

Making Loblaw the Best Again



2007
Annual Report

2007 Annual Report⁽¹⁾ : Contents

Report to Shareholders	44	Financial Results
1 Management's Discussion and Analysis	85	Glossary of Terms

Financial Highlights⁽²⁾

For the years ended December 29, 2007 and December 30, 2006 (\$ millions except where otherwise indicated)	2007 (52 weeks)	2006 (52 weeks)
Operating Results		
Sales	\$ 29,384	\$ 28,640
Sales excluding the impact of tobacco sales and VIEs ⁽³⁾	27,915	26,834
Operating expenses	28,648	28,351
Operating income	736	289
Adjusted operating income ⁽³⁾	1,034	1,326
Adjusted EBITDA ⁽³⁾	1,589	1,892
Interest expense	252	259
Net earnings (loss)	330	(219)
Cash Flow		
Cash flows from operating activities	1,245	1,180
Free cash flow ⁽³⁾	402	70
Capital investment	613	937
Per Common Share (\$)		
Basic net earnings (loss)	1.20	(.80)
Adjusted basic net earnings ⁽³⁾	2.05	2.72
Dividend rate at year end	0.84	0.84
Cash flows from operating activities	4.55	4.31
Book value	20.22	19.85
Market price at year end	34.07	48.79
Financial Ratios		
Adjusted EBITDA margin ⁽³⁾	5.7%	7.1%
Operating margin	2.5%	1.0%
Adjusted operating margin ⁽³⁾	3.7%	4.9%
Return on average total assets ⁽³⁾	5.8%	2.3%
Return on average shareholders' equity	6.0%	(3.9%)
Interest coverage	2.7:1	1.0:1
Net debt ⁽²⁾ to equity	.67:1	.72:1
Operating Statistics		
Retail square footage (in millions)	49.6	49.7
Average corporate store size (square feet)	60,800	57,400
Average franchise store size (square feet)	28,000	27,400
Corporate stores sales per average square foot (\$)	591	585
Same-store sales growth	2.4%	0.8%
Number of corporate stores	628	672
Number of franchised stores	408	405
Percentage of corporate real estate owned	73%	72%
Percentage of franchise real estate owned	46%	45%

(1) This Annual Report contains forward-looking information. See Forward-Looking Statements on page 2 of this Annual Report for a discussion of material factors that could cause actual results to differ materially from the conclusions, forecasts and projections herein and of the material factors and assumptions that were applied in presenting the conclusions, forecasts and projections presented herein. This Annual Report must be read in conjunction with Loblaw Companies Limited's filings with securities regulators made from time to time, all of which can be found at www.sedar.com and at www.loblaw.ca.

(2) For financial definitions and ratios refer to the Glossary of Terms on page 85.

(3) See Non-GAAP Financial Measures on page 40.

Report to Shareholders⁽¹⁾

2007 Highlights

For the years ended December 29, 2007 and December 30, 2006 (\$ millions except where otherwise indicated)	2007 (52 weeks)	2006 (52 weeks)	Change
Sales	\$ 29,384	\$ 28,640	2.6%
Operating income	736	289	154.7%
Net earnings (loss)	330	(219)	250.7%
Basic net earnings (loss) per common share (\$)	1.20	(0.80)	250.0%
Same-store sales growth (%)	2.4%	0.8%	
Adjusted EBITDA ⁽²⁾	1,589	1,892	(16.0%)
Adjusted operating income ⁽²⁾	1,034	1,326	(22.0%)
Adjusted operating margin ⁽²⁾	3.7%	4.9%	
Adjusted basic net earnings per common share ⁽²⁾ (\$)	2.05	2.72	(24.6%)
Free cash flow ⁽²⁾	402	70	474.3%

- Same-store sales growth of 2.4% during 2007 compared to 2006.
- Positive volume growth of 1.9% based on retail units sold compared to 2006.
- Sales increases were insufficient to offset margin declines as a result of targeted investments in pricing.
- Free cash flow⁽²⁾ for 2007 increased to \$402 million compared to \$70 million in 2006.

2007 was a year of transformational change, amid intense competition and consequent pressured earnings. Despite these challenges in a difficult year, we have made significant progress towards Making Loblaw the Best Again. We completed the first year of our three-to five-year turnaround and made good progress. Our single-most important accomplishment was the completion of our organizational restructuring. As would be expected, there were challenges with a change of this magnitude but Loblaw now, for the first time ever, can fully leverage its national scale.

We encourage you to read our Business Review Report (issued February 2008) which outlines our achievements in 2007 and priorities for 2008 in Making Loblaw the Best Again. The Business Review Report is available on our website at www.loblaw.ca within the Investor Zone.

We acknowledge and share the disappointment in the reduced earnings of the last two quarters of 2007. However, we view them in the context of the first year of a multi-year turnaround plan and some indications of progress were evident. We experienced sales growth in all of our regions and maintained our market share without adding square footage. We reduced capital expenditures and concentrated on same-store sales growth, rather than space-driven growth, which resulted in delivering significantly improved cash flow. Now we will use a more flexible array of means to maintain our market share by driving comparable sales growth in our existing asset base with the goal of improving returns throughout our business.

Cost reduction has lagged our required pricing investments, which resulted in lower earnings. Clearly maintaining price competitiveness has and will put pressure on margins. Cost control to help rebuild margins over time is a critical focus for management. We are committed to driving costs out of our business. We have made some progress but we need to make more.

(1) To be read in conjunction with "Forward Looking Statements" on page 2 of this Annual Report.

(2) See Non-GAAP Financial Measures on page 40.

Report to Shareholders⁽¹⁾

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

Simplify, Innovate, Grow. These are the three themes that underpin our objective of Making Loblaw the Best Again:

- **Simplify** and sharpen Loblaw by making accountabilities clear and centralizing where it counts, while fixing the basics that matter to customers and matter financially;
- Restore **innovation** to the heart of our culture in food and across all of our control label – make our brands and assortments “worth switching supermarkets for”; and
- **Grow** Loblaw through our Formula for Growth, but spend capital wisely in an over-spaced market.

In 2008, we intend that the progress we made in 2007 towards becoming a more efficient and more effective sales-driven business is solid and sustained. We look forward to 2008 with confidence, as we leave behind the disruption of our restructuring. We can now focus primarily on our customers and our stores.

[signed]

Galen G. Weston

Executive Chairman

Toronto, Canada

March 12, 2008

(1) To be read in conjunction with “Forward Looking Statements” on page 2 of this Annual Report.

Management's Discussion and Analysis

2	1. Forward-Looking Statements	26	11. Risks and Risk Management	
3	2. Overview	26	11.1 Operating Risks and Risk Management	
3	3. Vision and Strategies		Industry and Competitive Environment	
6	4. Key Performance Indicators		Change Management and Execution	
6	5. Financial Performance		Information Technology	
8	5.1 Results of Operations		Supply Chain	
	Sales		Food Safety and Public Health	
	Operating Income		Labour	
	Interest Expense		Franchisees	
	Income Taxes		Employee Future Benefit Contributions	
	Net Earnings		Multi-Employer Pension Plans	
12	5.2 Financial Condition		Third-Party Suppliers	
	Financial Ratios		Excess Inventory	
	Common Share Dividends		Real Estate	
	Outstanding Share Capital		Seasonality	
13	6. Liquidity and Capital Resources		Colleague Development and Retention	
13	6.1 Cash Flows	32	Utility and Fuel Prices	
	Cash Flows from Operating Activities		Environmental, Health and Safety	
	Cash Flows used in Investing Activities		Ethical Business Conduct	
	Cash Flows used in Financing Activities		Legal, Taxation and Accounting	
14	6.2 Sources of Liquidity		Insurance	
	Independent Funding Trust		Holding Company Structure	
16	6.3 Contractual Obligations		32	11.2 Financial Risks and Risk Management
17	6.4 Off-Balance Sheet Arrangements		Liquidity	
	Guarantees		Common Share Market Price	
	Securitization of Credit Card Receivables		Credit	
	Independent Funding Trust		Derivative Instruments	
18	6.5 Derivative Instruments		Foreign Currency Exchange Rate	
			Interest Rate	
19	7. Selected Consolidated Annual Information		33 12. Related Party Transactions	
21	8. Quarterly Results of Operations		34 13. Critical Accounting Estimates	
21	8.1 Results by Quarter	34	13.1 Inventories	
23	8.2 Fourth Quarter Results	35	13.2 Employee Future Benefits	
26	9. Internal Control over Financial Reporting	36	13.3 Goodwill	
26	10. Management's Certification of Disclosure Controls and Procedures	36	13.4 Income Taxes	
		37	13.5 Goods and Services Tax and Provincial Sales Taxes	
		37	13.6 Fixed Assets	
		37	14. Accounting Standards	
		37	14.1 Accounting Standards Implemented in 2007	
		38	14.2 Future Accounting Standards	
		39	15. Outlook	
		40	16. Non-GAAP Financial Measures	
		43	17. Additional Information	

Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") for Loblaw Companies Limited and its subsidiaries (collectively, the "Company" or "Loblaw") should be read in conjunction with the consolidated financial statements and the accompanying notes on pages 44 to 83 of this Financial Report. The consolidated financial statements and the accompanying notes have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are reported in Canadian dollars. The consolidated financial statements include the accounts of the Company and its subsidiaries and variable interest entities ("VIEs") that the Company is required to consolidate in accordance with Accounting Guideline 15, "*Consolidation of Variable Interest Entities*", ("AcG 15"). A glossary of terms used throughout this Financial Report can be found on page 85. The information in this MD&A is current to March 12, 2008, unless otherwise noted.

1. Forward-Looking Statements

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

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

In addition to these risks and uncertainties, the material assumptions used in making the forward looking statements contained herein and in particular in the Report to Shareholders, the section entitled "Key Performance Indicators" on page 6 and in the section entitled "Outlook" on page 39 of this Annual Report, include: there is no material change in economic conditions from those of 2007; patterns of consumer spending and preferences are reasonably consistent with historical trends; there is no significant change in competitive conditions, whether related to new competitors or current competitors; there is no unexpected change in the Company's or its competitors' current pricing strategies; the Company's franchised stores perform as expected; anticipated cost savings and operating efficiencies are achieved, including those from the Company's cost reduction and simplification initiatives; there is no unexpected change in the Company's access to liquidity; and there are no significant regulatory, tax or accounting changes or other significant events occurring outside the ordinary course of business.

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

2. Overview

Loblaw, a subsidiary of George Weston Limited, is Canada's largest food distributor and a leading provider of general merchandise, drugstore and financial products and services. Traditional food offerings remain at the core of the Company's business. Through its various operating banners, including 628 corporate stores and 408 franchised stores, Loblaw is committed to providing Canadians across the country with a one-stop destination in meeting their food and everyday household needs. For 50 years, the Company has supplied the Canadian market with innovative products and services through a portfolio of store formats across Canada.

Corporate owned store banners include *Atlantic Superstore*, *Dominion*⁽¹⁾ (in Newfoundland and Labrador only), *Extra Foods*, *Loblaws*, *Maxi*, *Maxi & Cie*, *Provigo*, the *Real Canadian Superstore* and *Zehrs* and wholesale outlets operating as *Cash & Carry*, *Presto* and *The Real Canadian Wholesale Club*. The Company's franchised and associated stores operate under the trade names *Atlantic SaveEasy*, *Fortinos*, *no frills*, *SuperValu*, *Valu-mart* and *Your Independent Grocer*. The store network is supported by 25 Company-operated and three third-party warehouse facilities located across Canada as well as temporary storage facilities when required.

The Company offers a strong control label program, including the *President's Choice*, *no name* and *Joe Fresh Style* brands. In addition, the Company makes available to consumers *President's Choice Financial* services and products, including the *President's Choice Financial MasterCard*®, and *PC Financial* auto, home, travel and pet insurance. The Company also offers *PC Mobile* phone service, as well as a loyalty program known as *PC points*.

The retail industry in Canada is highly competitive. The industry is driven primarily by consumer demand, which is impacted by economic trends, changing demographics, ethnic diversity, health and environmental awareness and time availability. Recent consumer trends that dominate the industry include customer's concerns for their own and their family's health, lack of time, increasing demand for value and premium products in one location, a willingness to buy certain general merchandise on food-focused shopping trips and an increasing demand that retailers source ethically and in a way that demonstrates care for the environment and the community.

The Company'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. Generally, the Canadian retail landscape has in recent years been characterized by an increase in square footage that is greater than the increase in consumer demand which has resulted in pressure on retailers to lower their prices and reduce operating and labour costs.

3. Vision and Strategies

Vision

The Company's vision is Making Loblaw the Best Again by implementing the three main imperatives of "Simplify, Innovate, Grow". The Company strives to be consumer focused, cost effective and agile. While accepting prudent operating risks, Loblaw seeks long term, stable growth supported by a strong balance sheet, with the goal of providing sustainable superior returns to its shareholders through a combination of common share price appreciation and dividends.

Strategies

Loblaw's mission is to be Canada's best food, health and home retailer by exceeding customer expectations through innovative products at great prices. Under the principles of Simplify, Innovate, Grow, the Company employs various operating and financial strategies which guide the Company over the long term and represent a philosophy for the way in which it conducts its business.

(1) Trademark used under license.

Management's Discussion and Analysis

Loblaw's three to five year turnaround commenced in 2007 and the Company has made good progress. Loblaw has simplified the organization by more clearly defining accountabilities, eliminating duplication and establishing consistent, simple and efficient processes. A less complex organizational structure and a short list of key performance indicators are expected to lead to more focus in 2008 on customers and store operations, and for the first time ever, to enable Loblaw to fully leverage its national scale.

Innovation is one of the many strengths of Loblaw, most clearly exhibited by its control label offerings. The Company supports innovation based on the belief that providing consumers with new products and convenient services at competitive prices and stimulating shopping environments is critical to its success. Innovation in food and across the Company's entire range of control label products and services make Loblaw brands and assortments "*worth switching supermarkets for*".

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

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

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

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

The Company's long term financial strategies are as follows:

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

The success of these and other plans and strategies discussed in this MD&A may be affected by risks and uncertainties, including those described in the Risks and Risk Management section of this MD&A, found on pages 26 to 33.

The table below summarizes the Company's strategic imperatives and the activities undertaken in 2007 to advance these Simplify and Innovate imperatives.

Simplify	<ul style="list-style-type: none">▪ Organizational restructuring completed for effectiveness and efficiency resulting in a net reduction of approximately 900 employees.▪ New tools and systems utilized for more effective store communication to improve customer service.▪ Improved on-shelf availability of grocery, dairy, frozen, natural value and health and beauty care using the Always Available program by eliminating ineffective store processes.▪ Detailed cost reduction plan initiated identifying cost reduction opportunities in shrink, store labour, the supply chain, and administrative expenses.▪ New Supply Chain and Information System infrastructure roadmaps developed for new forecasting, replenishment, distribution and transportation capabilities that will improve store availability and operational productivity over time.▪ New price checking processes and scorecards implemented to accurately monitor weekly price position against relevant competitors to improve value competitiveness.
Innovate	<ul style="list-style-type: none">▪ PC Signature Campaign resulted in strong sales of <i>PC</i> products such as <i>Blue Menu</i> Lean Burgers, <i>PC</i> Indian Naan flat bread, <i>PC 2X</i> Concentrated Detergent, and <i>PC Organics</i> Baby Food.▪ <i>Joe Fresh Style</i> extended into <i>Joe Kids</i> and intimates lines into 350 stores from 100 with positive sales and plans to expand into all stores over 80,000 square feet.▪ Repositioning of President's Choice Home Line of Products to offer superior functional advantage at a reduced cost.▪ Continued Product Development excellence resulted in the launch of over 600 new food products, primarily in the <i>PC</i> line e.g., <i>PC Organics</i>, <i>Blue Menu</i>, <i>Mini Chefs</i>, and <i>PC Green</i>, plus over 800 new home products.▪ Best Format teams which act as retail "brand managers" of Hard Discount, Superstore, and Great Food stores created go-to-market strategies for Hard Discount and Superstore formats based on competitive considerations and market opportunities. The strategy for Great Food stores is under development.
Grow ⁽¹⁾	<ul style="list-style-type: none">▪ Best Format reflects Loblaw's advantage of having three retail formats to place in the market to maximize the Company's ability to serve our customers and maximize our market share. The three formats offer distinctive shopping experiences for customers:<ul style="list-style-type: none">- Great Food stores will offer the best fresh and packaged food, knowledgeable staff, outstanding customer service, and an exciting shopping experience.- Hard discount stores will deliver the lowest effective prices and traffic oriented promotions for customers willing to make tradeoffs on brands and service for price and convenience.- Superstores will offer great value in an innovative and fun one-stop shop for great food, healthy living, and a stylish home.▪ Fresh First is Loblaw's goal to provide the best fresh food in Canadian grocery.▪ Control Label Advantage is at heart of the Company's innovation culture. Through continued product development excellence, Loblaw will strive to grow its control label sales to 30% of total sales, from the current penetration of 24%.▪ 10% Joe is the Company's vision to grow the <i>Joe Fresh Style</i> brand to a \$1 billion brand through line extensions into Kids and Intimates, as well as rolling out <i>Joe Fresh Style</i> departments from the current 350 stores to all stores larger than 80,000 square feet.▪ Health, Home and Wholesome is the Company's goal to be recognized as making healthy living affordable for all Canadians with such offerings as <i>Blue Menu</i> and <i>PC Organics</i> lines, as well as fresh foods.▪ Priced Right is Loblaw's commitment to provide the best value-for-money, when compared to all relevant shopping choices. Pricing investments will be made in those formats, categories and product lines that are most important to customers.▪ The continued roll out of the Always Available program will address the in-store replenishment processes focusing on providing the best availability of any food and general merchandise retailer in Canada.▪ The Company's single most important asset is its over 140,000 store and store support colleagues: "Friendly Colleagues, Motivated To Serve". Loblaw is investing so that the Company can deliver on this promise to our customers. This includes on the job training to allow Loblaw colleagues to better serve customers' needs.

