** | 9.8% |

## Report to Shareholders[4]

2013 was a transformational year for George Weston Limited. We made significant progress on our strategies at Loblaw and Weston Foods and are well-positioned for the future.

We continued to focus on long term value creation for shareholders through our support of the Shoppers Drug Mart acquisition, the launch of Choice Properties REIT and by raising our common share dividend by 9.2% in the second quarter, after a 5.6% increase in 2012.

Targeted investments to improve Loblaw's customer proposition yielded Retail segment sales growth of 2.1% and same-store sales growth of 1.1% in a competitive environment characterized by intense retail square footage growth. This investment as well as investments in Loblaw's IT system implementation were supported by efficiencies which were achieved in targeted areas. Loblaw's Financial Services segment continued to positively impact income growth in 2013, driven by customer growth in the credit card business. In 2014, Loblaw will accelerate the introduction of its IT infrastructure and expects to complete the rollout to corporate retail stores by the end of the year. This IT implementation is expected to increase Loblaw efficiencies.

Weston Foods delivered sales growth of 2.7% in 2013. Investments in growth, marketing and innovation were made to drive volume growth in response to changing consumer preferences. Weston Foods broadened its product offering through innovations such as the *All But Gluten* brand, the *D'Italiano* line of snack products, *Country Harvest* Veggie Bread, and range extensions with the *ACE Bakery* brand. Despite the positive impact investments had on volumes, results were negatively impacted by our increased investments and the performance of the frozen dough business in the second half of 2013. In 2014, Weston Foods will remain focused on improving the frozen dough business and optimizing sales mix as it continues to invest in growth, marketing and innovation.

In July, Loblaw entered into an agreement to acquire all of the outstanding common shares of Shoppers Drug Mart Corporation for approximately $12.4 billion in cash and Loblaw common shares. As part of Loblaw's financing of the acquisition, GWL has agreed to subscribe for additional Loblaw common shares, which is a reflection of our strong support for this transaction. This transaction, which is expected to be completed in the first quarter of 2014, will leverage combined strengths, scale and synergies to provide best-in-class offerings and deliver convenience and value to support future shareholder value creation.

Loblaw unlocked the value of its real estate portfolio by creating Choice Properties REIT. At closing of the IPO, approximately 35 million square feet of Loblaw-owned properties were sold to Choice Properties REIT at a market value of approximately $7 billion. Since the IPO, Choice Properties REIT has achieved results on plan and has acquired 12 commercial properties, 11 of which were from Loblaw. Choice Properties REIT is a leader in the Canadian real estate market and is uniquely positioned to drive growth and shareholder value.

Now, with a broader portfolio, George Weston Limited continues to be well positioned for sustained growth with leading market positions in food retail, fresh baking in Canada, North American frozen baking and biscuit manufacturing businesses, as well as real estate.

On behalf of the Board of Directors and shareholders, we thank our loyal customers for their support and our more than 140,000 employees for their dedication and continued commitment to the Company.

| | |
|---|---|
| **[*signed*]** | **[*signed*]** |
| **W. Galen Weston** | **Paviter S. Binning** |
| Executive Chairman | President |

# Management's Discussion and Analysis

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# Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") for George Weston Limited ("GWL") and its subsidiaries (collectively, the "Company") should be read in conjunction with the audited annual consolidated financial statements and the accompanying notes on pages 59 to 129 of this Annual Report. The Company's consolidated financial statements and the accompanying notes for the year ended December 31, 2013 have been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP"). The consolidated financial statements 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 26, 2014, unless otherwise noted. A Glossary of terms and ratios used throughout this Annual Report can be found beginning on page 134.

## 1. FORWARD-LOOKING STATEMENTS

This Annual Report for the Company, including this MD&A, contains forward-looking statements about the Company's objectives, plans, goals, aspirations, strategies, financial condition, results of operations, cash flows, performance, prospects and opportunities. 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, the proposed acquisition of Shoppers Drug Mart Corporation ("Shoppers Drug Mart") and targeted synergies expected following the close of this acquisition, future liquidity, amount of pension plan contributions, planned capital expenditures, status and impact of the information technology ("IT") systems implementation and future plans. These specific forward-looking statements are contained throughout this Annual Report including, without limitation, in Section 3, "Vision", Section 4, "Operating and Financial Strategies", and Section 21, "Outlook". Forward-looking statements are typically identified by words such as "expect", "anticipate", "believe", "foresee", "could", "estimate", "goal", "intend", "plan", "seek", "strive", "will", "may" 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 2014 is based on certain assumptions including assumptions about sales and volume growth, anticipated cost savings and operating efficiencies, and competitive square footage growth. 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 16, "Enterprise Risks and Risk Management" of this MD&A. Such risks and uncertainties include:

- failure by Loblaw Companies Limited ("Loblaw") to complete the acquisition of Shoppers Drug Mart or to realize the anticipated strategic benefits or operational, competitive and cost synergies;
- failure to realize benefits from investments in the Company's IT systems, including the Company's 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;
- public health events;
- risks associated with product defects, food safety and product handling;
- 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 foreign currency exchange rates and changes in derivative and commodity prices;
- changes in the Company's income, capital, commodity, property and other tax and regulatory liabilities including changes in tax laws, regulations or future assessments;

- 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;
- the inability of the Company to manage inventory to minimize the impact of obsolete or excess inventory and to control shrink;
- changes in the Company's estimate of inventory cost as a result of its IT system upgrade;
- failure to respond to changes in consumer and retail customer trends;
- reliance on the performance and retention of third-party service providers including those associated with the Company's supply chain and apparel business;
- supply and quality control issues with vendors in both advanced and developing markets;
- the impact of potential environmental liabilities;
- any requirement of the Company to make contributions to its registered funded defined benefit pension plans or the multi-employer pension plans ("MEPP") in which it participates in excess of those currently contemplated;
- 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;
- the inability of Loblaw to collect on its credit card receivables; and
- failure of Choice Properties Real Estate Investment Trust ("Choice Properties") to execute its plan and realize its forecasted results.

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.

## 2. OVERVIEW

GWL is a Canadian public company, founded in 1882, engaged in food processing and distribution. The Company has two reportable operating segments: Loblaw and Weston Foods, and holds cash, short term investments and a direct investment in Choice Properties. The Loblaw operating segment, which is operated by Loblaw Companies Limited and its subsidiaries, is Canada's largest food retailer and a leading provider of drugstore, general merchandise and financial products and services, and is the majority unitholder of Choice Properties, an owner, manager and developer of commercial real estate across Canada. The Weston Foods operating segment is a leading fresh and frozen baking company in Canada and operates a frozen baking manufacturing business in the United States ("U.S.") and a North American biscuit manufacturing business.

## 3. VISION

The Company's vision is to achieve long term, stable growth in its operating segments through customer focus and innovation. The Company is committed to making prudent capital investments while maintaining a strong balance sheet with the goal of providing sustainable returns to its shareholders over the long term through a combination of common share price appreciation and dividends.

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

Looking ahead, the Company plans to achieve these goals by focusing on its long term operating and financial strategies as described in Section 4, "Operational and Financial Strategies" of this MD&A.

## 4. OPERATING AND FINANCIAL STRATEGIES

To be successful in achieving its vision, the Company employs various operating and financial strategies. The Company engages in strategic acquisitions and dispositions when it is in the best long term interests of its shareholders to do so.

Each of the Company's two reportable operating segments has its own risk profile and operating risk management strategies as described in Section 16, "Enterprise Risks and Risk Management" of this MD&A.

Weston Foods' mission is to be a leading North American bakery company by participating across profitable segments of the bakery market, introducing innovative products and maintaining its highly effective cost management culture.

This mission will be achieved by focusing on innovation, cost management and continuous process improvements while exceeding consumer and retail customer expectations through superior service and product quality.

Weston Foods' long term operating strategies include:

- focusing on brand development by introducing innovative new products to meet the taste, nutritional and dietary needs of consumers;
- optimizing plant and distribution networks with capital investments designed to strategically position facilities to support growth and enhance quality, productivity and efficiencies;
- maintaining retail customer alignment;
- realizing ongoing cost reduction initiatives with the objective of ensuring a low cost operating structure and economies of scale;
- acquiring businesses and developing relationships to broaden market penetration and expand geographic presence; and
- building leadership talent.

Loblaw's mission is to be Canada's best food, health and home retailer by exceeding customer expectations through innovative products at great prices. As one of the country's leading retailers reaching 14 million consumers each week, Loblaw is uniquely positioned to deliver on its purpose – helping Canadians Live Life Well – and to provide customers with products, services, value and experience to enrich their lives. Loblaw delivers on this purpose through its strategy of offering the best customer experience in food, health, and beauty while striving for operational excellence and achieving growth through opportunities in emerging and complementary businesses.

Loblaw is committed to providing Canadians with a wide range of products and services to meet the everyday household and consumer needs. Loblaw is known for the quality, innovation and value of its food offering. It offers one of Canada's strongest control brand programs, including the unique *President's Choice*, *no name* and *Joe Fresh* brands. In addition, Loblaw, through its subsidiaries, makes available to consumers *President's Choice Financial* services and offers the *PC* points and *PC Plus* loyalty programs.

In 2014, Loblaw expects to advance a number of the strategic initiatives that were underway in 2013. Loblaw will continue to invest in innovative products, services and channels to maintain its competitive position. Loblaw expects to advance efficiency initiatives during the year, with a focus on continuing to roll out its IT system implementation and to achieve targeted synergies from the Shoppers Drug Mart acquisition following transaction closing. Loblaw's plans for 2014 include:

- completing the acquisition of Shoppers Drug Mart, and post-close, delivering on targeted synergies of approximately $100 million in the first 12 months and approximately $300 million over three years;
- focusing on cash flow generation and reducing leverage ratios following the close of the Shoppers Drug Mart acquisition;
- maintaining or growing market share in Loblaw's core food and drug businesses, which account for over 85% of total revenue;
- continuing to focus on execution and achieving efficiencies;

- exceeding customer expectations and achieving improved customer feedback scores with the right assortment, improved customer in-store experience, and competitive prices;
- offering customized assortment, compelling displays, and delivering competitive value across banners through ongoing development and implementation of strategic category reviews;
- leveraging its control brands to generate growth across food and general merchandise categories;
- expanding the *PC Plus* digital loyalty program to build customer loyalty by marketing on an individualized basis;
- growing the *PC Financial* services business including launching a newly designed in-store customer service pavilion;
- advancing initiatives to support colleague retention, succession planning, recognition and development to drive colleague engagement; and
- expanding the roll-out of Loblaw's IT systems to all of its distribution centres and corporate retail stores without negative impact to customers.

The success of these and other plans and strategies discussed in this MD&A may be affected by risks and uncertainties, including those described in Section 16, "Enterprise Risks and Risk Management" of this MD&A.

## 5. KEY FINANCIAL PERFORMANCE INDICATORS

The Company has identified specific key financial performance indicators to measure the progress of short and long term objectives. Certain key financial performance indicators are set out below:

**Key Financial Performance Indicators**[2]

As at or for the years ended December 31

| ($ millions except where otherwise indicated) | | **2013** | | 2012[5] |
|---|---|---|---|---|
| Sales growth | | **2.6%** | | 1.1% |
| Operating income | **$** | **1,621** | $ | 1,393 |
| Adjusted operating income[1] | **$** | **1,584** | $ | 1,570 |
| Adjusted operating margin[1] | | **4.7%** | | 4.8% |
| Adjusted EBITDA[1] | **$** | **2,471** | $ | 2,406 |
| Adjusted EBITDA margin[1] | | **7.4%** | | 7.3% |
| Basic net earnings per common share from continuing operations ($) | **$** | **4.48** | $ | 3.36 |
| Adjusted basic net earnings per common share from continuing operations[1] ($) | **$** | **4.49** | $ | 4.39 |
| Cash and cash equivalents, short term investments and security deposits | **$** | **6,150** | $ | 4,075 |
| Cash flows from operating activities of continuing operations | **$** | **1,738** | $ | 1,852 |
| Adjusted debt[1] to adjusted EBITDA[1] | | **2.9x** | | 2.3x |
| Free cash flow[1] | **$** | **529** | $ | 490 |
| Interest coverage[1] | | **3.2x** | | 3.2x |
| Return on average net assets[1] | | **11.9%** | | 10.7% |
| Return on average common shareholders' equity attributable to shareholders of the Company | | **11.0%** | | 9.1% |

Under GAAP, certain expenses and income must be recognized that are not necessarily reflective of the Company's underlying operating performance. Non-GAAP financial measures exclude the impact of certain items and are used internally when analyzing consolidated and segment underlying operating performance. These non-GAAP financial measures are also helpful in assessing underlying operating performance on a consistent basis. See Section 22, "Non-GAAP Financial Measures" of this MD&A for more information on the Company's non-GAAP financial measures.

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

## 6. OVERALL FINANCIAL PERFORMANCE

### 6.1 SIGNIFICANT ACCOMPLISHMENTS IN 2013

Significant accomplishments were achieved in 2013: the agreement to acquire Shoppers Drug Mart and the initial public offering ("IPO") of Choice Properties.

**Agreement to Acquire Shoppers Drug Mart Corporation** On July 14, 2013, Loblaw entered into an arrangement agreement to acquire all of the outstanding common shares of Shoppers Drug Mart for consideration of up to approximately $6.7 billion of cash and the issuance of up to approximately 119.9 million common shares. Based on Loblaw's closing common share price on that date, the purchase price would be approximately $12.4 billion.

In 2013, Loblaw completed the financing required to close the acquisition of all of the outstanding common shares of Shoppers Drug Mart, as described in Section 9.2, "Liquidity and Capital Structure" of this MD&A. As part of the financing of the acquisition, GWL has agreed to subscribe for approximately $500 million of additional Loblaw common shares.

On September 12, 2013, Shoppers Drug Mart shareholders voted in favour of the agreement and on September 16, 2013 a final order of the Ontario Superior Court of Justice approving the agreement was obtained. The transaction is subject to various regulatory approvals under the *Competition Act* (Canada) and by the Toronto Stock Exchange ("TSX") and the fulfillment of certain other closing conditions customary in transactions of this nature. The process of review under the *Competition Act* (Canada) is proceeding as expected and the Company anticipates that the transaction will be completed during the first quarter of 2014. Further information on the transaction and its expected effects on Loblaw can be found in the Information Statement filed by Loblaw on August 20, 2013, in respect of Shoppers Drug Mart shareholder approval of the transaction. There can be no assurance that all conditions will be met or waived or that Loblaw will be able to successfully consummate the proposed transaction as currently contemplated or at all.

**Choice Properties Real Estate Investment Trust** In 2013, Choice Properties completed a $460 million IPO of Trust Units ("Units"), including the exercise of a $60 million over-allotment option, in connection with its acquisition of approximately $7 billion of properties and related assets from Loblaw. In addition, Choice Properties completed a $200 million offering of Units to GWL.

Concurrent with the offering of Units, Choice Properties completed a public offering of $600 million aggregate principal amount of senior unsecured debentures ("Debentures"). A portion of the debt offering proceeds were used to replenish the cash used to repay the U.S. $150 million private placement ("USPP") note that matured in 2013 and to early-settle the remaining U.S. $150 million USPP note.

As at year end 2013, GWL held an effective interest of approximately 5.4% in Choice Properties through the ownership of 20,107,810 Units and Loblaw held an effective interest in Choice Properties of approximately 82.2% through the ownership of 21,500,000 Units and 284,074,754 Class B Limited Partnership units, which are economically equivalent to and exchangeable for Units. Included in the Class B Limited Partnership units are 11,576,883 units issued to Loblaw, in connection with the acquisition of an additional portfolio of investment properties subsequent to the IPO.

## 6.2 ADDITIONAL FACTORS AND INITIATIVES IN 2013

The Company's reportable operating segments were impacted by several additional factors and initiatives in 2013:

**Weston Foods** During 2013, Weston Foods made investments to support growth in response to changing consumer preferences and a highly competitive retail landscape. These investments included marketing, new manufacturing capacity and promotional activity. In addition, Weston Foods maintained its focus on productivity improvements and other cost reduction initiatives.

The Weston Foods operating segment was also impacted by the following key factors in 2013:

- a highly competitive retail landscape, economic uncertainty and overall market softness resulted in pressure on sales volumes;
- customer eating and buying preferences continued their trend towards healthier, more nutritious, value-added and convenience offerings. Weston Foods responded to these trends with innovative and expanded products across its product portfolio. Gluten free breads and sweet goods were introduced under the *All But Gluten* brand, and the *D'Italiano*, *Country Harvest* and *ACE Bakery* brands were expanded with on-trend offerings, including the *D'Italian*o line of snack products and *Country Harvest* Veggie breads; and
- the continuing shift in consumer food shopping patterns towards alternate format retail channels resulted in sales growth in these channels.

**Loblaw** During 2013, Loblaw advanced a number of strategic initiatives that were introduced in 2012. Targeted investments to improve the customer proposition yielded same-store sales growth of 1.1% in a competitive environment characterized by intense competitive square footage growth. Progress was made in Loblaw's IT system implementation, and efficiencies were achieved in targeted areas such as shrink, transportation costs, warehousing, supply chain and labour.

In addition to the significant strategic accomplishments noted in Section 6.1, "Significant Accomplishments in 2013" of this MD&A, Loblaw's key accomplishments in 2013 included:

- expanded the IT system implementation across eight distribution centres and 75 stores, with little to no negative impact on customers;
- achieved improved customer feedback net promoter scores in the conventional division for the third consecutive year by exceeding customer expectations through the right assortment, improved customer in-store experience and competitive prices;
- led by fresh categories, achieved growth in sales and tonnage in the discount division despite strong competitive square footage growth;
- ongoing development and implementation of strategic category reviews offered customized assortment, compelling displays and delivered competitive value across its banners;
- continued to invest to improve standards and in-store experience through renovations at 192 stores and strategically invested in new square footage, expanding to 51.9 million square feet, a net increase of 0.8% compared to 2012;
- launched over 550 new control brand products and redesigned or improved approximately 640 control brand products;
- reset the general merchandise in 29 stores to offer an enhanced selection in four key areas: Apparel, Beauty, Home, and Kids;
- grew the *PC Financial s*ervices business, setting a new high with 1.2 million new MasterCard® applications;
- launched a new digital loyalty marketing platform, *PC Plus*, in 44 Loblaw stores in May 2013 and expanded the program nationally across the conventional network and *Real Canadian Superstore* locations in November 2013;
- launched *Joe Fresh* online in October 2013; and
- effectively managed costs across the business with a focus on improved shrink, lower supply chain costs, labour and administrative expenses to drive efficient operations.

## 6.3 CONSOLIDATED RESULTS OF OPERATIONS

| As at or for the years ended December 31<br>($ millions except where otherwise indicated) | 2013 | 2012[5] |
|---|---|---|
| Sales | **$ 33,582** | $ 32,742 |
| Operating income | **$ 1,621** | $ 1,393 |
| Adjusted operating income[1] | **$ 1,584** | $ 1,570 |
| Adjusted operating margin[1] | **4.7%** | 4.8% |
| Adjusted EBITDA[1] | **$ 2,471** | $ 2,406 |
| Adjusted EBITDA margin[1] | **7.4%** | 7.3% |
| Net interest expense and other financing charges | **$ 497** | $ 441 |
| Income taxes | **$ 275** | $ 244 |
| Net earnings from continuing operations attributable to shareholders of the Company | **$ 616** | $ 475 |
| Net earnings from continuing operations | **$ 849** | $ 708 |
| Discontinued operations | **$ 58** | |
| Basic net earnings per common share from continuing operations ($) | **$ 4.48** | $ 3.36 |
| Adjusted basic net earnings per common share from continuing operations[1] ($) | **$ 4.49** | $ 4.39 |
| Adjusted debt[1] to adjusted EBITDA[1] | **2.9x** | 2.3x |
| Free cash flow[1] | **$ 529** | $ 490 |

Adjusted basic net earnings per common share from continuing operations[1] for 2013 increased to $4.49 compared to $4.39 in 2012, an increase of $0.10. The increase was primarily attributable to an improvement in the operating performance of Loblaw and a lower effective income tax rate[3], partially offset by a decline in the operating performance of Weston Foods.

Basic net earnings per common share from continuing operations increased to $4.48 compared to $3.36, an increase of $1.12, and was positively impacted by certain foreign currency translation and a number of other items. For a complete list of items which impacted basic net earnings per common share from continuing operations but that are excluded from adjusted basic net earnings per common share from continuing operations[1], see Section 22, "Non-GAAP Financial Measures" of this MD&A.

**Sales** The Company's 2013 consolidated sales increased 2.6% to $33.6 billion from $32.7 billion in 2012. Consolidated sales growth for 2013 was impacted by each reportable operating segment as follows:

- Positively by 0.1% due to sales growth of 2.7% at Weston Foods. Excluding the impact of the loss of distributed product and foreign currency translation, sales increased by 3.0% due to the combined positive impact of pricing and changes in sales mix of 2.3% and an increase in volume of 0.7%.
- Positively by 2.3% due to sales growth of 2.4% at Loblaw. Loblaw's Retail segment sales increased by 2.1% and same-store sales growth was 1.1% (2012 – decline of 0.2%). Loblaw's average annual internal food price inflation was lower than the average annual national food price inflation of 1.1% (2012 – 2.3%) as measured by "The Consumer Price Index for Food Purchased from Stores" ("CPI"). In the last 12 months, corporate and franchise store square footage increased 0.8% (2012 – 0.6%). Loblaw sales in 2013 were also positively impacted by an increase in revenue from its Financial Services segment, which includes President's Choice Bank ("PC Bank"), a subsidiary of Loblaw.

**Operating Income** The Company's 2013 consolidated operating income was $1,621 million compared to $1,393 million in 2012, an increase of $228 million, or 16.4%. Consolidated operating income was positively impacted by certain foreign currency translation and a number of other items. For a complete list of items which impacted operating income but that are excluded from adjusted operating income(1), see Section 22, "Non-GAAP Financial Measures" of this MD&A.

The Company's consolidated adjusted operating income(1) was $1,584 million compared to $1,570 million in 2012, an increase of $14 million, or 0.9%. Consolidated adjusted operating margin(1) was 4.7% in 2013 compared to 4.8% in 2012.

The Company's year-over-year change in consolidated adjusted operating income(1) was impacted by each of its reportable operating segments as follows:

- Negatively by 0.5% due to a decrease of 2.9% in adjusted operating income(1) at Weston Foods. Adjusted operating income(1) was positively impacted by higher sales volumes driven by certain investments, as well as higher pricing and the benefits realized from productivity improvements and other cost reduction initiatives. This improvement was more than offset by a decline in the performance of the frozen dough business in the second half of 2013, the cost impact of investments, including the impact of changes in sales mix, and higher commodity and other input costs.
- Positively by 1.4% due to an increase of 1.7% in adjusted operating income(1) at Loblaw, primarily driven by an improvement in its Financial Services segment, partially offset by a decline in its Retail segment. The increase in Loblaw's Financial Services segment was mainly attributable to higher revenues. The decrease in Loblaw's Retail segment was primarily driven by investments in, and changes to the value of Loblaw's franchise business, increased other operating costs, including depreciation and amortization, costs related to the growth in certain of Loblaw's emerging businesses and foreign exchange losses, partially offset by higher gross profit and supply chain efficiencies.

The Company's consolidated adjusted EBITDA margin(1) nominally increased to 7.4% when compared to 2012.

**Net Interest Expense and Other Financing Charges** Net interest expense and other financing charges increased in 2013 by $56 million to $497 million compared to 2012. Net interest and other financing charges includes the favourable year-over-year impact of the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares of $36 million, partially offset by the unfavourable year-over-year impact of a number of Choice Properties and Shoppers Drug Mart related items recorded in 2013 as follows:

- Choice Properties' IPO transaction costs of $44 million;
- early debt settlement costs of $18 million;
- a fair value adjustment related to the Trust Unit liability, reflecting the change in the fair value of Choice Properties' Units held by unitholders other than the Company, of $18 million; and
- net interest expense of $15 million relating to indebtedness incurred to finance the proposed acquisition of Shoppers Drug Mart.

Excluding the above impacts, net interest expense and other financing charges decreased by $3 million compared to 2012, driven by lower net interest expense related to certain financial derivative instruments and lower net interest on net defined benefit obligations, partially offset by Unit distributions by Choice Properties.

**Income Taxes** In 2013, income tax expense was $275 million compared to $244 million in 2012, and the Company's effective income tax rate decreased to 24.5% from 25.6% in 2012. This decrease was primarily due to non-taxable foreign currency translation gains (2012 – non-deductible foreign currency translation losses) and the reversal of previously recognized current tax assets in 2012 as described below, partially offset by an increase in non-deductible amounts (including fair value adjustments related to the Trust Unit liability).

In 2012, the Department of Finance substantively enacted amendments to the Income Tax Act relating to the taxation of Canadian corporations with foreign affiliates. The Company is no longer able to recognize a net tax benefit on realized foreign capital losses recognized by its foreign affiliates to the extent such losses cannot be

offset against realized foreign capital gains. In 2012, the Company (excluding Loblaw) expensed $8 million in previously recognized current tax assets relating to these amendments.

**Net Earnings from Continuing Operations Attributable to Shareholders of the Company** Net earnings from continuing operations attributable to shareholders of the Company for 2013 were $616 million compared to $475 million and basic net earnings per common share from continuing operations were $4.48 compared to $3.36 in 2012, an increase of $1.12.

Changes in non-controlling interests did not have a significant impact on the growth of the Company's net earnings attributable to shareholders of the Company over the past two years. GWL's ownership of Loblaw was 63.0% as at the end of 2013 (2012 – 62.9%; 2011 – 63.0%).

**Discontinued Operations** In 2013, the Company recorded income related to discontinued operations of $58 million, which included the settlement of a previously disclosed litigation of $48 million ($40 million, net of income taxes) and adjustments resulting in income of $18 million associated with the Company's (excluding Loblaw) previously owned operations.

## 6.4 SELECTED ANNUAL 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 December 31, 2013, and the annual consolidated financial statements of the Company dated December 31, 2012. The analysis of the data contained in the table focuses on the trends and significant events or items affecting the results of operations and financial condition of the Company over the latest three year period.

| For the years ended December 31<br>($ millions except where otherwise indicated) | 2013 | 2012(i) | 2011(ii) |
|---|---|---|---|
| Sales | **$ 33,582** | $ 32,742 | $ 32,376 |
| Net earnings from continuing operations | **849** | 708 | 919 |
| Discontinued operations | **58** | | |
| Net earnings | **907** | 708 | 919 |
| Net earnings from continuing operations attributable to shareholders of the Company | **616** | 475 | 635 |
| Net earnings per common share ($) – basic | | | |
| Continuing operations | **$ 4.48** | $ 3.36 | $ 4.58 |
| Discontinued operations | **$ 0.46** | | |
| Net earnings | **$ 4.94** | $ 3.36 | $ 4.58 |
| Net earnings per common share ($) – diluted | | | |
| Continuing operations | **$ 4.45** | $ 3.29 | $ 4.55 |
| Discontinued operations | **$ 0.46** | | |
| Net earnings | **$ 4.91** | $ 3.29 | $ 4.55 |
| Dividends declared per share type ($): | | | |
| Common shares | **$ 1.625** | $ 1.460 | $ 1.440 |
| Preferred shares – Series I | **$ 1.45** | $ 1.45 | $ 1.45 |
| Preferred shares – Series III | **$ 1.30** | $ 1.30 | $ 1.30 |
| Preferred shares – Series IV | **$ 1.30** | $ 1.30 | $ 1.30 |
| Preferred shares – Series V | **$ 1.19** | $ 1.19 | $ 1.19 |

(i) Certain 2012 figures have been restated due to the implementation of revised IAS 19, "Employee Benefits". See Section 19, "Accounting Standards Implemented in 2013 and Changes in Significant Accounting Policies" of the Company's 2013 Annual Report Management's Discussion and Analysis.

(ii) 2011 figures have not been restated for the impact of IAS 19.

| ($ millions) | Dec. 31, 2013 | Dec. 31, 2012 | Dec. 31, 2011[i] |
|---|---|---|---|
| | | As at | |
| Total assets | **$ 24,622** | $ 21,804 | $ 21,323 |
| Total long term debt | **$ 8,944** | $ 6,933 | $ 6,844 |
| Capital securities | **224** | 223 | 222 |
| Trust Unit liability | **478** | | |
| Total long term financial liabilities | **$ 9,646** | $ 7,156 | $ 7,066 |

(i) 2011 figures have not been restated for the impact of IAS 19.

**Sales** Over the past three years, Weston Foods sales have been impacted by pricing and changes in sales mix, foreign currency translation and key market trends such as changing consumer eating and buying preferences and the continuing shift in consumer food shopping patterns toward alternate format retail channels. Weston Foods sales volumes were flat in 2013, while 2012 was negatively impacted by lower sales volumes compared to 2011. Weston Foods sales and volumes in 2013 and 2012 were negatively impacted by the loss of certain frozen distributed products.

Loblaw's retail sales have been under pressure in a competitively intense retail market and uncertain economic environment. In 2013, same-store sales increased by 1.1% compared to a decline of 0.2% in 2012. Average annual national food price inflation as measured by CPI was 1.1% in 2013 and 2.3% in 2012. In 2013 and 2012, the Company's average annual internal retail food price index was lower than CPI. During 2013, the number of corporate and franchise stores increased to 1,066 (2012 – 1,053; 2011 – 1,046). Retail square footage in 2013 increased to 51.9 million (2012 – 51.5 million; 2011 – 51.2 million). In addition, *PC Financial* revenues have shown strong growth over the past two years, increasing by 14.8% in 2013 and 17.7% in 2012.

**Operating Income** Over the last three years, the Company's consolidated operating income was impacted by the following items:

- restructuring and other charges incurred by Weston Foods and Loblaw, including charges of $35 million and $61 million in 2013 and 2012, respectively, related to the reduction in head office and administrative positions recorded by Loblaw;
- gains related to defined benefit plan amendments recorded in 2013 and 2012;
- fixed asset and other related (recoveries) impairment charges, at Loblaw;
- certain items relating to the Shoppers Drug Mart and Choice Properties transactions in 2013;
- general and administrative costs at Choice Properties in 2013;
- fair value adjustment of commodity derivatives at Weston Foods;
- fluctuations in share-based compensation net of equity derivatives of both GWL and Loblaw;
- a charge related to the MEPP withdrawal liability incurred by Weston Foods in 2013 and 2012;
- a gain on disposal of property at Loblaw in 2012 and 2011;
- insurance proceeds recorded by Weston Foods in 2012 and 2011;
- the effect of certain prior years' commodity tax matters at Loblaw recorded in 2011; and
- the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin Holdings GmbH ("Dunedin"), a subsidiary of GWL, and certain of its affiliates.

In addition to the items above, Weston Foods' operating income during 2013 and 2012 was positively impacted by higher pricing and the benefits realized from productivity improvements and other cost reduction initiatives. In 2013, this improvement was more than offset by a decline in the performance of the frozen dough business in the second half of the year, the cost impact of certain investments, including the impact from changes in sales mix, and higher commodity and other input costs. Operating income in 2012 was negatively impacted by lower sales volumes and higher commodity and other input costs.

Loblaw operating income was also impacted by the items noted above. In addition, Loblaw made investments in its customer proposition in both 2013 and 2012 to better position itself in an intensely competitive market.

Compared to 2011, Loblaw's 2012 operating income was impacted by these investments, which were not covered by operations, as well as incremental IT and supply chain charges, start-up costs associated with the launch of the *Joe Fresh* brand in the U.S. incurred in 2011 and charges associated with transitioning certain Ontario conventional stores to the more cost effective and efficient operating terms of collective agreements ratified in 2010.

**Net Earnings from Continuing Operations Attributable to Shareholders of the Company** In addition to the items listed above, net earnings from continuing operations attributable to shareholders of the Company and basic net earnings per common share from continuing operations were impacted by the following items included in net interest expense and other financing charges:

- Choice Properties' IPO transaction costs in 2013;
- fair value adjustment related to the Trust Unit liability in 2013;
- net interest expense related to the indebtedness incurred to finance the proposed acquisition of Shoppers Drug Mart in 2013;
- early debt settlement costs in 2013; and
- fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares.

In addition, during 2013 and 2012 net earnings from continuing operations attributable to shareholders of the Company and basic net earnings per common share from continuing operations were positively impacted by lower effective income tax rates.

**Discontinued Operations** In 2013, the Company recorded income related to discontinued operations of $58 million, which included the settlement of a previously disclosed litigation of $48 million ($40 million, net of income taxes) and adjustments resulting in income of $18 million associated with the Company's (excluding Loblaw) previously owned operations.

**Total Assets and Long Term Financial Liabilities** In 2013, total assets and long term financial liabilities increased by 12.9% and 34.8% respectively, compared to 2012. The increases during the year were primarily driven by the Choice Properties and Shoppers Drug Mart transactions as described in Section 6.1, "Significant Accomplishments in 2013" and 9.2, "Liquidity and Capital Structure" of this MD&A. Excluding these impacts, the Company's total assets and long term financial liabilities have increased marginally over the last three years.

## 7. RESULTS OF REPORTABLE OPERATING SEGMENTS

The following discussion provides details of the 2013 results of operations of each of the Company's reportable operating segments.

### 7.1 WESTON FOODS OPERATING RESULTS

| For the years ended December 31<br>($ millions except where otherwise indicated) | 2013 | 2012[5] |
|---|---|---|
| Sales | **$ 1,812** | $ 1,765 |
| Operating income | **$ 238** | $ 230 |
| Adjusted operating income[1] | **$ 267** | $ 275 |
| Adjusted operating margin[1] | **14.7%** | 15.6% |
| Adjusted EBITDA[1] | **$ 330** | $ 334 |
| Adjusted EBITDA margin[1] | **18.2%** | 18.9% |
| Return on average net assets[1] | **23.3%** | 25.1% |

**Sales** Weston Foods sales for 2013 of $1,812 million increased by 2.7%, and volumes were flat compared to 2012. Excluding the impact of the loss of certain frozen products that Weston Foods distributed on behalf of certain customers in 2012 and foreign currency translation, sales increased by 3.0% due to the combined positive impact of pricing and changes in sales mix of 2.3% and an increase in volume of 0.7%. The loss of certain frozen distributed products negatively impacted sales and volume growth by approximately 1.6% and 0.7%, respectively. Foreign currency translation positively impacted sales by approximately 1.3%.

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

Fresh bakery sales, principally bread, rolls, bagels, tortillas and sweet goods, represented approximately 36% of total Weston Foods sales, up from approximately 35% in 2012. Fresh bakery sales increased by approximately 3.9% in 2013 compared to 2012 due to the positive impact of pricing and changes in sales mix, as well as higher sales volumes. Volumes increased in 2013 as growth was realized in the *Country Harvest* and *D'Italiano* brands. The introduction of new products, including *Country Harvest* Veggie, Sprouted Multigrain and Wheat breads, the *D'Italian*o line of snack products and the launch of gluten free bread and sweet goods, including the *All But Gluten* brand, contributed positively to sales and volumes in 2013.

Frozen bakery sales, principally bread, rolls, doughnuts, cakes and sweet goods, represented approximately 45% of total Weston Foods sales, down from approximately 47% in 2012. Frozen bakery sales decreased by approximately 1.8% in 2013 compared to 2012 primarily driven by the loss of certain distributed products. Excluding the impact of the loss of these distributed products, frozen bakery sales increased by approximately 1.6% in 2013 compared to 2012, driven by the positive impact of pricing and changes in sales mix, partially offset by lower volumes in certain product categories, including frozen dough products.

Biscuit sales, principally wafers, ice-cream cones, cookies and crackers, represented approximately 19% of total Weston Foods sales, up from approximately 18% in 2012. Biscuit sales increased by approximately 4.7% in 2013 compared to 2012 due to higher volumes as well as the positive impact of pricing and changes in sales mix. Volume growth was driven by higher cookie and cone sales, partially offset by a decline in wafer sales. Higher cookie sales and volumes in 2013 were driven by new product launches, including Mrs. Fields® branded pre-packaged cookies that were launched in the fourth quarter of 2012.

**Operating Income** Weston Foods operating income for 2013 increased by $8 million, or 3.5%, to $238 million compared to $230 million in 2012. Operating margin for 2013 was 13.1% compared to 13.0% in 2012. The impact of the MEPP withdrawal liability and a number of other items had a year-over-year favourable net impact on Weston Foods operating income in 2013. For a complete list of items which impacted operating income but that are excluded from adjusted operating income(1), see Section 22, "Non-GAAP Financial Measures" of this MD&A.

Gross margin, excluding the impact of the commodity derivatives fair value adjustment, remained relatively flat in 2013 compared to 2012.

Adjusted operating income(1) decreased by $8 million, or 2.9%, to $267 million in 2013 from $275 million in 2012. Adjusted operating margin(1) was 14.7% in 2013 compared to 15.6% in 2012.

Adjusted operating income(1) in 2013 was positively impacted by higher sales volumes driven by investments in growth, marketing and innovation, including new manufacturing capacity and promotional activity, as well as higher pricing and the benefits realized from productivity improvements and other cost reduction initiatives. This improvement was more than offset by a decline in the performance of the frozen dough business in the second half of 2013, the cost impact of investments, including the impact of changes in sales mix, and higher commodity and other input costs. The decline in the performance of the frozen dough business was as a result of lower sales due in part to certain retail customers focusing less on frozen dough products as well as some operational challenges.

Weston Foods continuously evaluates strategic and cost reduction initiatives related to its manufacturing assets, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. Restructuring activities related to these initiatives are ongoing and in 2013, charges of $6 million (2012 – $12 million) were recorded in operating income, including $4 million (2012 – $4 million) of accelerated depreciation.

Adjusted EBITDA[(1)] decreased by $4 million, or 1.2%, to $330 million in 2013 compared to $334 million in 2012. Adjusted EBITDA margin[(1)] for 2013 decreased to 18.2% from 18.9% in 2012.