(1) To be read in conjunction with "Forward Looking Statements" on page 2 of this Annual Report.

Management's Discussion and Analysis

Board Commitment

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

4. Key Performance Indicators

As a result of the priorities established under the new management's Formula for Growth and following the 100 Day Review, which was completed in early 2007, the Company has identified and is developing specific key performance indicators to measure the progress of short and long term strategies. These key performance indicators will measure format same-store sales, fresh first, penetration of control label sales, *Joe Fresh Style* brand sales in apparel and related merchandise, price index level targets, targeted on-shelf availability and employee satisfaction. In 2007, targets were developed that will enable management to assess progress made on each imperative as well as the effectiveness of implementation of the Company's strategy. The Company believes that if it successfully implements and executes its various strategic imperatives in support of its long term operating and financial strategies, it will be well positioned to pursue its vision of providing sustainable returns to its shareholders.

Additional key financial performance indicators are set out below:

Key Financial Performance Indicators

	2007 (52 weeks)	2006 (52 weeks)
Sales growth	2.6%	3.7%
Sales growth excluding the impact of tobacco sales and VIEs ⁽¹⁾	4.0%	5.0%
Basic net earnings per common share increase (decrease)	250.0%	(129.4%)
Adjusted basic net earnings per common share ⁽¹⁾ (decrease)	(24.6%)	(18.8%)
Cash flows from operating activities (\$ millions)	\$ 1,245	\$ 1,180
Free cash flow ⁽¹⁾ (\$ millions)	\$ 402	\$ 70
Net debt ⁽¹⁾ to equity ratio	.67:1	.72:1
Return on average shareholders' equity	6.0%	(3.9%)

By effectively implementing the Formula for Growth, management aspires to achieve, on average, 5% sales growth, 10% adjusted net earnings⁽¹⁾ growth and \$250 million of free cash flow^{(1),(2)}

5. Financial Performance

Financial results for 2007 were negatively affected by the short term costs associated with the largest transformation in the Company's history. The need for this transformative process was necessitated by the Company's recent poor financial performance, its assessment of a fast-changing retail environment and a strategic review of processes, structure and key drivers of its operations.

Operating income of \$736 million for 2007 increased by \$447 million, or 154.7%, compared to \$289 million in 2006, and resulted in an operating margin of 2.5% as compared to 1.0% in 2006. The 2006 operating income was negatively affected by an \$800 million non-cash goodwill impairment charge related to the goodwill associated with the acquisition of Provigo Inc. in 1998. Details of specific items that were included in operating income for 2007 and 2006 are described on page 10 of this MD&A.

(1) See Non-GAAP Financial Measures on page 40.

(2) To be read in conjunction with "Forward Looking Statements" on page 2 of this Annual Report.

Adjusted operating income⁽¹⁾ for 2007 decreased by \$292 million, or 22.0%, to \$1,034 million compared to \$1,326 million in 2006. Adjusted operating margin⁽¹⁾ decreased to 3.7% in 2007 compared to 4.9% in 2006 as growth in operating expenses exceeded growth in sales. Adjusted EBITDA margin⁽¹⁾ decreased to 5.7% from 7.1% in 2006. Details of specific items included in adjusted operating income⁽¹⁾ for 2007 and 2006 are described on pages 9 to 10 of this MD&A.

Basic net earnings per common share for 2007 were \$1.20, an increase of \$2.00 when compared to basic net loss per common share of \$0.80 in 2006. Basic net earnings per common share was impacted in 2007 by the following:

- a charge of \$0.04 per common share related to inventory liquidation;
- a charge of \$0.30 per common share for the net effect of stock-based compensation and the associated equity forwards;
- a charge of \$0.53 per common share related to restructuring and other charges;
- a charge of \$0.02 per common share related to the consolidation of VIEs;
- income of \$0.04 cents per common share related to the adjustment to future income tax balances resulting from changes in the Canadian federal and certain provincial statutory income tax rates.

After adjusting for the above-noted items, adjusted basic net earnings per common share⁽¹⁾ were \$2.05 for 2007 compared to \$2.72 in 2006, a decline of 24.6%, which excluded the impact of the following:

- a charge of \$0.17 per common share for the net effect of stock-based compensation and the associated equity forwards;
- a charge of \$0.11 per common share related to restructuring and other charges;
- a charge of \$0.16 cents per common share related to inventory liquidation;
- a charge of \$2.92 per common share related to a goodwill impairment charge;
- a charge of \$0.20 per common share related to an Ontario collective labour agreement;
- a charge of \$0.03 per common share related to a departure entitlement charge;
- income of \$0.06 per common share related to the adjustment to future income tax balances resulting from changes in the Canadian federal and certain provincial statutory income tax rates; and
- income of \$0.01 per common share related to the consolidation of VIEs.

Adjusted basic net earnings per common share⁽¹⁾ decreased in 2007 as a result of Loblaw's continued investment in lower retail prices to drive same-store sales growth in a targeted manner across the country. Sales increases in 2007 were insufficient to offset gross margin declines and increases in operating expenses. Operating expenses in 2007 compared to 2006 included significant incremental costs including restructuring charges and consulting.

In 2007, the Company reduced capital expenditures and concentrated on same-store sales growth, rather than space-driven growth, which resulted in significant improved cash flow. Capital investment, funded through cash flows from operating and financing activities, was \$613 million in 2007, a reduction of \$324 million compared to \$937 million capital investment in 2006. Despite the decision to reduce capital investment, Loblaw experienced total sales growth in all its regions and maintained its market share, during a period of low food price inflation in the market.

In pursuit of improving its value proposition, Loblaw invested in pricing in specific markets by adopting everyday low pricing strategies. The organizational restructuring has enhanced management's ability to identify cost reduction opportunities in shrink, store labour, supply chain, and administrative expenses. However, further cost reductions are required to help rebuild the reduction in margins resulting from the price investments. A detailed cost reduction plan was defined near the end of 2007. Cost reductions remain a critical focus for management moving forward.

The Company's three to five year turnaround commenced in 2007 and the Company has made good progress. The single most important accomplishment has been the organizational restructuring. This is a transformational change that will enable Loblaw, for the first time ever, to fully leverage its national scale. Supply Chain and Information Technology also produced roadmaps that will make the Company's infrastructure more competitive.

(1) See Non-GAAP Financial Measures on page 40.

Management's Discussion and Analysis

5.1 Results of Operations

Sales

Full year sales in 2007 increased \$744 million, or 2.6%, to \$29.4 billion compared to \$28.6 billion in 2006. Total sales excluding the impact of tobacco sales and VIEs⁽¹⁾ increased by \$1.1 billion or 4.0% over 2006.

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

For the years ended December 29, 2007 and December 30, 2006
(\$ millions)

	2007 (52 weeks)	2006 (52 weeks)
Total sales	\$ 29,384	\$ 28,640
Less: Sales attributable to tobacco sales	1,013	1,423
Sales attributable to the consolidation of VIEs	456	383
Sales excluding the impact of tobacco sales and VIEs ⁽¹⁾	\$ 27,915	\$ 26,834

Sales Growth and Same-Store Sales Growth

For the years ended December 29, 2007 and December 30, 2006
(percentage)

	2007 (52 weeks)	2006 (52 weeks)
Total sales growth	2.6%	3.7%
Less: Impact on sales growth attributable to tobacco sales	(1.7%)	(1.2%)
Impact on sales growth attributable to the consolidation of VIEs	0.3%	(0.1%)
Sales growth excluding the impact of tobacco sales and VIEs ⁽¹⁾	4.0%	5.0%
Same-store sales growth	2.4%	0.8%
Same-store sales growth excluding the impact of decreased tobacco sales ⁽¹⁾	3.4%	2.0%

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

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

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

(1) See Non-GAAP Financial Measures on page 40.

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

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

Operating Income

Operating income of \$736 million for 2007 increased \$447 million, or 154.7% compared to \$289 million in 2006 resulting in an increase in operating margin to 2.5% in 2007 from 1.0% in 2006.

Operating Income, Adjusted Operating Income⁽¹⁾, Adjusted EBITDA⁽¹⁾ and Margins⁽¹⁾

(\$ millions except where otherwise indicated)	2007 (52 weeks)	2006 (52 weeks)	Change
Operating income	\$ 736	\$ 289	154.7%
Adjusted operating income ⁽¹⁾	\$ 1,034	\$ 1,326	(22.0%)
Adjusted EBITDA ⁽¹⁾	\$ 1,589	\$ 1,892	(16.0%)
Operating margin	2.5%	1.0%	
Adjusted operating margin ⁽¹⁾	3.7%	4.9%	
Adjusted EBITDA margin ⁽¹⁾	5.7%	7.1%	

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

- charge of \$197 million (2006 – nil) related to Project Simplify involving restructuring and streamlining of merchandising and store operations. Costs were comprised of \$139 million for employee termination benefits including severance, additional pension costs resulting from the termination of employees and retention costs; and \$58 million of other costs, primarily consulting. Total restructuring costs under this plan, comprised primarily of severance costs, are now anticipated to be approximately \$200 million, with the remaining costs to be expensed in 2008;
- charge of \$9 million (2006 – \$8 million) in connection with the previously announced plan to restructure the Company's supply chain network;
- charge of \$16 million (2006 – \$35 million) in connection with the previously announced closure of certain stores in the Quebec and Atlantic markets and in the wholesale network that were part of store operations restructuring activities;
- charge of \$72 million (2006 – \$37 million) for the net effect of stock-based compensation and the associated equity forwards. The majority of the expense in 2007 included a non-cash loss on equity forwards of \$67 million (2006 – \$32 million) resulting from a decline in the Company's share price during the year;
- charge of \$15 million (2006 – \$68 million) for the liquidation of general merchandise inventory;
- income of \$11 million (2006 – \$8 million) resulting from the consolidation of VIEs;
- nil (2006 – charge of \$1 million) related to the head office move and reorganization of our operation support functions;
- nil (2006 – charge of \$800 million) for a non-cash goodwill impairment charge related to the goodwill established on the acquisition of Provigo Inc. in 1998;
- nil (2006 – charge of \$84 million) related to the ratification of a new four-year collective agreement with members of certain Ontario locals of the UFCW; and
- nil (2006 – charge of \$12 million) related to a departure entitlement charge.

(1) See Non-GAAP Financial Measures on page 40.

Management's Discussion and Analysis

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

(\$ millions)	Costs Recognized 2007 (52 weeks)	Costs Recognized 2006 (52 weeks)	Costs Recognized 2005 (52 weeks)	Total Expected Costs	Total Expected Costs Remaining
Project Simplify	\$ 197	\$ –	\$ –	\$ 200	\$ 3
Store operations	16	35	–	51	–
Supply chain network	9	8	62	90	11
Office move and reorganization of the operation support functions	–	1	24	25	–
Total restructuring and other charges	\$ 222	\$ 44	\$ 86	\$ 366	\$ 14

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

After adjusting for the above noted items, adjusted operating income⁽¹⁾ for 2007 decreased by \$292 million, or 22.0% to \$1,034 million compared to \$1,326 million in 2006. Adjusted operating margin⁽¹⁾ decreased to 3.7% in 2007 compared to 4.9% in 2006 as growth in operating expenses exceeded growth in sales. Adjusted EBITDA margin⁽¹⁾ decreased to 5.7% from 7.1% in 2006.

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

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

Interest Expense

Interest expense consists primarily of interest on short and long term debt, interest on financial derivative instruments net of interest income earned on short term investments and interest capitalized to fixed assets. In 2007, total interest expense decreased \$7 million, or 2.7%, to \$252 million from \$259 million in 2006.

Interest on long term debt was \$285 million compared to \$284 million in 2006. The 2007 weighted average fixed interest rate on long term debt (excluding capital lease obligations) was 6.6% (2006 – 6.7%) and the weighted average term to maturity was 16 years (2006 – 17 years).

(1) See Non-GAAP Financial Measures on page 40.

Interest on financial derivative instruments includes the net effect of the Company's interest rate swaps, cross currency basis swaps and equity forwards, and amounted to a charge of \$12 million in 2007 (2006 – \$7 million). The change in interest on financial derivative instruments was due mainly to an increase in United States short term interest rates and the cumulative loss transferred from Other Comprehensive Income and subsequent change in fair market value of the interest rate swaps previously designated as a cash flow hedge of the variable interest rate exposure on commercial paper. Net short term interest income in 2007 was \$23 million (2006 – \$11 million). This change was due primarily to a decrease in short term debt.

During 2007, \$22 million (2006 – \$21 million) of interest incurred on debt related to real estate properties under development was capitalized to fixed assets.

Analysis of Long Term Financing Costs

(\$ millions except where otherwise indicated)	2007 (52 weeks)	2006 (52 weeks)
Total long term debt at year end (including portion due within one year)	\$ 4,284	\$ 4,239
Interest on long term debt	\$ 285	\$ 284
Weighted average fixed interest rate on long term debt (excluding capital lease obligations)	6.6%	6.7%

Income Taxes

The Company's 2007 effective income tax rate decreased to 31.0% from 826.7% in 2006. The effective income tax rate in 2006 before the impact of the non-deductible goodwill impairment charge was 29.9%, as presented in note 7 to the consolidated financial statements. The increase from 29.9% in 2006 to 31.0% in 2007 was mainly the result of the following factors:

- a change in the proportion of taxable income earned across different tax jurisdictions; and
- an \$11 million reduction (2006 – \$16 million) to the future income tax expense recognized as a result of the change in the Canadian federal and certain provincial statutory income tax rates, the cumulative effect of which was included in the consolidated financial statements at the time of substantive enactment.

Net Earnings

In 2007, net earnings increased \$549 million to \$330 million from a net loss of \$219 million in 2006 and basic net earnings per common share increased \$2.00 to a basic net earnings per common share of \$1.20 from a basic net loss per common share of \$0.80 in 2006 due to the factors described in the preceding sections.

Management's Discussion and Analysis

5.2 Financial Condition

Financial Ratios

The net debt⁽¹⁾ to equity ratio continued to be within the Company's internal guideline of less than 1:1. The 2007 net debt⁽¹⁾ to equity ratio was .67:1 compared to the 2006 ratio of .72:1. In 2006, the non-cash goodwill impairment charge negatively impacted the net debt⁽¹⁾ to equity ratio by .10:1 as a result of an \$800 million reduction in shareholders' equity.

Cash flows from operating activities cover a large portion of the Company's funding requirements and in 2007 exceeded the capital investment program. In 2007, funding requirements resulted primarily from the capital investment program, the funding of the credit card receivables, after securitization and dividends paid on the Company's common shares.

In 2007, shareholders' equity increased \$104 million, or 1.9%, to \$5.5 billion. The increase in operating income resulted in an interest coverage ratio of 2.7 times in 2007 compared to 1.0 times in 2006. The goodwill impairment charge was a significant non-cash item in operating income in 2006, which adversely impacted the interest coverage ratio by approximately 3.1 times.

At year end, the working capital position increased over the prior year. The 2007 return on average total assets⁽¹⁾ was 5.8% compared to 2.3% in 2006. The 2007 return on average shareholders' equity was 6.0% compared to the 2006 return of (3.9)%. The five year average return on shareholders' equity was 10.2% (2006 – 12.5%).

Common Share Dividends

The Company has paid quarterly dividends on its common shares for over 50 years. The declaration and payment of dividends and the amount thereof are at the discretion of the Board, which takes into account the Company's financial results, capital requirements, available cash flow and other factors the Board considers relevant from time to time. Over the long term, the Company's objective is for its dividend payment ratio to be in the range of 20% to 25% of the prior year's adjusted basic net earnings per common share⁽¹⁾. Currently, there is no restriction that would prevent the Company from paying dividends at historical levels. During 2007, the Board declared quarterly dividends of 21 cents per common share. The 2007 annualized dividend per common share of 84 cents was equal to 30.9% of the 2006 adjusted basic net earnings per common share⁽¹⁾. Subsequent to year end, the Board declared a quarterly dividend of 21 cents per common share, payable April 1, 2008.

Outstanding Share Capital

The Company's outstanding share capital is comprised of common shares. An unlimited number of common shares is authorized and 274,173,564 common shares were issued and outstanding at year end. Further information on the Company's outstanding share capital is provided in note 19 to the consolidated financial statements.

At year end, a total of 6,532,756 stock options were outstanding and represented 2.4% of the Company's issued and outstanding common shares, which was within the Company's guideline of 5%. Further information on the Company's stock-based compensation is provided in note 21 to the consolidated financial statements.

(1) See Non-GAAP Financial Measures on page 40.

6. Liquidity and Capital Resources

6.1 Cash Flows

Major Cash Flow Components

(\$ millions)	2007 (52 weeks)	2006 (52 weeks)	Change
Cash flows from (used in):			
Operating activities	\$ 1,245	\$ 1,180	\$ 65
Investing activities	\$ (671)	\$ (1,308)	\$ 637
Financing activities	\$ (472)	\$ (120)	\$ (352)

Cash Flows from Operating Activities

2007 cash flows from operating activities increased to \$1,245 million compared to \$1,180 million in 2006. The improvement in cash flows from operating activities for the year was mainly due to an increase of \$552 million in net earnings before minority interest, an increase of \$178 million in restructuring charges, an increase of \$110 million in other operating activities and a decrease of \$800 million from the effect of a goodwill impairment charge recorded in 2006. The change in other operating activities was primarily driven by an increase in accrued benefit plan liability, due to changes in funding and expenses for pension, post-retirement and post-employment benefits, and an increase in unrealized equity forwards payable.

Cash Flows used in Investing Activities

2007 cash flows used in investing activities were \$671 million compared to \$1,308 million in 2006. The majority of the change in cash flows used in investing activities resulted from a decline in capital investments of \$324 million; less movement in short term investments from cash and cash equivalents relative to year end, when compared to the prior year, due to the change in the term to maturity profile of the Company's short term investments resulting in an inflow of \$292 million; and an increase in proceeds from fixed asset sales of \$124 million. These were partially offset by an outflow of \$156 million due to an increase in credit card receivables, after securitization.