### 7.2 LOBLAW OPERATING RESULTS

| For the years ended December 31<br>($ millions except where otherwise indicated) | 2013 | 2012[(5)] |
|---|---|---|
| Sales | **$ 32,371** | $ 31,604 |
| Operating income | **$ 1,308** | $ 1,187 |
| Adjusted operating income[(1)] | **$ 1,317** | $ 1,295 |
| Adjusted operating margin[(1)] | **4.1%** | 4.1% |
| Adjusted EBITDA[(1)] | **$ 2,141** | $ 2,072 |
| Adjusted EBITDA margin[(1)] | **6.6%** | 6.6% |
| Return on average net assets[(1)] | **10.4%** | 9.8% |

As at year end 2013, Loblaw held an 82.2% effective interest in Choice Properties which completed an IPO during the year, as described in Section 6.1, "Significant Accomplishments in 2013" of this MD&A. As a result, Loblaw now has three reportable operating segments: Retail, Financial Services and Choice Properties. Loblaw is one reportable operating segment of GWL.

**Sales** Loblaw sales for 2013 increased by 2.4% to $32.4 billion compared to $31.6 billion in 2012. The increase in retail sales in 2013 of $640 million, or 2.1%, compared to 2012 was a result of the following factors:

- same-store sales growth was 1.1% (2012 – decline of 0.2%) and excluding gas bar was 1.0% (2012 – decline of 0.2%);
- sales growth in food was moderate;
- sales in drugstore were flat;
- sales in general merchandise, excluding apparel, declined marginally;
- sales growth in apparel was modest;
- sales growth in gas bar was moderate;
- Loblaw's average annual internal food price inflation was lower than the average annual national food price inflation of 1.1% (2012 – 2.3%) as measured by CPI. CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores; and
- 26 (2012 – 18) corporate and franchise stores were opened and 13 (2012 – 11) corporate and franchise stores were closed, resulting in a net increase of 0.4 million square feet, or 0.8%.

In 2013, Loblaw launched over 550 new control brand products and redesigned and/or improved the product or packaging of approximately 640 other products. Sales of control brand products in 2013 were $9.6 billion, flat to 2012 on a comparable basis.

Loblaw sales for 2013 were also positively impacted by an increase in revenue of $95 million, or 14.8%, from its Financial Services segment when compared to 2012. The increase was primarily driven by higher interest income, interchange and other service fee related income, driven by higher credit card receivable balances and increased credit card transaction values. Higher *PC* Telecom revenues resulting from growth in the Mobile Shop business also contributed to the increase.

**Operating Income** Loblaw operating income of $1,308 million for 2013 increased $121 million, or 10.2%, compared to $1,187 million in 2012, resulting in an increase in operating margin to 4.0% in 2013 from 3.8% in 2012. Loblaw operating income was positively impacted by the gain related to the defined benefit plan amendments of $51 million, favourable year-over-year changes in fixed asset and other related (recoveries) impairments of $51 million partially offset by a number of other items. For a complete list of items which impacted operating income but that are excluded from adjusted operating income[1], see Section 22, "Non-GAAP Financial Measures" of this MD&A. In addition, operating income was positively impacted by an improvement in underlying operating performance of $22 million, or 1.7%, as described below.

Gross profit generated by Loblaw's Retail segment increased by $147 million in 2013 to $6,966 million compared to $6,819 million, driven by higher sales. Gross profit as a percentage of retail sales remained flat at 22.0% when compared to 2012 and included the negative impacts of continued investments in food margins, offset by lower transportation costs and margin improvements in general merchandise.

Loblaw adjusted operating income[1] increased to $1,317 million in 2013 from $1,295 million in 2012 and adjusted operating margin[1] remained flat at 4.1% in 2013 when compared to 2012. The increase in adjusted operating income[1] was primarily driven by an improvement in the underlying operating performance of Loblaw's Financial Services segment, partially offset by a decline in the underlying operating performance of Loblaw's Retail segment.

The improvement in the underlying operating performance of Loblaw's Financial Services segment was mainly attributable to the higher revenues described above, partially offset by continued investments in marketing, customer acquisitions and the Mobile Shop business. The decrease in Loblaw's Retail segment adjusted operating income[1] was primarily driven by investments in, and changes to the value of Loblaw's franchise business, increased other operating costs, including depreciation and amortization, costs related to the growth in certain of Loblaw's emerging businesses and foreign exchange losses, partially offset by higher gross profit and supply chain efficiencies.

In 2013, total restructuring charges recorded in operating income were approximately $35 million, including $32 million associated with the reduction of approximately 275 store-support positions. In 2012, restructuring charges of $61 million associated with the reduction in head office and administrative positions were recorded in operating income and other charges of $11 million were recorded in operating income related to changes in Loblaw's distribution network.

Adjusted EBITDA[1] increased by $69 million, or 3.3%, to $2,141 million in 2013 compared to $2,072 million in 2012. Adjusted EBITDA margin[1] remained flat at 6.6% when compared to 2012. Loblaw's depreciation and amortization increased by $47 million compared to 2012.

## 8. OTHER BUSINESS MATTERS

**IT and Other Systems Implementations** Loblaw is undertaking a major upgrade of its IT infrastructure which began in 2010. This project represents one of the largest technology infrastructure programs ever implemented by Loblaw and is fundamental to its long term growth strategies. During 2013, Loblaw continued to make progress with the implementation and to date has successfully implemented the system in eight distribution centres and 75 stores, including 16 *Joe Fresh* stores, with little to no impact on customers. Loblaw is focused on optimizing data, systems and processes to continue to build a stable foundation for the roll-out and now expects the system to be implemented in all of its distribution centres and corporate retail stores by the end of 2014.

**Inventory Valuation** Loblaw values merchandise inventories at the lower of cost and net realizable value and uses the retail method to measure the cost of the majority of its retail store inventories. With the upgrade of its IT infrastructure, Loblaw expects to complete the conversion of its corporate retail stores to a perpetual inventory management system in 2014. The implementation of a perpetual inventory system combined with visibility to integrated costing information provided by the new IT systems will enable Loblaw to estimate the cost of inventory using a system-generated weighted average cost. Any changes to inventory cost would be reflected as an adjustment to Loblaw's inventory with an offsetting adjustment recorded in gross profit.

## 9. LIQUIDITY AND CAPITAL RESOURCES

### 9.1 CASH FLOWS

| For the years ended December 31<br>($ millions) | 2013 | 2012 |
|---|---|---|
| Cash flows from (used in) continuing operations: | | |
| Operating activities | **$ 1,738** | $ 1,852 |
| Investing activities | **$ (1,675)** | $ (916) |
| Financing activities | **$ 1,142** | $ (711) |
| Cash flows from discontinued operations | **$ 48** | |

**Cash Flows from (used in) Continuing Operations**

***Cash flows from operating activities*** Cash flows from operating activities in 2013 were $1,738 million compared to $1,852 million in 2012. The decrease was due to higher investments in Loblaw's working capital and credit card receivables, partially offset by net proceeds from the settlement of derivatives, higher cash earnings and lower contributions to the Company's defined benefit plans.

Loblaw's working capital investments were affected by higher accounts receivable balances as a result of increases in the apparel business and vendor related receivables, the timing of the collection of other taxes recoverable and an increase in accrued liabilities due to costs related to the Shoppers Drug Mart acquisition.

***Cash flows used in investing activities*** Cash flows used in investing activities in 2013 were $1,675 million compared to $916 million in 2012, an increase of $759 million. The increase was primarily due to an increase in cash placed in security deposits, partially offset by a decrease in short term investments and lower fixed asset purchases.

The increase in security deposits in 2013 was primarily due to the funds placed in escrow related to the issuance of $1.6 billion aggregate principal amount of senior unsecured notes, which will be used to partially fund the acquisition of all the outstanding common shares of Shoppers Drug Mart as described in Section 6.1, "Significant Accomplishments in 2013" of this MD&A.

The Company's capital investment in 2013 was $1.0 billion (2012 – $1.1 billion). Weston Foods' capital investment was $111 million (2012 – $93 million). Loblaw's capital investment was $0.9 billion (2012 – $1.0 billion). Approximately 14% (2012 – 15%) of Loblaw's investment was for new store developments, expansions and land, approximately 45% (2012 – 31%) was for store conversions and renovations, and approximately 41% (2012 – 54%) was for infrastructure investments.

Loblaw's 2013 corporate and franchise store capital investment program, which included the impact of store openings and closures, resulted in an increase in net retail square footage of 0.8% compared to 2012 (2012 – 0.6%). During 2013, 26 (2012 – 18) corporate and franchise stores were opened and 13 (2012 – 11) corporate and franchise stores were closed, resulting in a net increase of 0.4 million (2012 – 0.3 million) square feet. In 2013, 192 (2012 – 181) corporate and franchise stores were renovated.

Loblaw expects to invest approximately $1.0 billion in capital expenditures in 2014. Approximately 21% of these funds are expected to be dedicated to investing in IT and supply chain projects, 63% will be spent on retail operations and 16% on other infrastructure.

***Cash flows from (used in) financing activities*** Cash flows from financing activities in 2013 were $1,142 million compared to $711 million used in 2012. The increase of $1,853 million cash inflows was primarily due to net issuances of long term debt and net proceeds from the offering of Choice Properties' Units, partially offset by the repayment of short term debt and the purchases of GWL and Loblaw common shares under their respective Normal Course Issuer Bid ("NCIB") programs as detailed below.

During 2013, the Company completed the following financing activities:

- GWL issued 258,418 common shares on the exercise of stock options for cash consideration of $17 million;
- GWL purchased under its NCIB 800,000 common shares for $57 million, of which 580,000 common shares were cancelled and the remaining 220,000 common shares were placed into trusts for future settlement of GWL's Restricted Share Unit ("RSU") and Performance Share Unit ("PSU") obligations;
- GWL issued $41 million of Series B Debentures;
- Loblaw repaid a $200 million 5.40% medium term note ("MTN");
- Loblaw issued 2,131,416 common shares on the exercise of stock options for cash consideration of $75 million;
- Loblaw purchased under its NCIB 2,603,500 common shares for $119 million, of which 1,500,000 common shares were cancelled and the remaining 1,103,500 common shares were placed into trusts for future settlement of Loblaw's RSU and PSU obligations;
- Loblaw issued $1.6 billion aggregate principal amount of senior unsecured notes to partially fund the acquisition of the outstanding common shares of Shoppers Drug Mart;
- *Eagle Credit Card Trust*® *("Eagle")* issued $400 million of senior and subordinated term notes and repaid $250 million of senior and subordinated term notes which matured;
- Loblaw repaid its U.S. $300 million USPP notes, of which $150 million was paid in advance of the original May 29, 2015 maturity date;
- Choice Properties' public offering of $600 million aggregate principal amount of Debentures and proceeds of $460 million from the offering of Units; and
- PC Bank issued $167 million of Guaranteed Investment Certificates ("GICs") and repaid $40 million in GICs.

During 2012, the Company completed the following financing activities:

- GWL issued $39 million of Series B Debentures;
- GWL issued 41,361 common shares on the exercise of stock options for cash consideration of $2 million;
- GWL purchased for cancellation 9,212 common shares for $1 million;
- Loblaw issued 718,544 common shares on the exercise of stock options for cash consideration of $22 million;
- Loblaw purchased for cancellation 423,705 common shares for $16 million; and
- PC Bank issued $76 million of GICs and repaid $49 million in GICs.

**Cash Flows from Discontinued Operations** In 2013, the Company settled a previously disclosed litigation associated with the Company's (excluding Loblaw) previously owned operations. The Company received net proceeds of $48 million.

**Free Cash Flow**[(1)]

| For the years ended December 31<br>(unaudited)<br>($ millions) | **2013** | 2012 |
|---|---|---|
| Free cash flow[(1)] | **$ 529** | $ 490 |

In 2013, free cash flow[(1)] of $529 million increased by $39 million compared to $490 million in 2012. The increase in free cash flow[(1)] was primarily due to a decrease in fixed asset purchases partially offset by lower cash flows from operating activities as described above.

**Defined Benefit Pension Plan Contributions** During 2014, the Company expects to contribute approximately $54 million (2013 – contributed $118 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. During 2014, the Company also expects to make contributions to its defined contribution plans and the MEPPs in which it participates as well as make benefit payments to the beneficiaries of the supplemental unfunded defined benefit pension plans, other defined benefit plans and other long term employee benefit plans.

### 9.2 LIQUIDITY AND CAPITAL STRUCTURE

The Company holds significant cash and cash equivalents, short term investments and security deposits denominated in Canadian and U.S. dollars. These funds are invested in highly liquid marketable short term investments consisting primarily of bankers' acceptances, government treasury bills, corporate commercial paper, bank term deposits and government agency securities. During 2013, cash and cash equivalents, short term investments and security deposits increased by $2,075 million largely driven by key financing activities completed by the Company including the financing related to the agreement to acquire Shoppers Drug Mart, as described below, and the $460 million and $600 million of proceeds from Choice Properties' IPO and debt offering, respectively, net of the repayment of U.S. $300 million USPP notes and a $200 million MTN which matured in 2013.

**Prospectuses** In 2013, GWL filed a Short Form Base Shelf Prospectus allowing for the issuance of up to $1 billion of unsecured debentures and/or preferred shares over a 25-month period subject to the availability of funding in capital markets.

In 2013, Loblaw amended its Short Form Base Shelf Prospectus dated December 21, 2012 to increase the amount issuable under the prospectus to $2.5 billion from $1 billion in order to assist with the financing of the Shoppers Drug Mart acquisition as described in Section 6.1, "Significant Accomplishments in 2013" of this MD&A.

In 2013, *Eagle* filed a Short Form Base Shelf Prospectus which allows for the potential issuance of up to $1.5 billion of notes over a 25-month period.

In 2013, Choice Properties filed a Short Form Base Shelf Prospectus allowing for the issuance of up to $2 billion of Units and debt securities over a 25-month period subject to the availability of funding in capital markets. Subsequent to the end of the year, Choice Properties issued $250 million principal amount of Series C senior unsecured debentures with a 7-year term and a coupon rate of 3.498% per annum and $200 million principal amount of Series D senior unsecured debentures with a 10-year term and a coupon rate of 4.293% per annum, under its Short Form Base Shelf Prospectus.

**Shoppers Drug Mart Financing** In connection with the agreement to acquire Shoppers Drug Mart, Loblaw entered into committed bank facilities, consisting of a $3.5 billion term loan facility and a $1.6 billion bridge loan facility. Loblaw subsequently issued $1.6 billion aggregate principal amount of senior unsecured notes under its Short Form Base Shelf Prospectus and concurrently cancelled the $1.6 billion bridge loan facility. These proceeds will be released from escrow upon satisfaction of the applicable release conditions of the agreement and used to partially fund the acquisition of all of the outstanding common shares of Shoppers Drug Mart.

**Committed Facilities** In 2013, Loblaw amended its $800 million committed credit facility to increase the amount to $1 billion, subject to the successful close of the Shoppers Drug Mart transaction, and extended the term to December 31, 2018. In addition, Loblaw incorporated certain adjustments to exclude the impact of Choice Properties from its covenant calculations. Loblaw was in compliance with these covenants throughout the year. As at year end 2013 and 2012, there were no amounts drawn under the committed credit facility.

In addition, in 2013, Choice Properties entered into an agreement for a $500 million, 5-year senior unsecured committed credit facility provided by a syndicate of lenders. This facility contains certain financial covenants. Choice Properties was in compliance with these covenants throughout the year and as at year end 2013, there were no amounts drawn under this facility.

**Future Liquidity** The Company (excluding Loblaw) expects that cash and cash equivalents, short term investments and future operating cash flows will enable it to finance its capital investment program and fund its ongoing business requirements, including working capital, pension plans and financial obligations over the next 12 months. The Company (excluding Loblaw) does not foresee any impediments in obtaining financing to satisfy its long term obligations.

Loblaw 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 Loblaw to finance its capital investment program and fund its ongoing business requirements, including working capital, pension plans and financial obligations over the next 12 months. If required, Loblaw expects it could obtain long term financing through its MTN program. Choice Properties expects to obtain its long term financing primarily through the issuance of equity and unsecured debentures. In addition, Loblaw expects that it has sufficient financing available to fund the cash portion of the proposed Shoppers Drug Mart purchase price.

**Adjusted Debt(1) to Adjusted EBITDA(1)**

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Adjusted debt(1) to Adjusted EBITDA(1) | **2.9x** | 2.3x |

The Company monitors its adjusted debt(1) to adjusted EBITDA(1) ratio as a measure to ensure it is operating under an efficient capital structure. The ratio increased in 2013 primarily due to the issuance of long term debt related to Choice Properties and the Shoppers Drug Mart transaction. The ratio is expected to further increase upon closing of the Shoppers Drug Mart acquisition as Loblaw draws up to $3.5 billion of its committed term loan to partially fund the cash consideration. The Company will continue to target leverage ratios consistent with those of investment grade ratings.

The following are excluded from adjusted debt(1):

**Independent Funding Trusts** Certain independent franchisees of Loblaw obtain financing through a structure involving independent funding trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets. These independent funding trusts are administered by a major financial institution. As at year end 2013, the independent funding trusts had drawn $475 million (2012 – $459 million) from the revolving committed credit facility that is the source of funding to the independent funding trusts. Loblaw intends to renew this committed credit facility, which expires in 2014.

Loblaw has agreed to provide a credit enhancement of $48 million (2012 – $48 million) in the form of a standby letter of credit for the benefit of the independent funding trusts representing not less than 10% (2012 – 10%) of the principal amount of loans outstanding. As at year end 2013, Loblaw had provided a letter of credit in the amount of $48 million (2012 – $48 million). This credit enhancement allows the independent funding trusts to provide financing to Loblaw'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 Loblaw 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 Loblaw and draw upon this standby letter of credit. This standby letter of credit has never been drawn upon. Loblaw has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit.

**Independent Securitization Trusts** Loblaw, 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 to Independent Securitization Trusts, including *Eagle* and Other Independent Securitization Trusts, from time to time depending on PC Bank's financing requirements.

Loblaw has arranged letters of credit on behalf of PC Bank, representing 9% (2012 – 9%) of the outstanding securitized liability for the benefit of the Other Independent Securitization Trusts in the amount of $54 million (2012 – $81 million). In 2013, PC Bank repurchased $300 million (2012 – nil) of co-ownership interests in the securitized receivables from Other Independent Securitization Trusts and, as a result, the letters of credit outstanding were reduced to $54 million. In the event of a major decline in the income flow from, or in the value of, the securitized credit card receivables, the Other Independent Securitization Trusts can draw upon these letters of credit to recover up to a maximum of the amount outstanding on the letters of credit. 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 throughout the year. During 2013, PC Bank amended and extended the maturity date for one of its Other Independent Securitization Trust agreements from the third quarter of 2014 to the third quarter of 2015, with no material impact to other terms and conditions.

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%.

In 2013, the three-year $250 million senior and subordinated term notes issued by *Eagle* matured and were repaid.

Subsequent to the end of 2013, 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.

**Guaranteed Investment Certificates** The following table summarizes PC Bank's GICs activity, before commissions:

| ($ millions) | **2013** | 2012 |
|---|---|---|
| Balance, beginning of year | **$ 303** | $ 276 |
| GICs issued | **167** | 76 |
| GICs matured | **(40)** | (49) |
| Balance, end of year | **$ 430** | $ 303 |

As at year end 2013, $52 million (2012 – $36 million) in GICs were recorded as long term debt due within one year.

### 9.3 CREDIT RATINGS

In 2013, following a review of the implications of Loblaw's agreement to acquire Shoppers Drug Mart, both Dominion Bond Rating Service and Standard & Poor's re-confirmed GWL, Loblaw and Choice Properties' credit ratings.

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

| | Dominion Bond Rating Service | | Standard & Poor's | |
|---|---|---|---|---|
| Credit Ratings (Canadian Standards) | Credit Rating | Trend | Credit Rating | Outlook |
| Issuer ratings | 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 Loblaw:

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

### 9.4 SHARE CAPITAL

**Outstanding Share Capital and Capital Securities** GWL's outstanding share capital is comprised of common shares and preferred shares. The following table details the authorized and outstanding common shares and preferred shares as at December 31, 2013:

| | | Authorized | Outstanding |
|---|---|---|---|
| Common shares | | Unlimited | 127,899,410 |
| Preferred shares | – Series I | 10,000,000 | 9,400,000 |
| | – Series II | 10,600,000 | |
| | – Series III | 10,000,000 | 8,000,000 |
| | – Series IV | 8,000,000 | 8,000,000 |
| | – Series V | 8,000,000 | 8,000,000 |

GWL may, at its option, redeem for cash, in whole or in part, the preferred shares Series I, Series III, Series IV and Series V outstanding on or after the redemption dates specified by the terms of each series of preferred shares. GWL may at any time after issuance give the holders of these preferred shares the right, at the option of the holder, to convert the holder's preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

At year end 2013, a total of 1,491,168 GWL stock options were outstanding, representing 1.2% of GWL's issued and outstanding common shares. The number of stock options outstanding was within the Company's guidelines of 5% of the total number of outstanding shares. Each stock option is exercisable into one common share of GWL at the price specified in the terms of the option agreement.

Twelve million non-voting Loblaw Second Preferred Shares, Series A, are authorized and 9.0 million were outstanding at year end 2013. These preferred shares are presented as capital securities and are included in long term liabilities on the consolidated balance sheets. Dividends on capital securities are presented in net interest expense and other financing charges on the consolidated statements of earnings.

**Dividends** The declaration and payment of dividends on the Company's common shares and the amount thereof are at the discretion of the Company's Board of Directors ("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. In the second quarter of 2013, the Board raised the quarterly common share dividend by $0.035 to $0.415 per share, following a $0.02 increase in the fourth quarter of 2012 to $0.38 per share. The Board declared dividends as follows:

| ($) | | | **2013** | | 2012 |
|---|---|---|---|---|---|
| Dividends declared per share[(i)] | – Common share | **$** | **1.625** | $ | 1.460 |
| | – Preferred share: | | | | |
| | Series I | **$** | **1.45** | $ | 1.45 |
| | Series III | **$** | **1.30** | $ | 1.30 |
| | Series IV | **$** | **1.30** | $ | 1.30 |
| | Series V | **$** | **1.19** | $ | 1.19 |

(i) Dividends declared on common shares and Preferred Shares, Series III, Series IV and Series V were paid on January 1, 2014. Dividends declared on Preferred Shares, Series I were paid on December 15, 2013.

The following table summarizes the Company's cash dividends declared subsequent to year end 2013:

| ($) | | | |
|---|---|---|---|
| Dividends declared per share[(i)] | – Common share | **$** | **0.415** |
| | – Preferred share: | | |
| | Series I | **$** | **0.36** |
| | Series III | **$** | **0.32** |
| | Series IV | **$** | **0.32** |
| | Series V | **$** | **0.30** |

(i) Dividends declared on common shares and Preferred Shares, Series III, Series IV and Series V are payable on April 1, 2014. Dividends declared on Preferred Shares, Series I are payable on March 15, 2014.

At the time such dividends are declared, GWL identifies on its website (www.weston.ca) the designation of eligible and ineligible dividends in accordance with the administrative position of the Canada Revenue Agency ("CRA").

**Normal Course Issuer Bid Programs** In 2013, GWL and Loblaw renewed their NCIB programs to purchase on the TSX or enter into equity derivative contracts to purchase up to 6,382,723 (2012 – 6,409,499) and 14,103,672 (2012 – 14,070,352) of their common shares, respectively, representing approximately 5% of the common shares outstanding. In accordance with the rules and regulations of the TSX, any purchases must be at the then market price of such shares. Also in 2013, Loblaw entered into an automatic share repurchase agreement under its NCIB that permits Loblaw to buy back its shares during blackout periods in accordance with predetermined instructions. Both GWL and Loblaw intend to renew their NCIB programs in 2014.

In 2013, GWL purchased 800,000 common shares under its NCIB for cash consideration of $57 million. Of the 800,000 common shares purchased, 580,000 common shares were cancelled and the remaining 220,000 common shares were placed into trusts for future settlement of GWL's RSU and PSU obligations.

In 2013, Loblaw purchased for cancellation 1,500,000 (2012 – 423,705) of its common shares under its NCIB for $73 million (2012 – $16 million).

Also in 2013, Loblaw purchased 1,103,500 common shares under its NCIB for $46 million and placed these shares into trusts for future settlement of Loblaw's RSU and PSU obligations.

In 2012, GWL purchased for cancellation 9,212 of its common shares for $1 million.

### 9.5 CONTRACTUAL OBLIGATIONS

The following table illustrates certain of the Company's significant contractual obligations and discusses other obligations as at year end 2013:

**Summary of Contractual Obligations**

| | Payments due by year | | | | | | |
|---|---|---|---|---|---|---|---|
| ($ millions) | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter | Total |
| Long term debt including fixed interest payments(i) | $ 1,597 | $ 772 | $ 1,137 | $ 452 | $ 1,334 | $ 8,702 | $ 13,994 |
| Operating leases(ii) | 214 | 196 | 165 | 137 | 112 | 453 | 1,277 |
| Contracts for purchase of real property and capital investment projects(iii) | 85 | 1 | 1 | | | | 87 |
| Purchase obligations(iv) | 243 | 99 | 62 | 43 | 43 | | 490 |
| Total contractual obligations | $ 2,139 | $ 1,068 | $ 1,365 | $ 632 | $ 1,489 | $ 9,155 | $ 15,848 |

(i) 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.

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

As at year end 2013, 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 in the table above as the timing and amount of future payments are uncertain.

In addition, in accordance with the July 14, 2013 arrangement agreement between Loblaw and Shoppers Drug Mart, Loblaw is required to pay consideration of up to approximately $6.7 billion in cash and issue up to approximately 119.9 million common shares in exchange for all of the outstanding common shares of Shoppers Drug Mart. As part of the financing of the acquisition, GWL has agreed to subscribe for approximately $500 million of additional Loblaw common shares as described in Section 6.1, "Significant Accomplishments in 2013" of this MD&A.

## 10. FINANCIAL 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 these swaps. The cross currency swaps were offset by the effect of translation (gains) losses related to U.S. dollar cash and cash equivalents, short term investments and security deposits. As at year end 2012, a cumulative unrealized foreign currency exchange rate receivable of $20 million was recorded in prepaid expenses and other assets, and a receivable of $93 million was recorded in other assets related to these swaps.

The following table summarizes the changes in fair value of the Glenhuron cross currency swaps and the underlying exposures:

| ($ millions) | 2013 | 2012 |
|---|---|---|
| Fair value loss (gain) related to swaps recorded in operating income | **$ 37** | $ (25) |
| Translation (gain) loss related to the underlying exposures | **$ (33)** | $ 27 |

In 2013, Loblaw settled its U.S. $300 million USPP cross currency swaps in conjunction with the settlement of the underlying U.S. $300 million USPP notes and received a net cash settlement of $18 million. The USPP cross currency swaps were used to manage the effect of translation (gains) losses on the underlying U.S. dollar USPP notes in long term debt. As part of the full settlement, Loblaw settled its U.S. $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 (loss) was realized in operating income.

As at year end 2012, a cumulative unrealized foreign currency exchange rate receivable of $2 million was recorded in prepaid expenses and other assets, and a receivable of $5 million was recorded in other assets related to the USPP cross currency swaps.

The following table summarizes the changes in fair value of the USPP cross currency swaps and the underlying exposures:

| ($ millions) | 2013 | 2012 |
|---|---|---|
| Fair value (gain) loss related to swaps recorded in operating income(i) | **$ (11)** | $ 7 |
| Translation loss (gain) related to the underlying exposures | **$ 14** | $ (6) |

(i) Excludes the gain of $7 million reclassified from accumulated other comprehensive income (loss) in 2013.

**Interest Rate Swaps** In 2013, Loblaw settled its notional $150 million in interest rate swaps. As at year end 2012, Loblaw held notional $150 million in interest rate swaps, on which Loblaw paid a fixed-rate of 8.38% and recorded a cumulative loss of $5 million in trade payables and other liabilities.

During 2013, Loblaw recognized a fair value gain of $5 million (2012 – $11 million) in operating income related to these swaps.

**Equity Derivative Contracts** As at year end 2013, Weston Holdings Limited ("WHL"), a subsidiary of GWL, held an outstanding equity forward sale agreement based on 9.6 million Loblaw common shares at an original forward price of $48.50 per Loblaw common share. As at year end 2013, the forward price had increased to $96.46 (2012 – $92.26) per Loblaw common share under the terms of the agreement and the fair value of this forward sale agreement of $524 million (2012 – $483 million) was recorded in other assets. In 2013, a fair value gain of $1 million (2012 – loss of $35 million) was recorded in net interest expense and other financing charges related to this agreement.

Also in 2013, GWL paid $29 million to settle its remaining equity swap contract representing 800,000 GWL common shares and recorded a nominal loss (2012 – fair value gain of $2 million) in operating income related to this equity swap contract. As at year end 2012, the unrealized market loss of $29 million was recorded in trade payables and other liabilities.

Also in 2013, Glenhuron paid $16 million to settle its remaining equity forward contract representing 1,103,500 Loblaw common shares and recorded a nominal loss (2012 – fair value gain of $5 million) in operating income related to this equity forward contract. As at year end 2012, the cumulative accrued interest and unrealized market loss of $16 million was included in trade payables and other liabilities.

**Other Loblaw Derivatives** In connection with Loblaw's issuance of $1.6 billion of senior unsecured notes in 2013, Loblaw hedged its exposure to interest rates in the period prior to the issuance. This relationship did not qualify for hedge accounting resulting in a gain of $10 million on the unwind of the hedge, which was recorded in net interest expense and other financing charges.

The nature of the risks that the Company may be subject to related to the above financial derivative instruments are described in Section 16.2, "Financial Risks and Risk Management" of this MD&A.

## 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 Loblaw's independent franchisees. The aggregate gross potential liability related to the Company's letters of credit is approximately $564 million (2012 – $570 million).

GWL and Loblaw had agreements to cash collateralize certain of these letters of credit up to amounts of $45 million (2012 – $45 million) and $136 million (2012 – $133 million), respectively. As at year end 2013, GWL and Loblaw had $45 million (2012 – $45 million) and $102 million (2012 – $97 million) deposited with major financial institutions, respectively, and classified as security deposits on the consolidated balance sheets.

**Guarantees** In addition to the letters of credit mentioned above, the Company has entered into various guarantee agreements including obligations to indemnify third parties in connection with leases, business dispositions and other transactions in the normal course of the Company's business. Additionally, Loblaw has provided a guarantee on behalf of PC Bank to MasterCard® International Incorporated for accepting PC Bank as a card member and licensee of MasterCard®. In 2013, Loblaw decreased its guarantee on behalf of PC Bank to MasterCard® International Incorporated to U.S. $170 million (2012 – U.S. $230 million).

## 12. QUARTERLY RESULTS OF OPERATIONS

### 12.1 QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

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 information derived from the Company's unaudited interim period condensed consolidated financial statements for each of the eight recently completed quarters.

**Selected Quarterly Information (unaudited)**

| | | | | | **2013** | | | | | 2012[5] |
|---|---|---|---|---|---|---|---|---|---|---|
| ($ millions except where otherwise indicated) | **First Quarter** | **Second Quarter** | **Third Quarter** | **Fourth Quarter** | **Total (audited)** | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Total (audited) |
| Sales | **$ 7,494** | **$ 7,792** | **$ 10,377** | **$ 7,919** | **$ 33,582** | $ 7,224 | $ 7,627 | $ 10,164 | $ 7,727 | $ 32,742 |
| Net earnings from continuing operations | **$ 225** | **$ 164** | **$ 228** | **$ 232** | **$ 849** | $ 166 | $ 193 | $ 237 | $ 112 | $ 708 |
| Discontinued operations | | | **$ 58** | | **$ 58** | | | | | |
| Net earnings | **$ 225** | **$ 164** | **$ 286** | **$ 232** | **$ 907** | $ 166 | $ 193 | $ 237 | $ 112 | $ 708 |
| Net earnings from continuing operations attributable to shareholders of the Company | **$ 162** | **$ 98** | **$ 171** | **$ 185** | **$ 616** | $ 121 | $ 135 | $ 156 | $ 63 | $ 475 |
| Net earnings per common share ($) - basic | | | | | | | | | | |
| Continuing operations | **$ 1.19** | **$ 0.69** | **$ 1.23** | **$ 1.37** | **$ 4.48** | $ 0.87 | $ 0.98 | $ 1.11 | $ 0.41 | $ 3.36 |
| Discontinued operations | | | **$ 0.46** | | **$ 0.46** | | | | | |
| Net earnings | **$ 1.19** | **$ 0.69** | **$ 1.69** | **$ 1.37** | **$ 4.94** | $ 0.87 | $ 0.98 | $ 1.11 | $ 0.41 | $ 3.36 |
| Net earnings per common share ($) - diluted | | | | | | | | | | |
| Continuing operations | **$ 1.18** | **$ 0.68** | **$ 1.22** | **$ 1.37** | **$ 4.45** | $ 0.87 | $ 0.97 | $ 1.03 | $ 0.32 | $ 3.29 |
| Discontinued operations | | | **$ 0.46** | | **$ 0.46** | | | | | |
| Net earnings | **$ 1.18** | **$ 0.68** | **$ 1.68** | **$ 1.37** | **$ 4.91** | $ 0.87 | $ 0.97 | $ 1.03 | $ 0.32 | $ 3.29 |
| Loblaw's average national food price inflation (as measured by CPI) | **1.4%** | **1.5%** | **0.9%** | **0.9%** | **1.1%** | 3.7 % | 2.5% | 1.8 % | 1.5% | 2.3 % |
| Loblaw's retail same-store sales growth (decline) | **2.8%** | **1.1%** | **0.4%** | **0.6%** | **1.1%** | (0.7)% | 0.2% | (0.2)% | | (0.2)% |

**Impact of Trends and Seasonality on Quarterly Results**

***Sales*** Consolidated quarterly sales for the last eight quarters were impacted by the following significant items: foreign currency exchange rates, seasonality and the timing of holidays. The impact of Weston Foods seasonality is greatest in the third and fourth quarters and least in the first quarter. The impact of Loblaw seasonality is greatest in the fourth quarter and least in the first quarter.

Weston Foods 2013 quarterly sales were negatively impacted by the loss of certain frozen distributed product and positively impacted by foreign currency when compared to the same periods in 2012. Excluding the impact of the loss of distributed product and foreign currency translation, quarterly sales were positively impacted by the combined impact of pricing and changes in sales mix in all four quarters and higher sales volumes in the second, third and fourth quarters. Sales volumes decreased in the first quarter of 2013.

Loblaw's average quarterly internal retail food price inflation for 2013 and 2012 remained lower than the average quarterly national retail food price inflation as measured by CPI. CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores.

Over the past eight quarters, Loblaw's net retail square footage increased by 0.7 million square feet to 51.9 million square feet.

***Net Earnings*** Over the last eight quarters, the Company's consolidated operating income has improved and was impacted by a number of items as outlined in Section 6.4, "Selected Annual Information" of this MD&A.

At Weston Foods, quarterly operating income during 2013 was positively impacted by higher pricing, the benefits realized from productivity improvements and other cost reduction initiatives and higher sales volumes in the second, third and fourth quarters. This improvement was more than offset by investments in growth, marketing and innovation and a decline in the performance of the frozen dough business in the second half of 2013. In addition, commodity and other input costs were higher in the second, third and fourth quarters.

At Loblaw, fluctuations in quarterly operating income during 2013 reflect the underlying operations of Loblaw and were impacted by seasonality and the timing of holidays mentioned above.

Consolidated quarterly net earnings for the last eight quarters were impacted by a number of items as outlined in Section 6.4, "Selected Annual Information" of this MD&A.

### 12.2 FOURTH QUARTER RESULTS (UNAUDITED)

The following is a summary of selected unaudited consolidated financial information for the fourth quarter. The analysis of the data contained in the table focuses on the results of operations and changes in the financial condition and cash flows in the fourth quarter.

**Selected Consolidated Information**

| (unaudited)<br>($ millions except where otherwise indicated) | Quarters Ended<br>**Dec. 31, 2013** | <br>Dec. 31, 2012[5] |
|---|---|---|
| Sales | **$ 7,919** | $ 7,727 |
| Operating income | **$ 394** | $ 321 |
| Adjusted operating income[1] | **$ 374** | $ 382 |
| Adjusted operating margin[1] | **4.7%** | 4.9% |
| Adjusted EBITDA[1] | **$ 585** | $ 583 |
| Adjusted EBITDA margin[1] | **7.4%** | 7.5% |
| Net interest expense and other financing charges | **$ 106** | $ 175 |
| Income taxes | **$ 56** | $ 34 |
| Net earnings attributable to shareholders of the Company | **$ 185** | $ 63 |
| Net earnings | **$ 232** | $ 112 |
| Basic net earnings per common share ($) | **$ 1.37** | $ 0.41 |
| Adjusted basic net earnings per common share[1] ($) | **$ 1.11** | $ 1.00 |
| Cash flows from (used in): | | |
| Operating activities | **$ 813** | $ 680 |
| Investing activities | **$ 605** | $ (94) |
| Financing activities | **$ (398)** | $ (68) |
| Free cash flow[1] | **$ 463** | $ 389 |
| Dividends declared per share ($): | | |
| Common shares | **$ 0.415** | $ 0.380 |
| Preferred shares – Series I | **$ 0.36** | $ 0.36 |
| Preferred shares – Series III | **$ 0.33** | $ 0.33 |
| Preferred shares – Series IV | **$ 0.33** | $ 0.33 |
| Preferred shares – Series V | **$ 0.30** | $ 0.30 |

Adjusted basic net earnings per common share[1] in the fourth quarter of 2013 increased to $1.11 compared to $1.00 in the same period in 2012, an increase of $0.11 or 11.0%. The increase was due to a lower effective income tax rate[3] partially offset by declines in the operating performance of the Company's two operating segments, Weston Foods and Loblaw, compared to the same period in 2012. The lower effective income tax rate[3] was primarily due to an increase in income tax recoveries related to prior year income tax matters and the reversal of previously recognized current tax assets in the fourth quarter of 2012.

Basic net earnings per common share increased to $1.37 compared to $0.41, an increase of $0.96, and was positively impacted by the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common

shares and a number of other items. For a complete list of items which impacted basic net earnings per common share but that are excluded from adjusted basic net earnings per common share[(1)], see Section 22, "Non-GAAP Financial Measures" of this MD&A.