Capital investment amounted to \$613 million (2006 – \$937 million) for the year as the Company restrained capital spending in an over-spaced market. Approximately 31% (2006 – 38%) of the capital investment was for new store development, expansions and land, approximately 43% (2006 – 51%) for store conversions and remodels, and approximately 26% (2006 – 11%) for infrastructure investment. The continued capital investment activity benefited all regions to varying degrees and strengthened the existing store base. Some of the new, larger stores replaced older, smaller, less efficient stores that did not offer the broad range of products and services demanded by today's consumer.

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

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

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

Management's Discussion and Analysis

During 2007, the Company also generated \$223 million (2006 – \$99 million) from fixed asset sales.

Capital Investment and Store Activity

	2007 (52 weeks)	2006 (52 weeks)	Change
Capital investment (\$ millions)	\$ 613	\$ 937	\$ (324)
Retail square footage (in millions)	49.6	49.7	(0.2%)
Number of corporate stores	628	672	(6.5%)
Number of franchised stores	408	405	0.7%
Percentage of corporate real estate owned	73%	72%	
Percentage of franchise real estate owned	46%	45%	
Average store size (sq. ft.)			
Corporate	60,800	57,400	5.9%
Franchised	28,000	27,400	2.2%

Cash Flows used in Financing Activities

Cash flows used in financing activities increased to \$472 million in 2007 compared to \$120 million in 2006 mainly due to the repayment of commercial paper and the timing of one additional quarterly dividend payment in 2007 compared to last year.

During the first quarter of 2007, Loblaw renewed its Normal Course Issuer Bid to purchase on the Toronto Stock Exchange, or enter into equity derivatives to purchase, up to 13,708,678 of the Company's common shares, representing approximately 5% of the common shares outstanding. In accordance with the requirements of the Toronto Stock Exchange, Loblaw may purchase its shares at the then market prices of such shares. The Company intends to renew its Normal Course Issuer Bid in 2008. The Company did not purchase any shares under its Normal Course Issuer Bid during 2007 or 2006.

6.2 Sources of Liquidity

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

In the first quarter of 2007, the Company entered into the 364-day revolving committed credit facility of \$500 million, provided by several banks for general corporate purposes, which matures in March 2008 and does not have any financial covenants. At the end of the year, no amounts were drawn on the committed or uncommitted facilities. Borrowings under these credit facilities are based on short term floating interest rates.

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

Securitization of credit card receivables provides President's Choice Bank ("PC" Bank), a wholly owned subsidiary of the Company, with an additional source of funds for the operation of its business. Under PC Bank's securitization program, a portion of the total interest in the credit card receivables is sold to independent trusts. PC Bank securitized an aggregate \$225 million of credit card receivables during 2007 (2006 – \$240 million). In the absence of securitization, the Company would be required to raise alternative financing by issuing additional debt or equity instruments. Further information about PC Bank's credit card receivables and securitization is provided in notes 1 and 10 to the consolidated financial statements and in the Off-Balance Sheet Arrangements section of this MD&A.

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

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

In the normal course of business, the Company enters into certain arrangements, such as providing comfort letters to third-party lenders in connection with financing activities of certain franchisees, with no recourse liability to the Company. In addition, the Company establishes standby letters of credit used in connection with certain obligations related to the financing program for its independent franchisees, securitization of *PC* Bank’s credit card receivables, real estate transactions and benefit programs. At year end, the aggregate gross potential liability related to the Company’s standby letters of credit was approximately \$354 million (2006 – \$333 million), against which the Company had \$444 million (2006 – \$371 million) in credit facilities available to draw on.

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

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

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

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

The Company’s ability to obtain funding from external sources may be restricted by further downgrades in the Company’s credit ratings, should the Company’s financial performance and condition deteriorate. In addition, credit and capital markets are subjected to inherent global risks that may negatively affect the Company’s access and ability to fund its short term and long term debt requirements. The Company mitigates these risks by actively maintaining appropriate levels of cash and cash equivalents, actively monitoring market conditions and diversifying its sources of funding and maturity profile. The Company also employs risk management strategies including forward-looking liquidity contingency plans.

Independent Funding Trust

Certain independent franchisees of the Company obtain financing through a structure involving independent trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. The gross principal amount of loans issued to the Company’s independent franchisees outstanding as of year end 2007 was \$418 million (2006 – \$419 million) including \$153 million (2006 – \$124 million) of loans payable by VIEs consolidated by the Company in 2007. Based on a formula, the Company has agreed to provide credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trust equal to approximately 10% of the principal amount of the loans outstanding at any point in time, \$44 million (2006 – \$44 million) as of year end 2007. This credit enhancement allows the independent funding trust to provide favourable financing terms to the Company’s independent franchisees. As well, each independent franchisee provides security to the

Management's Discussion and Analysis

independent funding trust for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and the Company has not, within a specified time period, assumed the loan, or the default is not otherwise remedied, the independent funding trust shall assign the loan to the Company and draw upon this standby letter of credit. The Company has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit.

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

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

6.3 Contractual Obligations

The following illustrates certain of the Company's significant contractual obligations and discusses other obligations as at December 29, 2007:

Summary of Contractual Obligations

(\$ millions)	Payments due by year						Total
	2008	2009	2010	2011	2012	Thereafter	
Long term debt (including capital lease obligations)	\$ 432	\$ 149	\$ 326	\$ 376	\$ 24	\$ 2,977	\$ 4,284
Operating leases ⁽¹⁾	192	172	150	128	108	673	1,423
Contracts for purchases of real property and capital investment projects ⁽²⁾	109	4					113
Purchase obligations ⁽³⁾	574	572	564	564	372	-	2,646
Total contractual obligations	\$ 1,307	\$ 897	\$ 1,040	\$ 1,068	\$ 504	\$ 3,650	\$ 8,466

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

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

(3) 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. These purchase obligations do not include purchase orders issued or agreements made in the ordinary course of business which are solely for goods which are meant for resale, nor do they include any contracts which may be terminated on relatively short notice or with relatively insignificant cost or liability to the Company.

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

- future payments of accrued benefit plan liability, principally post-retirement benefits, depend on when and if retirees submit claims;
- future payments of income taxes depend on the levels of taxable earnings and income tax rates;
- future payments of the share appreciation value on employee stock options depend on whether employees exercise their stock options, the market price of the Company's common shares on the exercise date and the manner in which they exercise those stock options;
- future payments of restricted share units depend on the market price of the Company's common shares;
- future payments related to equity forwards depend on the market price of the Company's common shares; and
- future payments of insurance claims can extend over several years and depend on the timing of anticipated settlements and results of litigation.

6.4 Off-Balance Sheet Arrangements

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

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

Guarantees

The Company has entered into various guarantee agreements including standby letters of credit in relation to the securitization of *PC* Bank's credit card receivables, third-party financing made available to the Company's independent franchisees, and obligations to indemnify third parties in connection with leases, business dispositions and other transactions in the normal course of the Company's business. For a detailed description of the Company's guarantees, see note 23 to the consolidated financial statements.

Securitization of Credit Card Receivables

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

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

Management's Discussion and Analysis

As at year end 2007, the total amount of securitized credit card receivables outstanding which *PC* Bank continues to service was \$1.5 billion (2006 – \$1.3 billion) and the associated retained interests amounted to \$8 million (2006 – \$5 million). The standby letter of credit supporting a portion of these securitized receivables amounted to approximately \$89 million (2006 – \$68 million). During 2007, *PC* Bank received income of \$141 million (2006 – \$114 million) in securitization revenue from the independent trusts relating to the securitized credit card receivables. In the absence of securitization, the Company would be required to raise alternative financing by issuing debt or equity instruments. Further disclosure regarding this arrangement is provided in notes 10 and 23 to the consolidated financial statements.

Independent Funding Trust

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

Neither the independent funding trust nor the Company can voluntarily terminate the agreement prior to December 2009, and following that date only upon six months' prior notice. Automatic termination of the agreement can only occur if specific, predetermined events occur and are not remedied within the time periods required including downgrades of the Company below a long term credit rating of "A (low)" or a short term credit rating of "R-1 (low)" as issued by DBRS. On February 7, 2008, DBRS downgraded the Company's long term credit rating to "BBB (high)" from "A (low)" and also lowered the Company's short term credit rating to "R-2 (high)" from "R-1 (low)". Subsequent to the DBRS downgrades, the Company was notified that an Event of Termination of the independent funding trust agreement for the Company's franchisees had occurred as a result of the credit rating downgrades. The \$44 million standby letter of credit provided to the independent funding trust by the Company has not been drawn upon. If such an event were to occur, long term debt in the amount of \$126 million would need to be reclassified to short term liabilities. This amount relates to certain franchisees that are VIEs that the Company currently consolidates. The Company is currently in the process of securing alternative financing with a syndicate of banks in the form of a 364-day committed credit facility for the benefit of its franchisees to address this issue. Any new alternative financing structure, which might be implemented, would need to be reviewed to determine if there are any implications with respect to the consolidation of VIEs.

6.5 Derivative Instruments

The Company uses derivative instruments to manage its exposure to changes in foreign currency exchange rates, interest rates, commodity prices, and the market price of the Company's common shares. Commencing December 31, 2006, the Company adopted accounting standards which impacted the presentation and disclosure of its derivative instruments. With the adoption of these standards, all financial derivative instruments are accounted for in the Company's balance sheet. In addition, non-financial derivative instruments, such as certain contracts that are linked to commodity prices, are recorded at fair value on the consolidated balance sheet unless they are exempt from this treatment based upon expected purchase, sale or usage requirements. Prior to December 31, 2006, interest rate swaps which were designated within a hedging relationship were not recorded on the balance sheet. For a detailed description of the Company's derivative instruments and the related accounting policies, see notes 1, 2 and 22 to the consolidated financial statements.

7. Selected Consolidated Annual Information

The following is a summary of selected consolidated annual information extracted from the Company's audited consolidated financial statements. This information was prepared in accordance with Canadian GAAP and is reported in Canadian dollars. The analysis of the data contained in the table focuses on the trends affecting the financial condition and results of operations over the latest two year period.

Selected Consolidated Annual Information

(\$ millions except where otherwise indicated)	2007 (52 weeks)	2006 (52 weeks)	2005 (52 weeks)
Sales ⁽²⁾	\$ 29,384	\$ 28,640	\$ 27,627
Sales excluding the impact of tobacco sales and VIEs ⁽¹⁾	27,915	26,834	25,558
Net earnings (loss)	330	(219)	746
Net earnings (loss) per common share(\$)			
Basic	1.20	(.80)	2.72
Adjusted basic ⁽¹⁾	2.05	2.72	3.35
Diluted	1.20	(.80)	2.71
Total assets	13,674	13,486	13,761
Long term debt (excluding amount due within one year)	3,852	4,212	4,194
Dividends declared per common share (\$)	.84	.84	.84

(1) See Non-GAAP financial measures on page 40.

(2) During 2006, the Company implemented Emerging Issues Committee Abstract 156, "Accounting by a Vendor for Consideration Given to a Customer (Including a Reseller of the Vendor's Products)" on a retroactive basis. Accordingly certain sales incentives paid to independent franchisees, associates and independent accounts for the prior years have been reclassified between sales and cost of sales, selling and administrative expenses. For a further discussion, see the Accounting Standards implemented in 2006 section included in this MD&A.

2007 was a year of transformational change amid intense competition and pressured earnings. Loblaw's declining financial performance since the beginning of 2005 required action to prevent further erosion. Late in 2006, a significant number of changes in the senior leadership occurred and a strategic review was undertaken which resulted in the identification of a turnaround plan to Make Loblaw the Best Again. The approach was built upon three core pillars:

- **Simplify** and sharpen Loblaw by making accountabilities clear and centralizing where it counts, while fixing the basics that matter to customers and matter financially;
- Restore **innovation** to the heart of the Company's culture in food and across all of its control label – make Loblaw brands and assortments "worth switching supermarkets for"; and
- **Grow** Loblaw through its Formula for Growth, but spend capital wisely in an over-spaced market.

Total sales increased 2.6% and same-store sales increased 2.4% in 2007 compared to 2006. The number of corporate stores decreased to 628 from 672 primarily as a result of the Company's store operations restructuring initiative which included the targeted closure of underperforming stores in early 2007. The number of franchised stores increased marginally to 408 in 2007 from 405 in 2006.

2007 was not an easy year for Loblaw. There were challenges, as would be expected, with an organizational change of such magnitude. Net earnings in 2007 were pressured by the Company's investment in lower retail prices and increased costs including significant expenses in restructuring and consulting. Sales for 2007 increased \$744 million, or 2.6%, to \$29.4 billion compared to \$28.6 billion in 2006. Total sales excluding the impact of tobacco sales and VIEs⁽¹⁾ increased by 4.0%. The factors explaining the change in 2007 sales compared to 2006 were previously discussed on pages 8 to 9 of this MD&A.

(1) See Non-GAAP Financial Measures on page 40.

Management's Discussion and Analysis

Corporate store sales per average square foot increased to \$591 in 2007 from \$585 in 2006.

2007 net earnings increased \$549 million to net earnings of \$330 million and basic net earnings per common share increased \$2.00 to a basic net earnings per common share of \$1.20. This increase included an increase of 154.7% in operating income and a 2.7% decrease in interest expense. The effective income tax rate decreased to 31.0% in 2007 from 826.7% in 2006.

Operating income of \$736 million for 2007 increased by \$447 million, or 154.7%, compared to \$289 million in 2006, and resulted in an operating margin of 2.5% as compared to 1.0% in 2006. The items included in operating income were previously described on page 9 of this MD&A.

Adjusted operating income⁽¹⁾ for 2007 decreased by \$292 million, or 22.0%, to \$1,034 million compared to \$1,326 million in 2006. Adjusted basic net earnings per common share⁽¹⁾ decreased 24.6% to \$2.05 in 2007 from \$2.72 in 2006 and decreased 18.8% to \$2.72 in 2006 from \$3.35 in 2005.

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

Sales in 2006 increased 3.7% to \$28.6 billion from \$27.6 billion in 2005. Sales growth in 2006 included a negative impact of approximately 1.2% from declining tobacco sales, and a negative impact of 0.1% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. Sales excluding the impact of tobacco sales and VIEs⁽¹⁾ were \$26.8 billion, or 5.0% higher, compared to \$25.6 billion in 2005. Same-store sales increased 0.8% and same-store sales growth excluding the impact of decreased tobacco sales⁽¹⁾ increased by 2.0%. Net retail square footage increased 1.2 million square feet, or 2.5%, in 2006 compared to 2005. Corporate store sales per average square foot increased to \$585 in 2006 from \$579 in 2005.

In 2006, net earnings decreased \$965 million compared to 2005, or 129.4%, to a net loss of \$219 million and basic net earnings per common share decreased \$3.52, or 129.4%, to a basic net loss per common share of 80 cents from basic net earnings per common share of \$2.72 in 2005. The decline included a decrease in operating income of \$1,112 million, or 79.4%, to \$289 million compared to \$1,401 million in 2005. Operating income in 2006 was lower than 2005 partially as a result of recording a \$800 million non-cash goodwill impairment charge. The effective income tax rate increased to 826.7% in 2006 from 34.8% in 2005.

Adjusted operating income⁽¹⁾ decreased \$274 million in 2006, or 17.1%, to \$1,326 million from \$1,600 million in 2005. Adjusted operating income⁽¹⁾ in 2006 was adversely impacted from challenges encountered in 2005 during the execution of planned changes to its systems, supply chain and general merchandise areas, including certain supply chain systems conversions and the start-up of a new third-party owned and operated general merchandise warehouse and distribution centre for eastern Canada which handles general merchandise and certain drugstore products. These challenges disrupted the flow of inventory to Loblaw's stores and resulted in additional operating costs. Fixed asset impairment charges were recorded, due in part to a decision in 2006 to suspend plans for a number of sites scheduled for future development as well as higher general merchandise mark downs taken to clear inventory through normal channels.

Adjusted basic net earnings per common share⁽¹⁾ decreased 18.8% to \$2.72 in 2006 from \$3.35 in 2005 and decreased 3.7% to \$3.35 in 2005 from \$3.48 in 2004.

(1) See Non-GAAP Financial Measures on page 40.

Total assets of the Company increased to \$13.7 billion in 2007 from \$13.5 billion in 2006. The increase in total assets was primarily driven by a \$157 million increase in accounts receivable, an increase in other assets of \$133 million, and a decrease in fixed assets of \$102 million. An increase in net credit card receivables was the primary reason for higher accounts receivable. A substantial portion of credit card receivables is sold to independent trusts and the unsecuritized balance net of the allowance for credit losses increased by \$227 million in 2007 and \$74 million in 2006 compared to the previous years respectively. The increase in other assets was primarily due to an increase in unrealized cross currency basis swaps receivable. Fixed assets declined in 2007 as a result of the decision to reduce capital expenditures and concentrate on same-store sales growth rather than space-driven growth in addition to increased sales of fixed assets. Inventory at the end of 2007 remained relatively flat compared to the previous two years. Inventory turns of general merchandise categories are lower than those of food categories, resulting in higher aggregate levels of investment in general merchandise inventory as compared to food inventory. In 2006, goodwill decreased as a result of the non-cash Loblaw goodwill impairment charge.

In 2007, cash flows from operating activities exceeded the funding requirements for the Company including capital expenditures and dividends. Additional details of cash flows were previously discussed on pages 13 to 14 of this MD&A. Free cash flow⁽¹⁾ improved to \$402 million in 2007 compared to \$70 million in 2006 and \$103 million in 2005. In 2006, cash flows from operating activities covered a large portion of the funding requirements for the Company including capital expenditures and dividends. While the Company issued long term debt net of amounts retired in 2005, long term debt was repaid in 2006.

The annualized dividend per common share was equal to 30.9% in 2007 and 25.1% in 2006 of the previous years adjusted basic net earnings per common share⁽¹⁾.