**Sales** Consolidated sales in the fourth quarter of 2013 were $7.9 billion compared to $7.7 billion for the same period in 2012, an increase of 2.5%.

Consolidated sales for the fourth quarter of 2013 were impacted by each reportable operating segment when compared to the same period in 2012 as follows:

- Positively by 0.2% due to the sales growth of 3.5% at Weston Foods despite challenging market conditions. Excluding the impact of the loss of certain frozen products that Weston Foods distributed on behalf of certain customers in 2012 and foreign currency translation, sales increased by 1.6% due to the combined positive impact of pricing and changes in sales mix of 1.4% and an increase in volume of 0.2%.
- Positively by 2.3% due to the sales growth of 2.3% at Loblaw. Same-store sales growth was 0.6% (2012 – flat), positively impacted by the timing of the Thanksgiving holiday, estimated to be between 0.6% and 0.8%, and negatively impacted by an ice storm in Eastern Canada and a strike in Western Canada which negatively impacted same-store sales growth by approximately 0.2% and 0.1%, respectively. The range of same-store sales growth for the quarter, after the impact of these items, was approximately 0.1% to 0.3%. Loblaw's average quarterly internal food price inflation during the fourth quarter of 2013 was lower than the average quarterly national food price inflation of 0.9% (2012 – 1.5%) as measured by CPI. In the last 12 months, corporate and franchise square footage increased 0.8% (2012 – 0.6%). Loblaw sales in the fourth quarter of 2013 were also positively impacted by an increase in Financial Services segment revenue.

**Operating Income** Consolidated operating income in the fourth quarter of 2013 was $394 million compared to $321 million in the same period in 2012. The increase was positively impacted by the favourable year-over-year impact of fixed asset and other related (recoveries) impairments at Loblaw and a number of other items. For a complete list of items which impacted operating income but that are excluded from adjusted operating income[(1)], see Section 22, "Non-GAAP Financial Measures" of this MD&A.

Consolidated adjusted operating income[(1)] in the fourth quarter of 2013 was $374 million compared to $382 million in the same period in 2012, a decrease of $8 million or 2.1%. The Company's consolidated adjusted operating margin[(1)] in the fourth quarter of 2013 decreased to 4.7% from 4.9% in the same period in 2012.

The Company's fourth quarter year-over-year change in consolidated adjusted operating income[(1)] was impacted by each of its reportable operating segments as follows:

- Negatively by 0.8% due to a decrease of 5.3% in adjusted operating income[(1)] at Weston Foods. Adjusted operating income[(1)] was positively impacted by higher sales volumes driven by certain investments, as well as higher pricing and the benefits realized from productivity improvements and other cost reduction initiatives. This improvement was more than offset by a decline in the performance of the frozen dough business, the cost impact of investments, including the impact of changes in sales mix, and higher commodity and other input costs.
- Negatively by 1.3% due to a decrease of 1.5% in adjusted operating income[(1)] at Loblaw. This decrease was primarily driven by a decline in Loblaw's Retail segment, partially offset by an improvement in Loblaw's Financial Services segment. The decrease in Loblaw's Retail segment was primarily driven by investments in, and changes to the value of Loblaw's franchise business, costs related to the growth in certain of Loblaw's emerging businesses and higher other operating costs, including depreciation and amortization, partially offset by higher gross profit and labour efficiencies. The increase in Loblaw's Financial Services segment was mainly attributable to higher revenues, partially offset by higher operating costs and continued investments in marketing and customer acquisitions.

The Company's consolidated adjusted EBITDA margin[1] for the fourth quarter of 2013 decreased to 7.4% from 7.5% in the same period in 2012. The margin was negatively impacted by both Weston Foods and Loblaw when compared to the same period in 2012.

**Net Interest Expense and Other Financing Charges** Net interest expense and other financing charges in the fourth quarter of 2013 decreased to $106 million from $175 million in the same period in 2012. The decrease included the favourable year-over-year impact of the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares of $111 million, partially offset by the unfavourable year-over-year impact of a number of Choice Properties and Shoppers Drug Mart related items recorded in the fourth quarter of 2013 as follows:

- a fair value adjustment related to the Trust Unit liability, reflecting the change in the fair value of Choice Properties' Units held by unitholders other than the Company, of $23 million; and
- net interest expense of $14 million relating to indebtedness incurred to finance the acquisition of Shoppers Drug Mart.

Excluding the above impacts, net interest expense and other financing charges in the fourth quarter of 2013 increased by $5 million, primarily driven by Unit distributions by Choice Properties.

**Income Taxes** In the fourth quarter of 2013 income taxes increased to $56 million from $34 million and the effective income tax rate decreased to 19.4% from 23.3% in the same period in 2012.

The decrease in the effective income tax rate when compared to 2012 was primarily due to an increase in income tax recoveries related to prior year matters, reversal of previously recognized current tax assets in the fourth quarter of 2012 and higher non-taxable foreign currency translation gains partially offset by an increase in non-deductible amounts (including fair value adjustments related to the Trust Unit liability). The Company (excluding Loblaw) expensed current tax assets of $8 million in the fourth quarter of 2012 due to amendments to the Income Tax Act relating to the taxation of Canadian corporations with foreign affiliates.

**Net Earnings Attributable to Shareholders of the Company** Net earnings attributable to shareholders of the Company for the fourth quarter of 2013 were $185 million compared to $63 million in the same period in 2012. Basic net earnings per common share were $1.37 compared to $0.41 in the same period in 2012, an increase of $0.96.

**Cash Flows**

| (unaudited) | Quarters Ended | |
|---|---|---|
| ($ millions) | **Dec. 31, 2013** | Dec. 31, 2012 |
| Cash flows from (used in): | | |
| Operating activities | **$ 813** | $ 680 |
| Investing activities | **$ 605** | $ (94) |
| Financing activities | **$ (398)** | $ (68) |

**Cash flows from operating activities** Fourth quarter 2013 cash flows from operating activities were $813 million compared to $680 million in 2012. The increase in cash flows from operating activities was a result of proceeds from the settlement of derivatives and a more moderate investment in credit card receivables, partially offset by a change in Loblaw's investment in working capital.

Loblaw's working capital investments in the fourth quarter of 2013 were affected by increases in accounts payable as a result of active vendor management, increases in accounts receivable as a result of increases in vendor related receivables and the timing of the collection of other taxes recoverable.

**Cash flows from (used in) investing activities** Fourth quarter 2013 cash flows from investing activities were $605 million compared to $94 million used in 2012. The change was primarily driven by a decrease 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** Fourth quarter 2013 cash flows used in financing activities were $398 million compared to $68 million in 2012. The increase of $330 million cash outflows was primarily due to the repayment of short term debt and net repayments of long term debt in the fourth quarter of 2013 compared to the fourth quarter of 2012.

During the fourth quarter of 2013, GWL and Loblaw completed the following financing activities:
- GWL issued 3,000 common shares on the exercise of stock options for nominal cash consideration;
- GWL issued $11 million of Series B Debentures;
- Loblaw repaid a $200 million 5.40% MTN;
- Loblaw issued 218,915 common shares on the exercise of stock options for cash consideration of $8 million;
- *Eagle* issued $400 million of senior and subordinated term notes and repaid $250 million of senior and subordinated term notes; and
- PC Bank issued $69 million of GICs and repaid $4 million in GICs.

During the fourth quarter of 2012, GWL and Loblaw completed the following financing activities:
- GWL issued $10 million of Series B Debentures;
- GWL issued 34,030 common shares on the exercise of stock options for cash consideration of $2 million;
- GWL purchased for cancellation 4,297 common shares for a nominal amount;
- Loblaw issued 474,747 common shares on the exercise of stock options for cash consideration of $15 million;
- Loblaw purchased for cancellation 246,228 common shares for $10 million; and
- PC Bank issued $61 million of GICs and repaid $2 million in GICs.

**Free Cash Flow**[(1)]

| (unaudited) ($ millions) | Quarters Ended Dec. 31, 2013 | Dec. 31, 2012 |
|---|---|---|
| Free cash flow[(1)] | **$ 463** | $ 389 |

The Company's free cash flow[(1)] was $463 million in the fourth quarter of 2013 compared to $389 million in the same period 2012. The increase was primarily due to an increase in cash flows from operating activities and a decrease in interest paid, partially offset by a decrease in credit card receivables.

## 13. FOURTH QUARTER RESULTS OF REPORTABLE OPERATING SEGMENTS

The following discussion provides details of the 2013 fourth quarter results of operations of each of the Company's reportable operating segments.

### 13.1 WESTON FOODS FOURTH QUARTER OPERATING RESULTS

**WESTON FOODS**

| (unaudited) ($ millions except where otherwise indicated) | Quarters Ended Dec. 31, 2013 | Dec. 31, 2012[(5)] |
|---|---|---|
| Sales | **$ 413** | $ 399 |
| Operating income | **$ 40** | $ 44 |
| Adjusted operating income[(1)] | **$ 54** | $ 57 |
| Adjusted operating margin[(1)] | **13.1%** | 14.3% |
| Adjusted EBITDA[(1)] | **$ 69** | $ 71 |
| Adjusted EBITDA margin[(1)] | **16.7%** | 17.8% |

For the fourth quarter of 2013, Weston Foods sales increased by 3.5% to $413 million from $399 million and volumes increased by 0.1% compared to the same period in 2012. Excluding the impact of the loss of certain frozen products that Weston Foods distributed on behalf of certain customers in 2012 and foreign currency translation, sales increased by 1.6% due to the combined positive impact of pricing and changes in sales mix of 1.4% and an increase in volume of 0.2%. The loss of certain frozen distributed products negatively impacted sales and volume growth by approximately 0.6% and 0.1%, respectively. Foreign currency translation positively impacted sales by approximately 2.5%.

The following sales analysis excludes the impact of foreign currency translation. In the fourth quarter of 2013:

- fresh bakery sales increased by approximately 5.8% mainly driven by the positive impact of pricing and changes in sales mix, as well as higher sales volumes. The introduction of new products, such as *Country Harvest* Veggie, Sprouted Multigrain and Wheat breads, *D'Italian*o line of snack products and the launch of gluten free bread and sweet goods, including the *All But Gluten* brand, contributed positively to branded sales;
- frozen bakery sales decreased by approximately 2.2% and were negatively impacted by the loss of certain distributed products. Excluding the effects of the loss of these distributed products, frozen bakery sales decreased by approximately 1.2% driven by lower volumes in certain product categories, including frozen dough products, partially offset by the positive impact of pricing and changes in sales mix; and
- biscuit sales increased by approximately 1.2% mainly due to higher volumes partially offset by the negative impact of pricing and changes in sales mix. Volumes increased in the fourth quarter of 2013 compared to the same period in 2012 due to growth in cone and wafer sales, partially offset by lower cookie sales, including Girl Scout products.

Weston Foods operating income was $40 million in the fourth quarter of 2013 compared to $44 million in the same period in 2012. Operating margin for the fourth quarter of 2013 was 9.7% compared to 11.0% in the same period in 2012.

Gross margin, excluding the impact of the commodity derivatives fair value adjustment, remained flat in the fourth quarter of 2013 compared to the same period in 2012.

Adjusted operating income[1] decreased by $3 million, or 5.3%, to $54 million in the fourth quarter of 2013 from $57 million in the same period in 2012. Adjusted operating margin[1] was 13.1% for the fourth quarter of 2013 compared to 14.3% in the same period in 2012.

Adjusted operating income[1] in the fourth quarter of 2013 was positively impacted by higher sales volumes driven by investments in growth, marketing and innovation, including new manufacturing capacity and promotional activity, as well as higher pricing and the benefits realized from productivity improvements and other cost reduction initiatives. This improvement was more than offset by a decline in the performance of the frozen dough business, the cost impact of investments, including the impact of changes in sales mix, and higher commodity and other input costs. Excluding the frozen dough business, adjusted operating income[1] was stable during the quarter.

Weston Foods participates in various MEPPs providing pension benefits to union employees pursuant to provisions of collective bargaining agreements. During 2012, Weston Foods withdrew from one of the U.S. MEPPs in which it participated and as a result, paid a withdrawal liability of $34 million. During the fourth quarter of 2012, another participating employer withdrew from the plan and a mass withdrawal was triggered. As a result of the mass withdrawal, the Company is subject to an incremental withdrawal liability and an additional provision of $5 million was recorded in operating income during the fourth quarter of 2013. The total liability recorded as at year end 2013 relating to the Company's mass withdrawal liability is $22 million, $17 million of which was recorded in the fourth quarter of 2012.

Weston Foods continuously evaluates strategic and cost reduction initiatives related to its manufacturing assets, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. Restructuring activities related to these initiatives are ongoing and in the fourth quarter

of 2013, charges of $3 million (2012 – $3 million) were recorded in operating income, including $1 million (2012 – $1 million) of accelerated depreciation.

Adjusted EBITDA[(1)] decreased by $2 million, or 2.8%, to $69 million in the fourth quarter of 2013 from $71 million in the same period in 2012. Adjusted EBITDA margin[(1)] decreased in the fourth quarter of 2013 to 16.7% from 17.8% in the same period in 2012.

### 13.2 LOBLAW FOURTH QUARTER OPERATING RESULTS

**LOBLAW**

| (unaudited) | Quarters Ended | |
|---|---|---|
| ($ millions except where otherwise indicated) | **Dec. 31, 2013** | Dec. 31, 2012[(5)] |
| Sales | **$ 7,640** | $ 7,465 |
| Operating income | **$ 312** | $ 259 |
| Adjusted operating income[(1)] | **$ 320** | $ 325 |
| Adjusted operating margin[(1)] | **4.2%** | 4.4% |
| Adjusted EBITDA[(1)] | **$ 516** | $ 512 |
| Adjusted EBITDA margin[(1)] | **6.8%** | 6.9% |

Loblaw sales in the fourth quarter of 2013 increased by 2.3% to $7.6 billion compared to $7.5 billion in the same period in 2012. In the fourth quarter of 2013, retail sales increased $130 million compared to the same period in 2012 and was impacted by the following factors:

- same-store sales growth was 0.6% (2012 – flat) and excluding gas bar was 0.6% (2012 – decline of 0.1%), positively impacted by the timing of the Thanksgiving holiday, estimated to be between 0.6% and 0.8%, and negatively impacted by an ice storm in Eastern Canada and a strike in Western Canada which negatively impacted same-store sales growth by approximately 0.2% and 0.1%, respectively. The range of same-store sales growth for the quarter, after the impact of these items, was approximately 0.1% to 0.3%;
- sales growth in food was moderate;
- sales in drugstore declined marginally;
- sales in general merchandise, excluding apparel, declined marginally;
- sales growth in apparel was modest;
- sales growth in gas bar was modest;
- Loblaw's average quarterly internal food price inflation during the fourth quarter of 2013 was lower than the average quarterly national food price inflation of 0.9% (2012 – 1.5%) as measured by CPI. CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores; and
- 26 corporate and franchise stores were opened and 13 corporate and franchise stores were closed in the last 12 months, resulting in a net increase of 0.4 million square feet, or 0.8%.

Loblaw sales in the fourth quarter of 2013 were also positively impacted by an increase in Financial Services segment revenue of $28 million, or 15.9%, compared to the same period in 2012. The increase was primarily driven by higher interest income from higher credit card receivable balances. Higher *PC* Telecom revenues resulting from growth in the Mobile Shop business also contributed to the increase.

Loblaw operating income increased by $53 million to $312 million in the fourth quarter of 2013 compared to $259 million in the same period in 2012. Loblaw operating income was positively impacted by the favourable year-over-year change in fixed asset and other related (recoveries) impairments and lower restructuring and other charges, partially offset by a number of other items. For a complete list of items which impacted operating income but that are excluded from adjusted operating income[(1)], see Section 22, "Non-GAAP Financial Measures" of this MD&A. In addition, operating income was negatively impacted by a decrease in underlying operating performance of $5 million, or 1.5%, as described below.

Gross profit generated by Loblaw's Retail segment increased by $68 million to $1,643 million in the fourth quarter of 2013 compared to $1,575 million in the same period in 2012 and gross profit percentage was 22.1%, an increase from 21.6% in the same period in 2012. The improvements in gross profit and gross profit percentage were primarily driven by improved shrink and transportation costs, and margin improvements in general merchandise, partially offset by the negative impact of continued investments in food margins.

Loblaw adjusted operating income[(1)] decreased by $5 million to $320 million in the fourth quarter of 2013 compared to $325 million in the same period in 2012. Adjusted operating margin[(1)] was 4.2% compared to 4.4% in the same period in 2012.

The decreases in adjusted operating income[(1)] and adjusted operating margin[(1)] in the fourth quarter of 2013 compared to the same period in 2012 were attributable to a decline in Loblaw's Retail segment, partially offset by an improvement in Loblaw's Financial Services segment. The decrease in Loblaw's Retail segment was primarily driven by investments in, and changes to the value of Loblaw's franchise business, costs related to the growth in certain of Loblaw's emerging businesses and higher other operating costs, including depreciation and amortization, partially offset by higher gross profit and labour efficiencies. The increase in Loblaw's Financial Services segment was mainly attributable to higher revenues, partially offset by higher operating costs and continued investments in marketing and customer acquisitions.

In the fourth quarter of 2013, Loblaw announced the reduction of approximately 275 store-support positions and incurred a charge of $32 million associated with this restructuring. In the fourth quarter of 2012, restructuring charges of $61 million associated with the reduction in head office and administrative positions were recorded in operating income and other charges of $2 million were recorded in operating income related to changes in Loblaw's distribution network.

Adjusted EBITDA[(1)] increased $4 million, or 0.8%, to $516 million in the fourth quarter of 2013 compared to $512 million in the same period in 2012. Adjusted EBITDA margin[(1)] decreased in the fourth quarter of 2013 to 6.8% compared to 6.9% in the same period in 2012. Loblaw's depreciation and amortization increased by $9 million compared to the fourth quarter 2012.

## 14. 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" ("NI 52-109") the Executive Chairman, as Chief Executive Officer, and Chief Financial Officer 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 December 31, 2013.

## 15. 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 consolidated financial statements for external purposes in accordance with IFRS.

As required by NI 52-109, the Executive Chairman, as Chief Executive Officer, and Chief Financial Officer have caused the effectiveness of the internal controls over financial reporting to be evaluated using the framework established in the "Internal Control – Integrated Framework (COSO Framework)" published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), 1992. 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 December 31, 2013.

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** Management has also evaluated whether there were changes in the Company's internal controls over financial reporting during the period beginning on October 6, 2013 and ending on December 31, 2013, that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Management determined that no material changes occurred during this period.

## 16. ENTERPRISE RISKS AND RISK MANAGEMENT

The Company is committed to establishing 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 GWL's and Loblaw's Enterprise Risk Management ("ERM") programs. The GWL and Loblaw Boards, respectively, have approved an ERM policy and oversee 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.

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 are both strategic and operational in nature. Key risks affecting the Company are prioritized under six categories: strategic; financial; operational (including safety); regulatory; human capital; and reputational risks. The annual ERM assessment is carried out through interviews, surveys and facilitated workshops with management and the GWL or Loblaw Boards. 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. At least semi-annually, management provides an update to a Committee of the GWL or Loblaw Boards 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 (three to five year) 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 GWL or Loblaw Boards either to the full Boards or to Committees of the Boards.

The strategic, financial, operational (including safety), regulatory, human capital and reputational risks and risk management strategies 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. 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 negatively affect the reputation, operations or financial condition or performance of the Company.

### 16.1 OPERATING RISKS AND RISK MANAGEMENT

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

| | |
|---|---|
| Acquisition of Shoppers Drug Mart Corporation | Vendor Management and Third-Party Service Providers |
| Systems Implementations | Employee Retention and Succession Planning |
| Change Management | Distribution and Supply Chain |
| Information Integrity and Reliability | Disaster Recovery and Business Continuity |
| Availability, Access and Security of Information Technology | Privacy and Information Security |
| Food Safety and Public Health | Commodity Prices |
| Labour Relations | Franchisee Independence and Relationships |
| Competitive Environment | Environmental |
| Consumer and Retail Customer Trends | Trademark and Brand Protection |
| Regulatory and Tax | Defined Benefit Pension Plans |
| Economic Environment | Multi-Employer Pension Plans |
| Inventory Management and Valuation | |
| Merchandising | |

**Acquisition of Shoppers Drug Mart Corporation** On July 14, 2013, Loblaw entered into an arrangement agreement to acquire all of the outstanding common shares of Shoppers Drug Mart for consideration of up to approximately $6.7 billion of cash and the issuance of up to approximately 119.9 million common shares. The transaction is subject to various regulatory approvals, including approvals under the *Competition Act* (Canada) and by the TSX, and the fulfillment of certain other closing conditions customary in transactions of this nature. The Company anticipates that the transaction will be completed in the first quarter of 2014.

The process of review under the *Competition Act* (Canada) is proceeding as expected. There is no certainty as to the outcome of the review on Loblaw and whether such outcome could affect properties held by either Choice Properties or by Loblaw. At this time, the Company has no reason to believe that any such outcome would be material to the Company.

The successful execution and implementation of the acquisition will require significant effort on the part of management of the Company. Failure to properly execute and implement this transaction or realize the anticipated strategic benefits or operational, competitive and cost synergies could adversely affect the reputation, operations and financial performance of the Company.

Information on risks and uncertainties related to Shoppers Drug Mart are disclosed in the Information Statement filed by Loblaw on August 20, 2013.

**Systems Implementations** Loblaw continues to undertake a major upgrade of its IT infrastructure. Completing the IT systems deployment will require continued focus and investment. Failure to properly execute and implement these systems, including failure to successfully migrate from legacy systems to the new IT systems or minimize disruption to Loblaw's current 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 causing significant disruptions to the business and potential financial losses. Failure to continue to implement appropriate processes to support the new systems could result in inefficiencies and duplication in processes, which could adversely affect the reputation, operations and financial performance of the Company.

**Change Management** Significant initiatives within the Company, including the execution of Loblaw's IT infrastructure plan, and planning for the acquisition of Shoppers Drug Mart, are underway. Ineffective change management could result in disruptions to the operations of the business or negatively affect the ability of the Company to implement and achieve its long term strategic objectives. Failure to properly integrate several large, complex initiatives in a timely manner will adversely impact the operations of the Company. If employees are not able to develop and perform new roles, processes and disciplines, the Company may not achieve the expected cost savings and other benefits of its initiatives. Failure to properly execute the various processes will increase the risk of customer dissatisfaction, which in turn could negatively affect the reputation, operations and financial performance of the Company.

**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 that enables management to effectively manage the business could preclude the Company from optimizing its overall performance. Any significant loss of data or failure to maintain reliable data could negatively affect the reputation, operations and 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 are critical elements 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 negatively affect the reputation, operations, and financial performance of the Company.

**Food Safety and Public Health** The Company is subject to risks associated with food safety and general merchandise product (including baked goods) defects, including the Company's control brand and contract manufactured 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 or general merchandise products (including baked goods). 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 and ingredients 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 Loblaw's store level, could negatively affect the reputation, operations and financial performance of the Company.

**Labour Relations** A majority of the Company's workforce is unionized. There can be no assurance as to the outcome of labour negotiations or the timing of their completion. Failure to renegotiate collective agreements could result in work stoppages or slowdowns, and if they occur, they could negatively affect the reputation, operations and financial performance of the Company.

**Competitive Environment** Weston Foods' competitors include multi-national food processing companies, as well as national and smaller-scale bakery operations in Canada and the U.S.

Loblaw's competitors include traditional supermarket operators, as well as mass merchandisers, warehouse clubs, drugstores, limited assortment stores, discount stores, convenience stores and specialty stores. Many of these competitors now offer a selection of food, drugstore and general merchandise. Others remain focused on supermarket-type merchandise. Loblaw is 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 Weston Foods or Loblaw to sustain their competitive position could negatively affect the financial performance of the Company.

**Consumer and Retail Customer Trends** The baking industry continues to experience a decline in the consumption of traditional products as consumer eating and buying preferences continue to trend towards

healthier, more nutritious, value-added and convenience offerings. In addition, retail customer trends are evolving in order to deliver products that satisfy changing consumer preferences in a highly competitive environment. Failure of Weston Foods to anticipate and react to shifting consumer and retail customer trends and preferences through successful innovation and enhanced manufacturing capability could negatively 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 income, capital, commodity, property and other 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 in a timely manner could subject the Company to civil or regulatory actions or proceedings, including fines, assessments, injunctions, recalls or seizures, which in turn could negatively affect the reputation, operations and 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 future periods.

In 2012, Loblaw received indication from the CRA that it intends to proceed with a reassessment of the tax treatment of Loblaw's wholly owned subsidiary, Glenhuron. At this stage, no reassessment has yet been received, and accordingly, it is not possible to quantify the amount of any potential reassessment. While Loblaw does not expect the ultimate outcome to be material, such matters cannot be predicted with certainty and could result in a material charge in future periods.

During 2010, GWL received a reassessment from the CRA challenging GWL's characterization of a gain reported in a previous year's tax return filing. Should the CRA be successful in its assertion, the maximum exposure to the Company's net earnings would be approximately $66 million. GWL is vigorously defending its filing position. No amount has been provided for in the Company's financial statements.

In 2013, all provinces and territories reduced the reimbursement rates for pharmacies on six common generic prescription drugs and certain other provinces implemented further generic prescription drug reimbursement rate reductions. In addition, Ontario eliminated all professional allowances paid by drug manufacturers to pharmacies. These actions, and any potential further announcements, impact pharmacy sales and therefore could have an adverse effect on the financial performance of the Company. The acquisition of Shoppers Drug Mart will increase the Company's exposure to this risk.

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. Should Choice Properties cease to qualify for these classifications and exceptions, the taxation of Choice Properties and its unitholders, including Loblaw and GWL, could be materially adversely different in certain respects, and therefore could have a material adverse effect on the trading price of the Units.

**Economic Environment** Economic factors that impact consumer spending patterns could deteriorate or remain unpredictable due to global, national or regional economic volatility. These factors could negatively affect the Company's revenue and margins. Inflationary trends are unpredictable and changes in the rate of inflation or

deflation will affect consumer prices, which in turn could negatively affect the financial performance of the Company.

**Inventory Management and Valuation** Inappropriate inventory management could lead to excess inventory or a shortage of inventory, which may impact customer satisfaction and the overall financial performance of the Company. Loblaw may hold excess inventory that cannot be sold profitably or which could increase levels of inventory shrink. Failure to manage inventory properly could negatively affect the operations and financial performance of the Company.

With the upgrade of its IT infrastructure, Loblaw expects to complete the conversion of its corporate retail stores to a perpetual inventory management system during 2014. Loblaw currently does not have sufficient information to determine whether there will be any changes to its estimate of average cost of its inventory. Any such difference could be material and therefore could negatively affect both the carrying amount of the Company's inventory and the financial results of the Company.

**Merchandising** The Company could have goods and services that customers do not want or need, are not reflective of current trends in customers' tastes, habits or regional preferences, are priced at a level customers are not willing to pay, are late in reaching the market or do not have optimal commercial product placement on store shelves. Innovation is critical if the Company is to respond to customer demands and stay competitive in the market place. If merchandising efforts are not effective or are unresponsive to customer demands, the operations and financial performance of the Company will be negatively affected.

**Vendor Management and Third-Party Service Providers** Certain aspects of the Company's business rely on third-party providers, 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 business practices and inadequate supply of products. Although contractual arrangements, sourcing guidelines, supplier audits and Corporate Social Responsibility guidelines are in place, the Company has no direct influence over how vendors are managed. Negative events affecting vendors or suppliers 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 negatively 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 for product development, design and sourcing of Loblaw's control brand apparel products and Weston Food's baked goods products. Ineffective selection, contract terms or relationship management could impact the Company's ability to source Weston Food's third-party manufactured products or Loblaw's 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 negatively affecting the operations and 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®. PC Bank and Loblaw actively manage and monitor their relationships with all third-party service providers and PC Bank has an outsourcing risk policy and a vendor governance team that provides regular reports on vendor governance and annual vendor risk assessments. Despite these activities, a significant disruption in the services provided by the chartered bank or by third-party service providers would negatively 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 the liquidity of the Company.

**Employee Retention and Succession Planning** Effective succession planning for senior management and employee retention are essential to sustaining the growth and success of the Company. In addition, loss of talent to the competition can be a significant risk to the Company's business strategy. If the Company is not effective in establishing appropriate succession planning processes and retention strategies, it could lead to a lack of requisite knowledge, skills and experience on the part of management. This, in turn, could adversely affect the Company's ability to execute its strategies, and could negatively affect its reputation, operations and financial performance.

**Distribution and Supply Chain** Failure to continue to improve the Company's supply chain could adversely affect the Company's capacity to effectively and efficiently attract and retain current and potential customers. Any delay or disruption in the flow of goods to stores could negatively affect the operations and financial performance of the Company.

**Disaster Recovery and Business Continuity** The Company's ability to continue critical operations and processes could be negatively impacted by adverse events resulting from various incidents, including severe weather, work stoppages, prolonged IT systems failure, power failures, border closures, a pandemic or other national or international catastrophe. Business interruptions, crises or potential disasters, could negatively affect the reputation, operations and financial performance of the Company.

**Privacy and Information Security** The Company is subject to various laws regarding the protection of personal information of its customers, cardholders and employees and has adopted a Privacy Policy setting out guidelines for the handling of personal information. The Company's IT systems contain personal information of customers, cardholders and employees. Any failures or vulnerabilities in these systems or non-compliance with laws or regulations, including those in relation to personal information belonging to the Company's customers and employees, could negatively affect the reputation, operations and financial performance of the Company.

**Commodity Prices** Weston Foods costs are directly impacted by fluctuations in the prices of commodity linked raw materials such as wheat flours, sugars, vegetable oils, cocoa powders and chocolate. Loblaw is also exposed to fluctuations in the commodity prices as a result of the indirect link between commodities and the cost of consumer products. In addition, both Weston Foods and Loblaw are exposed to increases in the prices of energy in operating, in the case of Weston Foods, its bakeries and distribution networks, and, in the case of Loblaw, its stores and distribution networks. Both Weston Foods and Loblaw use purchase commitments and derivative instruments in the form of futures contracts, option contracts and forward contracts to manage their current and anticipated exposure to fluctuations in commodity prices. Despite these strategies, high commodity prices could negatively affect the financial performance of the Company.

**Franchisee Independence and Relationships** A significant portion of the Loblaw's revenues and earnings comes from amounts paid by franchisees. Franchisees and independent operators are independent businesses and, as a result, their operations may be negatively affected by factors beyond Loblaw's control, which in turn could negatively affect the reputation, operations and financial performance of the Company. Revenues and earnings could also be negatively affected, and Loblaw'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 Loblaw for products, rent or fees. Loblaw'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 Loblaw's relationship with its franchisees. Loblaw provides various services to the franchisees to assist with management of store operations and dedicated personnel manage Loblaw's obligations to its franchisees. Despite these efforts, 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. In addition, reputational damage or adverse consequences for Loblaw, including litigation and disruption to revenue from franchise stores, could result.

**Environmental** The Company maintains a large portfolio of real estate and other facilities and is subject to environmental risks associated with the contamination of such properties and facilities, whether by previous owners or occupants, neighbouring properties or by the Company itself.

In particular, the Company has a number of underground storage tanks, the majority of which are used for the retailing of automotive fuel or for its distribution and supply chain transport fleets. Contamination resulting from leaks from these tanks is possible. The Company also operates refrigeration equipment in Weston Foods' production facilities and in Loblaw's stores and distribution centres to preserve perishable products as they pass through the supply chain and ultimately to customers. These systems contain refrigerant gases which could be released if the equipment fails or leaks. A release of these gases could have adverse effects on the environment. Failure to properly manage any of these environmental risks could negatively affect the reputation, operations and financial performance of the Company.

The Company is subject to legislation that imposes liabilities on retailers, brand owners and importers for costs associated with recycling and disposal of consumer goods packaging and printed materials distributed to customers. There is a risk that the Company will be subject to increased costs associated with these laws.

In addition, the Company could be subject to increased or unexpected costs associated with environmental incidents and the related remediation activities, including litigation and regulatory related costs, all of which could negatively affect the reputation and financial performance of the Company.

**Trademark and Brand Protection** A decrease in value of the Company's trademarks, banners or control brands, as a result of adverse events, including third party infringement, changes to the branding strategies or otherwise, could negatively affect the reputation, operations and financial performance of the Company.

**Defined Benefit Pension Plans** The Company's registered defined benefit pension plans are impacted by a number of variables, including the investment performance of the plans' assets and the discount rate used to value the liabilities of the plans. The Company manages the assets in its registered defined benefit pension plans by engaging professional investment managers who operate under prescribed investment policies and procedures in respect of permitted investments and asset allocations. The Company regularly monitors and assesses plan performance and the impact of changes in participant demographics, changes in capital markets and other economic factors that may impact funding requirements, net defined benefit costs and actuarial assumptions. If capital market returns are below assumed levels, or if discount rates decrease, the Company could be required to make contributions to its registered funded defined benefit pension plans in excess of those currently expected, which in turn could negatively affect the financial performance of the Company.

**Multi-Employer Pension Plans** In addition to the Company-sponsored pension plans, the Company participates in various MEPPs, providing pension benefits to union employees pursuant to provisions of collective bargaining agreements. Approximately 37% (2012 – 39%) of employees of the Company and of its independent franchisees 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 negatively affect the financial performance of the Company.

Loblaw, together with its independent franchisees, is the largest participating employer in the Canadian Commercial Workers Industry Pension Plan ("CCWIPP"), with approximately 53,000 (2012 – 54,000) employees as members. In 2013, Loblaw contributed $54 million (2012 – $52 million) to CCWIPP. The CCWIPP has historically been underfunded as the actuarial accrued benefit obligations have exceeded the value of the assets held in trust. Any benefit reductions would negatively affect the retirement benefits of Loblaw's employees, which in turn could negatively affect their morale and productivity and, in turn, could negatively affect the Company's reputation.

### 16.2 FINANCIAL RISKS AND RISK MANAGEMENT

**Financial Risks** 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 negatively impact the financial performance of the Company.

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

| | |
|---|---|
| Level of Indebtedness and Liquidity | Foreign Currency Exchange Rates |
| Choice Properties' Capital Availability | Common Share and Unit Prices |
| Interest Rates | Credit |

**Level of Indebtedness and Liquidity** To fund the cash portion of the Shoppers Drug Mart acquisition, Loblaw will utilize excess cash and significantly increase its indebtedness. There can be no assurances that Loblaw will generate sufficient free cash flow to reduce indebtedness and maintain adequate cash reserves which could result in adverse consequences on its credit ratings and its cost of funding.

Liquidity risk is the risk that the Company cannot meet its demands for cash or fund its obligations as they come due. In addition, it includes the risk of not being able to liquidate assets in a timely manner at a reasonable price.

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.

Despite these mitigation strategies, if GWL, Loblaw, PC Bank or Choice Properties' financial performance and condition deteriorate or downgrades in GWL's, Loblaw's or Choice Properties' current credit ratings occur, the ability to obtain funding from external sources could be restricted.

**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.

**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. GWL and Loblaw manage interest rate risk by monitoring their 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. Despite these mitigation strategies, changes in interest rates could negatively affect the Company's financial performance.

**Foreign Currency Exchange Rates** The Company's consolidated financial statements are expressed in Canadian dollars, however a portion of the Company's (excluding Loblaw's) net assets are denominated in U.S. dollars through both its net investment in foreign operations in the U.S. and its foreign subsidiaries held by Dunedin and certain of its affiliates with a functional currency that is the same as that of the Company. The U.S. dollar denominated net assets are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. As a result, the Company is exposed to foreign currency translation gains and losses. Those gains and losses arising from the translation of the U.S. dollar denominated assets of foreign subsidiaries

with a functional currency that is the same as that of the Company are included in operating income, while translation gains and losses on the net investment in foreign operations in the U.S. are recorded in accumulated other comprehensive income (loss).

Revenues and expenses of all 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 recognized. An appreciating U.S. dollar relative to the Canadian dollar will positively impact operating income and net earnings, while a depreciating U.S. dollar relative to the Canadian dollar will have the opposite impact.

Loblaw is exposed to foreign currency exchange rate variability, primarily on its U.S. dollar denominated purchases in trade payables and other liabilities. Weston Foods is also exposed to fluctuations in the prices of U.S. dollar denominated purchases as a result of changes in U.S. dollar exchange rates. A depreciating Canadian dollar relative to the U.S. dollar will negatively impact operating income and net earnings, while an appreciating Canadian dollar relative to the U.S. dollar will have the opposite impact. Subsequent to the end of 2013, Weston Foods entered into futures contracts to mitigate a portion of its current and anticipated exposure to fluctuations in U.S. dollar exchange rates.

**Common Share and Unit Prices** Changes in the Loblaw common share price impact the Company's net interest expense and other financing charges. In 2001, WHL entered into an equity forward sale agreement based on 9.6 million Loblaw common shares at an original forward price of $48.50 per Loblaw common share which, under the terms of the agreement, had increased to a forward price of $96.46 (2012 – $92.26) per Loblaw common share as at year end 2013. The forward matures in 2031 and will be settled in cash as follows: WHL will receive the forward price and will pay the market value of the underlying Loblaw common shares at maturity. The obligation of WHL under this forward is secured by the underlying Loblaw common shares. WHL recognizes a non-cash charge or income, which is included in consolidated net interest expense and other financing charges, representing the fair value adjustment of WHL's forward sale agreement for 9.6 million shares. The fair value adjustment in the forward contract is a non-cash item resulting from fluctuations in the market price of the underlying Loblaw shares that WHL owns. WHL does not record any change in the market price associated with the Loblaw common shares it owns. At maturity, if the forward price is greater (less) than the market price, WHL will receive (pay) cash equal to the difference between the notional value and the market value of the forward contract. Any cash paid under the forward contract could be offset by the sale of Loblaw common shares.

The Company is exposed to market price risk as a result of Choice Properties' Units that are held by the public. These Units are presented as a liability on the Company's consolidated balance sheet 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.

**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, Loblaw's franchise loans receivable, accounts receivable from Loblaw's franchisees, other receivables from Weston Foods' customers and suppliers and Loblaw's vendors, associated stores and independent accounts, and pension assets held in the Company's defined benefit plans.

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.

Loblaw's franchise loans receivable, accounts receivable from Loblaw's franchisees, other receivables from Weston Foods' customers and suppliers and Loblaw's vendors, associated stores and independent accounts are actively monitored on an ongoing basis and settled on a frequent basis in accordance with the terms specified in the applicable agreements.

Credit risk associated with investments in the Company's defined benefit pension plans is described in the Defined Benefit Pension Plans discussion in Section 16.1, "Operating Risks and Risk Management" of this MD&A.

Despite the mitigation strategies described above, it is possible that the Company's financial performance could be negatively impacted by the failure of a counterparty to fulfill its obligations.

## 17. RELATED PARTY TRANSACTIONS

The Company's majority shareholder is Mr. W. Galen Weston, who beneficially owns, directly and indirectly through private companies which he controls, including Wittington Investments, Limited ("Wittington"), a total of 80,724,599 of the Company's common shares, representing approximately 63% (2012 – 63%) 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 between the Company and its consolidated entities have been eliminated on consolidation and are not disclosed below.

In 2013, rental payments to Wittington by the Company amounted to $4 million (2012 – $4 million). As at year end 2013 and 2012, there were no rental payments outstanding.

In 2013, inventory purchases from Associated British Foods plc, a related party by virtue of Mr. W. Galen Weston being a director of such entity's parent company, amounted to $31 million (2012 – $26 million). As at year end 2013, $4 million (2012 – $2 million) was included in trade payables and other liabilities relating to these inventory purchases.

**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 discussed in Section 9.1, "Cash Flows" of this MD&A.

**Income Tax Matters** From time to time, the Company and Wittington may enter into agreements to make elections that are permitted or required under applicable income tax legislation with respect to affiliated corporations. In 2013, these elections and accompanying agreements did not have a material impact on the Company.

**Compensation of Key Management Personnel** The Company's key management personnel is comprised of certain members of the executive team of GWL, Loblaw, Weston Foods and Wittington, as well as members of the Boards of GWL, Loblaw 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.

Annual compensation of key management personnel that is directly attributable to the Company was as follows:

| ($ millions) | **2013** | 2012 |
|---|---|---|
| Salaries, director fees and other short term employee benefits | **$ 19** | $ 18 |
| Share-based compensation | **12** | 8 |
| Total compensation | **$ 31** | $ 26 |

## 18. 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 MD&A, 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.

**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 future retail prices, 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 cash generating units ("CGU") 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 indefinite life intangible assets are tested for impairment. Loblaw has determined that each location is a separate CGU for purposes of fixed asset impairment testing. For the purpose of goodwill and intangible assets impairment testing, CGUs are grouped at the lowest level at which goodwill and intangible assets 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 revenues, earnings and capital investment consistent with strategic plans presented to GWL's and Loblaw's Boards. 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 financial assets relating to its 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 Loblaw's five year forecast.

**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.

**Allowance for credit card receivables**

*Key sources of estimation* The allowance for credit card receivables is measured based upon statistical analysis that includes estimates for past and current performance, aging, arrears status, the level of allowance already in place, and management's interpretation of economic conditions and other trends specific to Loblaw's customer base, including but not limited to bankruptcies. Changes in circumstances may cause future assessments of credit risk to be materially different from current assessments, which could require an increase or decrease in the allowance for credit card receivables.

## 19. ACCOUNTING STANDARDS IMPLEMENTED IN 2013 AND CHANGES IN SIGNIFICANT ACCOUNTING POLICIES

**Fair Value Measurement** In 2011, the International Accounting Standards Board ("IASB") issued IFRS 13, "Fair Value Measurement" ("IFRS 13"), which establishes a single framework for the fair value measurement and disclosure of financial and non-financial assets and liabilities. The new standard unifies the definition of fair value and also introduces new concepts including 'highest and best use' and 'principal markets' for non-financial assets and liabilities. There are additional disclosure requirements, including increased fair value disclosure for financial instruments for interim and annual financial statements. The Company implemented this standard prospectively in the first quarter of 2013. There were no significant measurement impacts on the Company's consolidated financial statements as a result of the adoption of IFRS 13.

**Employee Benefits** In 2011, the IASB revised International Accounting Standard ("IAS") 19, "Employee Benefits" ("IAS 19"). The most significant amendments for the Company and its significant accounting policies are the requirement to immediately recognize all unvested past service costs and the replacement of interest cost and expected return on plan assets with a net interest amount that is calculated by applying a prescribed discount rate to the net defined benefit obligation (asset). Under the amendment, the Company continues to recognize actuarial gains and losses on plan assets and obligations through other comprehensive income (loss), but has chosen to reclassify these amounts from accumulated other comprehensive income (loss) and record these actuarial gains and losses in retained earnings, consistent with its previous presentation. The Company implemented this standard retrospectively in the first quarter of 2013. The impact arising from the adoption of the amendments to IAS 19 is summarized as follows:

**Consolidated Statements of Earnings**

Increase (decrease)

| ($ millions except where otherwise indicated) | | **2013** | | 2012 |
|---|---|---|---|---|
| Operating income | **$** | **20** | $ | 1 |
| Net interest expense and other financing charges | **$** | **32** | $ | 24 |
| Income taxes | **$** | **(3)** | $ | (5) |
| Net earnings | **$** | **(9)** | $ | (18) |
| Net earnings per common share ($) | | | | |
| Basic | **$** | **(0.05)** | $ | (0.09) |
| Diluted | **$** | **(0.05)** | $ | (0.09) |

**Consolidated Statements of Comprehensive Income**

Increase (decrease)

| ($ millions) | | **2013** | | 2012 |
|---|---|---|---|---|
| Net earnings | **$** | **(9)** | $ | (18) |
| Other comprehensive income | **$** | **24** | $ | 18 |

**Consolidated Balance Sheets**

| Increase (decrease) | As at | | |
|---|---|---|---|
| ($ millions) | **Dec. 31, 2013** | Dec. 31, 2012 | Jan. 1, 2012 |
| Deferred income tax asset | **$ (5)** | | $ 1 |
| Other liabilities | **$ (22)** | $ (2) | $ (1) |
| Equity | **$ 17** | $ 2 | $ 2 |

The amendments also require enhanced annual disclosures for defined benefit plans, including additional information on the characteristics and risks of those plans.

**Other Standards** In addition to the above standards, the Company implemented the following standards and amendments effective January 1, 2013: IFRS 10, "Consolidated Financial Statements" ("IFRS 10"); IFRS 11, "Joint Arrangements"; IFRS 12, "Disclosure of Interests in Other Entities"; IAS 28, "Investments in Associates"; and IAS 1, "Presentation of Financial Statements". There was no significant impact on the Company's consolidated financial statements as a result of the implementation of these standards. As a result of the implementation of IFRS 10, the Company consolidates structured entities 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 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.

In 2013, the IASB issued amendments to IAS 36, "Impairment of Assets", which clarify the disclosure requirements for recoverable amounts of CGUs. These amendments are required to be applied for periods beginning on or after January 1, 2014. The Company has elected to early adopt these amendments during 2013. There was no significant impact on the Company's consolidated financial statements as a result of these amendments.

## 20. FUTURE ACCOUNTING STANDARDS

**Financial Instruments** In 2011, the IASB issued amendments to IFRS 7, "Financial Instruments: Disclosures", and IAS 32, "Financial Instruments: Presentation". These amendments are required to be applied for periods beginning on or after January 1, 2014. The Company does not expect any significant impacts on its consolidated financial statements as a result of these amendments.

In 2013, the IASB issued amendments to IFRS 9, "Financial Instruments" ("IFRS 9"), issued in 2010, which will ultimately replace IAS 39, "Financial Instruments: Recognition and Measurement" ("IAS 39"). The replacement of IAS 39 is a three-phase project with the objective of improving and simplifying the reporting for financial instruments. The current issuance of IFRS 9 includes the first and third phases of the project, which provide guidance on the classification and measurement of financial assets and financial liabilities and hedge accounting. The mandatory effective date of the standard has not been determined due to the incomplete status of the second phase of the project, impairment. The effective date of the entire standard will be determined closer to the completion of the remaining phase. The Company continues to assess the impact of the new standard on its consolidated financial statements.

**Levies** In 2013, the International Financial Reporting Interpretations Committee ("IFRIC") issued IFRIC 21, "Levies" ("IFRIC 21"). IFRIC 21 addresses accounting for a liability to pay a levy within the scope of IAS 37, "Provisions, Contingent Liabilities and Contingent Assets". A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation, other than income taxes within the scope of IAS 12, "Income Taxes", and fines or other penalties imposed for breaches of the legislation. This interpretation is effective for annual periods beginning on or after January 1, 2014, and is to be applied retrospectively. The Company is currently assessing the impact of the new interpretation on its consolidated financial statements.

## 21. OUTLOOK[4]

This outlook reflects the underlying operating performance of the Company's operating segments as discussed below.

For full year 2014, Weston Foods expects modest sales growth driven primarily by volumes. Despite the anticipated growth in sales, adjusted operating income[1] is expected to decline due to continued investments in growth, including plant start-up costs, capabilities, marketing and innovation. In addition, results will be more challenged in the first half of the year by the performance of the frozen dough business and higher commodity and other input costs.

Loblaw will continue to focus on investing in its customer proposition in 2014 in its retail business - value, assortment and service - while focusing on balancing these investments with incremental efficiencies. In the first half of 2014 the environment is expected to remain extremely competitive driven by continued greater than historical square footage expansion, which is expected to moderate in the second half of the year.

## 22. NON-GAAP FINANCIAL MEASURES

The Company uses the following non-GAAP financial measures: adjusted operating income and adjusted operating margin, adjusted EBITDA and adjusted EBITDA margin, adjusted basic net earnings per common share from continuing operations, adjusted debt to adjusted EBITDA, free cash flow, interest coverage and return on average net assets. 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. Beginning in the third quarter of 2013, Loblaw began reporting its results of operations on an adjusted basis. The Company excludes the impact of items excluded by Loblaw management when reporting its consolidated and segment results.

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 they should not be construed as an alternative to other financial measures determined in accordance with GAAP.

**Adjusted Operating Income and Adjusted EBITDA** The Company believes adjusted operating income is useful in assessing the Company's underlying operating performance and in making decisions regarding the ongoing operations of its business. The Company believes adjusted EBITDA is also useful in assessing the underlying operating performance of the Company's ongoing operations and in assessing the Company's ability to generate cash flows to fund its cash requirements, including its capital investment program.

The following tables reconcile adjusted operating income and adjusted EBITDA to GAAP net earnings from continuing operations attributable to shareholders of the Company reported for the periods ended as indicated.

| | Quarters Ended | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Dec. 31, 2013** | | | | Dec. 31, 2012[i] | | | |
| (unaudited) ($ millions) | **Weston Foods** | **Loblaw** | **Other[ii]** | **Consolidated** | Weston Foods | Loblaw | Other[ii] | Consolidated |
| Net earnings attributable to shareholders of the Company | | | | **$ 185** | | | | $ 63 |
| Add impact of the following: | | | | | | | | |
| Non-controlling interests | | | | **47** | | | | 49 |
| Income taxes | | | | **56** | | | | 34 |
| Net interest expense and other financing charges | | | | **106** | | | | 175 |
| Operating income | **$ 40** | **$ 312** | **$ 42** | **$ 394** | $ 44 | $ 259 | $ 18 | $ 321 |
| Add (deduct) impact of the following: | | | | | | | | |
| Restructuring and other charges[iii] | **3** | **32** | | **35** | 3 | 63 | | 66 |
| Fair value adjustment of commodity derivatives at Weston Foods | **4** | | | **4** | 10 | | | 10 |
| Share-based compensation net of equity derivatives | **2** | **8** | | **10** | (4) | 2 | | (2) |
| Fixed asset and other related (recoveries) impairments | | **(42)** | | **(42)** | | 12 | | 12 |
| Shoppers Drug Mart acquisition costs | | **7** | | **7** | | | | |
| Choice Properties general and administrative costs | | **3** | | **3** | | | | |
| MEPP withdrawal liability incurred by Weston Foods | **5** | | | **5** | 17 | | | 17 |
| Gain on disposal of assets | | | | | | (11) | | (11) |
| Defined benefit plan amendments | | | | | (8) | | | (8) |
| Weston Foods insurance proceeds | | | | | (5) | | | (5) |
| Foreign currency translation gain | | | **(42)** | **(42)** | | | (18) | (18) |
| Adjusted operating income | **$ 54** | **$ 320** | **$** | **$ 374** | $ 57 | $ 325 | $ | $ 382 |
| Depreciation and amortization | **15** | **196** | | **211** | 14 | 187 | | 201 |
| Adjusted EBITDA | **$ 69** | **$ 516** | **$** | **$ 585** | $ 71 | $ 512 | $ | $ 583 |

(i) Certain 2012 figures have been restated due to the implementation of revised IAS 19. See Section 19, "Accounting Standards Implemented in 2013 and Changes in Significant Accounting Policies" of this MD&A.

(ii) Operating income in the fourth quarter of 2013 included a gain of $42 million (2012 – $18 million) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by foreign operations.

(iii) Restructuring and other charges included $1 million (2012 – $1 million) of accelerated depreciation incurred by Weston Foods.

| | Years Ended | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | **Dec. 31, 2013** | | | | Dec. 31, 2012[i] |
| (unaudited)<br>($ millions) | **Weston Foods** | **Loblaw** | **Other[ii]** | **Consolidated** | Weston Foods | Loblaw | Other[ii] | Consolidated |
| Net earnings from continuing operations attributable to shareholders of the Company | | | | **$ 616** | | | | $ 475 |
| Add impact of the following: | | | | | | | | |
| Non-controlling interests | | | | **233** | | | | 233 |
| Income taxes | | | | **275** | | | | 244 |
| Net interest expense and other financing charges | | | | **497** | | | | 441 |
| Operating income (loss) | **$ 238** | **$ 1,308** | **$ 75** | **$ 1,621** | $ 230 | $ 1,187 | $ (24) | $ 1,393 |
| Add (deduct) impact of the following: | | | | | | | | |
| Restructuring and other charges[iii] | **6** | **35** | | **41** | 12 | 72 | | 84 |
| Fair value adjustment of commodity derivatives at Weston Foods | **10** | | | **10** | (6) | | | (6) |
| Share-based compensation net of equity derivatives | **8** | **32** | | **40** | 1 | 28 | | 29 |
| Fixed asset and other related (recoveries) impairments | | **(32)** | | **(32)** | | 19 | | 19 |
| Shoppers Drug Mart acquisition costs | | **16** | | **16** | | | | |
| Choice Properties general and administrative costs | | **6** | | **6** | | | | |
| Choice Properties start-up costs | | **3** | | **3** | | | | |
| Defined benefit plan amendments | | **(51)** | | **(51)** | (8) | | | (8) |
| MEPP withdrawal liability incurred by Weston Foods | **5** | | | **5** | 51 | | | 51 |
| Gain on disposal of assets | | | | | | (11) | | (11) |
| Weston Foods insurance proceeds | | | | | (5) | | | (5) |
| Foreign currency translation (gain) loss | | | **(75)** | **(75)** | | | 24 | 24 |
| Adjusted operating income | **$ 267** | **$ 1,317** | **$** | **$ 1,584** | $ 275 | $ 1,295 | $ | $ 1,570 |
| Depreciation and amortization | **63** | **824** | | **887** | 59 | 777 | | 836 |
| Adjusted EBITDA | **$ 330** | **$ 2,141** | **$** | **$ 2,471** | $ 334 | $ 2,072 | $ | $ 2,406 |

(i) Certain 2012 figures have been restated due to the implementation of revised IAS 19. See Section 19, "Accounting Standards Implemented in 2013 and Changes in Significant Accounting Policies" of this MD&A.

(ii) Year-to-date operating income included a gain of $75 million (2012 – loss of $24 million) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by foreign operations.

(iii) Restructuring and other charges included $4 million (2012 – $4 million) of accelerated depreciation incurred by Weston Foods.

The year-over-year change in the following items influenced operating income in the fourth quarter of 2013 and year-to-date:

***Restructuring and other charges*** The Company continuously evaluates strategic and cost reduction initiatives related to its store infrastructure, manufacturing assets, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. Restructuring activities related to these initiatives are ongoing. The details of restructuring and other charges are included in Section 7, "Results of Reportable Operating Segments" and Section 13, "Fourth Quarter Results of Reportable Operating Segments" of this MD&A.

***Fair value adjustment of commodity derivatives at Weston Foods*** Weston Foods is exposed to commodity price fluctuations primarily as a result of purchases of certain raw materials, fuels and utilities. In accordance with the Company's commodity risk management policy, Weston Foods enters into commodity derivatives to reduce the impact of price fluctuations in forecasted raw material purchases over a specified period of time. These commodity derivatives are not acquired for trading or speculative purposes. Pursuant to Weston Foods' derivative instruments accounting policy, certain changes in fair value, which include realized and unrealized gains and losses related to future purchases of raw materials, are recorded in operating income. In the fourth quarter of 2013 and year-to-date, Weston Foods recorded a charge of $4 million (2012 – $10 million) and $10 million (2012 – income of $6 million), respectively, related to the fair value adjustment of exchange traded commodity derivatives. Despite the impact of accounting for these commodity derivatives on the Company's reported results, the derivatives have the economic impact of largely mitigating the associated risks arising from price fluctuations in the underlying commodities during the period that the commodity derivatives are held.

***Share-based compensation net of equity derivatives*** Until the first quarter of 2013, GWL and Glenhuron held equity derivatives to partially hedge the impact of increases in the value of GWL and Loblaw common shares on share-based compensation cost. The amount of net share-based compensation cost recorded in operating income has historically been mainly dependent upon changes in the value of GWL and Loblaw common shares and the number and vesting of RSUs and PSUs relative to the number of common shares underlying the equity derivatives. In the first quarter of 2013, GWL and Glenhuron settled their remaining equity derivative contracts and the RSU and PSU plans were amended to require settlement in common shares rather than in cash. As a result of the settlements and plan amendments, the components of share-based compensation and their exposure to changes in the value of GWL and Loblaw common shares have changed. In order to assess consolidated and segment operating performance on a consistent basis, management continues to exclude the impact of share-based compensation from operating income. In the fourth quarter of 2013 and year-to-date, a charge of $10 million (2012 – income of $2 million) and $40 million (2012 – $29 million), respectively, were recorded related to share-based compensation net of equity derivatives.

***Fixed asset and other related (recoveries) impairments*** 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 2013, Loblaw recorded net recoveries of $42 million (2012 – a charge of $12 million), and year-to-date recorded net recoveries of $32 million (2012 – a charge of $19 million).

***Shoppers Drug Mart acquisition costs*** In connection with the agreement to acquire all of the outstanding common shares of Shoppers Drug Mart, in the fourth quarter of 2013 and year-to-date, Loblaw incurred $7 million and $16 million, respectively, of acquisition costs.

***Choice Properties general and administrative costs*** In the fourth quarter of 2013 and year-to-date, Loblaw recorded incremental general and administrative costs relating to Choice Properties of $3 million and $6 million, respectively.

***Choice Properties start-up costs*** In connection with the IPO of Choice Properties, Loblaw incurred certain costs to facilitate the start-up of the new entity. In the third quarter of 2013, Loblaw recorded $3 million of Choice Properties start-up costs.

***Defined benefit plan amendments*** The Company announced amendments to certain of its defined benefit plans impacting certain employees retiring after January 1, 2015. As a result, during the first quarter of 2013, the Company recorded a gain of $51 million related to these defined benefit plan amendments. During the fourth quarter of 2012, Weston Foods negotiated the elimination of certain post-retirement benefits. As a result, a net gain of $8 million was recorded in operating income.

***Multi-employer pension plan withdrawal liability incurred by Weston Foods*** During 2012, Weston Foods withdrew from one of the U.S. MEPPs in which it participated and as a result, paid a withdrawal liability of $34 million. During the fourth quarter of 2012, another participating employer withdrew from the plan and a mass withdrawal was triggered. As a result of the mass withdrawal, the Company is subject to an incremental withdrawal liability and an additional provision of $5 million was recorded in operating income during the fourth quarter of 2013. The total liability recorded as at year end 2013 relating to the Company's mass withdrawal liability is $22 million, $17 million of which was recorded in the fourth quarter of 2012.

***Gain on disposal of assets*** In the fourth quarter of 2012, Loblaw recognized a gain of $11 million related to the sale of a property.

***Weston Foods insurance proceeds*** In the fourth quarter of 2012, Weston Foods recorded insurance proceeds of $5 million related to the loss of a Quebec facility in 2010.

***Foreign currency translation gains and losses*** The Company's consolidated financial statements are expressed in Canadian dollars. A portion of the Company's (excluding Loblaw's) net assets are denominated in U.S. dollars and as a result, the Company is exposed to foreign currency translation gains and losses. The impact of foreign currency translation on a portion of the U.S. dollar denominated net assets, primarily cash and short term investments held by foreign operations, is recorded in operating income. In the fourth quarter of 2013, a foreign currency translation gain of $42 million (2012 – $18 million) was recorded in operating income as a result of the appreciation (2012 – appreciation) of the U.S. dollar relative to the Canadian dollar. Year-to-date, a foreign currency translation gain of $75 million (2012 – loss of $24 million) was recorded in operating income as a result of the appreciation (2012 – depreciation) of the U.S. dollar relative to the Canadian dollar.

**Adjusted Basic Net Earnings per Common Share from Continuing Operations** The Company believes adjusted basic net earnings per common share from continuing operations is 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 basic net earnings per common share from continuing operations to GAAP basic net earnings per common share from continuing operations reported for the periods ended as indicated.

| (unaudited) | Quarters Ended | | Years Ended | |
|---|---|---|---|---|
| ($) | **Dec. 31, 2013** | Dec. 31, 2012[i] | **Dec. 31, 2013** | Dec. 31, 2012[i] |
| Basic net earnings per common share from continuing operations | **$ 1.37** | $ 0.41 | **$ 4.48** | $ 3.36 |
| (Deduct) Add impact of the following[ii]: | | | | |
| Fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares | **(0.21)** | 0.44 | **(0.01)** | 0.20 |
| Restructuring and other charges | **0.14** | 0.24 | **0.17** | 0.33 |
| Fair value adjustment of commodity derivatives at Weston Foods | **0.03** | 0.06 | **0.06** | (0.03) |
| Share-based compensation net of equity derivatives | **0.05** | (0.03) | **0.20** | 0.14 |
| Fixed asset and other related (recoveries) impairments | **(0.14)** | 0.05 | **(0.11)** | 0.07 |
| Shoppers Drug Mart acquisition costs and net financing charges | **0.08** | | **0.13** | |
| Choice Properties general and administrative costs | **0.02** | | **0.03** | |
| Choice Properties start-up and IPO transaction costs | | | **0.17** | |
| Defined benefit plan amendments | | (0.04) | **(0.18)** | (0.04) |
| MEPP withdrawal liability incurred by Weston Foods | **0.02** | 0.08 | **0.02** | 0.24 |
| Gain on disposal of assets | | (0.04) | | (0.04) |
| Weston Foods insurance proceeds | | (0.03) | | (0.03) |
| Early debt settlement costs | | | **0.06** | |
| Fair value adjustment of Trust Unit liability | **0.08** | | **0.06** | |
| Foreign currency translation (gain) loss | **(0.33)** | (0.14) | **(0.59)** | 0.19 |
| Adjusted basic net earnings per common share from continuing operations | **$ 1.11** | $ 1.00 | **$ 4.49** | $ 4.39 |

(i) Certain 2012 figures have been restated due to the implementation of revised IAS 19. See Section 19, "Accounting Standards Implemented in 2013 and Changes in Significant Accounting Policies" of this MD&A.

(ii) Net of interest, income taxes and non-controlling interests, as applicable.

In addition to the items described in the "Adjusted Operating Income and Adjusted EBITDA" section above, the year-over-year change in the following items also influenced basic net earnings per common share from continuing operations in the fourth quarter of 2013 and year-to-date:

***Fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares*** The fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares is non-cash and is included in net interest expense and other financing charges. The adjustment is determined by changes in the value of the underlying Loblaw common shares. In the fourth quarter of 2013, income of $34 million on a pre-tax basis (2012 – a charge of $77 million) was recorded in net interest expense and other financing charges as a result of the decrease (2012 – increase) in the market price of Loblaw common shares. Year-to-date, income of $1 million on a pre-tax basis (2012 – a charge of $35 million) was recorded as a result of the decrease (2012 – increase) in the market price of Loblaw common shares.

***Shoppers Drug Mart net financing charges*** In addition to the acquisition costs noted above, during the fourth quarter of 2013 and year-to-date, net charges of $14 million and $25 million, respectively, on a pre-tax basis were incurred in connection with the committed financing related to the acquisition. In addition, during the third quarter of 2013, in connection with the issuance of $1.6 billion unsecured notes in 2013, Loblaw hedged its exposure to interest rates in the period prior to the issuance. As this relationship did not qualify for hedge accounting, this resulted in a gain of $10 million on the unwind of the hedge. The net impact of the financing costs and gain was recorded in net interest expense and other financing charges.

***Choice Properties IPO transaction costs*** In addition to the start-up costs noted above, transaction costs of $1 million in the fourth quarter of 2013 and $44 million year-to-date, on a pre-tax basis were incurred related directly to the IPO. These transaction costs were recorded in net interest expense and other financing charges.

***Early debt settlement costs*** During 2013, Loblaw settled its remaining U.S. $150 million USPP note and related cross currency swap in advance of its May 29, 2015 maturity date. Loblaw incurred early-settlement costs related to the prepayment of $18 million on a pre-tax basis, which were recorded in net interest expense and other financing charges.

***Fair value adjustment of Trust Unit liability*** The Company is exposed to market price fluctuations as a result of the Choice Properties Units held by the public. These Units are presented as a liability on the Company's consolidated balance sheet 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 period based on the market price of Units. In the fourth quarter of 2013 and year-to-date, the Company recorded a loss of $23 million and $18 million, respectively, related to the fair value adjustment of the Trust Unit liability.

**Adjusted Debt** The Company believes adjusted debt to adjusted EBITDA is useful in assessing the amount of financial leverage employed.

The following table reconciles adjusted debt used in the adjusted debt to adjusted EBITDA to GAAP measures reported as at the years ended as indicated.

| (unaudited) | As at | |
|---|---|---|
| ($ millions) | **Dec. 31, 2013** | Dec. 31, 2012 |
| Short term debt | **$ 1,060** | $ 1,319 |
| Long term debt due within one year | **1,208** | 672 |
| Long term debt | **7,736** | 6,261 |
| Trust Unit liability | **478** | |
| Certain other liabilities | **39** | 39 |
| Fair value of financial derivatives related to the above debt | **(524)** | (440) |
| Total debt | **$ 9,997** | $ 7,851 |
| Less: Independent securitization trusts in short term debt | **605** | 905 |
| Independent securitization trusts in long term debt | **750** | 600 |
| Trust Unit liability | **478** | |
| Independent funding trusts | **475** | 459 |
| Guaranteed Investment Certificates | **430** | 303 |
| Adjusted debt | **$ 7,259** | $ 5,584 |

Capital securities are excluded from the calculation of adjusted debt.

**Free Cash Flow** In 2013, the Company refined its definition of free cash flow as calculated below. The Company believes that this definition of free cash flow is the appropriate measure in assessing the Company's cash available for additional funding and investing activities.

The following table reconciles free cash flow to GAAP measures reported for the periods ended as indicated.

| (unaudited) | Quarters Ended | | Years Ended | |
|---|---|---|---|---|
| ($ millions) | **Dec. 31, 2013** | Dec. 31, 2012 | **Dec. 31, 2013** | Dec. 31, 2012 |
| Cash flows from operating activities of continuing operations | **$ 813** | $ 680 | **$ 1,738** | $ 1,852 |
| Change in credit card receivables | **108** | 232 | **233** | 204 |
| Less: Interest paid | **117** | 125 | **466** | 456 |
| Fixed asset purchases | **341** | 398 | **976** | 1,110 |
| Free cash flow | **$ 463** | $ 389 | **$ 529** | $ 490 |

**Interest Coverage** The Company believes interest coverage is useful in assessing the Company's ability to cover its net interest expense with its operating income.

The Company calculates interest coverage as operating income divided by net interest expense and other financing charges adding back interest capitalized to fixed assets.

The following table reconciles interest expense used in the interest coverage ratio to GAAP measures reported for the years ended as indicated.

| (unaudited) ($ millions) | **2013** | 2012[5] |
|---|---|---|
| Net interest expense and other financing charges | **$ 497** | $ 441 |
| Add: Interest capitalized to fixed assets | **2** | 1 |
| Interest expense | **$ 499** | $ 442 |

**Net Assets** The Company believes the return on average net assets ratio is useful in assessing its return on operating assets.

The Company calculates return on average net assets as operating income divided by average net assets.

The following table reconciles net assets used in the return on average net assets ratio to GAAP measures reported as at the years ended as indicated.

| (unaudited) ($ millions) | | | | | | | | As at Dec. 31, 2013 |
|---|---|---|---|---|---|---|---|---|
| | | **Weston Foods** | | **Loblaw** | | **Other[(i)]** | | **Consolidated** |
| Total assets | **$** | **2,067** | **$** | **20,919** | **$** | **1,636** | **$** | **24,622** |
| Less: Cash and cash equivalents | | **151** | | **2,260** | | **458** | | **2,869** |
| Short term investments | | **22** | | **290** | | **1,178** | | **1,490** |
| Security deposits | | **90** | | **1,701** | | | | **1,791** |
| Fair value of the forward sale agreement for 9.6 million Loblaw common shares | | **524** | | | | | | **524** |
| Trade payables and other liabilities | | **192** | | **3,797** | | | | **3,989** |
| Net assets | **$** | **1,088** | **$** | **12,871** | **$** | | **$** | **13,959** |

(i) Other includes cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates.

| (unaudited) ($ millions) | | | | | | | | As at Dec. 31, 2012 |
|---|---|---|---|---|---|---|---|---|
| | | Weston Foods | | Loblaw | | Other[(i)] | | Consolidated |
| Total assets | $ | 1,979 | $ | 18,121 | $ | 1,704 | $ | 21,804 |
| Less: Cash and cash equivalents | | 197 | | 1,079 | | 313 | | 1,589 |
| Short term investments | | 31 | | 716 | | 1,391 | | 2,138 |
| Security deposits | | 96 | | 252 | | | | 348 |
| Fair value of the forward sale agreement for 9.6 million Loblaw common shares | | 483 | | | | | | 483 |
| Trade payables and other liabilities | | 217 | | 3,720 | | | | 3,937 |
| Net assets | $ | 955 | $ | 12,354 | $ | | $ | 13,309 |

(i) Other includes cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates.

## 23. ADDITIONAL INFORMATION

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

This Annual Report includes selected information on Loblaw Companies Limited, a 63.0%-owned public reporting company with shares trading on the TSX. For information regarding Loblaw, readers should also refer to the materials filed by Loblaw with the Canadian securities regulatory authorities from time to time. These filings are also available on Loblaw's corporate website at www.loblaw.ca.

Toronto, Canada

February 26, 2014

## Financial Results


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## Management's Statement of Responsibility for Financial Reporting

The management of George Weston 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. 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 for providing 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 is required to certify as to the design and operating effectiveness of internal controls over financial reporting. Internal auditors, who are employees of the Company, review and evaluate internal controls on management's behalf. 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.

**[*signed*]**
**W. Galen Weston**
Executive Chairman

**[*signed*]**
**Paviter S. Binning**
President

**[*signed*]**
**Richard Dufresne**
Executive Vice President,
Chief Financial Officer

February 26, 2014
Toronto, Canada

# Independent Auditors' Report

**To the Shareholders of George Weston Limited:**

We have audited the accompanying consolidated financial statements of George Weston Limited, which comprise the consolidated balance sheets as at December 31, 2013 and December 31, 2012, the consolidated statements of earnings, comprehensive income, changes in equity and cash flows for the 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 George Weston Limited as at December 31, 2013 and December 31, 2012, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Chartered Professional Accountants, Licensed Public Accountants

February 26, 2014
Toronto, Canada

## Consolidated Statements of Earnings

For the years ended December 31
(millions of Canadian dollars except where otherwise indicated)

| | 2013 | 2012[1] |
|---|---|---|
| **Revenue** | **$ 33,582** | $ 32,742 |
| **Operating Expenses** | | |
| Cost of inventories sold (note 14) | **25,286** | 24,700 |
| Selling, general and administrative expenses (note 34) | **6,675** | 6,649 |
| | **31,961** | 31,349 |
| **Operating Income** | **1,621** | 1,393 |
| Net Interest Expense and Other Financing Charges (note 7) | **497** | 441 |
| **Earnings Before Income Taxes** | **1,124** | 952 |
| Income Taxes (note 8) | **275** | 244 |
| **Net Earnings from Continuing Operations** | **849** | 708 |
| Attributable to: | | |
| Shareholders of the Company | **616** | 475 |
| Non-Controlling Interests | **233** | 233 |
| **Net Earnings from Continuing Operations** | **849** | 708 |
| Discontinued Operations (note 9) | **58** | |
| **Net Earnings** | **$ 907** | $ 708 |
| **Net Earnings per Common Share ($) - Basic** | | |
| Continuing Operations (note 10) | **$ 4.48** | $ 3.36 |
| Discontinued Operations | **$ 0.46** | |
| Net Earnings | **$ 4.94** | $ 3.36 |
| **Net Earnings per Common Share ($) - Diluted** | | |
| Continuing Operations (note 10) | **$ 4.45** | $ 3.29 |
| Discontinued Operations | **$ 0.46** | |
| Net Earnings | **$ 4.91** | $ 3.29 |

(1) Certain 2012 figures have been restated (see note 2).

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Comprehensive Income

For the years ended December 31
(millions of Canadian dollars)

| | 2013 | 2012[1] |
|---|---|---|
| Net earnings | **$ 907** | $ 708 |
| Other comprehensive income (loss) | | |
| Items that are or may be reclassified subsequently to profit or loss: | | |
| Foreign currency translation adjustment (note 34) | **44** | (13) |
| Reclassification of gain on derecognized derivative instruments (note 34) | **(5)** | |
| Items that will not be reclassified to profit or loss: | | |
| Net defined benefit plan actuarial gains (losses) (note 30) | **254** | (6) |
| Other comprehensive income (loss) | **293** | (19) |
| **Comprehensive Income** | **1,200** | 689 |
| Attributable to: | | |
| Shareholders of the Company | **882** | 457 |
| Non-Controlling Interests | **318** | 232 |
| **Comprehensive Income** | **$ 1,200** | $ 689 |

(1) Certain 2012 figures have been restated (see note 2).

See accompanying notes to the consolidated financial statements.

# Consolidated Balance Sheets

| As at December 31<br>(millions of Canadian dollars) | 2013 | 2012[1] |
|---|---|---|
| **ASSETS** | | |
| **Current Assets** | | |
| Cash and cash equivalents (note 11) | **$ 2,869** | $ 1,589 |
| Short term investments (note 11) | **1,490** | 2,138 |
| Accounts receivable (note 12) | **736** | 559 |
| Credit card receivables (note 13) | **2,538** | 2,305 |
| Inventories (note 14) | **2,231** | 2,132 |
| Income taxes recoverable | | 37 |
| Prepaid expenses and other assets | **84** | 83 |
| Assets held for sale (note 15) | **22** | 30 |
| **Total Current Assets** | **9,970** | 8,873 |
| Fixed Assets (note 16) | **9,655** | 9,452 |
| Investment Properties (note 17) | **99** | 100 |
| Goodwill and Intangible Assets (note 18) | **1,580** | 1,571 |
| Deferred Income Taxes (note 8) | **299** | 316 |
| Security Deposits (note 11) | **1,791** | 348 |
| Franchise Loans Receivable (note 34) | **375** | 363 |
| Other Assets (note 20) | **853** | 781 |
| **Total Assets** | **$ 24,622** | $ 21,804 |
| **LIABILITIES** | | |
| **Current Liabilities** | | |
| Trade payables and other liabilities | **$ 3,989** | $ 3,937 |
| Provisions (note 21) | **120** | 123 |
| Income taxes payable | **2** | |
| Short term debt (note 22) | **1,060** | 1,319 |
| Long term debt due within one year (note 23) | **1,208** | 672 |
| **Total Current Liabilities** | **6,379** | 6,051 |
| Provisions (note 21) | **81** | 94 |
| Long Term Debt (note 23) | **7,736** | 6,261 |
| Trust Unit Liability (note 24) | **478** | |
| Deferred Income Taxes (note 8) | **187** | 160 |
| Other Liabilities (note 25) | **618** | 943 |
| Capital Securities (note 26) | **224** | 223 |
| **Total Liabilities** | **15,703** | 13,732 |
| **EQUITY** | | |
| Share Capital (note 27) | **972** | 953 |
| Contributed Surplus (notes 28 & 31) | **65** | 28 |
| Retained Earnings | **5,272** | 4,736 |
| Accumulated Other Comprehensive Income (Loss) | **16** | (24) |
| **Total Equity Attributable to Shareholders of the Company** | **6,325** | 5,693 |
| Non-Controlling Interests | **2,594** | 2,379 |
| **Total Equity** | **8,919** | 8,072 |
| **Total Liabilities and Equity** | **$ 24,622** | $ 21,804 |

(1) Certain 2012 figures have been restated (see note 2).

Leases (note 33). Contingent liabilities (note 36). Financial guarantees (note 37). Subsequent events (notes 22 and 23).

See accompanying notes to the consolidated financial statements.