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

During the two year period ended December 29, 2007, the Company implemented several new accounting standards issued by the Canadian Institute of Chartered Accountants (“CICA”). The new accounting standards implemented in 2007 and the resulting impact on the financial position and results of operations are outlined in the Accounting Standards Implemented in 2007 section of this MD&A. The accounting standards implemented in 2006 did not have a material impact on the financial position and results of operations of the Company.

8. Quarterly Results of Operations

8.1 Results by Quarter

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

(1) See Non-GAAP Financial Measures on page 40.

Management's Discussion and Analysis

Summary of Quarterly Results (unaudited)

(\$ millions except where otherwise indicated)	2007					2006				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total (audited)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total (audited)
Sales	\$6,347	\$6,933	\$9,137	\$6,967	\$29,384	\$6,147	\$6,699	\$9,010	\$6,784	\$28,640
Net earnings (loss)	54	119	117	40	330	140	194	203	(756)	(219)
Net earnings (loss) per common share										
Basic (\$)	\$ 0.20	\$ 0.43	\$ 0.43	\$ 0.14	\$ 1.20	\$ 0.51	\$ 0.71	\$ 0.74	\$ (2.76)	\$ (0.80)
Diluted (\$)	\$ 0.20	\$ 0.43	\$ 0.43	\$ 0.14	\$ 1.20	\$ 0.51	\$ 0.71	\$ 0.74	\$ (2.76)	\$ (0.80)

Sales growth in 2007 was impacted by various factors. Sales and same-store sales growth were positive in all four quarters of 2007 compared to 2006. Sales growth during the first three quarters of 2007 continued to be negatively impacted by the loss of tobacco sales as discussed previously. Tobacco sales are not a large earnings contributor. Quarterly same-store sales growth for 2007 for the first through fourth quarters of 2007 were 2.4%, 2.7%, 1.6%, and 2.6%, respectively. Quarterly same-store sales growth excluding the impact of decreased tobacco sales⁽¹⁾ for the first through fourth quarters of 2007 were 4.0%, 4.2%, 2.8%, and 2.7%, respectively.

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

Net retail square footage decreased in 2007 by 0.1 million square feet, to 49.6 million square feet, with no significant changes in any quarters during the year.

Fluctuations in quarterly net earnings during 2007 reflect the impact of a number of specific charges outlined previously including the implementation of transformative changes. Solid sales were achieved in all four quarters of 2007 but earnings were pressured from investments in pricing, particularly in the third and fourth quarters as cost reduction lagged the pricing investments.

Interest expense was reasonably consistent during each quarter of 2007 and was \$252 million in 2007 compared to \$259 million in 2006.

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

(1) See Non-GAAP Financial Measures on page 40.

8.2 Fourth Quarter Results

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

Selected Consolidated Information for the Fourth Quarter (unaudited)

(\$ millions except where otherwise indicated)	2007 (12 weeks)	2006 (12 weeks)
Sales	\$ 6,967	\$ 6,784
Sales excluding the impact of tobacco sales and VIEs ⁽¹⁾	6,640	6,450
Operating income (loss)	134	(695)
Adjusted operating income ⁽¹⁾	221	286
Interest expense	59	60
Income taxes	27	2
Net earnings (loss)	40	(756)
Net earnings (loss) per common share (\$)		
Basic	0.14	(2.76)
Adjusted basic ⁽¹⁾	0.43	.58
Diluted	0.14	(2.76)
Cash flows from (used in):		
Operating activities	508	777
Investing activities	(230)	(409)
Financing activities	(166)	(267)
Dividends declared per common share (\$)	.21	.21

Total sales for the fourth quarter of 2007 increased \$183 million, or 2.7%, to \$7.0 billion compared to \$6.8 billion in the fourth quarter of 2006. Sales volume based on retail units sold grew by 3.6% (2006 – 2.4%) in the fourth quarter compared to the same period last year. Same-store sales increased by 2.6%. Total sales excluding the impact of tobacco sales and variable interest entities⁽¹⁾ increased by 2.9%.

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

For the periods ended December 29, 2007 and December 30, 2006 (unaudited) (\$ millions)	2007 (12 weeks)	2006 (12 weeks)
Total sales	\$ 6,967	\$ 6,784
Less: Sales attributable to tobacco sales	219	242
Sales attributable to the consolidation of VIEs	108	92
Sales excluding the impact of tobacco sales and VIEs ⁽¹⁾	\$ 6,640	\$ 6,450

(1) See Non-GAAP Financial Measures on page 40.

Management's Discussion and Analysis

Sales Growth and Same-Store Sales Growth

For the periods ended December 29, 2007 and December 30, 2006 (unaudited) (percentage)	2007 (12 weeks)	2006 (12 weeks)
Total sales growth	2.7%	3.5%
Less: Impact on sales growth attributable to tobacco sales	(0.4%)	(2.0%)
Impact on sales growth attributable to the consolidation of VIEs	0.2%	(0.2%)
Sales growth excluding the impact of tobacco sales and VIEs ⁽¹⁾	2.9%	5.7%
Same-store sales growth	2.6%	1.3%
Same-store sales growth excluding the impact of decreased tobacco sales ⁽¹⁾	2.7%	3.3%

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

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

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

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

Operating income of \$134 million for the fourth quarter of 2007 increased by \$829 million, or 119.3%, compared to an operating loss of \$695 million in 2006. Operating margin was 1.9% compared to (10.2%) in the fourth quarter of 2006. The 2006 operating loss was affected by an \$800 million non-cash goodwill impairment charge related to the goodwill associated with the acquisition of Provigo Inc. in 1998.

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

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

(1) See Non-GAAP Financial Measures on page 40.

- nil (2006 – charge of \$84 million) related to the ratification of a new four-year collective agreement with members of certain Ontario locals of the UFCW.

After adjusting for the above-noted items, adjusted operating income⁽¹⁾ in the fourth quarter of 2007 decreased by \$65 million, or 22.7%, to \$221 million compared to \$286 million in the fourth quarter of 2006. Adjusted operating margin⁽¹⁾ decreased to 3.3% in the fourth quarter of 2007 compared to 4.4% in 2006 as growth in operating expenses exceeded growth in sales.

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

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

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

Adjusted EBITDA⁽¹⁾ and EBITDA margin⁽¹⁾ for the fourth quarter were \$349 million and 5.3%, respectively. For the comparable period of 2006, adjusted EBITDA⁽¹⁾ and EBITDA margin⁽¹⁾ were \$414 million and 6.4%, respectively.

Total interest expense for the fourth quarter of 2007 was \$59 million, similar to the \$60 million interest expense in the fourth quarter of 2006.

The effective income tax rate for the fourth quarter of 2007 was 36.4% compared to negative 0.3% in 2006. This significant change in the effective income tax rate was due to the non-cash goodwill impairment charge recorded in the fourth quarter of 2006 which is non-deductible for income tax purposes. In addition, the effective income tax rate was impacted due to the change in the proportion of taxable income earned across the different tax jurisdictions in which the Company operated. A reduction to the future income tax expense was recognized in the fourth quarter of 2007 as a result of the change in the Canadian statutory income tax rates.

Net earnings for the quarter were \$40 million, an increase of \$796 million compared to a net loss of \$756 million during the same period in 2006. Basic net earnings per common share were \$0.14, an increase of \$2.90, or 105.1%, from a basic net loss per common share of \$2.76 in the fourth quarter of 2006. Adjusted basic net earnings per common share⁽¹⁾ decreased \$0.15, or 25.9%, to \$0.43 in 2007 from \$0.58 in 2006.

Fourth quarter cash flows from operating activities were \$508 million in 2007 compared to \$777 million in 2006. The decrease was mainly due to the change in non-cash working capital, primarily as a result of changes in inventory and accounts payable and accrued liabilities. Fourth quarter cash flows used in investing activities were \$230 million in 2007 compared to \$409 million in 2006, primarily driven by an increase in proceeds from fixed asset sales of \$157 million. Capital investment for the fourth quarter amounted to \$173 million (2006 – \$261 million). Fourth quarter cash flows used in financing activities were \$166 million in 2007 compared to \$267 million in 2006 mainly due to changes in commercial paper levels partially offset by changes in short term debt.

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

(1) See Non-GAAP Financial Measures on page 40.

Management's Discussion and Analysis

9. Internal Control over Financial Reporting

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

Management has concluded that, as of December 29, 2007, a previously reported weakness no longer exists in the design of the Company's internal control over financial reporting in the area of inventory controls. This design weakness was first identified in the first quarter of 2007 and was caused primarily by the lack of sufficient compensating controls in the absence of a perpetual inventory system.

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

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

Other than the remediation steps discussed above, there was no change in the Company's internal controls over financial reporting that occurred during the 12 weeks ended December 29, 2007 that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

10. Management's Certification of Disclosure Controls and Procedures

Management is responsible for designing disclosure controls and procedures to provide reasonable assurance that all material information relating to the Company and its subsidiaries is gathered and reported to senior management on a timely basis so that appropriate decisions can be made regarding public disclosure. As required by Multilateral Instrument 52-109 (Certification of Disclosure in Issuers' Annual and Interim Filings) of the Canadian Securities Administrators, the Executive Chairman, as Chief Executive Officer, and the Chief Financial Officer have evaluated the effectiveness of such disclosure controls and procedures and have concluded that the Company's disclosure controls and procedures were effective as at December 29, 2007.

11. Risks and Risk Management

11.1 Operating Risks and Risk Management

In 2007, the Company assessed key operating risks by conducting risk interviews with members of the senior management team. Risks identified through these interviews were analyzed and discussed as part of the Company's annual business planning process and were also factored into the development of a risk-based internal audit plan.

Descriptions of the risks and risk management strategies identified through risk interviews and the business planning process are included in the operational risks discussed below, any of which has the potential to negatively affect the financial performance of the Company. The Company has operating and risk management strategies, including insurance programs, which help to mitigate the potential financial impact of these operating risks. While the Company employs strategies to minimize these risks, these strategies do not guarantee that events or circumstances will not occur which could negatively affect the Company's financial condition and performance.

Industry and Competitive Environment

The retail industry in Canada is highly competitive. The industry is driven primarily by consumer demand, which is impacted by economic trends, changing demographics, ethnic diversity, health and environmental awareness and time availability. Recent consumer trends that dominate the industry include customer's concerns for their own and their family's health, lack of time, increasing demand for value and premium products in one location, a willingness to buy certain general merchandise on food-focused shopping trips and an increasing demand that retailers source ethically and in a way that demonstrates care for the environment and the community. If the Company is ineffective in responding to these trends or ineffective in executing its strategies, its financial performance could be negatively impacted.

The Company'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. The Company is also subject to competitive pressures from new entrants into the marketplace and from the expansion of existing competitors, particularly those expanding into the grocery market. These competitors may have extensive resources which will allow them to compete effectively with the Company in the long term. Increased competition could adversely affect the Company's ability to achieve its objectives. The Company's inability to compete effectively with its current or any future competitors could result in, among other things, lessening of market share and lower pricing in response to its competitors' pricing activities. Accordingly, the Company's competitive position and financial performance could be negatively impacted.

The Company monitors its market share and the markets in which it operates and will adjust its operating strategies, which include, but are not limited to, closing underperforming stores, relocating stores or reformatting them under a different banner, reviewing pricing and adjusting product offerings and marketing programs. The Company's control label program represents a competitive advantage because it enhances customer loyalty by offering superior value and provides some protection against national brand pricing strategies.

Change Management and Execution

2007 was a year of significant change for the Company. Project Simplify resulted in changes to the Company's structures and business processes. Other significant initiatives in support of the Company's multi-year turnaround plan are underway or planned. While these changes are expected to bring benefits to the Company in the form of a more agile and consumer-focused business, success is dependent on management effectively realizing the intended benefits. Ineffective change management may result in disruptions to the operations of the business or affect the ability of the Company to implement and achieve its strategic objectives due to a lack of clear accountabilities or lack of requisite knowledge, which may cause employees to act in a manner which is inconsistent with Company objectives. Any of these events could negatively impact the Company's performance. The Company may not always achieve the expected cost savings and other benefits of its initiatives.

Information Technology

To support the current and future requirements of the business in an efficient, cost-effective and well-controlled manner, the Company is reliant on information technology (IT) systems. These systems are essential in providing management with the appropriate information for decision making, including its key performance indicators. Any significant failure or disruption of these systems could negatively affect the Company's reputation, revenues and financial performance.

The Company has under invested in its IT infrastructure in the past and its systems were in need of being upgraded. These systems may not properly support the required business processes of the Company. During 2007, an IT strategic plan was developed to guide the new systems environment that Loblaw requires. This plan will begin to be implemented in 2008. Change management risk and other associated risks will arise from the various projects which will be undertaken to upgrade existing systems and introduce new systems to effectively manage the business going forward. Failure by the Company to appropriately invest in information technology or failure to implement information technology infrastructure in a timely or effective manner may negatively impact the Company's financial performance.

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

Management's Discussion and Analysis

Supply Chain

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

Food Safety and Public Health

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

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

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

Labour

A majority of the Company's store level and distribution centre workforce is unionized. Renegotiating collective agreements may result in work stoppages or slowdowns, which could negatively affect the Company's financial performance, depending on their nature and duration. The Company is willing to accept the short term costs of labour disruption in order to negotiate competitive labour costs and operating conditions for the longer term. Significant labour negotiations took place across the Company in 2007 as 73 collective agreements expired and 68 collective agreements were successfully negotiated, which represented a combination of agreements expiring in 2007, those carried over from prior years, and those negotiated early. In 2008, 73 collective agreements affecting approximately 14,000 employees will expire, with the single largest agreement covering approximately 3,100 employees. The Company will also continue to negotiate the 67 collective agreements carried over from 2005, 2006 and 2007. The Company has good relations with its employees and unions and, although it is possible, Loblaw does not anticipate any unusual difficulties in renegotiating these agreements.

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

Franchisees

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

Employee Future Benefit Contributions

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

During 2007, the Company contributed \$74 million (2006 – \$88 million) to its registered funded defined benefit pension plans. During 2008, the Company expects to contribute approximately \$76 million to these plans. This estimate may vary subject to actuarial valuations being completed, market performance and regulatory requirements. The Company also expects to make contributions in 2008 to defined contribution pension plans and multi-employer pension plans, as well as benefit payments to the beneficiaries of the unfunded defined benefit pension and other benefit plans.

Multi-Employer Pension Plans

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

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

Third-Party Suppliers

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

Management's Discussion and Analysis

A large portion of the Company's case-ready meat products are produced by a third party which operates facilities dedicated to Loblaw. The Company's control label products, which are among the most recognized brands in Canada, are manufactured under contract by third-party vendors. In order to preserve the brands' equity, these vendors are held to high standards of quality. The Company also uses third-party logistic services including those in connection with a dedicated warehouse and distribution centre in Pickering, Ontario, a planned warehouse and distribution centre in Ajax, Ontario, and third-party common carriers. Any disruption in these services could interrupt the delivery of merchandise to the stores and therefore could negatively impact sales.

President's Choice Financial banking services are provided by a major Canadian chartered bank. *PC Bank* uses third-party service providers to process credit card transactions, operate call centres and monitor a portion of credit and fraud for the *President's Choice Financial MasterCard®*. To minimize operating risk, *PC Bank* and the Company actively manage and monitor their relationships with all third-party service providers. *PC Bank* has developed a vendor management policy, approved by its Board of Directors, and has established a vendor management team that provides its Board with regular reports on vendor management and risk assessment. *PC Financial* home and auto insurance products are provided by companies within the Aviva Canada group, the Canadian subsidiary of a major international property and casualty insurance provider.

Excess Inventory

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

Real Estate

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

Seasonality

The Company's operations as they relate to food, specifically inventory levels, sales volume and product mix, are impacted to some degree by certain holiday periods in the year. Certain general merchandise items are subject to more seasonal fluctuations.

Colleague Development and Retention

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

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

Utility and Fuel Prices

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

Environmental, Health and Safety

Adverse environmental and health and safety events could negatively affect the Company's reputation and financial performance. The Company has environmental, health and workplace safety programs in place and has established policies and procedures aimed at ensuring compliance with applicable legislative requirements. To this end, the Company employs environmental risk assessments and audits using internal and external resources together with employee awareness programs throughout its operating locations. The Company endeavours to be socially and environmentally responsible, and recognizes that the competitive pressures for economic growth and cost efficiency must be integrated with sound environmental stewardship and ecological considerations. Environmental protection requirements do not and are not expected to have a material effect on the Company's financial performance.

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

Ethical Business Conduct

The Company has adopted a Code of Business Conduct which employees and directors of the Company are required to acknowledge and agree to on a regular basis. The Company has in place an Ethics and Business Conduct Committee which monitors compliance with the Code of Business Conduct and determines how the Company can best ensure it is conducting its business in an ethical manner. The Company has also adopted a Vendor Code of Conduct which outlines its ethical expectations to its vendor community in a number of areas, including social responsibility. Any failure of the Company or its vendors to adhere to these policies, the law or ethical business practices could significantly affect Loblaw's reputation and brands and could, therefore, negatively impact the Company's financial performance.

Legal, Taxation and Accounting

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

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

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

Insurance

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

Management's Discussion and Analysis

Holding Company Structure

Loblaw Companies Limited is a holding company. As such, it does not carry on business directly but does so through its subsidiaries. It has no major source of income or assets of its own, other than the interests it has in its subsidiaries, which are all separate legal entities. Loblaw Companies Limited is therefore financially dependent on dividends and other distributions it receives from its subsidiaries.

11.2 Financial Risks and Risk Management

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

Liquidity

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

Common Share Market Price

Fluctuations in the Company's earnings can occur from changes in the value of equity forward contracts and stock-based compensation costs resulting from movements in the Company's common share market price. The Company enters into equity forwards to manage its exposure to fluctuations in its stock-based compensation cost as a result of changes in the market price of its common shares. These equity forwards change in value as the market price of the underlying common shares changes, which results in a partial offset to fluctuations in the Company's stock-based compensation costs. The partial offset between the Company's stock-based compensation costs and the equity forwards exists as long as the market price of the Company's common shares exceeds the exercise price of employee stock options. As at year end 2007, 6,431,699 stock options had exercise prices which were greater than the market price of the Company's common shares at year end.