Approved on behalf of the Board

| | |
|---|---|
| ***[signed]*** | ***[signed]*** |
| **W. Galen Weston** | **A. Charles Baillie** |
| Director & Executive Chairman | Director |

# Consolidated Statements of Changes in Equity

| (millions of Canadian dollars except where otherwise indicated) | Common Shares | Preferred Shares | Total Share Capital | Contributed Surplus | Retained Earnings[1] | Foreign Currency Translation Adjustment | Cash Flow Hedges | Total Accumulated Other Comprehensive (Loss) Income | Non-Controlling Interests[1] | Total Equity[1] |
|---|---|---|---|---|---|---|---|---|---|---|
| **Balance as at Dec. 31, 2012** | $ 136 | $ 817 | **$ 953** | **$ 28** | **$ 4,736** | $ (28) | $ 4 | **$ (24)** | **$ 2,379** | **$ 8,072** |
| Net earnings | | | | | **674** | | | | **233** | **907** |
| Other comprehensive income (loss)[2] | | | | | **168** | 44 | (4) | **40** | **85** | **293** |
| Comprehensive income (loss) | | | | | **842** | 44 | (4) | **40** | **318** | **1,200** |
| Effect of share-based compensation (notes 27 & 31) | 20 | | **20** | **48** | | | | | **12** | **80** |
| Shares purchased for cancellation (note 27) | (1) | | **(1)** | | **(41)** | | | | | **(42)** |
| Shares purchased and held in trust (note 27) | | | | | **(15)** | | | | | **(15)** |
| Subsidiary capital transactions (notes 28 & 31) | | | | **(11)** | | | | | **(17)** | **(28)** |
| Dividends declared | | | | | | | | | | |
| Per common share ($) – $1.625 | | | | | **(207)** | | | | **(98)** | **(305)** |
| Per preferred share ($) | | | | | | | | | | |
| – Series I – $1.45 | | | | | **(13)** | | | | | **(13)** |
| – Series III – $1.30 | | | | | **(10)** | | | | | **(10)** |
| – Series IV – $1.30 | | | | | **(10)** | | | | | **(10)** |
| – Series V – $1.19 | | | | | **(10)** | | | | | **(10)** |
| | 19 | | **19** | **37** | **(306)** | | | | **(103)** | **(353)** |
| **Balance as at Dec. 31, 2013** | $ 155 | $ 817 | **$ 972** | **$ 65** | **$ 5,272** | $ 16 | | **$ 16** | **$ 2,594** | **$ 8,919** |

(1) Certain 2012 figures have been restated (see note 2).

(2) Other comprehensive income includes actuarial gains of $254, $168 of which is presented above in retained earnings and $86 in non-controlling interests.

| (millions of Canadian dollars except where otherwise indicated) | Common Shares | Preferred Shares | Total Share Capital | Contributed Surplus | Retained Earnings[1] | Foreign Currency Translation Adjustment | Cash Flow Hedges | Total Accumulated Other Comprehensive Loss | Non-Controlling Interests[1] | Total Equity[1] |
|---|---|---|---|---|---|---|---|---|---|---|
| **Balance as at Dec. 31, 2011** | $ 133 | $ 817 | **$ 950** | **$ 24** | **$ 4,497** | $ (15) | $ 4 | **$ (11)** | **$ 2,222** | **$ 7,682** |
| Net earnings | | | | | **475** | | | | **233** | **708** |
| Other comprehensive loss[2] | | | | | **(5)** | (13) | | **(13)** | **(1)** | **(19)** |
| Comprehensive income (loss) | | | | | **470** | (13) | | **(13)** | **232** | **689** |
| Effect of share-based compensation (notes 27 & 31) | 3 | | **3** | | | | | | **5** | **8** |
| Shares purchased for cancellation (note 27) | | | | | **(1)** | | | | | **(1)** |
| Subsidiary capital transactions (notes 28 & 31) | | | | **4** | | | | | **9** | **13** |
| Dividends declared | | | | | | | | | | |
| Per common share ($) – $1.460 | | | | | **(187)** | | | | **(89)** | **(276)** |
| Per preferred share ($) | | | | | | | | | | |
| – Series I – $1.45 | | | | | **(13)** | | | | | **(13)** |
| – Series III – $1.30 | | | | | **(10)** | | | | | **(10)** |
| – Series IV – $1.30 | | | | | **(10)** | | | | | **(10)** |
| – Series V – $1.19 | | | | | **(10)** | | | | | **(10)** |
| | 3 | | **3** | **4** | **(231)** | | | | **(75)** | **(299)** |
| **Balance as at Dec. 31, 2012** | $ 136 | $ 817 | **$ 953** | **$ 28** | **$ 4,736** | $ (28) | $ 4 | **$ (24)** | **$ 2,379** | **$ 8,072** |

(1) Certain 2012 figures have been restated (see note 2).

(2) Other comprehensive loss includes actuarial losses of $6, $5 of which is presented above in retained earnings and $1 in non-controlling interests.

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Cash Flows

For the years ended December 31

| (millions of Canadian dollars) | 2013 | 2012[1] |
|---|---|---|
| **Operating Activities** | | |
| Net earnings from continuing operations | **$ 849** | $ 708 |
| Income taxes (note 8) | **275** | 244 |
| Net interest expense and other financing charges (note 7) | **497** | 441 |
| Depreciation and amortization | **891** | 840 |
| Foreign currency translation (gain) loss (note 34) | **(75)** | 24 |
| Gain on defined benefit plan amendments (note 30) | **(51)** | |
| Income taxes paid | **(271)** | (261) |
| Interest received | **59** | 65 |
| Settlement of derivatives (note 34) | **59** | |
| Change in credit card receivables (note 13) | **(233)** | (204) |
| Change in non-cash working capital | **(250)** | 43 |
| Fixed asset and other related (recoveries) impairments | **(32)** | 19 |
| Gain on disposal of assets | **(1)** | (14) |
| Other | **21** | (53) |
| **Cash Flows from Operating Activities of Continuing Operations** | **1,738** | 1,852 |
| **Investing Activities** | | |
| Fixed asset purchases (note 16) | **(976)** | (1,110) |
| Change in short term investments | **730** | 181 |
| Business acquisition (note 5) | **(9)** | |
| Proceeds from fixed asset sales | **26** | 64 |
| Change in franchise investments and other receivables | **5** | (22) |
| Change in security deposits | **(1,435)** | 14 |
| Intangible asset additions (note 18) | **(12)** | (43) |
| Other | **(4)** | |
| **Cash Flows used in Investing Activities of Continuing Operations** | **(1,675)** | (916) |
| **Financing Activities** | | |
| Change in bank indebtedness | | (3) |
| Change in short term debt (note 22) | **(259)** | 39 |
| Long term debt – Issued, net of financing charges (note 23) | **2,749** | 111 |
| – Retired (note 23) | **(871)** | (115) |
| Trust Units – Issued, net of financing charges (note 6) | **416** | |
| Share capital – Issued (notes 27 & 31) | **17** | 2 |
| – Purchased and held in trust (note 27) | **(15)** | |
| – Retired (note 27) | **(42)** | (1) |
| Subsidiary share capital – Issued (notes 28 & 31) | **75** | 22 |
| – Purchased and held in trust (note 28) | **(46)** | |
| – Retired (note 28) | **(73)** | (16) |
| Interest paid | **(466)** | (456) |
| Dividends – To common shareholders | **(203)** | (185) |
| – To preferred shareholders | **(44)** | (44) |
| – To minority shareholders | **(96)** | (65) |
| **Cash Flows from (used in) Financing Activities of Continuing Operations** | **1,142** | (711) |
| Effect of foreign currency exchange rate changes on cash and cash equivalents | **27** | (8) |
| **Cash Flows from Continuing Operations** | **1,232** | 217 |
| **Cash Flows from Discontinued Operations** (note 9) | **48** | |
| Change in Cash and Cash Equivalents | **1,280** | 217 |
| Cash and Cash Equivalents, Beginning of Year | **1,589** | 1,372 |
| **Cash and Cash Equivalents, End of Year** | **$ 2,869** | $ 1,589 |

(1) Certain 2012 figures have been restated (see note 2).

See accompanying notes to the consolidated financial statements.

For the years ended December 31, 2013 and December 31, 2012
(millions of Canadian dollars except where otherwise indicated)

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

George Weston Limited ("GWL") is a Canadian public company incorporated in 1928, with its registered office located at 22 St. Clair Avenue East, Toronto, Canada M4T 2S7. GWL and its subsidiaries are together referred to as the "Company" in these consolidated financial statements. The Company's parent is Wittington Investments, Limited ("Wittington").

The Company has two reportable operating segments, Loblaw Companies Limited ("Loblaw") and Weston Foods, and holds cash, short term investments and a direct investment in Choice Properties Real Investment Trust ("Choice Properties"). The Loblaw operating segment is Canada's largest food retailer and a leading provider of drugstore, general merchandise and financial products and services, and is the majority unitholder of Choice Properties, an owner, manager and developer of commercial real estate across Canada. The Weston Foods operating segment is a leading fresh and frozen baking company in Canada and operates a frozen baking manufacturing business in the United States ("U.S.") and a North American biscuit manufacturing business.

In 2013, Choice Properties completed an Initial Public Offering ("IPO") (see note 6).

Also in 2013, Loblaw entered into a definitive agreement to acquire all of the outstanding common shares of Shoppers Drug Mart Corporation ("Shoppers Drug Mart") (see note 39). The Company anticipates that the transaction will be completed during the first quarter of 2014, subject to various regulatory approvals, including approvals under the *Competition Act* (Canada) and by the Toronto Stock Exchange ("TSX"), and the fulfillment of certain other closing conditions customary in transactions of this nature.

## 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.

These consolidated financial statements were authorized for issuance by the Company's Board of Directors ("Board") on February 26, 2014.

**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:

- amounts recognized for equity-settled and cash-settled share-based compensation arrangements as described in note 31;
- defined benefit plan assets with the obligations related to these pension plans measured at their discounted present value as described in note 30; and
- certain financial instruments as described in note 34.

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.

**Fiscal Year** The Company's year end is December 31. Activities are reported on a fiscal year ending on the Saturday closest to December 31.

As a result, the Company's fiscal year is usually 52 weeks in duration but includes a 53rd week every five to six years. Each of the years ended December 31, 2013 and December 31, 2012 contained 52 weeks. The next 53-week year will occur in fiscal year 2014.

**Basis of Consolidation** The consolidated financial statements include the accounts of GWL 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. The Company's interest in the voting share capital of its subsidiaries is 100% except for Loblaw, which is 63.0% (December 31, 2012 – 62.9%). GWL's ownership in Loblaw was impacted by changes in Loblaw's common share equity.

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 recorded in the consolidated financial statements and represent the non-controlling shareholders' portion of the net assets and net earnings of Loblaw. Transactions with non-controlling interests are treated as transactions with equity owners of the Company. Changes in GWL's ownership interest in its subsidiaries are accounted for as equity transactions.

**Business Combinations** Business combinations are accounted for using the acquisition method as at the acquisition date (i.e. 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. Transactions costs other than those associated with the issue of debt or equity securities, that the Company incurs in connection with a business combination are expensed as incurred.

**Net Earnings per Common Share ("EPS")** Basic 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 Company and when specific criteria have been met as described below.

Weston Foods recognizes sales upon delivery of its products to customers and acceptance of its products by customers net of provisions for returns, discounts and allowances.

*Retail* revenue includes sale of goods to customers through corporate stores operated by Loblaw and sales to franchised stores, associated 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. Loblaw recognizes revenue at the time the sale is made to its customers and at the time of delivery of inventory to its associated and franchised stores. Revenue also includes service fees from franchised stores, associated stores, and independent account customers, which are recognized when services are rendered.

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

*Financial Services* 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* revenue includes rental revenue from operating leases where Choice Properties is the lessor. The rental revenue is recognized on a straight-line basis over the term of the respective leases.

*Customer Loyalty Awards* Loblaw 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.

**Income Taxes** Current and deferred taxes are recognized in the consolidated statements of earnings, except when it relates to a business combination, or items recognized in equity or in other comprehensive income (loss).

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, but 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 Equivalents** Cash equivalents consist of highly liquid marketable investments with a maturity 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, which primarily include escrow deposits for pending acquisitions. Security deposits also include amounts which are required to be placed with counterparties as collateral to enter into and maintain certain outstanding letters of credit and certain financial derivative contracts.

**Accounts Receivable** Accounts receivable consist mainly of receivables from Loblaw's vendors, independent franchisees, associated stores, independent accounts and receivables from Weston Foods customers and suppliers, and are recorded net of allowances.

**Credit Card Receivables** Loblaw, through President's Choice Bank ("PC Bank"), a wholly owned subsidiary of Loblaw, 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, Loblaw estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

Periodically, PC Bank 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, Loblaw 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*® ("*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 Loblaw 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 Loblaw and draw upon a standby letter of credit. Loblaw 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 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. Loblaw's seasonal general merchandise, Loblaw's inventories at distribution centres and Weston Foods inventories are measured at weighted average cost. Loblaw uses the retail method to measure the cost of the majority of retail store inventories. Loblaw 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 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. 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 are reduced in the cost of the vendor's products or services and are recognized as a reduction in the cost of 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 costs incurred to promote the vendor's products. The consideration is then recognized as a reduction of the cost incurred in the consolidated statements of earnings.

**Fixed Assets** Fixed assets are recognized 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 if it is probable that the future economic benefits embodied within the component will flow to the Company and the cost can be measured reliably. The carrying amount of the replaced component is derecognized. 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 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 each 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 20 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[(1)] and useful life[(2)] |

(1) 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.

(2) 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 Loblaw that are held to either earn rental income, for capital appreciation, or both. Loblaw'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 Loblaw'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 significant 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.

**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 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 30 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"). Weston Foods' manufacturing assets are grouped together at the level of production categories which are capable of servicing their customers independently of other production categories. Loblaw 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 grouping. 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 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 grouping 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 grouping 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.

**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.

Certain non-financial derivative instruments that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the Company's expected purchase, sale or usage requirements are exempt from financial instrument accounting requirements ("own use exemption"). No amounts are recorded in the consolidated financial statements related to these contracts until the associated non-financial items are received by the Company.

***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 | Fair value |
| Short term investments | Fair value through profit and loss | Fair value |
| Derivatives included in accounts receivable | Fair value through profit and loss | Fair value |
| Other accounts receivables | Loans and receivables | Amortized cost |
| Credit card receivables | Loans and receivables | Amortized cost |
| Derivatives included in prepaid expenses and other assets | Fair value through profit and loss | Fair value |
| Security deposits | Fair value through profit and loss | Fair value |
| Franchise loans receivable | Loans and receivables | Amortized cost |
| Derivatives included in other assets | Fair value through profit and loss | Fair value |
| Certain other assets | Loans and receivables | Amortized cost |
| Trade payables and other liabilities | Other liabilities | Amortized cost |
| Derivatives included in trade payables and other liabilities | Fair value through profit and loss | Fair value |
| Short term debt | Other liabilities | Amortized cost |
| Long term debt | Other liabilities | Amortized cost |
| Trust Unit liability | Fair value through profit and loss | Fair value |
| Certain other liabilities | Other liabilities | Amortized cost |
| Capital securities | Other liabilities | Amortized cost |

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

***Fair Value*** The Company measures financial assets and 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 during 2013. 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, Trade Payables and Other Liabilities, Short Term Debt and Other Liabilities* | The carrying amount approximates fair value due to the short term maturity of these instruments. |
| *Franchise Loans Receivable* | The carrying amount approximates fair value due to the minimal fluctuations in the forward interest rate and the provisions recorded for all impaired receivables. |
| *Derivative Financial Instruments* | Specific valuation techniques used to value derivative financial instruments include:<br>• Quoted market prices or dealer quotes for similar instruments;<br>• 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<br>• The fair value of cross currency swaps is determined by forward and spot foreign exchange rates. The fair value of certain swaps is determined by an external valuator with experience in the financial markets. |
| *Long Term Debt, Trust Unit Liability, Capital Securities and 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. |

***Derecognition of Financial Instruments*** 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 tax.

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 tax.

***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 statements 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 statements 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 comprehensive income (loss). 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.

Remeasurements 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 (loss) and subsequently reclassified from accumulated other comprehensive income (loss) 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 ("MEPP") 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 MEPPs 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 MEPPs 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 Share-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 prices of the GWL or Loblaw common shares 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 GWL or 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.

During 2013, GWL and Loblaw established trusts 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 obligations.

Members of GWL's and Loblaw's Board, who are not management, 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.

**Cash-Settled Share-Based Compensation Plans** Unit Options, Restricted Units and Trustee Deferred Units issued by Choice Properties are accounted for as cash-settled awards.

The fair value of the amount payable to employees in respect of these cash settled awards plan is remeasured at each balance sheet date, and a compensation expense is recognized in selling, general and administrative expenses over the vesting period for each tranche with a corresponding change in the liability.

Prior to 2013, vested RSUs, vested PSUs, DSUs and EDSUs issued by the Company were settled in cash and were accounted for as cash-settled awards and entitled the holder to receive a GWL or Loblaw common share or the cash equivalent. The cash payment was equal to the weighted average of the trading prices of the GWL or

Loblaw common shares on the TSX for the five trading days prior to the valuation date. Compensation expense was recorded for each award granted equal to the market value of a GWL or Loblaw common share at the date on which the awards were granted, with a corresponding change to the liability. For RSUs and PSUs, the net present value of the expected dividend stream was deducted from the market value of the GWL or Loblaw common share. Compensation expense was prorated over the vesting period reflecting changes in the market value of a GWL or Loblaw common share, and in the case of PSUs, the number of awards expected to vest.

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

**Accounting Standards Implemented in 2013**

***Fair Value Measurement*** In 2011, the IASB issued IFRS 13, "Fair Value Measurement" ("IFRS 13"), which establishes a single framework for the fair value measurement and disclosure of financial and non-financial assets and liabilities. The new standard unifies the definition of fair value and also introduces new concepts including 'highest and best use' and 'principal markets' for non-financial assets and liabilities. There are additional disclosure requirements, including increased fair value disclosure for financial instruments for interim and annual financial statements. The Company implemented this standard prospectively in the first quarter of 2013. There were no significant measurement impacts on the Company's consolidated financial statements as a result of the adoption of IFRS 13. The Company has included the additional disclosures required by this standard (see note 34).

***Employee Benefits*** In 2011, the IASB revised International Accounting Standard ("IAS") 19, "Employee Benefits" ("IAS 19"). The most significant amendments for the Company and its significant accounting policies are the requirement to immediately recognize all unvested past service costs and the replacement of interest cost and expected return on plan assets with a net interest amount that is calculated by applying a prescribed discount rate to the net defined benefit obligation (asset). Under the amendment, the Company continues to recognize actuarial gains and losses on plan assets and obligations through other comprehensive income (loss), but has chosen to reclassify these amounts from accumulated other comprehensive income (loss) and record these actuarial gains and losses in retained earnings, consistent with its previous presentation. The Company implemented this standard retrospectively in the first quarter of 2013. The impact arising from the adoption of the amendments to IAS 19 is summarized as follows:

**Consolidated Statements of Earnings**

| Increase (decrease) | | **2013** | | 2012 |
|---|---|---|---|---|
| Operating income | **$** | **20** | $ | 1 |
| Net interest expense and other financing charges | **$** | **32** | $ | 24 |
| Income taxes | **$** | **(3)** | $ | (5) |
| Net earnings | **$** | **(9)** | $ | (18) |
| Net earnings per common share ($) | | | | |
| Basic | **$** | **(0.05)** | $ | (0.09) |
| Diluted | **$** | **(0.05)** | $ | (0.09) |

**Consolidated Statements of Comprehensive Income**

| Increase (decrease) | | **2013** | | 2012 |
|---|---|---|---|---|
| Net earnings | **$** | **(9)** | $ | (18) |
| Other comprehensive income | **$** | **24** | $ | 18 |

| **Consolidated Balance Sheets** | As at | | |
|---|---|---|---|
| Increase (decrease) | **Dec. 31, 2013** | Dec. 31, 2012 | Jan. 1, 2012 |
| Deferred income tax asset | **$ (5)** | | $ 1 |
| Other liabilities | **$ (22)** | $ (2) | $ (1) |
| Equity | **$ 17** | $ 2 | $ 2 |

The amendments also require enhanced annual disclosures for defined benefit plans, including additional information on the characteristics and risks of those plans. The Company has included the additional disclosures required by this standard (see note 30).

***Other Standards*** In addition to the above standards, the Company implemented the following standards and amendments effective January 1, 2013: IFRS 10, "Consolidated Financial Statements"; IFRS 11, "Joint Arrangements"; IFRS 12, "Disclosure of Interests in Other Entities"; IAS 28, "Investments in Associates"; and IAS 1, "Presentation of Financial Statements". There was no significant impact on the Company's consolidated financial statements as a result of the implementation of these standards. The Company has included the additional disclosures required by these standards (see note 19).

In 2013, the IASB issued amendments to IAS 36, "Impairment of Assets", which clarify the disclosure requirements for recoverable amounts of CGUs. These amendments are required to be applied for periods beginning on or after January 1, 2014. The Company has elected to early adopt these amendments during 2013. There was no significant impact on the Company's consolidated financial statements as a result of these amendments.

## 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.

### 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 future retail prices, 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 indefinite life intangible assets are tested for impairment. Loblaw has determined that each location is a separate CGU for purposes of fixed asset impairment testing. For the purpose of goodwill and intangible assets impairment testing, CGUs are grouped at the lowest level at which goodwill and intangible assets 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 revenues, earnings and capital investment consistent with strategic plans presented to GWL's and Loblaw's Boards. 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 financial assets relating to its 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 Loblaw's five year forecast.

**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.

**Allowance for credit card receivables**
*Key sources of estimation* The allowance for credit card receivables is measured based upon statistical analysis that includes estimates for past and current performance, aging, arrears status, the level of allowance already in place, and management's interpretation of economic conditions and other trends specific to Loblaw's customer base, including but not limited to bankruptcies. Changes in circumstances may cause future assessments of credit risk to be materially different from current assessments, which could require an increase or decrease in the allowance for credit card receivables.

## Note 4. Future Accounting Standards

**Financial Instruments** In 2011, the IASB issued amendments to IFRS 7, "Financial Instruments: Disclosures", and IAS 32, "Financial Instruments: Presentation". These amendments are required to be applied for periods beginning on or after January 1, 2014. The Company does not expect any significant impacts on its consolidated financial statements as a result of these amendments.

In 2013, the IASB issued amendments to IFRS 9, "Financial Instruments" ("IFRS 9"), issued in 2010, which will ultimately replace IAS 39, "Financial Instruments: Recognition and Measurement" ("IAS 39"). The replacement of IAS 39 is a three-phase project with the objective of improving and simplifying the reporting for financial

instruments. The current issuance of IFRS 9 includes the first and third phases of the project, which provide guidance on the classification and measurement of financial assets and financial liabilities and hedge accounting. The mandatory effective date of the standard has not been determined due to the incomplete status of the second phase of the project, impairment. The effective date of the entire standard will be determined closer to the completion of the remaining phase. The Company continues to assess the impact of the new standard on its consolidated financial statements.

**Levies** In 2013, the International Financial Reporting Interpretations Committee ("IFRIC") issued IFRIC 21, "Levies" ("IFRIC 21"). IFRIC 21 addresses accounting for a liability to pay a levy within the scope of IAS 37, "Provisions, Contingent Liabilities and Contingent Assets". A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation, other than income taxes within the scope of IAS 12, "Income Taxes", and fines or other penalties imposed for breaches of the legislation. This interpretation is effective for annual periods beginning on or after January 1, 2014, and is to be applied retrospectively. The Company is currently assessing the impact of the new interpretation on its consolidated financial statements.

### Note 5. Business Acquisition

In 2013, Weston Foods purchased a fresh bakery manufacturer for cash consideration of $9 and acquired net assets of $9.

### Note 6. Initial Public Offering of Choice Properties Real Estate Investment Trust

In 2013, Choice Properties completed a $460 IPO of Trust Units ("Units"), including the exercise of a $60 over-allotment option, in connection with its acquisition of approximately $7 billion of properties and related assets from Loblaw. In addition, Choice Properties completed a $200 offering of Units to GWL.

Loblaw recorded transaction costs of approximately $44 in net interest expense and other financing charges (see note 7) related to the IPO.

Concurrent with the offering of Units, Choice Properties completed a public offering of $600 aggregate principal amount of senior unsecured debentures (the "Debentures") (see note 23). A portion of the debt offering proceeds were used to replenish the cash used to repay the U.S. $150 private placement ("USPP") note that matured in 2013 and to early-settle the remaining U.S. $150 USPP note, including the associated early-settlement costs of approximately $18 which were recorded in net interest expense and other financing charges (see note 7).

As at year end 2013, GWL held an effective interest of approximately 5.4% in Choice Properties through the ownership of 20,107,810 Units and Loblaw held an effective interest in Choice Properties of approximately 82.2% through the ownership of 21,500,000 Units and 284,074,754 Class B Limited Partnership units, which are economically equivalent to and exchangeable for Units. Included in the Class B Limited Partnership units are 11,576,883 units issued to Loblaw, in connection with the acquisition of an additional portfolio of investment properties subsequent to the IPO.

## Note 7. Net Interest Expense and Other Financing Charges

The components of net interest expense and other financing charges were as follows:

| | 2013 | 2012[1] |
|---|---|---|
| Interest expense: | | |
| Long term debt | **$ 369** | $ 367 |
| Borrowings related to credit card receivables | **39** | 37 |
| Net interest on net defined benefit obligation (note 30) | **25** | 32 |
| Independent funding trusts | **15** | 15 |
| Trust Unit distributions | **15** | |
| Dividends on capital securities (note 26) | **14** | 14 |
| Choice Properties IPO transaction costs (note 6) | **44** | |
| Shoppers Drug Mart net financing charges[2] | **20** | |
| Early debt settlement costs (note 23) | **18** | |
| Fair value adjustment of Trust Unit liability (note 24) | **18** | |
| Interest associated with forward sale agreement[3] | | 12 |
| Financial derivative instruments | | 2 |
| Capitalized interest (capitalization rate 6.4% (2012 – 6.4%)) (note 16) | **(2)** | (1) |
| | **$ 575** | $ 478 |
| Interest income: | | |
| Interest associated with forward sale agreement[3] | **$ (23)** | |
| Accretion income | **(21)** | $ (18) |
| Short term interest income | **(18)** | (17) |
| Financial derivative instruments | **(9)** | |
| Security deposits[4] | **(7)** | (2) |
| | **$ (78)** | $ (37) |
| Net interest expense and other financing charges | **$ 497** | $ 441 |

(1) Certain 2012 figures have been restated (see note 2).

(2) Included charges of $30 incurred in connection with the committed financing, net of a gain of $10 on the unwind of the hedge entered into related to Loblaw's issuance of $1.6 billion senior unsecured notes (see note 34).

(3) Included non-cash income of $1 (2012 – a non-cash charge of $35) related to the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares (see note 34). The fair value adjustment of the forward sale agreement is non-cash and results from changes in the value of the underlying Loblaw shares. At maturity, any cash paid under the forward sale agreement could be offset by the sale of the underlying Loblaw common shares. Also included is forward accretion income of $40 (2012 – $40) and the forward fee of $18 (2012 – $17) associated with the forward sale agreement.

(4) Included interest income of $5 (2012 – nil) related to $1.6 billion of proceeds from the issuance of senior unsecured notes held in escrow (see notes 11 and 23), which will be used to partially fund the acquisition of all the outstanding common shares of Shoppers Drug Mart.

## Note 8. Income Taxes

The components of income taxes were as follows:

| | 2013 | 2012[1] |
|---|---|---|
| **Current income taxes** | | |
| Current period | **$ 327** | $ 285 |
| Adjustment in respect of prior periods | **(5)** | (23) |
| **Deferred income taxes** | | |
| Origination and reversal of temporary differences | **(36)** | (26) |
| Adjustment in respect of prior periods | **(11)** | 8 |
| Income taxes | **$ 275** | $ 244 |

(1) Certain 2012 figures have been restated (see note 2).

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

| | 2013 | 2012[1] |
|---|---|---|
| Defined benefit plan actuarial gains (losses) (note 30) | **$ 93** | $ (2) |
| Derecognized derivative instruments (note 34) | **(2)** | |
| Other comprehensive income (loss) | **$ 91** | $ (2) |

(1) Certain 2012 figures have been restated (see note 2).

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

| | 2013 | 2012[1] |
|---|---|---|
| Weighted average basic Canadian federal and provincial statutory income tax rate | **25.9%** | 26.0% |
| Net (decrease) increase resulting from: | | |
| Earnings in jurisdictions taxed at rates different from the Canadian statutory income tax rates | **(0.6)** | (0.9) |
| Unrecognized benefit of foreign currency translation (gains) losses | **(0.6)** | 1.2 |
| Non-taxable and non-deductible amounts | **0.4** | 0.8 |
| Impact of fair value adjustment of Trust Unit liability | **0.6** | |
| Impact of statutory income tax rate changes on deferred income tax balances | **(0.1)** | (0.4) |
| Impact of resolution of certain income tax matters from a previous year and other | **(1.1)** | (1.1) |
| Effective income tax rate applicable to earnings before income taxes | **24.5%** | 25.6% |

(1) Certain 2012 figures have been restated (see note 2).

In 2012, the Department of Finance substantively enacted amendments to the Income Tax Act relating to the taxation of Canadian corporations with foreign affiliates. The Company is no longer able to recognize a net tax benefit on realized foreign capital losses recognized by its foreign affiliates to the extent such losses cannot be offset against realized foreign capital gains. In 2012, the Company (excluding Loblaw) expensed $8 in previously recognized current tax assets relating to these amendments.

Deferred income tax assets as at December 31, 2013 and December 31, 2012 which were not recognized on the consolidated balance sheets were as follows:

| | **2013** | 2012 |
|---|---|---|
| Deductible temporary differences | **$ 28** | $ 28 |
| Income tax losses and credits | **39** | 49 |
| Unrecognized deferred income tax assets | **$ 67** | $ 77 |

The income tax losses and credits expire in the years 2014 to 2033. 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.

Deferred income tax assets and liabilities recognized on the consolidated balance sheets were attributable to the following:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Trade payables and other liabilities | **$ 72** | $ 73 |
| Other liabilities | **260** | 365 |
| Fixed assets | **(392)** | (343) |
| Goodwill and intangible assets | **(24)** | (13) |
| Other assets | **(84)** | (131) |
| Losses carried forward (expiring 2028 to 2033) | **227** | 184 |
| Other | **53** | 21 |
| Net deferred income tax assets | **$ 112** | $ 156 |
| Recorded on the consolidated balance sheets as follows: | | |
| Deferred income tax assets | **$ 299** | $ 316 |
| Deferred income tax liabilities | **(187)** | (160) |
| Net deferred income tax assets | **$ 112** | $ 156 |

### Note 9. Discontinued Operations

During 2013, the Company recorded income related to discontinued operations of $58, which included the settlement of a previously disclosed litigation against Domtar of $48 ($40 net of income taxes) and adjustments resulting in income of $18 associated with the Company’s (excluding Loblaw) previously owned operations.

## Note 10. Basic and Diluted Net Earnings per Common Share from Continuing Operations

| | 2013 | 2012[1] |
|---|---|---|
| Net earnings from continuing operations attributable to shareholders of the Company | **$ 616** | $ 475 |
| Prescribed dividends on preferred shares in share capital | **(44)** | (44) |
| Net earnings from continuing operations available to common shareholders | **$ 572** | $ 431 |
| Impact of GWL equity swaps | | (2) |
| Reduction in net earnings due to dilution at Loblaw | **(3)** | (5) |
| Net earnings from continuing operations available to common shareholders for diluted earnings per share | **$ 569** | $ 424 |
| Weighted average common shares outstanding (in millions) (note 27) | **127.6** | 128.2 |
| Dilutive effect of share-based compensation[2] (in millions) | **0.2** | |
| Dilutive effect of GWL equity swaps[2] (in millions) | | 0.6 |
| Diluted weighted average common shares outstanding (in millions) | **127.8** | 128.8 |
| Basic net earnings per common share from continuing operations ($) | **$ 4.48** | $ 3.36 |
| Diluted net earnings per common share from continuing operations ($) | **$ 4.45** | $ 3.29 |

(1) Certain 2012 figures have been restated (see note 2).
(2) Excluded from the computation of diluted net earnings per common share from continuing operations were 516,557 (2012 – 1,184,840) potentially dilutive instruments, as they were anti-dilutive.

## Note 11. 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**

| | As at | |
|---|---|---|
| | Dec. 31, 2013 | Dec. 31, 2012 |
| Cash | **$ 629** | $ 250 |
| Cash equivalents: | | |
| Bankers' acceptances | **325** | 361 |
| Government treasury bills | **1,712** | 444 |
| Corporate commercial paper | **100** | 425 |
| Government agency securities | **48** | 11 |
| Bank term deposits | **42** | |
| Other | **13** | 98 |
| Cash and cash equivalents | **$ 2,869** | $ 1,589 |

**Short Term Investments**

| | As at | |
|---|---|---|
| | Dec. 31, 2013 | Dec. 31, 2012 |
| Bankers' acceptances | **$ 349** | $ 289 |
| Government treasury bills | **584** | 835 |
| Corporate commercial paper | **230** | 316 |
| Government agency securities | **326** | 667 |
| Other | **1** | 31 |
| Short term investments | **$ 1,490** | $ 2,138 |

**Security Deposits**

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Cash | **$ 147** | $ 135 |
| Government treasury bills and notes[1] | **1,640** | 169 |
| Government agency securities | **4** | 44 |
| Security deposits | **$ 1,791** | $ 348 |

(1) Included in Government treasury bills is $1.6 billion of proceeds from the issuance of senior unsecured notes held in escrow which will be used to partially fund the acquisition of all the outstanding common shares of Shoppers Drug Mart (see note 39).

During 2013, GWL and Loblaw had agreements to cash collateralize certain uncommitted credit facilities up to amounts of $45 (2012 – $45) and $136 (2012 – $133), respectively. As at year end 2013, GWL and Loblaw had $45 (2012 – $45) and $102 (2012 – $97) deposited with major financial institutions, respectively, and classified as security deposits on the consolidated balance sheets.

### Note 12. Accounts Receivable

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

| | As at | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | **Dec. 31, 2013** | | | | Dec. 31, 2012 |
| | **Current** | **> 30 days** | **> 60 days** | **Total** | Current | > 30 days | > 60 days | Total |
| Accounts receivable | **$ 630** | **$ 59** | **$ 47** | **$ 736** | $ 493 | $ 52 | $ 14 | $ 559 |

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

| | **2013** | 2012 |
|---|---|---|
| Allowance, beginning of year | **$ (116)** | $ (119) |
| Net (additions) reversals | **(6)** | 3 |
| Allowance, end of year | **$ (122)** | $ (116) |

Accounts receivable of $43 that were past due as at year end 2013 (2012 – $29) were not classified as impaired as their past due status was reasonably expected to be remedied.

### Note 13. Credit Card Receivables

The components of credit card receivables were as follows:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Gross credit card receivables | **$ 2,585** | $ 2,348 |
| Allowance for credit card receivables | **(47)** | (43) |
| Credit card receivables | **$ 2,538** | $ 2,305 |
| Securitized to Independent Securitization Trusts | | |
| Securitized to *Eagle Credit Card Trust*® | **$ 750** | $ 600 |
| Securitized to Other Independent Securitization Trusts | **$ 605** | $ 905 |

Loblaw, 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 to Independent Securitization Trusts, including *Eagle* and Other Independent Securitization Trusts, from time to time depending on PC Bank's financing requirements.

During 2013, PC Bank securitized to *Eagle* $400 (2012 – nil) and repurchased from *Eagle* $250 (2012 – nil) of co-ownership interests in the securitized receivables. The associated liability of *Eagle* is recorded in long term debt (see note 23).

During 2013, PC Bank repurchased $300 (2012 – nil) of co-ownership interests in the securitized receivables from Other Independent Securitization Trusts. The associated liabilities related to credit card receivables securitized to the Other Independent Securitization Trusts are recorded in short term debt (see note 22). Loblaw has arranged letters of credit on behalf of PC Bank (see note 37). In the event of a major decline in the income flow from, or in the value of, the securitized credit card receivables, the Other Independent Securitization Trusts can draw upon these letters of credit to recover up to a maximum of the amount outstanding on the letters of credit. 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 throughout the year.

The following are continuities of Loblaw's allowances for credit card receivables:

| | **2013** | 2012 |
|---|---|---|
| Allowance, beginning of year | **$ (43)** | $ (37) |
| Provision for losses | **(105)** | (98) |
| Recoveries | **(14)** | (12) |
| Write-offs | **115** | 104 |
| Allowance, end of year | **$ (47)** | $ (43) |

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.

The following is an aging of Loblaw's gross credit card receivables:

| | As at | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | **Dec. 31, 2013** | | | | Dec. 31, 2012 |
| | **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 | **$ 2,416** | **$ 142** | **$ 27** | **$ 2,585** | $ 2,213 | $ 113 | $ 22 | $ 2,348 |

**Note 14. Inventories**

The components of inventories were as follows:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Raw materials and supplies | **$ 56** | $ 50 |
| Finished goods | **2,175** | 2,082 |
| Inventories | **$ 2,231** | $ 2,132 |

For inventories recorded as at year end 2013, Loblaw recorded $16 (2012 – $14) for the write-down of inventories below cost to net realizable value. The write-down was included in cost of inventories sold in the consolidated statements of earnings. There were no reversals of previously recorded write-downs of inventories during 2013 and 2012.

Cost of inventories sold in 2013 included a charge of $10 (2012 – income of $6) related to the fair value adjustment of commodity derivatives at Weston Foods.

### Note 15. Assets Held for Sale

Loblaw holds land and buildings that it intends to dispose of in the next 12 months as assets held for sale. These assets were previously used in Loblaw's Retail segment. There were no impairment and other charges recognized on these properties during 2013 (2012 – $1). Also during 2013, Loblaw recorded a gain of $7 (2012 – $4) from the sale of these assets.

### Note 16. Fixed Assets

The following is a continuity of the cost and accumulated depreciation of fixed assets for the year ended December 31, 2013:

| | Land | Buildings | Equipment and fixtures | Buildings and leasehold improvements | Finance leases - land, buildings, equipment and fixtures | Assets under construction | Total |
|---|---|---|---|---|---|---|---|
| Cost, beginning of year | $ 1,678 | $ 6,795 | $ 6,715 | $ 804 | $ 555 | $ 727 | $ 17,274 |
| Additions | 1 | | 17 | 9 | 62 | 945 | 1,034 |
| Disposals | (2) | (4) | (58) | (7) | (53) | | (124) |
| Transfer from assets held for sale | 1 | | | | | | 1 |
| Transfer (to) from investment properties | (2) | (1) | | | 4 | (5) | (4) |
| Transfer from assets under construction | 30 | 316 | 570 | 54 | | (970) | |
| Business acquisition (note 5) | | | 6 | | | | 6 |
| Foreign exchange | | 8 | 23 | | | 1 | 32 |
| **Cost, end of year** | **$ 1,706** | **$ 7,114** | **$ 7,273** | **$ 860** | **$ 568** | **$ 698** | **$ 18,219** |
| Accumulated depreciation and impairment losses, beginning of year | $ 7 | $ 2,408 | $ 4,689 | $ 442 | $ 269 | $ 7 | $ 7,822 |
| Depreciation | | 193 | 583 | 45 | 44 | | 865 |
| Impairment losses | | 20 | 5 | 24 | 3 | | 52 |
| Reversal of impairment losses | (4) | (71) | (2) | (3) | (3) | | (83) |
| Disposals | (1) | (1) | (49) | (5) | (53) | | (109) |
| Transfer (to) from investment properties | | (1) | | | 1 | | |
| Foreign exchange | | 3 | 14 | | | | 17 |
| **Accumulated depreciation and impairment losses, end of year** | **$ 2** | **$ 2,551** | **$ 5,240** | **$ 503** | **$ 261** | **$ 7** | **$ 8,564** |
| **Carrying amount as at:** | | | | | | | |
| December 31, 2013 | **$ 1,704** | **$ 4,563** | **$ 2,033** | **$ 357** | **$ 307** | **$ 691** | **$ 9,655** |

The following is a continuity of the cost and accumulated depreciation of fixed assets for the year ended December 31, 2012:

| | Land | Buildings | Equipment and fixtures | Buildings and leasehold improvements | Finance leases - land, buildings, equipment and fixtures | Assets under construction | Total |
|---|---|---|---|---|---|---|---|
| Cost, beginning of year | $ 1,686 | $ 6,549 | $ 6,157 | $ 736 | $ 511 | $ 666 | $ 16,305 |
| Additions | | 23 | 36 | 22 | 73 | 1,032 | 1,186 |
| Disposals | (8) | (21) | (104) | (9) | (28) | | (170) |
| Transfer to assets held for sale | (9) | (25) | | | | | (34) |
| Transfer (to) from investment properties | (3) | 1 | | | (1) | | (3) |
| Transfer from assets under construction | 12 | 271 | 633 | 55 | | (971) | |
| Foreign exchange | | (3) | (7) | | | | (10) |
| Cost, end of year | $ 1,678 | $ 6,795 | $ 6,715 | $ 804 | $ 555 | $ 727 | $ 17,274 |
| Accumulated depreciation and impairment losses, beginning of year | $ 9 | $ 2,236 | $ 4,236 | $ 400 | $ 245 | $ 7 | $ 7,133 |
| Depreciation | | 186 | 536 | 47 | 43 | | 812 |
| Impairment losses | 2 | 32 | 7 | 4 | 4 | | 49 |
| Reversal of impairment losses | (3) | (25) | | | | | (28) |
| Disposals | | (9) | (85) | (9) | (24) | | (127) |
| Transfer to assets held for sale | | (15) | | | | | (15) |
| Transfer (to) from investment properties | (1) | 4 | | | 1 | | 4 |
| Foreign exchange | | (1) | (5) | | | | (6) |
| Accumulated depreciation and impairment losses, end of year | $ 7 | $ 2,408 | $ 4,689 | $ 442 | $ 269 | $ 7 | $ 7,822 |
| Carrying amount as at: | | | | | | | |
| December 31, 2012 | $ 1,671 | $ 4,387 | $ 2,026 | $ 362 | $ 286 | $ 720 | $ 9,452 |

***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 year end 2013, the net carrying amount of leased land and buildings was $274 (2012 – $259) and the net carrying amount of leased equipment and fixtures was $33 (2012 – $27).

***Assets under Construction*** The cost of additions to properties under construction for 2013 was $945 (2012 – $1,032). Included in this amount were capitalized borrowing costs of $2 (2012 – $1) with a weighted average capitalization rate of 6.4% (2012 – 6.4%).

***Security and Assets Pledged*** As at year end 2013, Loblaw had fixed assets with a carrying amount of $187 (2012 – $191) which were encumbered by mortgages of $87 (2012 – $93).

***Fixed Asset Commitments*** As at year end 2013, the Company had entered into commitments of $87 (2012 – $76) for the construction, expansion and renovation of buildings and the purchase of real property.

***Impairment Reversals and Losses*** In 2013, Loblaw recorded $83 (2012 – $28) of impairment reversals on fixed assets in respect of 26 CGUs (2012 – 11 CGUs) in its Retail segment. Impairment reversals are recorded where the recoverable amount of the retail location exceeds its carrying amount. Approximately 92% (2012 – 55%) of CGUs with impairment reversals had fair value less costs to sell which were $75 (2012 – $15) greater than their carrying values. The remaining 8% (2012 – 45%) of CGUs with impairment reversals had value in use which were $8 (2012 – $13) greater than their carrying values.

In 2013, Loblaw recorded $52 (2012 – $49) of impairment losses on fixed assets in respect of 21 CGUs (2012 – 17 CGUs) in its Retail segment. 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 10% (2012 – 35%) of impaired CGUs had carrying values which were $6 (2012 – $26) greater than their fair value less costs to sell. The remaining 90% (2012 – 65%) of impaired CGUs had carrying values which were $46 (2012 – $23) greater than their value in use.

When determining the value in use of a retail location, Loblaw 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 asset 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 are consistent with strategic plans presented to Loblaw'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 the end of 2013 (2012 – 8.0% to 8.5%).

In 2013, Weston Foods recorded accelerated depreciation of $4 (2012 – $4) related to restructuring activities.

**Note 17. Investment Properties**

The following are continuities of investment properties:

| | **2013** | 2012 |
|---|---|---|
| Cost, beginning of year | **$ 169** | $ 158 |
| Additions | **1** | |
| Disposals | **(2)** | |
| Transfer from fixed assets | **4** | 3 |
| Transfer from assets held for sale | | 8 |
| **Cost, end of year** | **$ 172** | $ 169 |
| Accumulated depreciation and impairment losses, beginning of year | **$ 69** | $ 76 |
| Disposals | **(1)** | |
| Depreciation | **2** | 2 |
| Impairment losses | | 1 |
| Reversal of impairment losses | **(1)** | (4) |
| Transfer to fixed assets | | (4) |
| Transfer from (to) assets held for sale | **4** | (2) |
| **Accumulated depreciation, end of year** | **$ 73** | $ 69 |

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Carrying amount | **$ 99** | $ 100 |
| Fair value | **$ 144** | $ 125 |

During 2013, Loblaw recognized in operating income $4 (2012 – $5) of rental income and incurred direct operating costs of $3 (2012 – $3) related to its investment properties. In addition, Loblaw recognized direct operating costs of $1 (2012 – $1) 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 Loblaw's investment properties. For the other investment properties, Loblaw determined the fair value by relying on comparable market information and the independent manager of Loblaw's investment properties.

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. As at year end 2013, the pre-tax discount rates used in the valuations for investment properties ranged from 6.50% to 9.75% (2012 – 6.0% to 9.75%) and the terminal capitalization rates ranged from 5.75% to 8.75% (2012 – 5.75% to 8.75%).

In 2013, Loblaw recorded reversals of impairment losses on investment properties of $1 (2012 – $4) and recorded no impairment losses on investment properties (2012 – $1) in operating income.

### Note 18. Goodwill and Intangible Assets

The following is a continuity of the cost and accumulated amortization of goodwill and intangible assets for the year ended December 31, 2013:

| | Indefinite Life Intangible Assets and Goodwill | | Definite Life Intangible Assets | | | |
|---|---|---|---|---|---|---|
| | Goodwill | Trademarks and brand names | Internally generated intangible assets | Trademarks and brand names | Other intangible assets | Total |
| Cost, beginning of year | $ 2,417 | $ 62 | $ 20 | $ 23 | $ 176 | $ 2,698 |
| Additions | | 9 | | | 3 | 12 |
| Business acquisition (note 5) | | | | | 3 | 3 |
| Write-off cost of fully amortized assets | | | | | (8) | (8) |
| Impact of foreign currency translation | 10 | | | | 5 | 15 |
| **Cost, end of year** | $ 2,427 | $ 71 | $ 20 | $ 23 | $ 179 | $ 2,720 |
| Accumulated amortization and impairment losses, beginning of year | $ 1,062 | | $ 14 | $ 5 | $ 46 | $ 1,127 |
| Amortization | | | 5 | | 16 | 21 |
| Write-off amortization of fully amortized assets | | | | | (8) | (8) |
| **Accumulated amortization and impairment losses, end of year** | $ 1,062 | | $ 19 | $ 5 | $ 54 | $ 1,140 |
| **Carrying amount as at:** | | | | | | |
| December 31, 2013 | $ 1,365 | $ 71 | $ 1 | $ 18 | $ 125 | $ 1,580 |

The following is a continuity of the cost and accumulated amortization of goodwill and intangible assets for the year ended December 31, 2012:

| | Indefinite Life Intangible Assets and Goodwill | | Definite Life Intangible Assets | | | |
|---|---|---|---|---|---|---|
| | Goodwill | Trademarks and brand names | Internally generated intangible assets | Trademarks and brand names | Other intangible assets | Total |
| Cost, beginning of year | $ 2,425 | $ 51 | $ 20 | $ 23 | $ 146 | $ 2,665 |
| Additions | | 11 | | | 32 | 43 |
| Write-off cost of fully amortized assets | | | | | (4) | (4) |
| Reclassification | (5) | | | | 5 | |
| Impact of foreign currency translation | (3) | | | | (3) | (6) |
| Cost, end of year | $ 2,417 | $ 62 | $ 20 | $ 23 | $ 176 | $ 2,698 |
| Accumulated amortization and impairment losses, beginning of year | $ 1,062 | | $ 8 | $ 4 | $ 36 | $ 1,110 |
| Amortization | | | 6 | 1 | 14 | 21 |
| Write-off amortization of fully amortized assets | | | | | (4) | (4) |
| Accumulated amortization and impairment losses, end of year | $ 1,062 | | $ 14 | $ 5 | $ 46 | $ 1,127 |
| Carrying amount as at: | | | | | | |
| December 31, 2012 | $ 1,355 | $ 62 | $ 6 | $ 18 | $ 130 | $ 1,571 |

During 2013, Loblaw had intangible asset additions of $12 (2012 – $43). The additions in 2012 included $31 related to the purchase of prescription files from 106 Zellers Inc. stores, which were classified as definite life intangible assets.

**Goodwill and Indefinite Life Intangible Assets** For purposes of goodwill impairment testing, the Company's CGUs were grouped at the lowest level at which goodwill was monitored for internal management purposes. The carrying amount of goodwill attributed to each CGU grouping was as follows:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Fresh and Frozen – Weston Foods | **$ 262** | $ 252 |
| Quebec region – Loblaw | **700** | 700 |
| T&T Supermarket Inc. | **129** | 129 |
| Other | **274** | 274 |
| Carrying amount of goodwill | **$ 1,365** | $ 1,355 |

Indefinite life intangible assets recorded by Loblaw are comprised of trademark, brand names and import purchase quota. The trademark and brand names are a result of Loblaw's acquisition of T&T Supermarket Inc. Loblaw expects to renew the registration of the trademark, brand names and import purchase quota at each expiry date indefinitely, and expects these assets to generate economic benefit to perpetuity. As such, Loblaw assessed these intangibles to have an indefinite useful life.

The Company completed its 2013 and 2012 annual goodwill and indefinite life intangible assets impairment tests 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 considered to be Level 3 in the fair value hierarchy.

The weighted average cost of capital was determined to be in the range of 6.5% to 7.0% (2012 – 6.5% to 7.0%) and was based on a risk-free rate, equity risk premium adjusted for betas of comparable publicly traded companies, an unsystematic risk premium, after-tax cost of debt based on corporate bond yields and capital structure of the Company.

Cash flow projections were 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. As at year end 2013, the after-tax discount rate used in the recoverable amount calculations was approximately 9.5% (2012 – 9.5%). The pre-tax discount rates ranged from 12.8% to 13.0% (2012 – 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 an estimated long term growth rate of 2.0% (2012 – 0.9% to 2.0%). The budgeted adjusted EBITDA growth is based on the Company's five year strategic plan approved by GWL's and Loblaw's Boards.

**Definite Life Intangible Assets** The Company completed its assessments of impairment indicators for definite life intangible assets and concluded that there were no indications of impairment during 2013 and 2012.

## Note 19. Interest in Other Entities

### Consolidated Structured Entities

***Independent Funding Trusts*** Certain independent franchisees of Loblaw 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. Loblaw provides a standby letter of credit for the benefit of the independent funding trusts (see note 37).

***Eagle Credit Card Trust***® Loblaw, 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.

***Share-Based Compensation Trusts*** During 2013, GWL and Loblaw established trusts for each of the RSU and PSU plans to facilitate the purchase of shares for future settlement upon vesting. Each company is the sponsor of their respective trusts and has assigned Computershare as the trustee. GWL and Loblaw fund the purchase of shares for settlement and earn 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. Loblaw arranged standby letters of credit for the benefit of these trusts (see note 37).

## Note 20. Other Assets

The components of other assets were as follows:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Fair value of equity forward (note 34) | **$ 524** | $ 483 |
| Sundry investments and other receivables | **136** | 159 |
| Fair value of cross currency swaps (note 34) | | 98 |
| Net accrued benefit plan asset (note 30) | **138** | |
| Other | **55** | 41 |
| Other assets | **$ 853** | $ 781 |

## Note 21. Provisions

Provisions consist primarily of amounts recorded in respect of restructuring, self-insurance, commodity taxes, environmental and decommissioning liabilities, onerous lease arrangements and a MEPP withdrawal liability.

The following are continuities relating to the Company's provisions:

| | **2013** | 2012 |
|---|---|---|
| Provisions, beginning of year | **$ 217** | $ 161 |
| Additions | **48** | 107 |
| Payments | **(53)** | (41) |
| Reversals | **(15)** | (9) |
| Impact of foreign currency translation | **4** | (1) |
| Provisions, end of year | **$ 201** | $ 217 |

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Carrying amount of provisions recorded in: | | |
| Current provisions | **$ 120** | $ 123 |
| Non-current provisions | **81** | 94 |
| Provisions | **$ 201** | $ 217 |

The Company's accrued insurance liabilities were $70 (2012 – $73), of which $40 (2012 – $48) was included in non-current provisions and $30 (2012 – $25) in current provisions. Included in total accrued insurance liabilities were $34 (2012 – $37) of U.S. workers' compensation liabilities. The related cost and accrued workers' compensation liabilities are based on actuarial valuations which are dependent on assumptions determined by management. The discount rate used in determining the 2013 workers' compensation cost and liability was 2.00% (2012 – 3.50%). The total workers' compensation liability is equal to the ultimate actuarial loss estimate less any actual losses paid to date. Any change in the workers' compensation liability is recognized immediately in operating income.

The U.S. workers' compensation cost associated with the worker's compensation liabilities was $4 in 2013 (2012 – $5).

During 2013, Loblaw announced the reduction of approximately 275 store-support positions. Loblaw recorded a charge of $32 in operating income, reflecting the costs of the reductions. During 2012, Loblaw reduced a number of head office and administrative positions, affecting approximately 700 jobs and recorded a charge of $61 in operating income to reflect the costs of these reductions, which included $6 recorded in other liabilities. As at year end 2013, $39 (2012 – $45) was included in provisions relating to these restructuring initiatives.

During 2012, Weston Foods withdrew from one of the U.S. MEPPs in which it participated. As a result, the Company was subject to and paid a withdrawal liability of $34. Also during 2012, another participating employer withdrew from the plan and a mass withdrawal was triggered. As a result of the mass withdrawal, the Company is subject to an incremental withdrawal liability. The total liability included in current provisions relating to the Company's mass withdrawal liability as at year end 2013 is $22, $5 of which was recorded in 2013 (2012 – $17).

**Note 22. Short Term Debt**

The components of short term debt were as follows:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| Other Independent Securitization Trusts[1] (note 13) | **$ 605** | $ 905 |
| Series B Debentures[2] | **455** | 414 |
| Short term debt | **$ 1,060** | $ 1,319 |

(1) Balances relate to the credit card receivables securitized to the Other Independent Securitization Trusts, excluding *Eagle* which is included in long term debt (see note 23). During 2013, PC Bank did not securitize any credit card receivables (2012 – nil).

During 2013, PC Bank repurchased $300 (2012 – nil) of co-ownership interests in the securitized receivables from Other Independent Securitization Trusts, and recorded a corresponding decrease to short term debt.

Also during 2013, PC Bank amended and extended the maturity date for one of its Other Independent Securitization Trust agreements from the third quarter of 2014 to the third quarter of 2015, with no material impact to other terms and conditions.

In addition to PC Bank's securitized credit card receivables, the Other Independent Securitization Trusts' recourse is limited to standby letters of credit arranged by Loblaw (see note 37).

Subsequent to the end of 2013, 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.

(2) Series B Debentures issued by GWL are due on demand, and pay a current weighted average interest rate of 1.78% (2012 – 1.79%). The Series A, 7.00% (see note 23) and Series B Debentures are secured by a pledge of 9.6 million Loblaw common shares.

## Note 23. Long Term Debt

The components of long term debt were as follows:

| | As at Dec. 31, 2013 | As at Dec. 31, 2012 |
|---|---|---|
| **George Weston Limited** | | |
| Debentures | | |
| Series A, 7.00%, due 2031[i] | **$ 466** | $ 466 |
| Notes | | |
| 5.05%, due 2014 | **200** | 200 |
| 3.78%, due 2016 | **350** | 350 |
| 7.10%, due 2032 | **150** | 150 |
| 6.69%, due 2033 | **100** | 100 |
| **Loblaw Companies Limited** | | |
| Notes | | |
| 5.40%, due 2013[ii] | | 200 |
| 6.00%, due 2014 | **100** | 100 |
| 4.85%, due 2014 | **350** | 350 |
| 7.10%, due 2016 | **300** | 300 |
| 5.22%, due 2020 | **350** | 350 |
| 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 | **(67)** | (76) |
| 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 |
| Senior unsecured notes[iii] | | |
| 3.75%, due 2019 | **800** | |
| 4.86%, due 2023 | **800** | |
| U.S. Private placement notes[iv] | | |
| 6.48%, due 2013 (U.S. $150) | | 150 |
| 6.86%, due 2015 (U.S. $150) | | 150 |
| Long term debt secured by mortgage | | |
| 5.49%, due 2018 (note 16) | **83** | 86 |
| Guaranteed investment certificates[v] | | |
| due 2014 – 2018 (0.85% – 3.78%) | **430** | 303 |
| Independent securitization trusts[vi] | | |
| *Eagle*, 2.88%, due 2013 | | 250 |
| *Eagle*, 3.58%, due 2015 | **350** | 350 |
| *Eagle*, 2.91%, due 2018 | **400** | |
| Independent funding trusts[vii] | **475** | 459 |
| Finance lease obligations (note 33) | **388** | 366 |
| Choice Properties (note 6) | | |
| Series A 3.55%, due 2018 | **400** | |
| Series B 4.90%, due 2023 | **200** | |
| Transaction costs and other | **(12)** | (2) |
| Total long term debt | **8,944** | 6,933 |
| Less – amount due within one year | **(1,208)** | (672) |
| Long term debt | **$ 7,736** | $ 6,261 |

The schedule of repayment of long term debt, based on maturity, is as follows: 2014 – $1,208; 2015 – $408; 2016 – $792; 2017 – $137; 2018 – $1,022 thereafter – $5,461. See note 34 for the fair value of long term debt.

(i) The Series A, 7.00% and Series B Debentures (see note 22) are secured by a pledge of 9.6 million Loblaw common shares.

(ii) During 2013, Loblaw's $200 5.40% medium term note ("MTN") due November 20, 2013 matured and was repaid.

(iii) During 2013, Loblaw issued $1.6 billion aggregate principal amount of senior unsecured notes, consisting of $800 of Senior Unsecured Notes, Series 2019 due March 12, 2019 (the "Series 2019 Notes") and $800 of Senior Unsecured Notes, Series 2023 due September 12, 2023 (the "Series 2023 Notes"). The Series 2019 Notes carry a coupon of 3.75% per annum and were issued at par and the Series 2023 Notes carry a coupon of 4.86% per annum and were issued at par. The net proceeds from the offering have been placed in escrow and will be released upon satisfaction of the applicable release conditions in connection with Loblaw's agreement to acquire all of the outstanding common shares of Shoppers Drug Mart (see note 39).

(iv) During 2013, Loblaw settled its U.S. $300 USPP notes and related cross currency swaps (see note 34). Loblaw incurred approximately $18 of early-settlement costs related to the settlement of the USPP note due May 29, 2015, which was recorded in net interest expense and other financing charges (see note 7).

(v) The following table summarizes PC Bank's Guaranteed Investment Certificates ("GICs") activity, before commissions:

| | **2013** | 2012 |
|---|---|---|
| Balance, beginning of year | **$ 303** | $ 276 |
| GICs issued | **167** | 76 |
| GICs matured | **(40)** | (49) |
| Balance, end of year | **$ 430** | $ 303 |

As at year end 2013, $52 (2012 – $36) in GICs were recorded as long term debt due within one year.

(vi) The notes issued by *Eagle* are MTNs, which are collateralized by PC Bank's credit card receivables (see note 13). During 2013, *Eagle* issued $400 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 of senior and subordinated term notes which matured on December 17, 2013.

(vii) As at year end 2013, the independent funding trusts had drawn $475 (2012 – $459) from the revolving committed credit facility that is the source of funding to the independent funding trusts. The revolving committed credit facility matures on May 6, 2014 and has been recorded as long term debt due within one year.

Loblaw 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 loans outstanding. As at year end 2013, Loblaw had provided a letter of credit in the amount of $48 (2012 – $48) (see note 37).

**Committed Facilities** During 2013, Loblaw increased the $800 committed credit facility amount to $1 billion, subject to the successful close of the Shoppers Drug Mart transaction, and extended the term to December 31, 2018. In connection with the Choice Properties IPO, Loblaw amended its committed credit facility agreement to incorporate certain adjustments to exclude the impact of Choice Properties from its covenant calculations (see note 29). As at year end 2013 and 2012, Loblaw had not drawn on its committed credit facility.

Also during 2013, Choice Properties entered into an agreement for a $500, 5-year senior unsecured committed credit facility provided by a syndicate of lenders. This facility contains certain financial covenants (see note 29) and accrues interest based on short term floating interest rates. As at year end 2013, Choice Properties had not drawn on its committed credit facility.

Subsequent to year end 2013, Choice Properties issued $250 principal amount of Series C senior unsecured debentures with a 7-year term and a coupon rate of 3.498% per annum and $200 principal amount of Series D senior unsecured debentures with a 10-year term and a coupon rate of 4.293% per annum, under its Short Form Base Shelf Prospectus.

### Note 24. Trust Unit Liability

As at year end 2013, 46,006,419 Choice Properties Units were held by the public. As at year end 2013, the fair value of the Trust Unit liability was $478, resulting in a fair value loss of $18 (see note 7).

### Note 25. Other Liabilities

The components of other liabilities were as follows:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012[1] |
| Net defined benefit plan obligation (note 30) | **$ 292** | $ 594 |
| Other long term employee benefit obligation | **117** | 127 |
| Deferred vendor allowances | **16** | 24 |
| Share-based compensation liability (note 31) | **1** | 36 |
| Other | **192** | 162 |
| Other liabilities | **$ 618** | $ 943 |

(1) Certain 2012 figures have been restated (see note 2).

### Note 26. Capital Securities ($ except where otherwise indicated)

Loblaw has 9.0 million 5.95% non-voting Second Preferred Shares, Series A, outstanding (authorized – 12.0 million), 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, 2013, 2014 and 2015, Loblaw may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares at $25.75, $25.50 and $25.00 per share, respectively. On and after July 31, 2013, Loblaw may, at its option, convert these preferred shares into that number of common shares of Loblaw 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 per share 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 Loblaw determined by dividing $25.00 per share, together with accrued and unpaid dividends to but excluding the date of conversion, by the greater of $2.00 per share and 95% of the then current market price of the common shares. This option is subject to Loblaw's right to redeem the preferred shares for cash or arrange for their sale to substitute purchasers.

Dividends on capital securities are presented in net interest expense and other financing charges in the consolidated statements of earnings (see note 7).

**Note 27**. **Share Capital ($ except where otherwise indicated)**

The components of share capital were as follows:

| ($ millions) | As at Dec. 31, 2013 | | Dec. 31, 2012 | |
|---|---|---|---|---|
| Common share capital | **$** | **155** | $ | 136 |
| Preferred shares, Series I | | **228** | | 228 |
| Preferred shares, Series III | | **196** | | 196 |
| Preferred shares, Series IV | | **197** | | 197 |
| Preferred shares, Series V | | **196** | | 196 |
| Share capital | **$** | **972** | $ | 953 |

**Common Share Capital (authorized – unlimited)** The following table summarizes the activity in the Company's common shares issued and outstanding for the years ended December 31, 2013 and December 31, 2012:

| | **2013** | | | 2012 | | |
|---|---|---|---|---|---|---|
| ($ millions) | **Number of Common Shares** | | **Common Share Capital** | Number of Common Shares | | Common Share Capital |
| Issued and outstanding, beginning of year | **128,221,841** | **$** | **136** | 128,188,843 | $ | 133 |
| Issued for settlement of stock options (note 31) | **257,569** | **$** | **20** | 42,210 | $ | 3 |
| Purchased for cancellation | **(580,000)** | **$** | **(1)** | (9,212) | | |
| Issued and outstanding, end of year | **127,899,410** | **$** | **155** | 128,221,841 | $ | 136 |
| Shares held in trust (note 31) | **(218,726)** | | | | | |
| Issued and outstanding net of shares held in trust, end of year | **127,680,684** | **$** | **155** | 128,221,841 | $ | 136 |
| Weighted average outstanding, net of shares held in trust | **127,580,415** | | | 128,189,901 | | |

**Preferred Shares, Series I (authorized – 10.0 million)** GWL has 9.4 million 5.80% non-voting Preferred Shares, Series I outstanding, with a face value of $235 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.45 per share per annum which will, if declared, be payable quarterly. GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**Preferred Shares, Series III (authorized – 10.0 million)** GWL has 8.0 million 5.20% non-voting Preferred Shares, Series III outstanding, with a face value of $200 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.30 per share per annum which will, if declared, be payable quarterly. GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares as follows:

Until June 30, 2014 at $25.25 per share, together with all accrued and unpaid dividends to the redemption date; and
On or after July 1, 2014 at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**Preferred Shares, Series IV (authorized – 8.0 million)** GWL has 8.0 million 5.20% non-voting Preferred Shares, Series IV outstanding, with a face value of $200 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.30 per share per annum which will, if declared, be payable quarterly. GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares as follows:

Until September 30, 2014 at $25.25 per share, together with all accrued and unpaid dividends to the redemption date; and
On or after October 1, 2014 at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**Preferred Shares, Series V (authorized – 8.0 million)** GWL has 8.0 million 4.75% non-voting Preferred Shares, Series V outstanding, with a face value of $200 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.1875 per share per annum which will, if declared, be payable quarterly. GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares as follows:

Until June 30, 2014 at $25.50 per share, together with all accrued and unpaid dividends to the redemption date;
On or after July 1, 2014 at $25.25 per share, together with all accrued and unpaid dividends to the redemption date; and
On or after July 1, 2015 at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**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. In the second quarter of 2013, the Board raised the quarterly common share dividend by $0.035 to $0.415 per share, following a $0.02 increase in the fourth quarter of 2012 to $0.38 per share. The Board declared dividends as follows:

| ($) | | | **2013** | | 2012 |
|---|---|---|---|---|---|
| Dividends declared per share[(1)] | – Common share | **$** | **1.625** | $ | 1.460 |
| | – Preferred share: | | | | |
| | Series I | **$** | **1.45** | $ | 1.45 |
| | Series III | **$** | **1.30** | $ | 1.30 |
| | Series IV | **$** | **1.30** | $ | 1.30 |
| | Series V | **$** | **1.19** | $ | 1.19 |

(1) Dividends declared on common shares and Preferred Shares, Series III, Series IV and Series V were paid on January 1, 2014. Dividends declared on Preferred Shares, Series I were paid on December 15, 2013.

The following table summarizes the Company's cash dividends declared subsequent to year end 2013:

| ($) | | | |
|---|---|---|---|
| Dividends declared per share[1] | – Common share | $ | **0.415** |
| | – Preferred share: | | |
| | Series I | $ | **0.36** |
| | Series III | $ | **0.32** |
| | Series IV | $ | **0.32** |
| | Series V | $ | **0.30** |

(1) Dividends declared on common shares and Preferred Shares, Series III, Series IV and Series V are payable on April 1, 2014. Dividends declared on Preferred Shares, Series I are payable on March 15, 2014.

**Normal Course Issuer Bid ("NCIB") Program** In 2013, GWL renewed its NCIB program to purchase on the TSX or enter into equity derivative contracts to purchase up to 6,382,723 of its common shares, representing approximately 5% of the common shares outstanding. In accordance with the rules and regulations of the TSX, any purchases must be at the then market price of such shares.

In 2013, GWL purchased 800,000 common shares under its NCIB for cash consideration of $57 million, resulting in a charge of $56 million to retained earnings and a reduction of $1 million in share capital. Of the 800,000 common shares purchased, 580,000 common shares were cancelled and the remaining 220,000 common shares were placed into trusts for future settlement of GWL's RSU and PSU obligations (see note 31).

During 2012, GWL purchased for cancellation 9,212 of its common shares for $1 million, resulting in a charge of $1 million to retained earnings and a nominal reduction in share capital.

## Note 28. Subsidiary Capital Transactions

During 2013, Loblaw issued 2,167,593 (2012 – 718,544) of its common shares in connection with its share-based compensation plans including shares settled from the trusts established for the RSU and PSU plans. As a result, contributed surplus increased by $25 (2012 – $8).

During 2013, Loblaw purchased under its NCIB 2,603,500 (2012 – 423,705) of its common shares. As a result, contributed surplus decreased by $36 (2012 – $4).

## Note 29. 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 program, 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 expenditures 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.

As at year end 2013 and 2012, the items that the Company includes in its definition of capital were as follows:

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012[1] |
| Short term debt | **$ 1,060** | $ 1,319 |
| Long term debt due within one year | **1,208** | 672 |
| Long term debt[2] | **7,736** | 6,261 |
| Certain other liabilities | **39** | 39 |
| Fair value of financial derivatives related to the above debt | **(524)** | (440) |
| Total debt | **$ 9,519** | $ 7,851 |
| Capital securities | **224** | 223 |
| Equity attributable to shareholders of the Company | **6,325** | 5,693 |
| Total capital under management | **$ 16,068** | $ 13,767 |

(1) Certain 2012 figures have been restated (see note 2).
(2) Includes $1.6 billion aggregate principal amount of senior unsecured notes issued under Loblaw's $2.5 billion Short Form Base Shelf Prospectus mentioned below. The net proceeds from the offering were placed in escrow and classified as security deposits in the Company's consolidated financial statements (see note 11).

In 2013, GWL filed a Short Form Base Shelf Prospectus allowing for the issuance of up to $1 billion of unsecured debentures and/or preferred shares over a 25-month period subject to the availability of funding in capital markets.

In 2013, Loblaw amended its Short Form Base Shelf Prospectus dated December 21, 2012 to increase the amount issuable under the prospectus to $2.5 billion from $1 billion.

In 2013, *Eagle* filed a Short Form Base Shelf Prospectus which allows for the potential issuance of up to $1.5 billion of notes over a 25-month period.

In 2013, Choice Properties filed a Short Form Base Shelf Prospectus allowing for the issuance of up to $2 billion of Units and debt securities over a 25-month period subject to the availability of funding in capital markets.

**Covenants and Regulatory Requirements** Loblaw is subject to certain key financial and non-financial covenants under its existing committed credit facility, the $3.5 billion 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 Loblaw on a quarterly basis to ensure compliance. During 2013, in connection with the Choice Properties IPO, Loblaw amended its committed credit facility agreement to incorporate certain adjustments to exclude the impact of Choice Properties from its covenant calculations. During and as at year end 2013, Loblaw was in compliance with each of the covenants under these agreements.

Choice Properties has certain key financial and non-financial covenants under its Debentures and committed credit facility which include debt service ratios and leverage ratios. These ratios are measured by Choice Properties on a quarterly basis to ensure compliance. During and as at year end 2013, Choice Properties was in compliance with each of the covenants under these agreements.

Loblaw 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 is subject to the Basel III regulatory capital management framework which includes a common equity Tier 1 capital ratio of 3.5%, a Tier 1 capital ratio of 4.5% and a total capital ratio of 8%. In addition to the regulatory capital ratios requirement, financial institutions are expected to meet an assets to capital multiple test. PC Bank has met all applicable capital requirements and the assets to capital multiple test as at year end 2013. During 2012, PC Bank was subject to the Basel II regulatory capital management framework and met all applicable capital requirements as at year end 2012.

In addition, the Company has wholly owned subsidiaries that engage in insurance related activities. These subsidiaries each exceeded the minimum regulatory capital and surplus requirements as at year end 2013.

## Note 30. Post-Employment and Other Long Term Employee Benefits

**Post-Employment 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.

GWL's and Loblaw's Pension Committees ("the Committees") oversee the Company's pension plans. The Committees are responsible for assisting the GWL and Loblaw Boards in fulfilling its general oversight responsibilities for the plans. The Committees assist the Boards 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 MEPPs, 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 2014 to its defined benefit and defined contribution plans and the MEPPs in which it participates as well as make 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.

**(i) 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:

| | As at | | | |
|---|---|---|---|---|
| | **Dec. 31, 2013** | | Dec. 31, 2012[1] | |
| | **Defined Benefit Pension Plans** | **Other Defined Benefit Plans** | Defined Benefit Pension Plans | Other Defined Benefit Plans |
| Present value of funded obligations | **$ (1,903)** | | $ (2,066) | |
| Fair value of plan assets | **2,044** | | 1,847 | |
| Status of funded surpluses (obligations) | **$ 141** | | $ (219) | |
| Present value of unfunded obligations | **(114)** | **$ (174)** | (119) | $ (253) |
| Total funded status of surpluses (obligations) | **$ 27** | **$ (174)** | $ (338) | $ (253) |
| Liability arising from minimum funding requirement for past service | **(7)** | | (3) | |
| **Total net defined benefit plan surplus (obligation)** | **$ 20** | **$ (174)** | $ (341) | $ (253) |
| **Recorded on the consolidated balance sheets as follows:** | | | | |
| Other assets (note 20) | **$ 138** | | | |
| Other liabilities (note 25) | **$ (118)** | **$ (174)** | $ (341) | $ (253) |

(1) Certain 2012 figures have been restated (see note 2).

The following are the continuities of the fair value of plan assets and the present value of the defined benefit plan obligations:

| | 2013 | | | 2012[1] | | |
|---|---|---|---|---|---|---|
| | **Defined Benefit Pension Plans** | **Other Defined Benefit Plans** | **Total** | Defined Benefit Pension Plans | Other Defined Benefit Plans | Total |
| **Changes in the fair value of plan assets** | | | | | | |
| Fair value, beginning of year | **$ 1,847** | | **$ 1,847** | $ 1,621 | | $ 1,621 |
| Employer contributions | **118** | | **118** | 176 | | 176 |
| Employee contributions | **3** | | **3** | 3 | | 3 |
| Benefits paid | **(105)** | | **(105)** | (113) | | (113) |
| Interest income | **74** | | **74** | 70 | | 70 |
| Actuarial gains in other comprehensive income (loss) | **109** | | **109** | 96 | | 96 |
| Other | **(2)** | | **(2)** | (6) | | (6) |
| Fair value, end of year | **$ 2,044** | | **$ 2,044** | $ 1,847 | | $ 1,847 |
| **Changes in the present value of the defined benefit plan obligations** | | | | | | |
| Balance, beginning of year | **$ 2,185** | **$ 253** | **$ 2,438** | $ 2,059 | $ 235 | $ 2,294 |
| Current service cost | **56** | **9** | **65** | 58 | 15 | 73 |
| Interest cost | **86** | **9** | **95** | 88 | 10 | 98 |
| Benefits paid | **(111)** | **(7)** | **(118)** | (120) | (7) | (127) |
| Employee contributions | **3** | | **3** | 3 | | 3 |
| Actuarial (gains) losses in other comprehensive income (loss) | **(182)** | **(60)** | **(242)** | 92 | 9 | 101 |
| Plan amendments[2] | **(28)** | **(23)** | **(51)** | | (9) | (9) |
| Contractual termination benefits[3] | **2** | | **2** | 5 | | 5 |
| Special termination benefits[3] | | | | 3 | | 3 |
| Other | **6** | **(7)** | **(1)** | (3) | | (3) |
| Balance, end of year | **$ 2,017** | **$ 174** | **$ 2,191** | $ 2,185 | $ 253 | $ 2,438 |

(1) Certain 2012 figures have been restated (see note 2).
(2) Relates to the 2013 announced amendments to certain of the Company's defined benefit plans impacting certain employees retiring after January 1, 2015 and the elimination of certain post-retirement benefits for employees of one of the Company's other defined benefit plans in 2012.
(3) Contractual and special termination benefits include $2 (2012 – $6) related to the reduction of head office and administrative positions at Loblaw (see note 21).

For the year ended 2013, the actual return on plan assets was $183 (2012 – $166).