Credit

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

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

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

Credit risk from *PC* Bank's credit card receivables and receivables from independent franchisees, associates and independent accounts results from the possibility that customers may default on their payment obligation. *PC* Bank manages the credit card receivable risk by employing stringent credit scoring techniques and 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.

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

Derivative Instruments

The Company uses over-the-counter financial derivative instruments, specifically cross currency basis swaps, interest rate swaps and equity forwards to manage its risks and costs associated with its financing and stock-based compensation plans. The Company uses financial and non-financial derivatives instruments in the form of future contracts, option contracts and forward contracts to manage its current and anticipated exposure to fluctuations in commodity prices. The fair value of derivative instruments is subject to changing market conditions which could negatively impact earnings. The Company maintains treasury centres that operate under policies and guidelines approved by the Board covering funding, investing, equity, commodity, foreign currency exchange and interest rate management. The Company's policies and guidelines prohibit the use of any financial derivative instrument for trading or speculative purposes. See notes 1 and 22 to the consolidated financial statements for additional information about the Company's financial derivative instruments.

Foreign Currency Exchange Rate

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

Interest Rate

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

12. Related Party Transactions

The Company's majority shareholder, George Weston Limited and its affiliates other than Loblaw ("Weston"), are related parties. It is the Company's policy to conduct all transactions and settle all balances with related parties on market terms and conditions. Related party transactions include:

Inventory Purchases Purchases of inventory from related parties for resale in the distribution network represented approximately 3% (2006 – 3%) of the cost of sales, selling and administrative expenses.

Management's Discussion and Analysis

Cost Sharing Agreements Weston has entered into certain contracts with third parties for administrative and corporate services, including telecommunication services and information technology related matters on behalf of the Company. Through cost sharing agreements that have been established between the Company and Weston concerning these costs, the Company has agreed to be responsible to Weston for its proportionate share of the costs incurred on its behalf. Payments by the Company pursuant to these cost sharing agreements in 2007 were approximately \$27 million (2006 – \$25 million).

Real Estate Matters The Company leases certain properties from an affiliate of Weston, namely office space for approximately \$2 million (2006 – \$4 million). During 2006, the Company purchased from an affiliate of Weston, a property designated for future development for consideration of \$8 million, which was prepaid in accordance with a former ground lease between the parties.

Borrowings/Lendings The Company, from time to time, may borrow funds from or may lend funds to Weston on a short term basis at short term market borrowing rates. There were no such amounts outstanding as at year end.

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

Management Agreements The Company has an agreement with Weston to provide certain administrative services by each company to the other. The services to be provided under this agreement include those related to commodity management, pension and benefits, tax, medical, travel, information system, risk management, treasury and legal. Payments are made quarterly based on the actual costs of providing these services. Where services are provided on a joint basis for the benefit of the Company and Weston together, each party pays the appropriate proportion of such costs. Net payments under this agreement in 2007 were \$9 million. Fees paid under this agreement are reviewed each year by the Audit Committee.

The Company, through Glenhuron Bank Limited ("Glenhuron"), a wholly-owned subsidiary of the Company, manages certain United States cash, cash equivalents and short term investments for wholly owned non-Canadian subsidiaries of Weston and management fees earned are based on market rates. Glenhuron has an agreement with a subsidiary of Weston for the administration of a loan portfolio of third-party long term loans receivable.

13. Critical Accounting Estimates

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

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

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

13.1 Inventories

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

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

Changes or differences in these estimates may result in changes to inventories on the consolidated balance sheet and a charge or credit to operating income in the consolidated statement of earnings.

The Company will be implementing the new Section 3031, "Inventories", issued by the CICA, in the first quarter of 2008 to the opening inventory for the period with an adjustment to opening retained earnings, net of income taxes, for the difference in measurement of the opening inventory with no prior periods restated. The Company expects to record, upon implementation of this standard, a decrease in the measurement of opening inventory of less than 4% of the inventory value with a corresponding decrease to opening retained earnings of less than \$50 million net of income taxes. Additional information on inventories is provided in note 1 to the consolidated financial statements.

13.2 Employee Future Benefits

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

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

The discount rates are based on market interest rates as at the Company's measurement date of September 30 on a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the accrued benefit plan obligations. The discount rates used to determine the 2007 net cost for defined benefit pension and other benefit plans were 5.0% and 5.0%, respectively, on a weighted average basis, compared to 5.25% and 5.2%, respectively, in 2006. The discount rates used to determine the net 2008 defined benefit pension and other benefit plans costs increased to 5.5% and 5.3%, respectively.

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

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

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

Management's Discussion and Analysis

Additional information regarding the Company's pension and other benefit plans, including a sensitivity analysis for changes in key assumptions, is provided in note 14 to the consolidated financial statements and in the Employee Future Benefit Contributions discussion in the Operating Risks and Risk Management section of this MD&A.

13.3 Goodwill

Goodwill is not amortized and is assessed for impairment at the reporting unit level at least annually. Any potential goodwill impairment is identified by comparing the fair value of a reporting unit to its carrying value. If the fair value of the reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value of the reporting unit exceeds its fair value, a more detailed goodwill impairment assessment must be undertaken. A goodwill impairment charge is recognized to the extent that, at the reporting unit level, the carrying value of goodwill exceeds the implied fair value.

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

The Company performed the annual goodwill impairment test in 2007 and it was determined that the fair value of each of the reporting units exceeded its respective carrying value and therefore, no goodwill impairment was identified.

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

13.4 Income Taxes

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

13.5 Goods and Services Tax and Provincial Sales Taxes

During 2005, the Company recorded a charge relating to an audit and proposed assessment by the Canada Revenue Agency relating to GST on certain products sold on which GST was not appropriately charged and remitted. In light of this proposed assessment, the Company assessed and estimated the potential liabilities for GST and PST in other areas of its operations for various periods. Accordingly, a charge of \$40 million was recorded in operating income in 2005. Approximately \$4 million was paid in 2007 (2006 – \$1 million) and approximately \$20 million remains accrued as at December 29, 2007. The ultimate remaining amount paid will depend on the outcome of audits performed by or settlements reached with the various tax authorities, and therefore may differ from this estimate. Management will continue to assess the remaining accrual as progress towards resolution with the various tax authorities is made and will adjust the remaining accrual accordingly. Changes in this accrual may result in a charge or credit to operating income in the consolidated statement of earnings.

13.6 Fixed Assets

Fixed assets to be held and used are reviewed for impairment annually and when events or circumstances indicate that their carrying value exceeds the sum of the undiscounted cash flows expected from their use and eventual disposition. An impairment loss is measured as the amount by which the fixed assets carrying value exceeds the fair value. As discussed in notes 4 and 12 to the consolidated financial statements, the Company recorded fixed asset impairment charge of \$33 million (2006 – \$27 million), accelerated depreciation charge of \$3 million (2006 – \$5 million), and a charge of nominal amount (2006 – \$27 million) was recorded in restructuring and other charges.

The factor that most significantly influences the impairment assessments and calculations is estimates of future cash flows. The Company uses its internal plans in estimating future cash flows. These plans reflect the Company's current best estimate of future cash flows but may change due to uncertain competitive and economic market conditions or changes in business strategies. Changes or differences in these estimates may result in changes to fixed assets on the consolidated balance sheet and a charge to operating income on the consolidated statement of earnings.

14. Accounting Standards

14.1 Accounting Standards Implemented in 2007

On December 31, 2006, the Company implemented the CICA Handbook Section 3855 "Financial Instruments – Recognition and Measurement", Section 3865 "Hedges", Section 1530 "Comprehensive Income", Section 3251 "Equity" and Section 3861 "Financial Instruments – Disclosure and Presentation". These standards have been applied without restatement of prior periods. The transitional adjustments resulting from these standards are recognized in the opening balances of retained earnings and accumulated other comprehensive income.

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

Management's Discussion and Analysis

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

	Transitional Adjustments
Consolidated Balance Sheet	
Other assets	\$ 35
Future income taxes	(7)
Other liabilities	41
Retained earnings	(15)
Accumulated other comprehensive income	16

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

14.2 Future Accounting Standards

The Company closely monitors new accounting standards to assess the impact, if any, on its consolidated financial statements. In 2008, the Company will be reviewing the implications of the following standards and implementing the recommendations as required:

Capital Disclosures and Financial Instruments – Disclosure and Presentation In December 2006, the CICA issued three new accounting standards: Section 1535 “Capital Disclosures” (“Section 1535”), Section 3862 “Financial Instruments-Disclosures” (“Section 3862”) and Section 3863 “Financial Instruments-Presentation” (“Section 3863”).

Section 1535 establishes guidelines for the disclosure of information regarding a company's capital and how it is managed. The standard requires enhanced disclosures with respect to (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; and (iii) whether the entity has complied with any capital requirements, and if it has not complied, the consequences of such non-compliance.

Section 3862 and Section 3863 replace Section 3861, “Financial Instruments – Disclosure and Presentation”. Section 3862 requires increased disclosures regarding the risks associated with financial instruments such as credit risk, liquidity risk and market risks and the techniques used to identify, monitor and manage these risks. Section 3863 carries forward standards for presentation of financial instruments and non-financial derivative instruments and provides additional guidance for the classification of financial instruments, from the perspective of the issuer, between liabilities and equity.

These standards are effective for fiscal years beginning on or after October 1, 2007 and therefore the Company will implement them in the first quarter of 2008.

Inventories In June 2007, the CICA issued a new Section 3031, "Inventories", which will replace existing Section 3030 of the same title. The new standard requires inventories to be measured at the lower of cost and net realizable value with more specific guidance of costs to include in the cost of inventory. Costs such as storage costs and administrative overhead that do not contribute to bringing inventories to their present location and condition are specifically excluded from the cost of inventories and expensed in the period incurred. This standard is effective for fiscal years beginning on or after January 1, 2008 and will be implemented by the Company in the first quarter of 2008 to the opening inventory for the period with an adjustment to opening retained earnings, net of income taxes, for the difference in measurement of the opening inventory with no prior periods restated. The Company expects to record, upon implementation of this standard, a decrease in the measurement of opening inventory of less than 4% of the inventory value with a corresponding decrease of less than \$50 million to opening retained earnings net of income taxes.

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

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

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

15. Outlook⁽¹⁾

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

(1) To be read in conjunction with "Forward Looking Statements" on page 2 of this Annual Report.

Management's Discussion and Analysis

16. Non-GAAP Financial Measures

The Company reports its financial results in accordance with Canadian GAAP. However, the Company has included certain non-GAAP financial measures and ratios, which it believes provide useful information to both management and readers of this Annual Report in measuring the financial performance and financial condition of the Company for the reasons set out below. These measures do not have a standardized meaning prescribed by Canadian GAAP and, therefore, may not be comparable to similarly titled measures presented by other publicly traded companies. They should not be construed as an alternative to other financial measures determined in accordance with Canadian GAAP. For the following tables, the annual non-GAAP financial measures for the years 2007 through to 2003, are for the 52 or 53 weeks ended or as at December 29, 2007; December 30, 2006; December 31, 2005; January 1, 2005; and January 3, 2004, respectively.

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

These financial measures exclude the impact on sales from the decrease in tobacco sales and from the consolidation by the Company of certain independent franchisees. Tobacco sales continued to decrease through the end of third quarter 2007 as a result of a major tobacco supplier shipping directly to certain customers of the Company's cash & carry and wholesale club network commencing in the third quarter of 2006. These impacts on sales are excluded because the Company believes this allows for a more effective analysis of the operating performance of the Company. A reconciliation of the financial measures to the Canadian GAAP financial measures is included in the table "Total Sales and Sales Excluding the Impact of Tobacco Sales and VIEs" on page 23 of this Annual Report. Same-store sales growth and same-store sales growth excluding the impact of decreased tobacco sales is included in the tables "Sales Growth and Same-Store Sales Growth" on page 24 of this Annual Report.

Adjusted Operating Income and Margin

The following table reconciles operating income and adjusted operating income to Canadian GAAP net earnings measures based on the audited results for the twelve and fifty-two week periods ended December 29, 2007 and December 30, 2006 and the years ended as previously indicated. Items listed in the reconciliation are excluded because the Company believes this allows for a more effective analysis of the operating performance of the Company. In addition, the excluded items affect the comparability of the financial results and could potentially distort the analysis of trends. The exclusion of these items does not imply they are non-recurring. Adjusted operating income and margin are useful to management in assessing the Company's performance and in making decisions regarding the ongoing operations of its business.

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

Adjusted EBITDA and Margin

The following table reconciles adjusted earnings before interest, income taxes, depreciation and amortization ("EBITDA") to adjusted operating income which is reconciled to Canadian GAAP net earnings measures based on management's review of the audited results for the twelve and fifty-two week periods ended December 29, 2007 and December 30, 2006 and the years ended as previously indicated. Adjusted EBITDA is useful to management in assessing the Company's performance of its ongoing operations and its ability to generate cash flows to fund its cash requirements, including the Company's capital investment program.

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

The following table outlines items which were excluded in arriving at adjusted operating income, adjusted operating margin, adjusted EBITDA and adjusted EBITDA margin:

(\$ millions)	(unaudited) 2007 (12 weeks)	(unaudited) 2006 (12 weeks)	2007 (52 weeks)	2006 (52 weeks)	2005 (52 weeks)	2004 (52 weeks)	2003 (53 weeks)
Net earnings (loss)	\$ 40	\$ (756)	\$ 330	\$ (219)	\$ 746	\$ 968	\$ 845
Add (deduct) impact of the following:							
Minority interest	8	(1)	4	1	3	-	-
Income taxes	27	2	150	248	400	445	426
Interest expense	59	60	252	259	252	239	196
Operating income (loss)	134	(695)	736	289	1,401	1,652	1,467
Add (deduct) impact of the following:							
Net effect of stock-based compensation and the associated equity forwards	52	(6)	72	37	43	-	(4)
Restructuring and other charges	36	35	222	44	86	-	-
Inventory liquidation	3	68	15	68	-	-	-
VIEs	(4)	-	(11)	(8)	-	-	-
Goodwill impairment charge	-	800	-	800	-	-	-
Ontario collective labour agreement	-	84	-	84	-	-	-
Departure entitlement charge	-	-	-	12	-	-	-
Goods and Services Tax and provincial sales taxes	-	-	-	-	40	-	-
Direct costs associated with supply chain disruptions	-	-	-	-	30	-	-
<i>The Real Canadian Superstore</i> labour arrangement	-	-	-	-	-	-	25
Adjusted operating income	221	286	1,034	1,326	1,600	1,652	1,488
Add (deduct) impact of the following:							
Depreciation and amortization	134	133	588	590	558	473	393
VIE depreciation and amortization	(6)	(5)	(33)	(24)	(26)	-	-
Adjusted EBITDA	\$ 349	\$ 414	\$ 1,589	\$ 1,892	\$ 2,132	\$ 2,125	\$ 1,881

Management's Discussion and Analysis

Adjusted Basic Net Earnings per Common Share

The following table reconciles adjusted basic net earnings per common share to Canadian GAAP basic net earnings (loss) per common share measures based on management's review of the audited results for the twelve and fifty-two week periods ended December 29, 2007 and December 30, 2006 and the years ended as previously indicated. Items listed in the reconciliation are excluded because the Company believes this allows for a more effective analysis of the operating performance of the Company. In addition, the excluded items affect the comparability of the financial results and could potentially distort the analysis of trends. The exclusion of these items does not imply they are non-recurring. Adjusted basic net earnings per common share is useful to management in assessing the Company's performance and in making decisions regarding the ongoing operations of its business.

	(unaudited) 2007 (12 weeks)	(unaudited) 2006 (12 weeks)	2007 (52 weeks)	2006 (52 weeks)	2005 (52 weeks)	2004 (52 weeks)	2003 (53 weeks)
Basic net earnings (loss) per common share	\$ 0.14	\$ (2.76)	\$ 1.20	\$ (0.80)	\$ 2.72	\$ 3.53	\$ 3.07
Add (deduct) impact of the following:							
Net effect of stock-based compensation and the associated equity forwards	0.21	(0.02)	0.30	0.17	0.22	-	(0.06)
Restructuring and other charges	0.09	0.09	0.53	0.11	0.20	-	-
Inventory liquidation	0.01	0.16	0.04	0.16	-	-	-
VIEs	0.02	(0.01)	0.02	(0.01)	0.03	-	-
Changes in statutory income tax rates	(0.04)	-	(0.04)	(0.06)	0.01	-	0.03
Goodwill impairment charge	-	2.92	-	2.92	-	-	-
Ontario collective labour agreement	-	0.20	-	0.20	-	-	-
Departure entitlement charge	-	-	-	0.03	-	-	-
Goods and Services Tax and provincial sales taxes	-	-	-	-	0.10	-	-
Direct costs associated with supply chain disruptions	-	-	-	-	0.07	-	-
Resolution of certain income tax matters	-	-	-	-	-	(0.05)	-
<i>The Real Canadian Superstore</i> labour arrangement	-	-	-	-	-	-	0.06
Adjusted basic net earnings per common share	\$ 0.43	\$ 0.58	\$ 2.05	\$ 2.72	\$ 3.35	\$ 3.48	\$ 3.10

Net Debt

The following table reconciles net debt used in the net debt to equity ratio to Canadian GAAP measures reported in the audited consolidated balance sheets as at the years ended as previously indicated. The Company calculates net debt as the sum of long term debt and short term debt less cash, cash equivalents and short term investments. The net debt to equity ratio is useful in assessing the amount of leverage employed.