The net defined benefit obligation can be allocated to the plans' participants as follows:

- Active plan participants – 42% (2012 – 44%)
- Deferred plan participants – 12% (2012 – 12%)
- Retirees – 46% (2012 – 44%)

During 2014, the Company expects to contribute approximately $54 (2013 – contributed $118) 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:

| | 2013 | | | 2012[1] | | |
|---|---|---|---|---|---|---|
| | **Defined Benefit Pension Plans** | **Other Defined Benefit Plans** | **Total** | Defined Benefit Pension Plans | Other Defined Benefit Plans | Total |
| Current service cost | **$ 56** | **$ 9** | **$ 65** | $ 58 | $ 15 | $ 73 |
| Interest cost on net defined benefit plan obligations | **12** | **9** | **21** | 18 | 10 | 28 |
| Contractual and special termination benefits[2] | **2** | | **2** | 8 | | 8 |
| Past service costs[3] | **(28)** | **(23)** | **(51)** | | (9) | (9) |
| Other | **8** | **(3)** | **5** | 2 | | 2 |
| **Net post-employment defined benefit costs** | **$ 50** | **$ (8)** | **$ 42** | $ 86 | $ 16 | $ 102 |

(1) Certain 2012 figures have been restated (see note 2).
(2) Includes $2 (2012 – $6) of contractual and special termination benefits related to the reduction of head office and administrative positions at Loblaw (see note 21).
(3) Relates to the 2013 announced amendments to certain of the Company's defined benefit plans impacting certain employees retiring after January 1, 2015 and the elimination of certain post-retirement benefits for employees of one of the Company's other defined benefit plans in 2012.

The actuarial (gains) losses recognized in other comprehensive income (loss) for defined benefit plans was as follows:

| | 2013 | | | 2012[1] | | |
|---|---|---|---|---|---|---|
| | **Defined Benefit Pension Plans** | **Other Defined Benefit Plans** | **Total** | Defined Benefit Pension Plans | Other Defined Benefit Plans | Total |
| Return on plan assets excluding amounts included in interest income | **$ (109)** | | **$ (109)** | $ (96) | | $ (96) |
| Experience adjustments | **(12)** | **$ (48)** | **(60)** | 5 | $ (1) | 4 |
| Actuarial losses from change in demographic assumptions | **81** | **4** | **85** | | 10 | 10 |
| Actuarial (gains) losses from change in financial assumptions | **(251)** | **(16)** | **(267)** | 87 | | 87 |
| Change in liability arising from minimum funding requirements for past service | **4** | | **4** | 3 | | 3 |
| Total net actuarial (gains) losses recognized in other comprehensive income (loss) before income taxes | **$ (287)** | **$ (60)** | **$ (347)** | $ (1) | $ 9 | $ 8 |
| Income tax expense (recovery) on actuarial (gains) losses (note 8) | **77** | **16** | **93** | | (2) | (2) |
| Actuarial (gains) losses net of income tax expense (recovery) | **$ (210)** | **$ (44)** | **$ (254)** | $ (1) | $ 7 | $ 6 |

(1) Certain 2012 figures have been restated (see note 2).

The cumulative actuarial losses (gains) before income taxes recognized in equity for the Company's defined benefit plans were as follows:

| | | 2013 | | | | 2012[(1)] |
|---|---|---|---|---|---|---|
| | **Defined Benefit Pension Plans** | **Other Defined Benefit Plans** | **Total** | Defined Benefit Pension Plans | Other Defined Benefit Plans | Total |
| Cumulative amount, beginning of year | **$ 427** | **$ 34** | **$ 461** | $ 428 | $ 25 | $ 453 |
| Net actuarial (gains) losses recognized in the year before income taxes | **(287)** | **(60)** | **(347)** | (1) | 9 | 8 |
| Cumulative amount, end of year | **$ 140** | **$ (26)** | **$ 114** | $ 427 | $ 34 | $ 461 |

(1) Certain 2012 figures have been restated (see note 2).

**Composition of Plan Assets** The defined benefit pension plan assets are held in trust and consisted of the following asset categories:

| | As at | | | |
|---|---|---|---|---|
| | **Dec. 31, 2013** | | Dec. 31, 2012 | |
| **Equity securities** | | | | |
| Canadian – common | **$ 152** | **7%** | $ 134 | 7% |
| – pooled funds | **208** | **10%** | 291 | 16% |
| Foreign – pooled funds | **603** | **30%** | 644 | 35% |
| Total equity securities | **$ 963** | **47%** | $ 1,069 | 58% |
| **Debt securities** | | | | |
| Fixed income securities – government | **$ 549** | **27%** | $ 431 | 23% |
| – corporate | **177** | **9%** | 189 | 10% |
| Fixed income pooled funds[(1)] – government | **234** | **11%** | 75 | 4% |
| – corporate | **55** | **3%** | 68 | 4% |
| Total debt securities | **$ 1,015** | **50%** | $ 763 | 41% |
| **Cash and cash equivalents** | **$ 66** | **3%** | $ 15 | 1% |
| Total | **$ 2,044** | **100%** | $ 1,847 | 100% |

(1) Both government and corporate securities may be included within the same fixed income pooled fund.

As at year end 2013 and 2012, the defined benefit pension plans did not directly include any GWL or Loblaw securities.

All equity and debt securities 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 fixed income investments, which are sensitive to interest rates, and equities, which are expected to provide both higher returns and inflation-sensitive 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.

## Notes to the Consolidated Financial Statements

**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):

| | **2013** | | 2012 | |
|---|---|---|---|---|
| | **Defined Benefit Pension Plans** | **Other Defined Benefit Plans** | Defined Benefit Pension Plans | Other Defined Benefit Plans |
| **Defined Benefit Plan Obligations** | | | | |
| 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-RPP2014Priv Generational** | **CPM-RPP2014Priv Generational** | UP94@Fully Generational | UP94@Fully Generational |
| **Net Defined Benefit Plan Cost** | | | | |
| Discount rate | **4.00%** | **4.00%** | 4.25% | 4.25% |
| Rate of compensation increase | **3.50%** | **n/a** | 3.50% | n/a |
| Mortality table | **UP94@Fully Generational** | **UP94@Fully Generational** | UP94@Fully Generational | UP94@Fully Generational |

n/a – not applicable

The weighted average duration of the defined benefit obligations as at year end 2013 is 15.4 years (2012 – 15.4 years).

The growth rate of health care costs, primarily drug and other medical costs, for the other defined benefit plan obligations as at year end 2013 was estimated at 4.00% and was assumed to increase to 4.50% by year end 2014, remaining at that level thereafter.

**Sensitivity of Key Actuarial Assumptions** The following table outlines the key assumptions for 2013 (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.

| | | Defined Benefit Pension Plans | | Other Defined Benefit Plans | |
|---|---|---|---|---|---|
| Increase (Decrease) | | Defined Benefit Plan Obligations | Net Defined Benefit Plan Cost[1] | Defined Benefit Plan Obligations | Net Defined Benefit Plan Cost[1] |
| Discount rate | | 4.75% | 4.00% | 4.50% | 4.00% |
| Impact of: | 1% increase | $ (289) | $ (24) | $ (20) | $ (1) |
| | 1% decrease | $ 339 | $ 25 | $ 25 | $ 1 |
| Expected growth rate of health care costs | | | | 4.00% | 5.75% |
| Impact of: | 1% increase | n/a | n/a | $ 19 | $ 2 |
| | 1% decrease | n/a | n/a | $ (16) | $ (2) |

n/a – not applicable

(1) Discount rate and expected growth rate of health care costs sensitivity is for current service and interest costs only.

**(ii) Multi-Employer Pension Plans**

During 2013, the Company recognized an expense of $61 (2012 – $104) in selling, general and administrative expenses, which represents the contributions made in connection with MEPPs. During 2014, the Company expects to continue to make contributions into these MEPPs.

Loblaw, together with its independent franchisees, is the largest participating employer in the Canadian Commercial Workers Industry Pension Plan ("CCWIPP"), with approximately 53,000 (2012 – 54,000) employees as members. Included in the 2013 expense described above are contributions of $54 (2012 – $52) to CCWIPP.

During 2012, Weston Foods withdrew from one of the U.S. MEPPs in which it participated. As a result, the Company was subject to and paid a withdrawal liability. Also during 2012, another participating employer withdrew from the plan and a mass withdrawal was triggered. As a result of the mass withdrawal, the Company is subject to an incremental withdrawal liability (see note 21).

**(iii) 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:

| | **2013** | 2012[1] |
|---|---|---|
| Net post-employment defined benefit cost | **$ 42** | $ 102 |
| Defined contribution costs[2] | **25** | 22 |
| Multi-employer pension plan costs[3] | **61** | 104 |
| Total net post-employment benefit costs | **$ 128** | $ 228 |
| Other long term employee benefit costs[4] | **22** | 30 |
| Net post-employment and other long term employee benefit costs | **$ 150** | $ 258 |
| Recorded on the consolidated statements of earnings as follows: | | |
| Operating income (note 32) | **$ 125** | $ 226 |
| Net interest expense and other financing charges (note 7) | **25** | 32 |
| Net post-employment and other long term employee benefits costs | **$ 150** | $ 258 |

(1) Certain 2012 figures have been restated (see note 2).
(2) Amounts represent the Company's contributions made in connection with defined contribution plans.
(3) Amounts represent the Company's contributions made in connection with MEPPs. In 2013, $5 (2012 – $51) was included related to the Company's MEPP withdrawal (see note 21).
(4) Other long term employee benefit costs include $4 (2012 – $4) of net interest expense and other financing charges.

## Note 31. Share-Based Compensation ($ except where otherwise indicated)

The following table summarizes the Company's cost recognized in selling, general and administrative expenses related to its share-based compensation arrangements and GWL's and Glenhuron Bank Limited's ("Glenhuron") equity derivatives:

| ($ millions) | **2013** | 2012 |
|---|---|---|
| Stock option plans expense | **$ 20** | $ 21 |
| RSU and PSU plans expense | **20** | 16 |
| Equity derivative contracts income | | (8) |
| Net share-based compensation expense | **$ 40** | $ 29 |

The following is the carrying amount of the Company's share-based compensation arrangements including stock option plans, RSU plans, PSU plans, DSU plans, and EDSU plans and Choice Properties' unit option plan, restricted unit plan and trustee deferred unit plan:

| ($ millions) | As at Dec. 31, 2013 | As at Dec. 31, 2012 |
|---|---|---|
| Trade payables and other liabilities | **$ 1** | $ 14 |
| Other liabilities (note 25) | **$ 1** | $ 36 |
| Contributed surplus | **$ 94** | $ 45 |

During 2013, GWL's and Loblaw's RSU, PSU, DSU and EDSU plans were amended to require settlement in common shares rather than in cash. As a result, $40 million previously recorded in trade payables and other liabilities and other liabilities was reclassified to contributed surplus.

**Stock Option Plans** GWL maintains a stock option plan for certain employees. Under this plan, GWL may grant options for up to 6,453,726 of its common shares, representing approximately 5% of outstanding common shares.

Loblaw maintains a stock option plan for certain employees. Under this plan, Loblaw may grant options for up to 28,137,162 of its common shares, representing approximately 10% of outstanding common shares.

The following is a summary of GWL's stock option plan activity:

| | **2013** | | 2012 | |
|---|---|---|---|---|
| | **Options (number of shares)** | **Weighted Average Exercise Price/Share** | Options (number of shares) | Weighted Average Exercise Price/Share |
| Outstanding options, beginning of year | **1,436,234** | **$ 66.55** | 1,414,504 | $ 75.43 |
| Granted | **314,777** | **$ 73.74** | 381,146 | $ 62.96 |
| Exercised | **(258,418)** | **$ 65.93** | (41,361) | $ 57.83 |
| Forfeited/cancelled | **(1,425)** | **$ 65.30** | (49,328) | $ 67.65 |
| Expired | | | (268,727) | $ 109.32 |
| Outstanding options, end of year[1] | **1,491,168** | **$ 68.18** | 1,436,234 | $ 66.55 |
| Options exercisable, end of year | **629,961** | **$ 67.10** | 616,453 | $ 67.96 |

(1) Options outstanding of 1,491,168 (2012 – 1,436,234) represented approximately 1.2% (2012 – 1.1%) of GWL's issued and outstanding common shares, which was within GWL's guideline of approximately 5%.

The following table summarizes information about GWL's outstanding stock options:

| | | | | 2013 | | | |
|---|---|---|---|---|---|---|---|
| | Outstanding Options | | | | Exercisable Options | | |
| Range of Exercise Prices ($) | Number of Options Outstanding | Weighted Average Remaining Contractual Life (years) | | Weighted Average Exercise Price/Share | Number of Exercisable Options | | Weighted Average Exercise Price/Share |
| $46.24 - $63.01 | **492,604** | **4** | **$** | **60.22** | **213,208** | **$** | **57.14** |
| $63.02 - $72.97 | **553,270** | **3** | **$** | **69.08** | **337,745** | **$** | **70.15** |
| $72.98 - $83.64 | **445,294** | **5** | **$** | **75.86** | **79,008** | **$** | **80.93** |
| | **1,491,168** | | | | **629,961** | | |

During 2013, GWL issued 258,418 (2012 – 41,361) common shares on the exercise of stock options with a weighted average share price of $83.27 (2012 – $69.39) per common share and received cash consideration of $17 million (2012 – $2 million).

During 2013, GWL granted stock options with a weighted average exercise price of $73.74 (2012 – $62.96) per common share and a fair value of $5 million (2012 – $5 million). The assumptions used to measure the grant date fair value of the GWL options granted during 2013 and 2012 under the Black-Scholes stock option valuation model were as follows:

| | 2013 | 2012 |
|---|---|---|
| Expected dividend yield | **2.0%** | 2.3% - 2.4% |
| Expected share price volatility | **21.0% - 24.7%** | 24.2% - 25.8% |
| Risk-free interest rate | **1.3% - 2.3%** | 1.5% - 1.8% |
| Expected life of options | **4.8 - 6.7 years** | 4.8 - 6.6 years |

Estimated forfeiture rates are incorporated into the measurement of stock option plan expense. The forfeiture rate applied as at year end 2013 was 3.7% (2012 – 4.2%).

The following is a summary of Loblaw's stock option plan activity:

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | Options (number of shares) | | Weighted Average Exercise Price/Share | Options (number of shares) | | Weighted Average Exercise Price/Share |
| Outstanding options, beginning of year | **12,538,928** | **$** | **36.74** | 10,750,993 | $ | 38.90 |
| Granted | **1,484,264** | **$** | **40.62** | 4,605,970 | $ | 34.91 |
| Exercised | **(2,131,416)** | **$** | **35.25** | (718,544) | $ | 31.00 |
| Forfeited/cancelled | **(847,039)** | **$** | **38.03** | (1,506,608) | $ | 36.74 |
| Expired | **(48,742)** | **$** | **54.71** | (592,883) | $ | 68.64 |
| Outstanding options, end of year[(1)] | **10,995,995** | **$** | **37.37** | 12,538,928 | $ | 36.74 |
| Options exercisable, end of year | **4,200,472** | **$** | **38.04** | 4,120,017 | $ | 38.72 |

(1) Options outstanding of 10,995,995 (2012 – 12,538,928) represented approximately 3.9% (2012 – 4.5%) of Loblaw's issued and outstanding common shares, which was within Loblaw's guideline of approximately 10%.

The following table summarizes information about Loblaw's outstanding stock options:

| | 2013 | | | | |
|---|---|---|---|---|---|
| | Outstanding Options | | | Exercisable Options | |
| Range of Exercise Prices ($) | Number of Options Outstanding | Weighted Average Remaining Contractual Life (years) | Weighted Average Exercise Price/Share | Number of Exercisable Options | Weighted Average Exercise Price/Share |
| $28.95 - $35.55 | **4,984,391** | **4** | **$ 33.63** | **1,662,506** | **$ 31.70** |
| $35.56 - $39.92 | **3,475,944** | **4** | **$ 38.07** | **1,387,094** | **$ 37.80** |
| $39.93 - $50.79 | **2,535,660** | **3** | **$ 43.75** | **1,150,872** | **$ 47.47** |
| | **10,995,995** | | | **4,200,472** | |

During 2013, Loblaw issued 2,131,416 (2012 – 718,544) common shares on the exercise of stock options with a weighted average share price of $46.54 (2012 – $36.90) per common share and received cash consideration of $75 million (2012 – $22 million).

During 2013, Loblaw granted stock options with a weighted average exercise price of $40.62 (2012 – $34.91) per common share and a fair value of $11 million (2012 – $27 million). The assumptions used to measure the grant date fair value of the Loblaw options granted during 2013 and 2012 under the Black-Scholes stock option valuation model were as follows:

| | 2013 | 2012 |
|---|---|---|
| Expected dividend yield | **2.1%** | 2.4% - 2.7% |
| Expected share price volatility | **19.2% - 23.8%** | 21.1% - 24.8% |
| Risk-free interest rate | **1.2% - 2.0%** | 1.3% - 1.6% |
| Expected life of options | **4.2 - 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 year end 2013 was 12.0% (2012 – 15.0%).

**Restricted Share Unit Plans** The following is a summary of GWL's and Loblaw's RSU plan activity:

| | GWL | | Loblaw | |
|---|---|---|---|---|
| (Number of Awards) | 2013 | 2012 | 2013 | 2012 |
| Outstanding RSUs, beginning of year | **147,926** | 139,813 | **1,038,271** | 1,119,496 |
| Granted | **60,672** | 82,249 | **379,899** | 379,746 |
| Settled | **(24,210)** | (66,546) | **(273,937)** | (382,871) |
| Forfeited | **(146)** | (7,590) | **(59,719)** | (78,100) |
| Outstanding RSUs, end of year | **184,242** | 147,926 | **1,084,514** | 1,038,271 |
| RSUs settled ($ millions) | **$ 2** | $ 4 | **$ 10** | $ 13 |

The fair value of GWL's and Loblaw's RSUs granted during 2013 was $4 million (2012 – $6 million) and $15 million (2012 – $15 million), respectively.

**Performance Share Unit Plans** The following is a summary of GWL's and Loblaw's PSU plan activity:

| | GWL | | Loblaw | |
|---|---|---|---|---|
| (Number of Awards) | **2013** | 2012 | **2013** | 2012 |
| Outstanding PSUs, beginning of year | **41,101** | | **50,818** | |
| Granted | **44,016** | 43,012 | **283,569** | 50,818 |
| Settled | | | **(2,794)** | |
| Forfeited | | (1,911) | **(22,483)** | |
| Outstanding PSUs, end of year | **85,117** | 41,101 | **309,110** | 50,818 |

The fair value of GWL's and Loblaw's PSUs granted during 2013 was $3 million (2012 – $3 million) and $11 million (2012 – $2 million), respectively.

**Director Deferred Share Unit Plans** The following is a summary of GWL's and Loblaw's DSU plan activity:

| | GWL | | Loblaw | |
|---|---|---|---|---|
| (Number of Awards) | **2013** | 2012 | **2013** | 2012 |
| Outstanding DSUs, beginning of year | **172,830** | 143,754 | **198,780** | 158,017 |
| Granted | **20,079** | 25,507 | **24,582** | 36,570 |
| Reinvested | **3,716** | 3,569 | **3,239** | 4,193 |
| Settled | **(8,428)** | | | |
| Outstanding DSUs, end of year | **188,197** | 172,830 | **226,601** | 198,780 |

In 2013, the Company recorded a compensation cost of $5 million (2012 – $2 million) related to these plans in selling, general and administrative expenses. The fair value of GWL's and Loblaw's DSUs granted during 2013 was $2 million (2012 – $2 million) and $1 million (2012 – $1 million), respectively.

**Executive Deferred Share Unit Plans** The following is a summary of GWL's and Loblaw's EDSU plan activity:

| | GWL | | Loblaw | |
|---|---|---|---|---|
| (Number of Awards) | **2013** | 2012 | **2013** | 2012 |
| Outstanding EDSUs, beginning of year | **3,598** | 4,130 | **26,707** | 43,928 |
| Granted | **273** | 711 | **2,606** | 3,553 |
| Reinvested | **79** | 84 | **421** | 1,007 |
| Settled | | (1,327) | **(7,608)** | (21,781) |
| Outstanding EDSUs, end of year | **3,950** | 3,598 | **22,126** | 26,707 |

In 2013, the Company recorded a nominal compensation cost (2012 – nominal) related to these plans in selling, general and administrative expenses. The fair value of GWL's and Loblaw's EDSUs granted during 2013 and 2012 was nominal.

**Equity Derivative Contracts** The following is a summary of GWL's equity swap contracts (see note 34):

| ($ millions unless otherwise indicated) | As at Dec. 31, 2012 |
|---|---|
| Outstanding contracts (in millions) | 0.8 |
| Forward price per share ($) | $ 107.26 |
| Unrealized loss recorded in trade payables and other liabilities | $ 29 |

During 2013, GWL paid $29 million to settle its remaining equity swap contract representing 800,000 GWL common shares and recorded a nominal loss (2012 – fair value gain of $2 million) in operating income related to this equity swap contract.

The following is a summary of Glenhuron's equity forward contracts (see note 34):

| ($ millions unless otherwise indicated) | As at Dec. 31, 2012 |
|---|---|
| Outstanding contracts (in millions) | 1.1 |
| Average forward price per share ($) | $ 56.59 |
| Interest expense per share ($) | $ 0.16 |
| Unrealized loss recorded in trade payables and other liabilities | $ 16 |

During 2013, Glenhuron paid $16 million to settle its remaining equity forward contract representing 1,103,500 Loblaw common shares and recorded a nominal loss (2012 – fair value gain of $5 million) in operating income related to this equity forward contract.

**Note 32. Employee Costs**

Included in operating income were the following employee costs:

| | **2013** | 2012[1] |
|---|---|---|
| Wages, salaries and other short term employee benefits | **$ 3,411** | $ 3,366 |
| Post-employment benefits (note 30) | **107** | 200 |
| Other long term employee benefits (note 30) | **18** | 26 |
| Share-based compensation (note 31) | **40** | 37 |
| Capitalized to fixed assets | **(10)** | (24) |
| Employee costs | **$ 3,566** | $ 3,605 |

(1) Certain 2012 figures have been restated (see note 2).

**Note 33. 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 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:

| | Payments due by year | | | | | | As at | |
|---|---|---|---|---|---|---|---|---|
| | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter | **Dec. 31, 2013** | Dec. 31, 2012 |
| Operating lease payments | $ 214 | $ 196 | $ 165 | $ 137 | $ 112 | $ 453 | **$ 1,277** | $ 1,288 |
| Sub-lease income | (51) | (38) | (27) | (19) | (13) | (57) | **(205)** | (187) |
| Net operating lease payments | $ 163 | $ 158 | $ 138 | $ 118 | $ 99 | $ 396 | **$ 1,072** | $ 1,101 |

In 2013, the Company recorded $220 (2012 – $212) as an expense in operating income in respect of operating leases. Contingent rent recognized as an expense in respect of operating leases was $1 (2012 – $1), while sub-lease income earned was $53 (2012 – $51) which was recognized in operating income.

**Operating Leases – As Lessor** As at year end 2013, Loblaw leased certain owned land and buildings with a cost of $2,076 (2012 – $2,037) and related accumulated depreciation of $562 (2012 – $539). For the year ended 2013, rental income was $136 (2012 – $132) and contingent rent was $2 (2012 – $2), both of which were recognized in operating income. Contingent rent is based on store performance measured against specified thresholds.

Future rental income relating to Loblaw's operating leases is as follows:

| | Payments to be received by year | | | | | | As at | |
|---|---|---|---|---|---|---|---|---|
| | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter | **Dec. 31, 2013** | Dec. 31, 2012 |
| Net operating lease income | $ 133 | $ 114 | $ 92 | $ 69 | $ 45 | $ 106 | **$ 559** | $ 520 |

**Finance Leases – As Lessee** Loblaw has finance leases for certain property, plant and equipment.

Future minimum lease payments relating to Loblaw's finance leases are as follows:

| | Payments due by year | | | | | | As at | |
|---|---|---|---|---|---|---|---|---|
| | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter | **Dec. 31, 2013** | Dec. 31, 2012 |
| Finance lease payments | $ 54 | $ 52 | $ 52 | $ 47 | $ 40 | $ 526 | **$ 771** | $ 755 |
| Less future finance charges | (27) | (26) | (24) | (23) | (21) | (262) | **(383)** | (389) |
| Present value of minimum lease payments | $ 27 | $ 26 | $ 28 | $ 24 | $ 19 | $ 264 | **$ 388** | $ 366 |

In 2013, contingent rent recognized by Loblaw as an expense in respect of finance leases was $1 (2012 – $1).

Future sub-lease income relating to Loblaw's sub-lease agreements is as follows:

| | Payments to be received by year | | | | | | As at | |
|---|---|---|---|---|---|---|---|---|
| | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter | **Dec. 31, 2013** | Dec. 31, 2012 |
| Sub-lease income | $ (14) | $ (11) | $ (8) | $ (6) | $ (2) | $ (4) | **$ (45)** | $ (57) |

As at year end 2013, the sub-lease payments receivable under finance leases was $14 (2012 – $16).

**Note 34. Financial Instruments**

The following table provides a comparison of the carrying and fair values and specifies the classification of the Company's financial instruments as at year end 2013:

| | Financial instruments required to be classified as fair value through profit or loss | Financial instruments designated as fair value through profit or loss | Loans and receivables (amortized cost) | Other financial liabilities (amortized cost) | Total carrying amount | Total fair value |
|---|---|---|---|---|---|---|
| Cash and cash equivalents | | $ 2,869 | | | $ 2,869 | $ 2,869 |
| Short term investments | | 1,490 | | | 1,490 | 1,490 |
| Derivatives included in accounts receivable | $ (4) | | | | (4) | (4) |
| Other accounts receivable | | | $ 740 | | 740 | 740 |
| Credit card receivables | | | 2,538 | | 2,538 | 2,538 |
| Derivatives included in prepaid expenses and other assets | 2 | | | | 2 | 2 |
| Security deposits | | 1,791 | | | 1,791 | 1,791 |
| Franchise loans receivable | | | 375 | | 375 | 375 |
| Derivatives included in other assets | 524 | | | | 524 | 524 |
| Certain other assets | | | 67 | | 67 | 67 |
| Total financial assets | $ 522 | $ 6,150 | $ 3,720 | | $ 10,392 | $ 10,392 |
| Trade payables and other liabilities | | | | $ 3,985 | $ 3,985 | $ 3,985 |
| Derivatives included in trade payables and other liabilities | $ 4 | | | | 4 | 4 |
| Short term debt | | | | 1,060 | 1,060 | 1,060 |
| Long term debt | | | | 8,944 | 8,944 | 9,503 |
| Trust Unit liability | 478 | | | | 478 | 478 |
| Certain other liabilities | | | | 40 | 40 | 40 |
| Capital securities | | | | 224 | 224 | 236 |
| Total financial liabilities | $ 482 | | | $ 14,253 | $ 14,735 | $ 15,306 |

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, as at year end 2013:

| | Level 1 | Level 2 | Level 3 | Total fair value |
|---|---|---|---|---|
| Financial assets | | | | |
| Required to be classified as fair value through profit or loss | $ (4) | $ 526 | | $ 522 |
| Designated as fair value through profit or loss | $ 776 | $ 5,374 | | $ 6,150 |
| Loans and receivables (amortized cost) | | $ 8 | $ 434 | $ 442 |
| Financial liabilities | | | | |
| Required to be classified as fair value through profit or loss | $ 478 | | $ 4 | $ 482 |
| Other financial liabilities (amortized cost) | $ 236 | $ 9,503 | $ 40 | $ 9,779 |

The following table provides a comparison of the carrying and fair values and specifies the classification of the Company's financial instruments as at year end 2012:

| | Financial instruments required to be classified as fair value through profit or loss | Financial instruments designated as fair value through profit or loss | Loans and receivables (amortized cost) | Other financial liabilities (amortized cost) | Total carrying amount | Total fair value |
|---|---|---|---|---|---|---|
| Cash and cash equivalents | | $ 1,589 | | | $ 1,589 | $ 1,589 |
| Short term investments | | 2,138 | | | 2,138 | 2,138 |
| Derivatives included in accounts receivable | $ | | | | | |
| Other accounts receivable | | | $ 559 | | 559 | 559 |
| Credit card receivables | | | 2,305 | | 2,305 | 2,305 |
| Security deposits | | 348 | | | 348 | 348 |
| Franchise loans receivable | | | 363 | | 363 | 363 |
| Derivatives included in other assets | 603 | | | | 603 | 603 |
| Certain other assets | | | 75 | | 75 | 75 |
| Total financial assets | $ 603 | $ 4,075 | $ 3,302 | | $ 7,980 | $ 7,980 |
| Trade payables and other liabilities | | | | $ 3,886 | $ 3,886 | $ 3,886 |
| Derivatives included in trade payables and other liabilities | $ 51 | | | | 51 | 51 |
| Short term debt | | | | 1,319 | 1,319 | 1,319 |
| Long term debt | | | | 6,933 | 6,933 | 7,901 |
| Certain other liabilities | | | | 44 | 44 | 44 |
| Capital securities | | | | 223 | 223 | 243 |
| Total financial liabilities | $ 51 | | | $ 12,405 | $ 12,456 | $ 13,444 |

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, as at year end 2012:

| | Level 1 | Level 2 | Level 3 | Total fair value |
|---|---|---|---|---|
| Financial assets | | | | |
| Required to be classified as fair value through profit or loss | | $ 603 | | $ 603 |
| Designated as fair value through profit or loss | $ 385 | $ 3,690 | | $ 4,075 |
| Loans and receivables (amortized cost) | | $ 11 | $ 427 | $ 438 |
| Financial liabilities | | | | |
| Required to be classified as fair value through profit or loss | | $ 50 | $ 1 | $ 51 |
| Other financial liabilities (amortized cost) | $ 243 | $ 7,901 | $ 44 | $ 8,188 |

There were no transfers between the levels of the fair value hierarchy during 2013 and 2012.

The level 3 financial instruments classified as fair value through profit or loss 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.

As at year end 2013, the fair value of the embedded foreign currency derivative classified as level 3 and recorded in trade payables and other liabilities was $4 (2012 – $1). In addition, in 2013, a fair value loss of $3 (2012 – gain of $1) was recognized in operating income. A 1% increase (decrease) in foreign currency exchange rates would result in an additional gain (loss) of $1 in fair value.

During 2013, a gain of $32 (2012 – loss of $27) was recognized in earnings before income taxes on financial instruments designated as fair value through profit or loss. In addition, a loss of $31 (2012 – gain of $13) was recognized in earnings before income taxes on financial instruments required to be classified as fair value through profit or loss.

During 2013, net interest expense of $511 (2012 – $414) was recorded related to financial instruments not classified or designated as fair value through profit or loss.

**Cash and Cash Equivalents, Short Term Investments and Security Deposits** As at year end 2013, the Company had cash and cash equivalents, short term investments and security deposits of $6,150 (2012 – $4,075), including U.S. $1,143 (2012 – U.S. $2,239) that was held primarily by Dunedin Holdings GmbH ("Dunedin"), a subsidiary of GWL, and certain of its affiliates and Glenhuron (see note 11).

In 2013, a gain of $44 (2012 – loss of $13) was recognized in other comprehensive income (loss) related to the effect of foreign currency translation on the Company's (excluding Loblaw's) U.S. net investment in foreign operations. In addition, a gain of $75 (2012 – loss of $24) was recorded in selling, general and administrative expenses related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and cash equivalents and short term investments held by foreign operations that have the same functional currency as that of the Company.

See cross currency swaps section below for the (gain) loss recognized in Loblaw's operating income as a result of translating U.S. dollar denominated cash and cash equivalents, short term investments and security deposits.

**Cross Currency Swaps** In 2013, Glenhuron unwound its cross currency swaps and received a net cash settlement of $76, representing the cumulative fair value gain on these swaps. The cross currency swaps were offset by the effect of translation (gains) losses related to U.S. dollar cash and cash equivalents, short term investments and security deposits. As at year end 2012, a cumulative unrealized foreign currency exchange rate receivable of $20 was recorded in prepaid expenses and other assets, and a receivable of $93 was recorded in other assets related to these swaps.

The following table summarizes the changes in fair value of the Glenhuron cross currency swaps and the underlying exposures:

| | | **2013** | | 2012 |
|---|---|---|---|---|
| Fair value loss (gain) related to swaps recorded in operating income | **$** | **37** | $ | (25) |
| Translation (gain) loss related to the underlying exposures | **$** | **(33)** | $ | 27 |

In 2013, Loblaw settled its U.S. $300 USPP cross currency swaps in conjunction with the settlement of the underlying U.S. $300 USPP notes and received a net cash settlement of $18. The USPP cross currency swaps were used to manage the effect of translation (gains) losses on the underlying U.S. dollar USPP notes in long term debt. As part of the full settlement, Loblaw settled its U.S. $150 USPP cross currency swap, which matured on May 29, 2013. On settlement of the swap, an unrealized fair value gain of $5, net of tax of $2, which had been deferred in accumulated other comprehensive income (loss) was realized in operating income.

As at year end 2012, a cumulative unrealized foreign currency exchange rate receivable of $2 was recorded in prepaid expenses and other assets, and a receivable of $5 was recorded in other assets related to the USPP cross currency swaps.

The following table summarizes the changes in fair value of the USPP cross currency swaps and the underlying exposures:

| | **2013** | 2012 |
|---|---|---|
| Fair value (gain) loss related to swaps recorded in operating income[1] | **$ (11)** | $ 7 |
| Translation loss (gain) related to the underlying exposures | **$ 14** | $ (6) |

(1) Excludes the gain of $7 reclassified from accumulated other comprehensive income (loss) in 2013.

**Interest Rate Swaps** In 2013, Loblaw settled its notional $150 in interest rate swaps. As at year end 2012, Loblaw held notional $150 in interest rate swaps, on which Loblaw paid a fixed-rate of 8.38% and recorded a cumulative loss of $5 in trade payables and other liabilities.

During 2013, Loblaw recognized a fair value gain of $5 (2012 – $11) in operating income related to these swaps.

**Equity Derivative Contracts ($, except where otherwise indicated)** GWL and Glenhuron had equity derivative contracts to purchase GWL and Loblaw common shares, respectively. These contracts were settled during 2013. See note 31 for details relating to these equity derivative contracts.

In 2001, Weston Holdings Limited ("WHL"), a subsidiary of GWL, entered into an equity forward sale agreement based on 9.6 million Loblaw common shares at an original forward price of $48.50 per Loblaw common share. As at year end 2013, the forward price had increased to $96.46 (2012 – $92.26) per Loblaw common share under the terms of the agreement and the fair value of this forward sale agreement of $524 million (2012 – $483 million) was recorded in other assets (see note 20). In 2013, a fair value gain of $1 million (2012 – loss of $35 million) was recorded in net interest expense and other financing charges related to this agreement (see note 7).

**Weston Foods Commodity Derivatives** Weston Foods uses commodity futures, options and forward contracts to manage its anticipated exposure to fluctuations in commodity prices.

As at year end 2013, the unrealized loss related to Weston Foods' commodity futures of $4 (2012 – nominal loss) was recorded in accounts receivable. As at year end 2013, a nominal cumulative fair value loss related to Weston Foods' commodity options (2012 – nominal loss) was recorded in accounts receivable.

**Franchise Loans Receivable and Franchise Investments in Other Assets** The value of Loblaw franchise loans receivable of $375 (2012 – $363) was recorded on the consolidated balance sheets. During 2013, Loblaw recorded an impairment loss of $14 (2012 – $12) in operating income related to these loans receivable.

The value of Loblaw franchise investments of $58 (2012 – $64) was recorded in other assets. During 2013, Loblaw recorded a loss of $6 (2012 – $7) in operating income related to these investments.

**Other Loblaw Derivatives** Loblaw also maintains other financial derivatives including foreign exchange forwards and fuel exchange traded futures and options. During 2013, Loblaw recognized a gain of $7 (2012 – nominal) in operating income. As at year end 2013, a cumulative unrealized gain of $2 was recorded in prepaid expenses and other assets (2012 – nominal cumulative unrealized gain).

In connection with Loblaw's issuance of $1.6 billion of senior unsecured notes in 2013 (see note 23), Loblaw hedged its exposure to interest rates in the period prior to the issuance. This relationship did not qualify for hedge accounting resulting in a gain of $10 on the unwind of the hedge, which was recorded in net interest expense and other financing charges (see note 7).

## Note 35. Financial Risk Management

As a result of holding and issuing financial instruments, the Company is exposed to level of indebtedness and liquidity risk, capital availability risk, market risk and credit risk. The following is a description of those risks and how the exposures are managed:

**Level of Indebtedness and Liquidity Risk** To fund the cash portion of the Shoppers Drug Mart acquisition, Loblaw will utilize excess cash and significantly increase its indebtedness. There can be no assurances that Loblaw will generate sufficient free cash flow to reduce indebtedness and maintain adequate cash reserves which could result in adverse consequences on its credit ratings and its cost of funding.

Liquidity risk is the risk that the Company cannot meet its demands for cash or fund its obligations as they come due. In addition, it includes the risk of not being able to liquidate assets in a timely manner at a reasonable price.

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.

Despite these mitigation strategies, if GWL, Loblaw, PC Bank or Choice Properties' financial performance and condition deteriorate or downgrades in GWL's, Loblaw's or Choice Properties' current credit ratings occur, the ability to obtain funding from external sources could be restricted.

***Maturity Analysis*** The following are the undiscounted contractual maturities of significant financial liabilities as at December 31, 2013:

| | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter[(4)] | Total |
|---|---|---|---|---|---|---|---|
| Long term debt including fixed interest payments[(1)] | $ 1,597 | $ 772 | $ 1,137 | $ 452 | $ 1,334 | $ 8,702 | $ 13,994 |
| Foreign exchange forward contracts | 70 | | | | | | 70 |
| Short term debt[(2)] | 1,060 | | | | | | 1,060 |
| Other liabilities[(3)] | 35 | | 4 | | | | 39 |
| | $ 2,762 | $ 772 | $ 1,141 | $ 452 | $ 1,334 | $ 8,702 | $ 15,163 |

(1) 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.
(2) See note 22 for a breakdown of the components of short term debt.
(3) Contractual amount of Loblaw's obligation related to certain other liabilities.
(4) The Trust Unit liability and the Loblaw capital securities and their related dividends have been excluded as the Company is not contractually obligated to pay these amounts. The Company also excluded trade payables and other liabilities which are due within the next 12 months.