(\$ millions)	2007	2006	2005	2004	2003
Bank indebtedness	\$ 3	\$ 1	\$ 30	\$ 28	\$ 38
Commercial paper	418	647	436	473	603
Long term debt due within one year	432	27	161	216	106
Long term debt	3,852	4,212	4,194	3,935	3,956
Less: Cash and cash equivalents	674	669	916	549	618
Short term investments	303	327	4	275	378
Net debt	\$ 3,728	\$ 3,891	\$ 3,901	\$ 3,828	\$ 3,707

Free Cash Flow

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

(\$ millions)	2007	2006	2005	2004	2003
Cash flows from operating activities	\$ 1,245	\$ 1,180	\$ 1,489	\$ 1,443	\$ 1,032
Less: Fixed asset purchases	613	937	1,156	1,258	1,271
Dividends	230	173	230	209	198
Free cash flow	\$ 402	\$ 70	\$ 103	\$ (24)	\$ (437)

Total Assets

The following table reconciles total assets used in the return on average total assets to Canadian GAAP measures reported in the audited consolidated balance sheets as at the years ended as previously indicated. The Company believes the return on average total assets ratio is useful in assessing the performance of its operating assets and therefore excludes cash, cash equivalents and short term investments from the total assets used in the ratio.

(\$ millions)	2007	2006	2005	2004	2003
Total assets	\$ 13,674	\$ 13,486	\$ 13,761	\$ 12,949	\$ 12,113
Less: Cash and cash equivalents	674	669	916	549	618
Short term investments	303	327	4	275	378
Total assets	\$ 12,697	\$ 12,490	\$ 12,841	\$ 12,125	\$ 11,117

17. Additional Information

Additional information about the Company, including its Annual Information Form and other disclosure documents, has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR) and is available online at www.sedar.com and with the Office of the Superintendent of Financial Institutions (OSFI) as the primary regulator for the Company's subsidiary, President's Choice Bank.

March 12, 2008
Toronto, Canada

Financial Results

- 45 Management's Statement of Responsibility for Financial Reporting**
- 45 Independent Auditors' Report**
- 46 Consolidated Financial Statements**
 - 46 Consolidated Statements of Earnings (Loss)**
 - 47 Consolidated Statements of Changes in Shareholders' Equity**
 - 47 Consolidated Statement of Comprehensive Income**
 - 48 Consolidated Balance Sheets**
 - 49 Consolidated Cash Flow Statements**
 - 50 Notes to the Consolidated Financial Statements**
 - 50 Note 1. Summary of Significant Accounting Policies
 - 56 Note 2. Implementation of New Accounting Standards
 - 59 Note 3. Goodwill
 - 60 Note 4. Restructuring and Other Charges
 - 62 Note 5. Collective Agreement
 - 62 Note 6. Interest Expense
 - 62 Note 7. Income Taxes
 - 63 Note 8. Basic and Diluted Net Earnings (Loss) per Common Share
 - 64 Note 9. Cash and Cash Equivalents
 - 64 Note 10. Accounts Receivable
 - 65 Note 11. Inventory Liquidation
 - 66 Note 12. Fixed Assets
 - 66 Note 13. Other Assets
 - 67 Note 14. Employee Future Benefits
 - 72 Note 15. Short Term Debt
 - 72 Note 16. Long Term Debt
 - 73 Note 17. Other Liabilities
 - 73 Note 18. Leases
 - 74 Note 19. Common Share Capital
 - 75 Note 20. Accumulated Other Comprehensive Income
 - 75 Note 21. Stock-Based Compensation
 - 77 Note 22. Financial Instruments
 - 80 Note 23. Contingencies, Commitments and Guarantees
 - 81 Note 24. Variable Interest Entities
 - 82 Note 25. Related Party Transactions
 - 83 Note 26. Subsequent Events
 - 83 Note 27. Other Information
- 84 Five Year Summary**
- 85 Glossary of Terms**

Management's Statement of Responsibility for Financial Reporting

The management of Loblaw Companies Limited is responsible for the preparation, presentation and integrity of the accompanying consolidated financial statements, Management's Discussion and Analysis and all other information in the Annual Report. 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 Canadian generally accepted accounting principles. It also includes ensuring that the financial information presented elsewhere in the Annual Report is consistent with that in the consolidated financial statements.

To provide reasonable assurance that assets are safeguarded and that relevant and reliable financial information is produced, management is required to design a system of internal controls and certify as to the design 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 of the Company, is responsible for determining that management fulfills its responsibilities in the preparation of the consolidated financial statements and the financial control of operations. The Audit Committee recommends the independent auditors for appointment by the shareholders. The Audit Committee meets regularly with senior and financial management, internal auditors and the independent auditors to discuss internal controls, auditing activities and financial reporting matters. The independent auditors and internal auditors have unrestricted access to the Audit Committee. These consolidated financial statements and Management's Discussion and Analysis have been approved by the Board of Directors for inclusion in the Annual Report based on the review and recommendation of the Audit Committee.

Toronto, Canada
March 12, 2008

[signed]
Galen G. Weston
Executive Chairman

[signed]
Mark Foote
President and Chief Merchandising Officer

[signed]
William M. Wells
Chief Financial Officer

Independent Auditors' Report


To the Shareholders of Loblaw Companies Limited:

We have audited the consolidated balance sheets of Loblaw Companies Limited as at December 29, 2007 and December 30, 2006, the consolidated statements of earnings (loss), changes in shareholders' equity, and the consolidated cash flow statements for the 52 week years then ended and the consolidated statement of comprehensive income for the 52 week year ended December 29, 2007. These consolidated financial statements are the responsibility of the Company's management. 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 plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 29, 2007 and December 30, 2006 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.


Toronto, Canada
March 12, 2008


Chartered Accountants, Licensed Public Accountants

Consolidated Statements of Earnings (Loss)

For the years ended December 29, 2007 and December 30, 2006

(\$ millions except where otherwise indicated)

	2007 (52 weeks)	2006 (52 weeks)
Sales	\$ 29,384	\$ 28,640
Operating Expenses		
Cost of sales, selling and administrative expenses (note 2)	27,838	26,917
Depreciation and amortization	588	590
Goodwill impairment (note 3)	-	800
Restructuring and other charges (note 4)	222	44
	28,648	28,351
Operating Income	736	289
Interest Expense (note 6)	252	259
Earnings Before Income Taxes and Minority Interest	484	30
Income Taxes (note 7)	150	248
Net Earnings (Loss) Before Minority Interest	334	(218)
Minority Interest	4	1
Net Earnings (Loss)	\$ 330	\$ (219)
Net Earnings (Loss) Per Common Share (\$) (note 8)		
Basic	\$ 1.20	\$ (.80)
Diluted	\$ 1.20	\$ (.80)

See accompanying notes to the consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity

For the years ended December 29, 2007 and December 30, 2006 (\$ millions except where otherwise indicated)	2007 (52 weeks)	2006 (52 weeks)
Common Share Capital, End of Year (note 19)	\$ 1,196	\$ 1,196
Retained Earnings, Beginning of Year	\$ 4,245	\$ 4,694
Cumulative impact of implementing new accounting standards (note 2)	(15)	-
Net earnings (loss)	330	(219)
Dividends declared per common share – 84¢ (2006 – 84¢)	(230)	(230)
Retained Earnings, End of Year	\$ 4,330	\$ 4,245
Accumulated Other Comprehensive Income, Beginning of Year	\$ -	
Cumulative impact of implementing new accounting standards (note 2)	16	
Other comprehensive income	3	
Accumulated Other Comprehensive Income, End of Year (note 20)	\$ 19	
Total Shareholders' Equity	\$ 5,545	\$ 5,441

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Comprehensive Income

For the year ended December 29, 2007 (\$ millions)	2007 (52 weeks)
Net earnings	\$ 330
Other comprehensive income	
Net unrealized loss on available-for-sale financial assets	(56)
Reclassification of loss on available-for-sale financial assets to net earnings	33
	(23)
Net gain on derivative instruments designated as cash flow hedges	57
Reclassification of gain on derivative instruments designated as cash flow hedges to net earnings	(31)
	26
Other comprehensive income	3
Total Comprehensive Income	\$ 333

See accompanying notes to the consolidated financial statements.

Consolidated Balance Sheets

As at December 29, 2007 and December 30, 2006

(\$ millions)

	2007	2006
Assets		
Current Assets		
Cash and cash equivalents (note 9)	\$ 674	\$ 669
Short term investments	303	327
Accounts receivable (note 10)	885	728
Inventories (note 11)	2,032	2,037
Income taxes (note 7)	111	63
Future income taxes (note 7)	56	85
Prepaid expenses and other assets	32	39
Total Current Assets	4,093	3,948
Fixed Assets (note 12)	7,953	8,055
Goodwill (note 3)	806	794
Other Assets (note 13)	822	689
Total Assets	\$ 13,674	\$ 13,486
Liabilities		
Current Liabilities		
Bank indebtedness	\$ 3	\$ 1
Commercial paper	418	647
Accounts payable and accrued liabilities	2,769	2,598
Long term debt due within one year (note 16)	432	27
Total Current Liabilities	3,622	3,273
Long Term Debt (note 16)	3,852	4,212
Future Income Taxes (note 7)	180	234
Other Liabilities (note 17)	459	314
Minority Interest	16	12
Total Liabilities	8,129	8,045
Shareholders' Equity		
Common Share Capital (note 19)	1,196	1,196
Retained Earnings	4,330	4,245
Accumulated Other Comprehensive Income (notes 2 and 20)	19	-
Total Shareholders' Equity	5,545	5,441
Total Liabilities and Shareholders' Equity	\$ 13,674	\$ 13,486

Contingencies, commitments and guarantees (note 23). Leases (note 18).

See accompanying notes to the consolidated financial statements.

Approved on Behalf of the Board

[signed]
Galen G. Weston
 Director

[signed]
Thomas C. O'Neill
 Director

Consolidated Cash Flow Statements

For the years ended December 29, 2007 and December 30, 2006
(\$ millions)

	2007 (52 weeks)	2006 (52 weeks)
Operating Activities		
Net earnings (loss) before minority interest	\$ 334	\$ (218)
Depreciation and amortization	588	590
Goodwill impairment (note 3)	-	800
Restructuring and other charges (note 4)	222	44
Future income taxes	(17)	(18)
Change in non-cash working capital	(43)	(69)
Other	161	51
Cash Flows from Operating Activities	1,245	1,180
Investing Activities		
Fixed asset purchases	(613)	(937)
Short term investments	(31)	(323)
Proceeds from fixed asset sales	223	99
Credit card receivables, after securitization (note 10)	(238)	(82)
Franchise investments and other receivables	19	(18)
Other	(31)	(47)
Cash Flows used in Investing Activities	(671)	(1,308)
Financing Activities		
Bank indebtedness	2	(29)
Commercial paper	(229)	211
Long term debt (note 16)		
Issued	25	29
Retired	(39)	(162)
Common share capital issued (notes 19 and 21)	-	4
Dividends	(230)	(173)
Other	(1)	-
Cash Flows used in Financing Activities	(472)	(120)
Effect of foreign currency exchange rate changes on cash and cash equivalents (note 9)	(97)	1
Change in Cash and Cash Equivalents	5	(247)
Cash and Cash Equivalents, Beginning of Year	669	916
Cash and Cash Equivalents, End of Year	\$ 674	\$ 669
See accompanying notes to the consolidated financial statements.		

Notes to the Consolidated Financial Statements

For the years ended December 29, 2007 and December 30, 2006
(\$ millions except where otherwise indicated)

Note 1. Summary of Significant Accounting Policies

The consolidated financial statements were prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are reported in Canadian dollars.

Basis of Consolidation The consolidated financial statements include the accounts of Loblaw Companies Limited and its subsidiaries, collectively referred to as the "Company" or "Loblaw". The Company's interest in the voting share capital of its subsidiaries is 100%.

The Company also consolidates variable interest entities ("VIEs") pursuant to Canadian Institute of Chartered Accountants ("CICA") Accounting Guideline ("AcG") 15, "Consolidation of Variable Interest Entities" ("AcG 15"), that are subject to control by Loblaw on a basis other than through ownership of a majority of voting interest. AcG 15 defines a variable interest entity as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. AcG 15 requires the primary beneficiary to consolidate VIEs and considers an entity to be the primary beneficiary of a VIE if it holds variable interests that expose it to a majority of the VIE's expected losses or that entitle it to receive a majority of the VIE's expected residual returns or both.

Fiscal Year The fiscal year of the Company ends 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 5 to 6 years. The years ended December 29, 2007 and December 30, 2006 each contained 52 weeks.

Revenue Recognition Sales include revenues, net of estimated returns, from customers through corporate stores operated by the Company and independent franchisee stores that are consolidated by the Company pursuant to AcG 15. In addition, sales include sales to and service fees from associated stores and independent account customers and franchised stores excluding VIE stores net of sales incentives offered by Loblaw. The Company recognizes revenue at the time the sale is made to its customers.

Earnings (Loss) per Share ("EPS") Basic EPS is calculated by dividing the net earnings (loss) available to common shareholders by the weighted average number of common shares outstanding during the year. Diluted EPS is calculated using the treasury stock method, which assumes that all outstanding stock options with an exercise price below the average market price during the year are exercised and the assumed proceeds are used to purchase the Company's common shares at the average market price during the year.

Cash, Cash Equivalents and Bank Indebtedness Cash equivalents consist primarily of highly liquid marketable investments with a maturity of 90 days or less. The Company has the ability and intent to offset cash balances to reduce reported bank indebtedness, except for VIEs consolidated by the Company. Commencing December 31, 2006, cash equivalents are either designated as held-for-trading financial assets or classified as available-for-sale financial assets and are carried at quoted market value. See note 2 for more information.

Prior to December 31, 2006, cash equivalents were carried at the lower of cost or quoted market value.

Short Term Investments Short term investments consist primarily of government treasury bills, government-sponsored debt securities, corporate commercial paper and bank term deposits. Commencing December 31, 2006, short term investments are either designated as held-for-trading financial assets or classified as available-for-sale financial assets and are carried at quoted market value. See note 2 for more information.

Prior to December 31, 2006, short term investments were carried at the lower of cost or quoted market value.

Credit Card Receivables The Company, through *President's Choice Bank* ("PC Bank"), a wholly owned subsidiary of the Company, has credit card receivables that are stated net of an allowance for credit losses. Any credit card receivable with a payment that is contractually 180 days in arrears, or where the likelihood of collection is considered remote, is written off. Interest income on credit card receivables is recorded on an accrual basis and is recognized in operating income.

Allowance for Credit Losses PC Bank maintains an allowance for probable credit losses on aggregate exposures for which losses cannot be determined on an item-by-item basis. The allowance is based upon a statistical analysis of past and current performance, the level of allowance already in place and management's judgment. The allowance for credit losses is deducted from the credit card receivables balance. The net credit loss experience for the year is recognized in operating income.

Securitization PC Bank securitizes credit card receivables through the sale of a portion of the total interest in these receivables to independent trusts and does not exercise any control over the trusts' management or assets. PC Bank does retain certain servicing and administrative responsibilities. The credit card receivables are removed from the consolidated balance sheet when PC Bank has surrendered control and are considered sold for accounting purposes pursuant to AcG 12, "Transfers of Receivables". When PC Bank sells credit card receivables in a securitization transaction, it has a retained interest in the securitized receivables represented by the rights to future cash flows after obligations to investors have been met. Although PC Bank remains responsible for servicing all credit card receivables, it does not receive additional compensation for servicing those credit card receivables sold to the trusts and accordingly a service liability is recorded. The service liability is recorded at fair value. In the absence of quoted market rates for servicing securitized assets, fees payable to a replacement servicer, in the event that a replacement servicer was to be appointed, formed the basis of determination of fair value of the servicing liability. Gains or losses on the sale of these receivables depends, in part, on the previous carrying amount of receivables involved in the securitization, allocated between the receivables sold and the retained interest, based on their relative fair values at the date of securitization. The fair value is determined as the best estimate of the net present value of expected future cash flows using management's best estimates of key assumptions such as monthly payment rates, weighted average life, expected annual credit losses and discount rates. Any gain or loss on a sale is recognized in operating income at the time of the securitization. Commencing December 31, 2006, retained interests are designated as held-for-trading financial assets (see note 2) and are recorded at fair value on the consolidated balance sheet. Prior to December 31, 2006 the carrying value of retained interests was periodically reviewed and when a decline in value was identified as other than temporary, the carrying value was written down to fair value.

Vendor Allowances The Company receives allowances from certain of its vendors whose products it purchases for resale. These allowances are received for a variety of buying and/or merchandising activities, including vendor programs such as volume purchase allowances, purchase discounts, listing fees and exclusivity allowances. Consideration received from a vendor is a reduction in the cost of the vendor's products or services and is recognized as a reduction in the cost of sales, selling and administrative expenses and the related inventory when recognized in the consolidated statement of earnings and the consolidated balance sheet. 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, provided that these costs are separate, incremental and identifiable.

Inventories The Company utilizes the retail method for retail store inventories which are stated at the lower of cost and estimated net realizable value less normal gross profit margin. Distribution centre inventories and seasonal general merchandise inventories are stated at the lower of cost and estimated net realizable value. Cost is determined substantially using the first-in, first-out method.

Fixed Assets Fixed assets are recorded at cost including capitalized interest. Depreciation commences when the assets are put into use and is recognized on a straight-line basis to depreciate the cost of these assets over their estimated useful lives. Estimated useful lives range from 20 to 40 years for buildings, 10 years for building improvements and from 3 to 10 years for equipment and fixtures. Leasehold improvements are depreciated over their estimated useful lives and may include renewal options when an improvement is made after inception of the lease to a maximum of 25 years, which approximates economic life. Equipment under capital leases is depreciated over the term of the lease.

Notes to the Consolidated Financial Statements

Fixed assets are reviewed for impairment when events or changes in circumstances indicate that the carrying value exceeds the sum of the undiscounted future cash flows expected from use and eventual disposal. These events or changes in circumstances include a commitment to close a store or distribution centre or to relocate or convert a store. Fixed assets are also reviewed for impairment annually. For purposes of annually reviewing store assets for impairment, asset groups are reviewed at their lowest level for which identifiable cash flows are largely independent of cash flows of other assets and liabilities. Therefore, store net cash flows are grouped together by primary market areas, where cash flows are largely dependent on each other. Primary markets are regional areas where a number of store formats operate within close proximity to one another. If an indicator of impairment exists, such as sustained negative operating cash flows of the respective asset group, then an estimate of undiscounted future cash flows of each such store within this group is prepared and compared to its carrying value. For purposes of annually reviewing distribution centre assets for impairment, distribution centre net cash flows are grouped with the respective net cash flows of the stores they service. An impairment in the store network serviced by the distribution centre would indicate an impairment in the distribution centre assets as well. If these assets are determined to be impaired, the impairment loss is measured as the excess of the carrying value over fair value. In addition, the carrying value of fixed assets is evaluated whenever events or changes in circumstances indicate that the carrying value of fixed assets may not be recoverable. These events or changes in circumstances include a commitment to close a store or distribution centre or to relocate or convert a store where the carrying value of its assets is greater than the expected undiscounted future cash flows.

Deferred Charges Deferred charges are amortized over the related assets' estimated useful lives, to a maximum of 15 years.

Goodwill Goodwill represents the excess of the purchase price of a business acquired over the fair value of the underlying net assets acquired at the date of acquisition. Goodwill is not amortized and is assessed for impairment at a minimum on an annual basis, at the reporting unit level. Any potential goodwill impairment is identified by comparing the fair value of a reporting unit to its carrying value. If the fair value of the reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value of the reporting unit exceeds its fair value, a more detailed goodwill impairment assessment must be undertaken. A goodwill impairment charge is recognized to the extent that, at the reporting unit level, the carrying value of goodwill exceeds the implied fair value and is recorded in operating income.

The Company determines the fair value using a discounted cash flow model corroborated by other valuation techniques such as market multiples. The process of determining these fair values requires management to make estimates and assumptions including, but not limited to, projected future sales, earnings and capital investment, discount rates and terminal growth rates. Projected future sales, earnings and capital investment are consistent with strategic plans presented to the Company's Board of Directors. Discount rates are based on an industry weighted average cost of capital. These estimates and assumptions are subject to change in the future due to uncertain competitive and economic market conditions or changes in business strategies. Additional disclosure regarding the results of the goodwill impairment test is provided in note 3.

Derivative Instruments The Company uses financial derivative instruments in the form of cross currency basis swaps, interest rate swaps and equity forwards to manage its current and anticipated exposure to fluctuations in foreign currency exchange rates, interest rates and the market price of the Company's common shares. The Company uses financial and non-financial derivative instruments in the form of futures contracts, option contracts and forward contracts to manage its current and anticipated exposure to fluctuations in commodity prices. The Company does not enter into derivative agreements for trading or speculative purposes.

Commencing December 31, 2006, all financial derivative instruments are recorded at fair value on the consolidated balance sheet in accordance with CICA Section 3855 "Financial Instruments – Recognition and Measurement" ("Section 3855"). Non-financial derivative instruments, such as certain contracts that are linked to commodity prices, are recorded at fair value on the consolidated balance sheet unless they are exempt from this treatment based upon expected purchase, sale or usage requirements. Embedded derivative instruments are separated from their host contract and recorded on the consolidated balance sheet at fair value. Fair values are based on quoted market prices where available from active markets, otherwise fair values are estimated using valuation methodologies, primarily discounted cash flow analysis. Derivative instruments are recorded in current or non-current assets and liabilities based on their remaining terms to maturity. All changes in fair value of the derivative instruments are recorded in net earnings unless cash flow hedge accounting is applied.

The Company formally identifies, designates and documents the relationship between hedging instruments and hedged items including cross currency basis swaps and interest rate swaps as cash flow hedges against its exposure to fluctuations in the foreign currency exchange rate and variable interest rates on a portion of its United States dollar cash equivalents and short term investments. The Company assesses whether each derivative instrument continues to be highly effective in offsetting the change in the cash flows of hedged items. If and when a derivative instrument is no longer expected to be highly effective, hedge accounting is discontinued. Hedge ineffectiveness, if any, is included in current period net earnings.

Prior to December 31, 2006, all financial derivative instruments were recorded at fair value on the consolidated balance sheet with the exception of interest rate swaps which were designated in cash flow hedging relationships. These interest rate swaps were not recorded on the comparative period consolidated balance sheet. Non-financial derivative instruments and embedded derivative instruments were also not recorded on the comparative period consolidated balance sheet.

Foreign Currency Translation Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. Commencing December 31, 2006, exchange gains or losses arising from the translation of these balances denominated in foreign currencies are recognized in operating income except for cross currency basis swaps and available-for-sale cash equivalents and short term investments denominated in United States dollars which are designated in a cash flow hedge and are deferred in accumulated other comprehensive income and reclassified to net earnings when realized. Prior to December 31, 2006, all exchange gains or losses arising from the translation of assets and liabilities denominated in foreign currencies are recognized in operating income. Revenues and expenses denominated in foreign currencies are translated into Canadian dollars at the average foreign currency exchange rate for the year.

Income Taxes The asset and liability method of accounting is used for income taxes. Under the asset and liability method, future income tax assets and liabilities are recognized for the future income tax consequences attributable to temporary differences between the financial statement carrying values of existing assets and liabilities and their respective income tax bases. Future income tax assets and liabilities are measured using enacted or substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in income tax rates is recognized in income tax expense when enacted or substantively enacted. Future income tax assets are evaluated and a valuation allowance, if required, is recorded against any future income tax asset if it is more likely than not that the asset will not be realized.

Employee Future Benefits The Company sponsors a number of pension plans including registered funded defined benefit pension plans, defined contribution pension plans and supplemental unfunded arrangements providing pension benefits in excess of statutory limits. The Company also offers certain employee post-retirement and post-employment benefit plans and a long term disability benefit plan. Post-retirement and post-employment benefit plans are generally not funded, are mainly non-contributory and include health care, life insurance and dental benefits. The Company also contributes to various multi-employer pension plans which provide pension benefits.

Defined Benefit Plans The cost and accrued benefit plan obligations of the Company's defined benefit pension plans and other benefit plans, including post-retirement, post-employment and long term disability benefits, are accrued based on actuarial valuations. The actuarial valuations for the defined benefit plans are determined using the projected benefit method prorated on service and management's best estimate of the discount rate, the expected long term rate of return on plan assets, the rate of compensation increase, retirement ages, termination rates, mortality rates and expected growth rate of health care costs. Actuarial valuations are performed using a September 30 measurement date for accounting purposes. Market values used to value benefit plan assets are as at the measurement date. The discount rate used to value the accrued benefit plan obligation is based on market interest rates as at the measurement date, assuming a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the accrued benefit plan obligations.

Notes to the Consolidated Financial Statements

Past service costs arising from plan amendments are amortized over the expected average remaining service period of the active employees. The unamortized net actuarial gain or loss that exceeds 10% of the greater of the accrued benefit plan obligation or the fair value of the benefit plan assets at the beginning of the year is amortized over the expected average remaining service period of the active employees for defined benefit pension and post-retirement benefit plans. The unamortized net actuarial gain or loss for post-employment and long term disability benefits is amortized over periods not exceeding three years. The expected average remaining service period of the active employees covered by the defined benefit pension plans ranges from 6 to 17 years, with a weighted average of 13 years. The expected average remaining service period of the employees covered by the post-retirement benefit plans ranges from 6 to 22 years, with a weighted average of 18 years.

The net accrued benefit plan asset or liability represents the cumulative difference between the cost and the funding contributions and is recorded in other assets and other liabilities.

Defined Contribution and Multi-Employer Pension Plans The costs of pension benefits for defined contribution pension plans and multi-employer pension plans are expensed as contributions are due.

Stock Option Plan The Company recognizes a compensation cost in operating income and a liability related to employee stock option grants that allow for settlement in shares or in the share appreciation value in cash at the option of the employee, using the intrinsic value method. Under the intrinsic value method, the stock-based compensation liability is the amount by which the market price of the common shares at the balance sheet date exceeds the exercise price of the stock options. A year-over-year change in the stock-based compensation liability is recognized in operating income on a prescribed vesting basis.

The Company accounts for stock options issued prior to December 30, 2001 that will be settled by issuing common shares as capital transactions. Consideration paid by employees on the exercise of this type of stock option is credited to common share capital. This type of option was last issued in 2001 and represents approximately 0.6% of all options outstanding at year end.

Restricted Share Unit (“RSU”) Plan The Company recognizes a compensation cost in operating income on a prescribed vesting basis for each RSU granted equal to the market value of a Loblaw common share at the date on which RSUs are awarded to each participant prorated over the performance period and adjusts for changes in the market value until the end of the performance date. The cumulative effect of the change in market value is recognized in operating income in the period of change.

Employee Share Ownership Plan The Company maintains an Employee Share Ownership Plan which allows employees to acquire the Company's common shares through regular payroll deductions of up to 5% of their gross regular earnings. The Company contributes an additional 25% of each employee's contribution to the plan, which is recognized in operating income as a compensation cost when the contribution is made.

Deferred Share Units Members of the Company's Board of Directors, who are not management of the Company, may elect annually to receive all or a portion of their annual retainer(s) and fees in the form of deferred share units, which are accounted for using the intrinsic value method. Under the intrinsic value method, the deferred share unit compensation liability is the amount by which the market price of the common shares at the balance sheet date exceeds the initial value of the deferred share unit. The year-over-year change in the deferred share unit compensation liability is recognized in operating income.

Use of Estimates and Assumptions The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts and disclosures made in the consolidated financial statements and accompanying notes. These estimates and assumptions are based on management's historical experience, best knowledge of current events and conditions and activities that may be undertaken in the future. Actual results could differ from these estimates.

Certain estimates, such as those related to valuation of inventories, goodwill, income taxes, Goods and Services Tax and provincial sales taxes, fixed assets and employee future benefits, depend upon subjective or complex judgments about matters that may be uncertain, and changes in those estimates could materially impact the consolidated financial statements.

Future Accounting Standards

Capital Disclosures and Financial Instruments – Disclosure and Presentation In December 2006, the CICA issued three new accounting standards: Section 1535 “Capital Disclosures” (“Section 1535”), Section 3862 “Financial Instruments – Disclosures” (“Section 3862”) and Section 3863 “Financial Instruments – Presentation” (“Section 3863”).

Section 1535 establishes guidelines for the disclosure of information regarding a company's capital and how it is managed. The standard requires enhanced disclosures with respect to (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; and (iii) whether the entity has complied with any capital requirements, and if it has not complied, the consequences of such non-compliance.

Section 3862 and Section 3863 replace Section 3861, “Financial Instruments – Disclosure and Presentation”. Section 3862 requires increased disclosures regarding the risks associated with financial instruments such as credit risk, liquidity risk and market risks and the techniques used to identify, monitor and manage these risks. Section 3863 carries forward standards for presentation of financial instruments and non-financial derivative instruments and provides additional guidance for the classification of financial instruments, from the perspective of the issuer, between liabilities and equity.

These standards are effective for fiscal years beginning on or after October 1, 2007 and therefore the Company will implement them in the first quarter of 2008.

Inventories In June 2007, the CICA issued Section 3031, “Inventories”, that will replace existing Section 3030 of the same title. The new standard requires inventories to be measured at the lower of cost and net realizable value with more specific guidance of costs to include in the cost of inventory. Costs such as storage costs and administrative overhead that do not contribute to bringing inventories to their present location and condition are specifically excluded from the cost of inventories and expensed in the period incurred. Reversal of previous write-downs to net realizable value when there is a subsequent increase in the value of inventories is now required. The cost of the inventories should be based on a first-in, first-out or a weighted average cost formula. Techniques used for the measurement of cost of inventories, such as the retail method, may be used for convenience if the results approximate cost. The new standard also requires additional disclosures including the accounting policies used in measuring inventories, the carrying amount of the inventories, amounts recognized as an expense during the period, write-downs and the amount of any reversal of any write-downs recognized as a reduction in expenses.

This standard is effective for fiscal years beginning on or after January 1, 2008 and will be implemented by the Company in the first quarter of 2008 to the opening inventory for the period with an adjustment to opening retained earnings, net of income taxes, for the difference in measurement of the opening inventory with no prior periods restated. The Company expects to record, upon implementation of this standard, a decrease in the measurement of opening inventory of less than 4% of the inventory value with a corresponding decrease of less than \$50 to opening retained earnings net of income taxes.

In addition to the changes in the cost of inventory, the Company is reviewing the additional presentation and disclosure requirements which will be required in the consolidated financial statements and/or in the accompanying notes.

Notes to the Consolidated Financial Statements

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

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

Note 2. Implementation of New Accounting Standards

Accounting Standards Implemented in 2007

On December 31, 2006, the Company implemented the CICA Handbook Section 3855 “Financial Instruments – Recognition and Measurement”, Section 3865 “Hedges”, Section 1530 “Comprehensive Income”, Section 3251 “Equity” and Section 3861 “Financial Instruments – Disclosure and Presentation”. These standards have been applied without restatement of prior periods. The transitional adjustments resulting from these standards are recognized in the opening balances of retained earnings and accumulated other comprehensive income.

Section 3855 establishes guidance for recognizing and measuring financial assets, financial liabilities and non-financial derivative instruments. All financial instruments must be classified into a defined category, namely, held-for-trading financial assets or financial liabilities, held-to-maturity investments, loans and receivables, available-for-sale financial assets, or other financial liabilities. The standard requires that financial instruments within scope, including derivative instruments, be included on the Company's balance sheet and measured at fair value, except for loans and receivables, held-to-maturity financial assets and other financial liabilities which are measured at cost or amortized cost. Gains and losses on held-for-trading financial assets and financial liabilities are recognized in net earnings in the period in which they arise. Unrealized gains and losses, including changes in foreign exchange rates on available-for-sale financial assets are recognized in other comprehensive income until the financial asset is derecognized or impaired, at which time any unrealized gains or losses are recorded in net earnings. Transaction costs other than those related to financial instruments classified as held-for-trading, which are expensed as incurred, are amortized using the effective interest method.

Section 3855 allows management to elect to measure financial instruments that would not otherwise be accounted for at fair value as held-for-trading instruments with changes in fair value recorded in net earnings provided they meet certain criteria. Financial instruments must have been designated when the standard was implemented or when the new financial instrument was acquired and the designation is irrevocable.

Fair values are based on quoted market prices where available from active markets, otherwise fair values are estimated using valuation methodologies, primarily discounted cash flow analysis.

As a result of the implementation of Section 3855, the following classifications were assumed:

- Cash and cash equivalents and short term investments are designated as held-for-trading with the exception of certain United States dollar denominated cash equivalents and short term investments designated in a cash flow hedging relationship, which are classified as available-for-sale financial assets.
- Accounts receivable are classified as loans and receivables.
- Investments in equity instruments are classified as available-for-sale.
- Bank indebtedness, commercial paper, accounts payable and certain accrued liabilities, short term debt, long term debt and capital lease obligations have been classified as other financial liabilities.

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

The above classifications resulted in the following re-measurement impacts:

- The re-measurement of financial assets classified as available-for-sale at fair value resulted in an increase in other assets of \$9 with a corresponding increase in accumulated other comprehensive income of \$6 net of income taxes.
- As a result of classifying certain United States dollar denominated cash equivalents and short term investments designated in a cash flow hedging relationship as available-for-sale, the net unrealized gain previously recorded in retained earnings was reclassified to accumulated other comprehensive income for an amount of \$14 net of income taxes.
- The retained interest held by *PC* Bank in securitized receivables has been designated as held-for-trading and has resulted in an increase in other assets of \$2 with a corresponding increase in opening retained earnings of \$1 net of income taxes.
- The re-measurement of financial assets classified as loans and receivables and financial liabilities classified as other liabilities at amortized cost was insignificant.

Non-financial derivative instruments must be recorded at fair value on the consolidated balance sheet unless they are exempt from derivative instrument treatment based upon expected purchase, sale or usage requirements. All changes in their fair value are recorded in net earnings unless cash flow hedge accounting is applied, in which case changes in fair value are recorded in other comprehensive income for the effective portion of the hedge. As a result of re-measuring a non-financial derivative instrument at fair value an increase in other assets of \$7 and an increase in opening retained earnings of \$5 net of income taxes was recognized. The standard requires embedded derivative instruments to be separated from their host contract and fair valued if certain criteria are met. Under an election provided for by the standard, December 29, 2002 was elected as the transition date to apply this accounting treatment to embedded derivative instruments. The impact of this change in accounting treatment related to embedded derivative instruments was not significant.

Section 3855 also requires that obligations undertaken in issuing a guarantee that meets the definition of a guarantee pursuant to AcG 14, "Disclosure of Guarantees" be recognized at fair value at inception. No subsequent re-measurement at fair value is required unless the financial guarantee qualifies as a derivative instrument. As a result, a liability of \$7 related to the fair value of the standby letter of credit issued by a major Canadian chartered bank for the benefit of an independent funding trust which provides loans to the Company's independent franchisees was recognized, with a corresponding decrease of \$6 net of income taxes to opening retained earnings.

Section 3865, "Hedges" ("Section 3865") replaces AcG 13, "Hedging Relationships". The requirements for identification, designation, documentation and assessment of effectiveness of hedging relationships remain substantially unchanged. Section 3865 addresses the accounting treatment of qualifying hedging relationships and the necessary disclosures and also requires all derivative instruments in hedging relationships to be recorded at fair value.

Upon implementation of these requirements with respect to cash flow hedges, an increase in other assets of \$17 and an increase in other liabilities of \$34 related to the fair value of the interest rate swaps not previously recognized on the consolidated balance sheet and an increase in accumulated other comprehensive income of \$10 net of income taxes were recorded. A decrease in opening retained earnings of \$15 net of income taxes resulting from the financing element of off-market interest rate swaps was also recorded. In addition, a decrease in accumulated other comprehensive income of \$14 net of income taxes was recorded related to the effective portion of the unrealized gains and losses on the cross currency basis swaps previously recognized in retained earnings. The ineffective portion of the gains or losses on the derivatives within the hedging relationships was insignificant.