**Capital Availability Risk** 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.

**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 prices and the impact these factors may have on other counterparties.

***Interest Rate Risk*** 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. GWL and Loblaw manage interest rate risk by monitoring their 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 100 basis point increase in short term interest rates, with all other variables held constant, would result in a decrease of $51 in net interest expense and other financing charges.

***Foreign Currency Exchange Rate Risk*** The Company's consolidated financial statements are expressed in Canadian dollars, however a portion of the Company's (excluding Loblaw's) net assets are denominated in U.S. dollars through both its net investment in foreign operations in the U.S. and its foreign subsidiaries held by Dunedin and certain of its affiliates with a functional currency that is the same as that of the Company. The U.S. dollar denominated net assets are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. As a result, the Company is exposed to foreign currency translation gains and losses. Those gains and losses arising from the translation of the U.S. dollar denominated assets of foreign subsidiaries with a functional currency that is the same as that of the Company are included in operating income, while translation gains and losses on the net investment in foreign operations in the U.S. are recorded in accumulated other comprehensive income (loss). The Company estimates that based on the U.S. net assets held by foreign operations at the end of 2013, an appreciation in the Canadian dollar of one cent relative to the U.S. dollar would result in a loss of $9 in earnings before income taxes.

Revenues and expenses of all 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 recognized. An appreciating U.S. dollar relative to the Canadian dollar will positively impact operating income and net earnings, while a depreciating U.S. dollar relative to the Canadian dollar will have the opposite impact.

Loblaw is exposed to foreign currency exchange rate variability, primarily on its U.S. dollar denominated purchases in trade payables and other liabilities. Weston Foods is also exposed to fluctuations in the prices of U.S. dollar denominated purchases as a result of changes in U.S. dollar exchange rates. A depreciating Canadian dollar relative to the U.S. dollar will negatively impact operating income and net earnings, while an appreciating Canadian dollar relative to the U.S. dollar will have the opposite impact. Subsequent to the end of 2013, Weston Foods entered into futures contracts to mitigate a portion of its current and anticipated exposure to fluctuations in U.S. dollar exchange rates.

***Commodity Price Risk*** Weston Foods costs are directly impacted by fluctuations in the prices of commodity linked raw materials such as wheat flours, sugars, vegetable oils, cocoa powders and chocolate. Loblaw is also exposed to fluctuations in the commodity prices as a result of the indirect link between commodities and the cost of consumer products. In addition, both Weston Foods and Loblaw are exposed to increases in the prices of energy in operating, in the case of Weston Foods, its bakeries and distribution networks, and, in the case of Loblaw, its stores and distribution networks. Both Weston Foods and Loblaw use purchase commitments and derivative instruments in the form of futures contracts, option contracts and forward contracts to manage their current and anticipated exposure to fluctuations in commodity prices. The Company estimates that based on the outstanding derivative contracts held by the Company at the end of 2013, a 10% decrease in relevant commodity prices, with all other variables held constant, would result in a net loss of $6 in earnings before income taxes. This amount excludes the offsetting impact of the commodity price risk inherent in the transactions being hedged.

***Common Share and Unit Price Risk*** Changes in the Loblaw common share price impact the Company's net interest expense and other financing charges. The obligation of WHL under the equity forward sale agreement based on 9.6 million Loblaw common shares, which matures in 2031, is secured by the underlying Loblaw common shares. If the market value of the underlying Loblaw common shares exceeds the obligation of WHL

under this forward, a portion of the proceeds from a future sale of these shares may be used to satisfy the obligation under this forward contract upon termination or maturity. At maturity, if the forward price is greater (less) than the market price of the Loblaw common shares, WHL will receive (pay) cash equal to the difference between the notional value and the market value of the forward contract. A one dollar decrease in the market value of the underlying shares of the equity forward, with all other variables held constant, would result in a loss of $10 in net interest expense and other financing charges.

The Company is exposed to market price risk as a result of Choice Properties' Units that are held by the public. These Units are presented as a liability on the Company's consolidated balance sheet 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 a loss of $46 in net interest expense and other financing charges.

**Credit Risk** 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, Loblaw's franchise loans receivable, accounts receivable from Loblaw's franchisees, other receivables from Weston Foods' customers and suppliers and Loblaw's vendors, associated stores and independent accounts, and pension assets held in the Company's defined benefit plans.

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.

Loblaw's franchise loans receivable, accounts receivable from Loblaw's franchisees, other receivables from Weston Foods' customers and suppliers and Loblaw's vendors, associated stores and independent accounts are actively monitored on an ongoing basis and settled on a frequent basis in accordance with the terms specified in the applicable agreements.

The Company's maximum exposure to credit risk as it relates to derivative instruments is approximated by the positive fair market value of the derivatives on the consolidated balance sheets (see note 34).

Refer to notes 12 and 13 for additional information on the credit quality performance of credit card receivables and other receivables from Weston Foods' customers and suppliers and Loblaw's vendors, independent franchisees, associated stores and independent accounts.

## Note 36. Contingent Liabilities

The Company is involved in, and potentially subject to, various claims and matters arising out of the normal course and conduct of its business including, but not limited to, product liability, labour and employment, regulatory and environmental claims. 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, except for Income and Other Taxes as disclosed below.

**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.

**Income and Other Taxes** The Company is subject to tax audits from various government and regulatory agencies relating to income, capital, commodity, property and other taxes 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.

During 2012, Loblaw received indication from the Canada Revenue Agency ("CRA") that it intends to proceed with a reassessment of the tax treatment of Loblaw's wholly owned subsidiary, Glenhuron. At this stage, no reassessment has yet been received, and accordingly, it is not possible to quantify the amount of any potential reassessment. While Loblaw does not expect the ultimate outcome to be material, such matters cannot be predicted with certainty and could result in a material charge in future periods.

During 2010, GWL received a reassessment from the CRA challenging GWL's characterization of a gain reported in a previous year's tax return filing. Should the CRA be successful in its assertion, the maximum exposure to the Company's net earnings would be approximately $66. GWL is vigorously defending its filing position. No amount has been provided for in the Company's financial statements.

**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, and 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 37. Financial Guarantees

The Company establishes letters of credit used in connection with certain obligations mainly related to real estate transactions, benefit programs, purchase orders and performance guarantees. The aggregate gross potential liability related to these letters of credit, not including the standby letters of credit for Choice Properties and for the benefit of the independent funding trusts and other independent securitization trusts described below, is approximately $442 (2012 – $441). Letters of credit related to the financing program for Loblaw's independent franchisees and securitization of PC Bank's credit card receivables have been identified as guarantees and are described further below.

**Independent Funding Trusts** The full balance relating to the debt of the independent funding trusts has been consolidated on the balance sheets of the Company as at year end 2013 and 2012. Loblaw has agreed to provide a credit enhancement of $48 (2012 – $48) in the form of a standby letter of credit for the benefit of the independent funding trusts representing not less than 10% (2012 – 10%) of the principal amount of the loans outstanding. This credit enhancement allows the independent funding trusts to provide financing to Loblaw'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 Loblaw 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 Loblaw and draw upon this standby letter of credit. This standby letter of credit has never been drawn upon. Loblaw has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit.

**Other Independent Securitization Trusts** Letters of credit for the benefit of other independent securitization trusts with respect to the securitization programs of PC Bank have been issued by major financial institutions. These standby letters of credit could be drawn upon in the event of a major decline in the income flow from or in the value of the securitized credit card receivables. Loblaw has agreed to reimburse the issuing banks for any amount drawn on the standby letters of credit. The aggregate gross potential liability under these arrangements, which represented 9% (2012 – 9%) on a portion of the securitized credit card receivables amount, was approximately $54 (2012 – $81) (see note 22). The undrawn commitments on the independent securitization trusts as at year end 2013 was $120 (2012 – $120).

**Lease Obligations** In connection with historical dispositions of certain of its assets, Loblaw has assigned leases to third parties. Loblaw remains contingently liable for these lease obligations in the event any of the assignees are in default of their lease obligations. The estimated amount for minimum rent, which does not include other lease related expenses such as property tax and common area maintenance charges, was in aggregate of $14 (2012 – $13). Additionally, Loblaw has guaranteed lease obligations of a third-party distributor in the amount of $17 (2012 – $19).

**Choice Properties** Letters of credit to support performance guarantees related to its investment properties including maintenance and development obligations to municipal authorities are issued by Choice Properties. As at year end 2013, the aggregate gross potential liability related to these letters of credit totaled $20.

Choice Properties' credit facility and 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.

**PC Bank** Loblaw 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®. During 2013, Loblaw decreased its guarantee on behalf of PC Bank to MasterCard® to U.S. $170 (2012 – U.S. $230).

**Note 38. Related Party Transactions**

The Company's majority shareholder is Mr. W. Galen Weston, who beneficially owns, directly and indirectly through private companies which he controls, including Wittington, a total of 80,724,599 of the Company's common shares, representing approximately 63% (2012 – 63%) 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 between the Company and its consolidated entities have been eliminated on consolidation and are not disclosed in this note.

In 2013, rental payments to Wittington by the Company amounted to $4 (2012 – $4). As at year end 2013 and 2012, there were no rental payments outstanding.

In 2013, inventory purchases from Associated British Foods plc, a related party by virtue of Mr. W. Galen Weston being a director of such entity's parent company, amounted to $31 (2012 – $26). As at year end 2013, $4 (2012 – $2) was included in trade payables and other liabilities relating to these inventory purchases.

**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 30.

**Income Tax Matters** From time to time, the Company and Wittington may enter into agreements to make elections that are permitted or required under applicable income tax legislation with respect to affiliated corporations. In 2013, these elections and accompanying agreements did not have a material impact on the Company.

**Compensation of Key Management Personnel** The Company's key management personnel is comprised of certain members of the executive team of GWL, Loblaw, Weston Foods and Wittington, as well as members of the Boards of GWL, Loblaw 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.

Annual compensation of key management personnel that is directly attributable to the Company was as follows:

| | **2013** | 2012 |
|---|---|---|
| Salaries, director fees and other short term employee benefits | **$ 19** | $ 18 |
| Share-based compensation | **12** | 8 |
| Total compensation | **$ 31** | $ 26 |

## Note 39. Agreement to Acquire Shoppers Drug Mart Corporation

On July 14, 2013, Loblaw entered into an arrangement agreement to acquire all of the outstanding common shares of Shoppers Drug Mart for consideration of up to approximately $6.7 billion of cash and the issuance of up to approximately 119.9 million common shares. Based on Loblaw's closing common share price on that date, the purchase price would be approximately $12.4 billion. GWL has provided the TSX with a written consent confirming that it is in favour of the transaction, which satisfies the shareholder approval requirements of the TSX.

In connection with the acquisition of Shoppers Drug Mart, Loblaw entered into committed bank facilities consisting of a $3.5 billion term loan facility and a $1.6 billion bridge loan facility. On September 10, 2013, Loblaw subsequently issued $1.6 billion aggregate principal amount of senior unsecured notes under its Short Form Base Shelf Prospectus and concurrently cancelled the $1.6 billion bridge loan facility (see note 23). The net proceeds from the offering have been placed in escrow and will be released from escrow upon satisfaction of the applicable release conditions in connection with Loblaw's proposed acquisition of the outstanding common shares of Shoppers Drug Mart. As part of the financing of the acquisition, GWL has agreed to subscribe for approximately $500 of additional Loblaw common shares.

On September 12, 2013, Shoppers Drug Mart shareholders voted in favour of the agreement and on September 16, 2013 a final order of the Ontario Superior Court of Justice approving the agreement was obtained. The transaction is subject to various regulatory approvals under the *Competition Act* (Canada) and by the TSX, and the fulfillment of certain other closing conditions customary in transactions of this nature. The process of review under the *Competition Act* (Canada) is proceeding as expected and the Company anticipates that the transaction will be completed during the first quarter of 2014. Further information on the transaction and its expected effects on Loblaw can be found in the Information Statement filed by Loblaw on August 20, 2013, in respect of Shoppers Drug Mart shareholder approval of the transaction. There can be no assurance that all conditions will be met or waived or that Loblaw will be able to successfully consummate the proposed transaction as currently contemplated or at all.

## Note 40. Segment Information

The Company has two reportable operating segments: Weston Foods and Loblaw. The accounting policies of the reportable operating segments are the same as those described in the Company's summary of significant accounting policies (see note 2). The Company measures each reportable operating segment's performance based on adjusted EBITDA[2] and adjusted operating income[2]. Neither reportable operating segment is reliant on any single external customer.

| | 2013 | 2012[1] |
|---|---|---|
| **Revenue** | | |
| Weston Foods | **$ 1,812** | $ 1,765 |
| Loblaw | **32,371** | 31,604 |
| Intersegment | **(601)** | (627) |
| Consolidated | **$ 33,582** | $ 32,742 |
| **Adjusted EBITDA[2]** | | |
| Weston Foods | **$ 330** | $ 334 |
| Loblaw | **2,141** | 2,072 |
| Total | **$ 2,471** | $ 2,406 |
| **Depreciation and Amortization[3]** | | |
| Weston Foods | **$ 63** | $ 59 |
| Loblaw | **824** | 777 |
| Total | **$ 887** | $ 836 |
| **Adjusted Operating Income[2]** | | |
| Weston Foods | **$ 267** | $ 275 |
| Loblaw | **1,317** | 1,295 |
| Impact of certain items[4] | **(38)** | (153) |
| Other[5] | **75** | (24) |
| Consolidated operating income | **$ 1,621** | $ 1,393 |
| **Net Interest Expense and Other Financing Charges** | | |
| Weston Foods | **$ 54** | $ 90 |
| Loblaw | **458** | 351 |
| Other[6] | **(6)** | |
| Intersegment[7] | **(9)** | |
| Consolidated net interest expense and other financing charges | **$ 497** | $ 441 |

(1) Certain 2012 figures have been restated (see note 2).
(2) Excludes certain items and is used internally by management when analyzing segment underlying operating performance.
(3) Excludes accelerated depreciation of $4 (2012 – $4) incurred by Weston Foods, included in restructuring and other charges.
(4) The impact of certain items excluded by management includes restructuring and other charges, the fair value adjustment of commodity derivatives at Weston Foods, share-based compensation net of equity derivatives, fixed asset and other related impairments at Loblaw net of recoveries, certain costs relating to Choice Properties and the Shoppers Drug Mart acquisition, the MEPP withdrawal liability incurred by Weston Foods, defined benefit plan amendments, gain on disposal of assets at Loblaw, and Weston Foods insurance proceeds.
(5) Operating income for the year included a gain of $75 (2012 – loss of $24) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by foreign operations.
(6) Represents the Unit distributions from Choice Properties to GWL.
(7) Represents the elimination of the fair value adjustment of the Trust Unit liability related to GWL's direct investment in Choice Properties (see notes 6 and 24).

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| **Total Assets** | | |
| Weston Foods | **$ 2,067** | $ 1,979 |
| Loblaw | **20,919** | 18,121 |
| Other[(1)] | **1,845** | 1,704 |
| Intersegment | **(209)** | |
| Consolidated | **$ 24,622** | $ 21,804 |

(1) Other includes cash and cash equivalents and short term investments held by foreign operations that have the same functional currency as that of the Company and GWL's direct investment in Choice Properties (see note 6).

| | **2013** | 2012 |
|---|---|---|
| **Additions to Fixed Assets and Intangible Assets** | | |
| Weston Foods | **$ 120** | $ 93 |
| Loblaw | **877** | 1,060 |
| Consolidated | **$ 997** | $ 1,153 |

The Company operates primarily in Canada and the United States.

| | 2013 | 2012 |
|---|---|---|
| **Revenue (excluding intersegment)** | | |
| Canada | **$ 32,771** | $ 31,992 |
| United States | **811** | 750 |
| Consolidated | **$ 33,582** | $ 32,742 |

| | As at | |
|---|---|---|
| | **Dec. 31, 2013** | Dec. 31, 2012 |
| **Fixed Assets and Goodwill and Intangible Assets** | | |
| Canada | **$ 10,808** | $ 10,616 |
| United States | **427** | 407 |
| Consolidated | **$ 11,235** | $ 11,023 |

# Three Year Summary

**CONSOLIDATED INFORMATION**[1]

As at or for the years ended December 31

| ($ millions except where otherwise indicated) | **2013** | 2012[2] | 2011[3] |
|---|---|---|---|
| **Operating Results** | | | |
| Sales | **33,582** | 32,742 | 32,376 |
| Operating income | **1,621** | 1,393 | 1,609 |
| Adjusted operating income[4] | **1,584** | 1,570 | 1,700 |
| Adjusted EBITDA[4] | **2,471** | 2,406 | 2,459 |
| Net interest expense and other financing charges[5] | **497** | 441 | 366 |
| Net earnings from continuing operations | **849** | 708 | 919 |
| Discontinued operations | **58** | | |
| Net earnings | **907** | 708 | 919 |
| Net earnings from continuing operations attributable to shareholders of the Company | **616** | 475 | 635 |
| **Financial Position** | | | |
| Fixed assets | **9,655** | 9,452 | 9,172 |
| Goodwill and intangible assets | **1,580** | 1,571 | 1,555 |
| Total assets | **24,622** | 21,804 | 21,323 |
| Cash and cash equivalents, short term investments and security deposits | **6,150** | 4,075 | 4,101 |
| Adjusted debt[4] | **7,259** | 5,584 | 5,536 |
| Total equity attributable to shareholders of the Company | **6,325** | 5,693 | 5,459 |
| Total equity | **8,919** | 8,072 | 7,680 |
| **Cash Flows** | | | |
| Cash flows from operating activities of continuing operations | **1,738** | 1,852 | 1,974 |
| Fixed asset purchases | **976** | 1,110 | 1,027 |
| Free cash flow[4] | **529** | 490 | 562 |
| **Per Common Share** ($) | | | |
| Basic net earnings from continuing operations | **4.48** | 3.36 | 4.58 |
| Adjusted basic net earnings from continuing operations[4] | **4.49** | 4.39 | 4.86 |
| Dividend rate at year end | **1.66** | 1.52 | 1.44 |
| Book value | **43.06** | 38.03 | 36.21 |
| Market value at year end | **77.15** | 70.75 | 68.09 |
| **Financial Measures and Ratios** | | | |
| Sales growth (%) | **2.6** | 1.1 | 1.7 |
| Adjusted operating margin (%)[4] | **4.7** | 4.8 | 5.3 |
| Adjusted EBITDA margin (%)[4] | **7.4** | 7.3 | 7.6 |
| Interest coverage[4] | **3.2x** | 3.2x | 4.4x |
| Adjusted debt[4] to adjusted EBITDA[4] | **2.9x** | 2.3x | 2.3x |
| Return on average net assets (%)[4] | **11.9** | 10.7 | 12.8 |
| Return on average common shareholders' equity attributable to shareholders of the Company (%) | **11.0** | 9.1 | 13.1 |
| Price/net earnings ratio at year end | **17.2** | 21.1 | 14.9 |

(1) For financial definitions and ratios refer to the Glossary beginning on page 134.
(2) Certain 2012 figures have been restated (see note 2 to the consolidated financial statements).
(3) 2011 figures have not been restated for the impact of International Accounting Standards 19.
(4) See non-GAAP financial measures beginning on page 49.
(5) 2013 included non-cash income of $1 (2012 – a non-cash charge of $35) related to the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares. Also included in 2013 is a non-cash charge of $18 (2012 – nil) related to the fair value adjustment of the Trust Unit liability (see note 7 to the consolidated financial statements).

## SEGMENT INFORMATION[1]

As at or for the years ended December 31

| ($ millions except where otherwise indicated) | | 2013 | 2012[2] | 2011[3] |
|---|---|---|---|---|
| **OPERATING RESULTS** | | | | |
| **Sales** | Weston Foods | **1,812** | 1,765 | 1,772 |
| | Loblaw | **32,371** | 31,604 | 31,250 |
| | Intersegment | **(601)** | (627) | (646) |
| | Consolidated | **33,582** | 32,742 | 32,376 |
| **Operating Income** | Weston Foods | **238** | 230 | 208 |
| | Loblaw | **1,308** | 1,187 | 1,376 |
| | Other[4] | **75** | (24) | 25 |
| | Consolidated | **1,621** | 1,393 | 1,609 |
| **Adjusted Operating Income**[5] | Weston Foods | **267** | 275 | 265 |
| | Loblaw | **1,317** | 1,295 | 1,435 |
| | Consolidated | **1,584** | 1,570 | 1,700 |
| **Adjusted EBITDA**[5] | Weston Foods | **330** | 334 | 325 |
| | Loblaw | **2,141** | 2,072 | 2,134 |
| | Consolidated | **2,471** | 2,406 | 2,459 |
| **FINANCIAL POSITION** | | | | |
| **Fixed Assets** | Weston Foods | **550** | 479 | 447 |
| | Loblaw | **9,105** | 8,973 | 8,725 |
| | Consolidated | **9,655** | 9,452 | 9,172 |
| **Total Assets** | Weston Foods | **2,067** | 1,979 | 1,875 |
| | Loblaw | **20,919** | 18,121 | 17,588 |
| | Other[6] | **1,845** | 1,704 | 1,860 |
| | Intersegment | **(209)** | | |
| | Consolidated | **24,622** | 21,804 | 21,323 |
| **CASH FLOWS** | | | | |
| **Fixed Asset Purchases** | Weston Foods | **111** | 93 | 40 |
| | Loblaw | **865** | 1,017 | 987 |
| | Consolidated | **976** | 1,110 | 1,027 |
| **FINANCIAL MEASURES AND RATIOS** | | | | |
| **Sales Growth (Decline)** (%) | Weston Foods | **2.7** | (0.4) | 9.1 |
| | Loblaw | **2.4** | 1.1 | 1.3 |
| | Consolidated | **2.6** | 1.1 | 1.7 |
| **Operating Margin** (%) | Weston Foods | **13.1** | 13.0 | 11.7 |
| | Loblaw | **4.0** | 3.8 | 4.4 |
| | Consolidated | **4.8** | 4.3 | 5.0 |
| **Adjusted Operating Margin** (%)[5] | Weston Foods | **14.7** | 15.6 | 15.0 |
| | Loblaw | **4.1** | 4.1 | 4.6 |
| | Consolidated | **4.7** | 4.8 | 5.3 |
| **Adjusted EBITDA Margin** (%)[5] | Weston Foods | **18.2** | 18.9 | 18.3 |
| | Loblaw | **6.6** | 6.6 | 6.8 |
| | Consolidated | **7.4** | 7.3 | 7.6 |
| **Return on Average Net Assets** (%)[5] | Weston Foods | **23.3** | 25.1 | 24.5 |
| | Loblaw | **10.4** | 9.8 | 11.7 |
| | Consolidated | **11.9** | 10.7 | 12.8 |

(1) For financial definitions and ratios refer to the Glossary beginning on page 134.
(2) Certain 2012 figures have been restated (see note 2 to the consolidated financial statements).
(3) 2011 figures have not been restated for the impact of International Accounting Standards 19.
(4) Operating income for the year included a gain of $75 (2012 – a loss of $24) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by foreign operations.
(5) See non-GAAP financial measures beginning on page 49.
(6) Other includes cash and cash equivalents and short term investments held by foreign operations that have the same functional currency as that of the Company and GWL's direct investment in Choice Properties (see note 6 to the consolidated financial statements).

## Earnings Coverage Exhibit to the Audited Annual Consolidated Financial Statements

The following is the Company's updated earnings coverage ratio for the year ended December 31, 2013 in connection with the Company's Short Form Base Shelf Prospectus dated October 17, 2013. The following earnings coverage ratio gives effect to the issuance of $450 million in senior unsecured debentures by Choice Properties Real Estate Investment Trust subsequent to year end 2013. The following earnings coverage ratio does not (i) give effect to the pro-forma impact of the Acquisition of Shoppers Drug Mart Corporation and (ii) purport to be indicative of earnings coverage ratios for any future periods.

| | |
|---|---|
| Earnings coverage on financial liabilities | 2.28 times |

The earnings coverage ratio on financial liabilities is equal to consolidated net earnings from continuing operations attributable to shareholders of the Company (before interest on short term and long term debt, dividends on capital securities, Trust Unit distributions, the fair value adjustment of the Trust Unit liability and income taxes) divided by consolidated interest on short term and long term debt, dividends on capital securities, Trust Unit distributions, and the fair value adjustment of the Trust Unit liability. For purposes of calculating the earnings coverage ratio set forth above, long term debt includes the current portion of long term debt.

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# Glossary

**Adjusted basic net earnings per common share from continuing operations**
Basic net earnings from continuing operations available to common shareholders of the Company adjusted for items that are not necessarily reflective of the Company's underlying operating performance divided by the weighted average number of common shares outstanding during the year (see non-GAAP financial measures beginning on page 49).

**Adjusted debt**
Short term debt, long term debt, Trust Unit liability, 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 non-GAAP financial measures beginning on page 49).

**Adjusted debt to adjusted EBITDA**
Adjusted debt divided by adjusted EBITDA (see non-GAAP financial measures beginning on page 49).

**Adjusted EBITDA**
Adjusted operating income before depreciation and amortization (see non-GAAP financial measures beginning on page 49).

**Adjusted EBITDA margin**
Adjusted EBITDA divided by sales (see non-GAAP financial measures beginning on page 49).

**Adjusted operating income**
Operating income adjusted for items that are not necessarily reflective of the Company's underlying operating performance (see non-GAAP financial measures beginning on page 49).

**Adjusted operating margin**
Adjusted operating income divided by sales (see non-GAAP financial measures beginning on page 49).

**Basic net earnings per common share from continuing operations**
Net earnings from continuing operations available to common shareholders of the Company divided by the weighted average number of common shares outstanding during the period.

**Book value per common share**
Total equity attributable to shareholders of the Company less preferred shares outstanding divided by the number of common shares outstanding at year end.

**Capital investment**
Fixed asset purchases.

**Control label**
A brand and associated trademark that is owned by Loblaw for use in connection with its own products and services.

**Conversion**
A store that changes from one Loblaw banner to another Loblaw banner.

**Corporate stores sales per average square foot**
Sales by corporate stores excluding gas bar sales divided by the average corporate stores' square footage at year end.

**Diluted net earnings per common share from continuing operations**
Net earnings from continuing operations available to common shareholders of the Company less the impact of dilutive items divided by the weighted average number of common shares outstanding during the period adding back the impact of dilutive items.

**Dividend rate per common share at year end**
Dividend per common share declared in the fourth quarter multiplied by four.

**Free cash flow**
Cash flows from operating activities of continuing operations excluding the net change in credit card receivables less interest paid and fixed asset purchases (see non-GAAP financial measures beginning on page 49).

**Gross margin**
Sales less cost of inventories sold including inventory shrink divided by sales.

**Interest coverage**
Operating income divided by net interest expense and other financing charges adding back interest capitalized to fixed assets (see non-GAAP financial measures beginning on page 49).

**Major expansion**
Expansion of a store that results in an increase in square footage that is greater than 25% of the square footage of the store prior to the expansion.

**Minor expansion**
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.

**Net earnings from continuing operations attributable to shareholders of the Company**
Net earnings from continuing operations less non-controlling interests.

**Net earnings from continuing operations available to common shareholders of the Company**
Net earnings from continuing operations attributable to shareholders of the Company less preferred dividends.

**New store**
A newly constructed store, conversion or major expansion.

**Operating income**
Net earnings before net interest expense and other financing charges and income taxes.

**Operating margin**
Operating income divided by sales.

**Price/net earnings ratio at year end**
Market price per common share at year end divided by basic net earnings per common share from continuing operations for the year.

**Renovation**
A capital investment in a store resulting in no significant change to the store square footage.

**Retail sales**
Combined sales of stores owned by Loblaw and those owned by Loblaw's independent franchisees.

**Retail square footage**
Retail square footage includes corporate and independent franchised stores.

**Return on average common shareholders' equity attributable to shareholders of the Company**
Net earnings from continuing operations available to common shareholders of the Company divided by average total equity attributable to common shareholders of the Company.

**Return on average net assets**
Operating income divided by average total assets excluding cash and cash equivalents, short term investments, security deposits, fair value of the forward sale agreement for 9.6 million Loblaw common shares and trade payables and other liabilities (see non-GAAP financial measures beginning on page 49).

**Same-store sales**
Retail 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 or contraction in the period.

**Total equity attributable to common shareholders of the Company**
Total equity less preferred shares outstanding and non-controlling interests.

**Total equity attributable to shareholders of the Company**
Total equity less non-controlling interests.

**Weighted average common shares outstanding**
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 year.

**Year**
The Company's year end is December 31. Activities are reported on a fiscal year ending on the Saturday closest to December 31, usually 52 weeks in duration, but includes 53 weeks every 5 to 6 years. The years ended December 31, 2013 and December 31, 2012 contained 52 weeks.

# Corporate Directory

## Board of Directors

**W. Galen Weston**, O.C., B.A., LL.D.(1*)
Executive Chairman of the Corporation; Chairman, Holt, Renfrew & Co., Limited, Brown Thomas Group Limited and Selfridges & Co. Ltd.; President, The W. Garfield Weston Foundation; former Chairman, Loblaw Companies Limited and former Director Associated British Foods, plc.

**A. Charles Baillie**, O.C., B.A., M.B.A., LL.D.(2*,3)
Corporate Director; Chair, Alberta Investment Management Corporation; Retired Chairman and Chief Executive Officer, The Toronto-Dominion Bank; Director, Canadian National Railway Company and TELUS Corporation; Chancellor Emeritus, Queen's University; past President and Chair, Art Gallery of Ontario's Board of Trustees.

**Paviter S. Binning**, F.C.M.A.
President of the Corporation and former Chief Financial Officer; 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; former Director, Loblaw Companies Limited.

**Peter B.M. Eby**, B. Comm., M.B.A.(3)
Corporate Director; former Executive, Nesbitt Burns Inc., and its predecessor companies; former Vice-Chairman and Director, Nesbitt Burns Inc.; Director, Leon's Furniture Limited and TD Asset Management USA Funds Inc.; former Director, R. Split II Corp. and Sixty Split Corp.; former Chairman, Olympic Trust.

**Darren Entwistle**, B.A., M.B.A., LL.D.(5)
President, Chief Executive Officer and Director, TELUS Corporation; Director, Canadian Board Diversity Council, Canadian Council of Chief Executives; former Director, TD Bank Financial Group and The Toronto-Dominion Bank.

**Anthony R. Graham**, LL.D.(1,3,4)
President and Director, Wittington Investments, Limited, Selfridges Group Limited; President and Chief Executive Officer, Sumarria Inc.; Director, Loblaw Companies Limited, Power Corporation of Canada, Power Financial Corporation, Graymont Limited, Brown Thomas Group Limited, Holt, Renfrew & Co., Limited, Selfridges & Co. Ltd. and Grupo Calidra, S.A. de C.V.; Chairman and Director, President's Choice Bank; Director, Art Gallery of Ontario, Canadian Institute for Advanced Research, Luminato, St. Michael's Hospital and Trans Canada Trail Foundation and Chairman of the Ontario Arts Foundation, the Shaw Festival Theatre Endowment Foundation; former Director, Garbell Holdings Limited.

**John S. Lacey**, B.A.
Chairman of the Advisory Board, Brookfield Private Equity Group; Consultant to the Board and to the Board of Loblaw Companies Limited; former President and Chief Executive Officer, The Oshawa Group; Director, Loblaw Companies Limited, TELUS Corporation and Ainsworth Lumber Co. Ltd.; former Chairman of Alderwoods Group, Inc.; former Director, Canadian Imperial Bank of Commerce.

**Isabelle Marcoux**, B.A., LL.B.(5*)
Chair, Transcontinental Inc.; Director, Rogers Communications Inc., Power Corporation of Canada; Board Member, Board of Trade of Metropolitan Montreal.

**Sarabjit S. Marwah**, B.A., M.A., M.B.A.(2)
Vice-Chairman and Chief Operating Officer, The Bank of Nova Scotia; Director, Cineplex Inc.; Trustee, Hospital for Sick Children; former Director, Torstar Corporation; past Chair, Humber River Regional Hospital.

**J. Robert S. Prichard**, O.C., O.Ont., LL.B., M.B.A., LL.M., LL.D.(1,3*,4)
Non-Executive Chair, Torys LLP; Chair, Bank of Montreal and Metrolinx; former President and Chief Executive Officer, Metrolinx and Torstar Corporation; President Emeritus, University of Toronto; Director, Onex Corporation; former Director, Torstar Corporation, Four Seasons Hotels Inc.; Trustee, Hospital for Sick Children; Member, Canada's Economic Advisory Council and Ontario's Economic Advisory Panel.

**Thomas F. Rahilly**, B.A., M.A., LL.B.(2,3,4,5)
Corporate Director; former Vice-Chairman, RBC Capital Markets; former Director, Wittington Investments, Limited.

**Barbara G. Stymiest,** B.A., F.C.A., F.C.P.A.(2,4*)
Corporate Director; former member of the Group Executive, Royal Bank of Canada; former Chief Executive Officer, TSX Group Inc.; former Executive Vice-President and Chief Financial Officer, BMO Nesbitt Burns; former Partner of Ernst & Young LLP; Director, Blackberry Limited, Sun Life Financial Inc., Canadian Institute for Advanced Research and University Health Network.

(1) Executive Committee
(2) Audit Committee
(3) Governance, Human Resource, Nominating and Compensation Committee
(4) Pension Committee
(5) Environmental, Health and Safety Committee
* Chair of the Committee

## Corporate Officers (includes age and years of service)

**W. Galen Weston**, O.C. (73 and 42 years)
Executive Chairman

**Paviter S. Binning** (53 and 4 years)
President

**Gordon A.M. Currie** (55 and 9 years)
Executive Vice President,
Chief Legal Officer

**Rashid Wasti** (46 and 6 months)
Executive Vice President,
Chief Talent Officer

**Richard Dufresne** (48 and 2 years)
Executive Vice President,
Chief Financial Officer

**Robert A. Balcom** (52 and 20 years)
Senior Vice President,
General Counsel - Canada and Secretary

**Khush Dadyburjor** (47 and 3 years)
Senior Vice President,
Strategy

**Geoffrey H. Wilson** (58 and 27 years)
Senior Vice President,
Investor Relations, Business Intelligence and Communications

**Stacey Caney** (38 and 9 years)
Vice President,
Risk Management and Technology

**Allison Doner** (37 and 9 years)
Vice President,
Controller

**David Farnfield** (50 and 17 years)
Vice President,
Commodities

**Nadeem Mansour** (42 and 1 year)
Vice President,
Internal Audit Services

**John Poos** (57 and 3 years)
Vice President,
Pension and Benefits

**Tamara Rebanks** (46 and 13 years)
Vice President,
Community Affairs

**Adam Walsh** (40 and 9 years)
Vice President,
Legal Counsel

**John Williams** (48 and 3 years)
Vice President,
Treasurer

# Shareholder and Corporate Information

**Executive Office**
George Weston Limited
22 St. Clair Avenue East
Toronto, Canada M4T 2S7
Tel: 416.922.2500
Fax: 416.922.4395
www.weston.ca

**Stock Exchange Listing and Symbols**
The Company's common and preferred shares are listed on the Toronto Stock Exchange and trade under the symbols: "WN", "WN.PR.A", "WN.PR.C", "WN.PR.D" and "WN.PR.E".

**Common Shares**
At year end 2013, there were 127,899,410 common shares issued and outstanding.

The average 2013 daily trading volume of the Company's common shares was 108,435.

**Preferred Shares**
At year end 2013, there were 9,400,000 preferred shares Series I, 8,000,000 preferred shares Series III, 8,000,000 preferred shares Series IV and 8,000,000 preferred shares Series V issued and outstanding.

The average 2013 daily trading volume of the Company's preferred shares was:

Series I: 7,769
Series III: 8,067
Series IV: 6,981
Series V: 8,279

**Common Dividend Policy**
The declaration and payment of dividends on the Company's common shares and the amount thereof 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. 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.

**Common Dividend Dates**
The declaration and payment of quarterly common dividends are made subject to approval by the Board of Directors. The anticipated record and payment dates for 2014 are:

| Record Date | Payment Date |
|---|---|
| March 15 | April 1 |
| June 15 | July 1 |
| Sept. 15 | Oct. 1 |
| Dec. 15 | Jan. 1 |

**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, adjusted for the 4 for 1 stock split (effective May 27, 1986) and the 3 for 1 stock split (effective May 8, 1998), is $1.50 per share. The value on February 22, 1994 was $13.17 per share.

**Printing**: TC Transcontinental Printing www.tcprinting.tc

**Registrar and Transfer Agent**
Computershare Investor Services Inc.
100 University Avenue
Toronto, Canada M5J 2Y1

| | |
|---|---|
| Toll Free Tel: | 1.800.564.6253 (Canada and U.S.A.) |
| International Tel: | 514.982.7555 (direct dial) |
| Fax: | 416.263.9394 |
| Toll Free Fax: | 1.888.453.0330 |

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

**Independent Auditors**
KPMG LLP
Chartered Professional Accountants, Licensed Public Accountants
Toronto, Canada

**Annual Meeting**
The George Weston Limited Annual Meeting of Shareholders will be held on Tuesday May 6, 2014, at 11:00 a.m. at The Royal Conservatory, TELUS Centre for Performance and Learning, Koerner Hall, 273 Bloor Street West, Toronto, Ontario, Canada.

**Trademarks**
George Weston Limited and its subsidiaries own a number of trademarks. These trademarks are the exclusive property of George Weston Limited and its subsidiary companies. Trademarks where used in this report are in italics.

**Investor Relations**
Shareholders, security analysts and investment professionals should direct their requests to Mr. Geoffrey H. Wilson, Senior Vice President, Investor Relations, Business Intelligence and Communications at the Company's Executive Office or by e-mail at investor@weston.ca.

Additional financial information has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR). 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.

This Annual Report includes selected information on Loblaw Companies Limited, a 63.0%-owned public reporting subsidiary company with shares trading on the Toronto Stock Exchange.

Ce rapport est disponible en français.

This 2013 Annual Report was printed in Canada on
Enviro 100, which contains 100% post-consumer waste
and is processed chlorine-free, using biogas energy.

Weston

www.weston.ca