Notes to the Consolidated Financial Statements

Section 1530, "Comprehensive Income" introduces a statement of comprehensive income, which is comprised of net earnings and other comprehensive income. Other comprehensive income represents the change in shareholders' equity from transactions and other events from non-owner sources and includes unrealized gains and losses on financial assets that are classified as available-for-sale, and changes in the fair value of the effective portion of cash flow hedging instruments. The Company has included in the consolidated financial statements a new consolidated statement of comprehensive income for the changes in these items, while the cumulative changes in other comprehensive income are included in accumulated other comprehensive income, which is presented as a new category of shareholders' equity on the consolidated balance sheet. See note 20 for further details of the accumulated other comprehensive income balance.

Section 3251, "Equity", which replaced Section 3250, "Surplus", establishes standards for the presentation of equity and changes in equity during the reporting period and requires the Company to present separately equity components and changes in equity arising from i) net earnings; ii) other comprehensive income; iii) other changes in retained earnings; iv) changes in contributed surplus; v) changes in share capital; and vi) changes in reserves. New consolidated statements of changes in shareholders' equity are included in the consolidated financial statements.

Section 3861, "Financial Instruments – Disclosure and Presentation", which replaces Section 3860, of the same title, establishes standards for presentation of financial instruments and non-financial derivatives, and identifies the information that should be disclosed about them.

The following tables summarize the transitional adjustments recorded upon implementation:

	Transitional Adjustments
Consolidated Balance Sheet	
Other assets	\$ 35
Future income taxes	(7)
Other liabilities	41
Retained earnings	(15)
Accumulated other comprehensive income	16

	Retained Earnings		Accumulated Other Comprehensive Income	
	Gross	Net of Income Taxes	Gross	Net of Income Taxes
Classification of financial assets as available-for-sale	\$ (14)	\$ (14)	\$ 23	\$ 20
Classification of financial assets as held-for-trading	2	1	-	-
Non-financial derivative instrument	7	5	-	-
Guarantees	(7)	(6)	-	-
Cash flow hedges	(9)	(1)	(8)	(4)
	\$ (21)	\$ (15)	\$ 15	\$ 16

Accounting Standards Implemented in 2006

Effective January 1, 2006, the Company implemented EIC Abstract 156, "Accounting by a Vendor for Consideration Given to a Customer (Including a Reseller of the Vendor's Products)", ("EIC 156") issued by the CICA in September 2005. EIC 156 addresses cash consideration, including sales incentives, given by a vendor to a customer. This consideration is presumed to be a reduction of the selling price of the vendor's products and should therefore be classified as a reduction of sales in the vendor's statement of earnings.

Note 3. Goodwill

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

In 2006, the Company performed the annual goodwill impairment test and it was determined that the carrying value of the goodwill established on the acquisition of Provigo Inc. in 1998 exceeded its respective fair value. As a result, in 2006 the Company recorded in operating income a non-cash goodwill impairment charge of \$800 relating to this goodwill. The Company had no income tax deduction from this non-cash goodwill impairment charge. The determination that the fair value of goodwill was less than its carrying value resulted from a decline in market multiples, both from an industry and Company perspective, and a reduction of fair value as determined using the discounted cash flow methodology, incorporating both current Company and market assumptions, which in combination resulted in the goodwill impairment. In the second quarter of 2007, the Company completed its work and finalized the non-cash goodwill impairment charge of \$800 that was recorded in 2006.

In the normal course of business, the Company may acquire from time to time franchisee stores and convert them to corporate stores. In 2007, the Company acquired 4 franchisee businesses (2006 – 7 franchisee businesses). The acquisitions were accounted for using the purchase method of accounting with the results of the business acquired included in the consolidated financial statements from the date of acquisition. The fair value of the net assets acquired consisted of fixed assets of \$3 (2006 – \$2), other assets principally inventory of \$1 (2006 – \$2) and goodwill of \$8 (2006 – \$7) for cash consideration of \$9 (2006 – \$9), net of accounts receivable due from the franchisees of \$3 (2006 – \$2).

The consolidated balance sheet as at year end 2007 includes goodwill of independent franchisees that were consolidated by the Company pursuant to the requirements of AcG 15.

The following table discloses the changes in goodwill over 2007 and 2006.

	2007	2006
Balance, beginning of year	\$ 794	\$ 1,587
Goodwill acquired	8	7
Goodwill impairment	-	(800)
Other	4	-
Balance, end of year	\$ 806	\$ 794

Notes to the Consolidated Financial Statements

Note 4. Restructuring and Other Charges

Project Simplify

During 2007, the Company approved and announced the restructuring of its merchandising and store operations into more streamlined functions as part of Project Simplify. In 2007, the Company recognized \$197 of restructuring costs resulting from this plan, comprised of \$139 for employee termination benefits including severance, additional pension costs resulting from the termination of employees and retention costs; and \$58 of other costs, primarily consulting directly associated with the restructuring. The total restructuring costs under this plan, comprised primarily of severance costs, are estimated to be approximately \$200 million, with the remaining costs to be expensed in 2008.

Store Operations

During 2007, the Company completed the previously announced restructuring of its store operations. The total restructuring costs under these plans was \$51 compared to the original estimate of \$54. Of the \$51 total costs, approximately \$8 was attributable to employee termination benefits which included severance resulting from the termination of employees, \$25 to fixed asset impairment and accelerated depreciation of assets relating to these restructuring activities and \$18 to site closing and other costs including lease obligations. In 2007, the Company recognized \$16 (2006 – \$35) of these restructuring costs, which relate to site closing and other costs including lease obligations. The components of the store operations restructuring plan are described below.

As part of a review of the Quebec store operations, the Company approved and communicated a plan in 2006 to close 19 underperforming stores, mainly within the *Provigo* banner. During 2007, the Company concluded that 16 stores, 3 less than originally planned, would close under this initiative. The closure of these 16 stores was completed in 2007. The total restructuring cost under this initiative was \$37 compared to the original estimate of \$40, of which \$9 (2006 – \$28) was recognized in 2007.

Based on the Company's review of the impact on the Cash & Carry and wholesale club network of the loss in tobacco sales following the decision by a major tobacco supplier to sell directly to certain customers of the Company, the Company approved and communicated a plan in 2006 to close 24 wholesale outlets which were impacted most significantly by this change. The total restructuring cost under this initiative was \$12 compared to the original estimate of \$10, of which \$6 (2006 – \$6) was recognized in 2007.

As part of a review of the Atlantic store operations, the Company approved and communicated a plan in 2006 to close 8 stores in the Atlantic region. The total restructuring cost under this initiative was \$2 compared to the original estimate of \$4, of which \$1 (2006 – \$1) was recognized in 2007.

Supply Chain Network

During 2005, the Company approved a comprehensive plan to restructure its supply chain operations nationally. The restructuring plan is expected to be completed by the first quarter of 2009 and the total restructuring costs under this plan is estimated to be approximately \$90. Of the \$90 total estimated costs, approximately \$57 is attributable to employee termination benefits which include severance and additional pension costs resulting from the termination of employees, \$13 to fixed asset impairment and accelerated depreciation of assets relating to this restructuring activity and \$20 to site closing and other costs directly attributable to the restructuring plan. In 2007, the Company recognized \$9 (2006 – \$8) of restructuring costs resulting from this plan which is composed of \$7 (2006 – \$4) for employee termination benefits resulting from planned involuntary terminations, nil (2006 – \$2) for fixed asset impairment and accelerated depreciation and \$2 (2006 – \$2) for other costs directly associated with those initiatives. At the end of the year, \$11 in estimated costs remain to be incurred and will be recognized as appropriate criteria are met.

Office Move and Reorganization of the Operation Support Functions

In 2005, the Company consolidated several administrative and operating offices from across southern Ontario into a new national head office in Brampton, Ontario and reorganized the merchandising, procurement and operations groups which included the transfer of the general merchandise operations from Calgary, Alberta to the new office. All of the expected \$25 of costs related to these initiatives had been recognized by the end of 2006.

The following table provides a summary of the costs recognized and cash payments made, as well as the corresponding net liability as at December 29, 2007 and December 30, 2006:

	Employee Termination Benefits	Site Closing Costs and Other	2007 Total	2006 Total
Net liability, beginning of year	\$ 40	\$ -	\$ 40	\$ 41
Costs recognized:				
Project Simplify	\$ 139	\$ 58	\$ 197	\$ -
Store operations	(1)	17	16	35
Supply chain network	7	2	9	8
Office move and reorganization of the operation support functions	-	-	-	1
	\$ 145	\$ 77	\$ 222	\$ 44
Cash payments:				
Project Simplify	\$ 100	\$ 49	\$ 149	\$ -
Store operations	7	15	22	1
Supply chain network	4	1	5	6
Office move and reorganization of the operation support functions	-	-	-	2
	\$ 111	\$ 65	\$ 176	\$ 9
Charges against fixed assets	\$ -	\$ -	\$ -	\$ 27
Charges against other assets ⁽¹⁾	15	-	15	9
Net liability, end of year	\$ 59	\$ 12	\$ 71	\$ 40
Recorded in the consolidated balance sheet as follows:				
Accounts payable and accrued liabilities	38	12	50	19
Other liabilities (note 17)	21	-	21	21
Net liability, end of year	\$ 59	\$ 12	\$ 71	\$ 40

(1) Represents defined benefit pension plan cost applied to other assets. Charges against other assets relates to the contractual termination benefits cost recognized which reduced the accrued benefit plan asset.

Notes to the Consolidated Financial Statements

Note 5. Collective Agreement

During 2006, members of certain Ontario locals of the United Food and Commercial Workers union ratified a new four-year collective agreement. The new agreement enables the Company to convert 44 stores in Ontario to the *Real Canadian Superstore* banner or food stores with equivalent labour economics, and the flexibility to invest in additional store labour where appropriate. As a result of securing this agreement, the Company recognized a one-time charge in 2006 of \$84 in operating income, including a \$36 amount due to a multi-employer pension plan which was paid in 2007 (see note 14) and a payment of \$38 which was paid to employees in 2006 upon ratification.

Note 6. Interest Expense

	2007	2006
Interest on long term debt	\$ 285	\$ 284
Interest expense on financial derivative instruments	12	7
Net short term interest income (note 9)	(23)	(11)
Capitalized to fixed assets	(22)	(21)
Interest expense	\$ 252	\$ 259

During 2007, net interest expense of \$261 was recorded related to the financial assets and financial liabilities not classified as held-for-trading. In addition, \$41 (2006 – \$40) of income from cash, cash equivalents and short term investments, held by Glenhuron Bank Limited (“Glenhuron”), a wholly owned subsidiary of the Company in Barbados, was recognized in net short term interest income (see note 9).

Interest paid in 2007 was \$403 (2006 – \$405), and interest received in 2007 was \$134 (2006 – \$127).

Note 7. Income Taxes

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

	2007	2006
Weighted average basic Canadian federal and provincial statutory income tax rate	33.2%	33.7%
Net increase (decrease) resulting from:		
Earnings in jurisdictions taxed at rates different from the Canadian statutory income tax rates	1.4	(0.6)
Non-taxable amounts	(1.5)	(1.1)
Impact of statutory income tax rate changes on future income tax balances	(2.3)	(2.1)
Other	0.2	-
Effective income tax rate before impact of non-deductible goodwill impairment charge	31.0%	29.9%
Non-deductible goodwill impairment charge	-	796.8
Effective income tax rate	31.0%	826.7%

Net income taxes paid in 2007 were \$220 (2006 – \$325).

The cumulative effects of changes in Canadian federal and certain provincial statutory income tax rates on future income tax assets and liabilities are included in the consolidated financial statements at the time of substantive enactment. Accordingly, in 2007 an \$11 (2006 – \$16) net reduction to the future income tax expense was recognized as a result of the change in the Canadian federal and certain provincial statutory income tax rates.

The income tax effects of temporary differences that gave rise to significant portions of the future income tax assets (liabilities) were as follows:

	2007	2006
Accounts payable and accrued liabilities	\$ 47	\$ 55
Other liabilities	120	117
Fixed assets	(259)	(278)
Other assets	(89)	(103)
Losses carried forward (expiring 2008 to 2027)	41	20
Other	16	40
Net future income tax liabilities	\$ (124)	\$ (149)
	2007	2006
Recorded in the consolidated balance sheets as follows:		
Current future income tax assets	\$ 56	\$ 85
Non-current future income tax liabilities	(180)	(234)
Net future income tax liabilities	\$ (124)	\$ (149)

Note 8. Basic and Diluted Net Earnings (Loss) per Common Share (\$, except where otherwise indicated)

	2007	2006
Net earnings (loss) (\$ millions)	\$ 330	\$ (219)
Weighted average common shares outstanding (in millions) (note 19)	274.2	274.1
Dilutive effect of stock-based compensation (in millions)	-	.2
Diluted weighted average common shares outstanding (in millions)	274.2	274.3
Basic net earnings (loss) per common share	\$ 1.20	\$ (.80)
Dilutive effect of stock-based compensation per common share	-	-
Diluted net earnings (loss) per common share	\$ 1.20	\$ (.80)

Stock options outstanding with an exercise price greater than the market price of the Company's common shares at December 29, 2007 were not recognized in the computation of diluted net earnings (loss) per common share. Accordingly, for 2007, 6,390,459 (2006 – 4,027,406) stock options, with a weighted average exercise price of \$52.67 (2006 – \$61.55) per common share, were excluded from the computation of diluted net earnings (loss) per common share.

Notes to the Consolidated Financial Statements

Note 9. Cash and Cash Equivalents

The components of cash and cash equivalents as at December 29, 2007 and December 30, 2006 were as follows:

	2007	2006
Cash	\$ 61	\$ 89
Cash equivalents – short term investments with a maturity of 90 days or less:		
Bank term deposits	77	3
Government treasury bills	257	208
Government-sponsored debt securities	155	227
Corporate commercial paper	124	106
Bank-sponsored asset-backed commercial paper	–	36
Cash and cash equivalents	\$ 674	\$ 669

The Company recognized an unrealized foreign currency exchange loss of \$155 (2006 – gain of \$2) as a result of translating its United States dollar denominated cash, cash equivalents and short term investments, of which a loss of \$97 (2006 – income of \$1) related to cash and cash equivalents. The resulting loss or gain on cash, cash equivalents and short term investments is offset in operating income and accumulated other comprehensive income by the unrealized foreign currency exchange gain or loss on the cross currency basis swaps as described in note 22.

Note 10. Accounts Receivable

	2007	2006
Credit card receivables	\$ 2,023	\$ 1,571
Amount securitized	(1,475)	(1,250)
Net credit card receivables	548	321
Other receivables	337	407
Accounts receivable	\$ 885	\$ 728

The Company, through *PC* Bank, securitizes certain credit card receivables by selling them to independent special purpose entities or trusts that issue interest bearing securities. When *PC* Bank sells credit card receivables, it retains servicing responsibilities, certain administrative responsibilities and the right to future cash flows after obligations to investors have been met. Commencing December 31, 2006, these retained interests have been designated as held-for-trading upon the implementation of Section 3855 and are carried at their fair value in other assets. The fair value of these retained interests was estimated using management's best estimate of the net present value of expected future cash flows using key assumptions. Prior to December 31, 2006 these retained interests were carried at their original carrying amount that was periodically reviewed and written down to fair value when there was an other than temporary decline in value. Although *PC* Bank remains responsible for servicing all credit card receivables, it does not receive additional compensation for servicing those credit card receivables sold to the trusts.

During 2007, \$225 (2006 – \$240) of credit card receivables were securitized through the sale of a portion of the total interest in these receivables to independent trusts, yielding \$1 gain (2006 – nominal net loss) on the initial sale inclusive of nil (2006 – nil) servicing liability. During 2007, *PC* Bank received income of \$141 (2006 – \$114) in securitization revenue from the independent trusts relating to the securitized credit card receivables. An increase in servicing liability of \$2 (2006 – nil) was recognized during the year on securitization and the fair value at year end of recognized servicing liabilities was \$10 (2006 – \$8). The trusts' recourse to *PC* Bank's assets is limited to *PC* Bank's retained interests and is further supported by the Company through a standby letter of credit for 9% (2006 – 9%) on a portion of the securitized amount (see note 23).

Net credit loss experience of \$11 (2006 – \$9) includes \$57 (2006 – \$45) of credit losses on the total portfolio of credit card receivables net of credit losses of \$46 (2006 – \$36) relating to securitized credit card receivables.

The following table displays the sensitivity of the current fair value of retained interests to an immediate 10% and 20% adverse change in the 2007 key economic assumptions. 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.

	2007	Change in Assumptions	
		10%	20%
Carrying value of retained interests	\$ 8		
Payment rate (monthly)	43.0%		
Weighted average life (years)	0.7		
Expected credit losses (annual)	3.25%	\$ (0.9)	\$ (1.8)
Discount rate applied to residual cash flows (annual)	15.21%	\$ (0.02)	\$ (0.05)

The details on the cash flows from securitization are as follows:

	2007	2006
Proceeds from new securitizations	\$ 225	\$ 240
Net cash flows received on retained interests	\$ 143	\$ 116

Note 11. Inventory Liquidation

During 2007, the Company recognized a charge of \$15 in operating income, comprising mainly storage and shipping costs, related to certain excess inventory, primarily general merchandise, as a result of its decision in 2006 to proceed with the liquidation of this inventory. In 2006, the Company recognized a charge of \$68 to adjust inventory identified for liquidation to the lower of cost and net realizable value. The charge reflected the write-down of inventory to recovery values and the associated costs of facilitating the disposition incurred to the end of 2007. The excess inventory liquidation was completed in 2007.

Notes to the Consolidated Financial Statements

Note 12. Fixed Assets

	2007			2006		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
Properties held for development	\$ 525		\$ 525	\$ 500		\$ 500
Properties under development	89		89	226		226
Land	1,709		1,709	1,699		1,699
Buildings	5,292	\$ 1,254	4,038	4,955	\$ 1,012	3,943
Equipment and fixtures	4,108	2,857	1,251	3,788	2,475	1,313
Building and leasehold improvements	518	238	280	611	269	342
	12,241	4,349	7,892	11,779	3,756	8,023
Capital leases – buildings and equipment	164	103	61	129	97	32
	\$ 12,405	\$ 4,452	\$ 7,953	\$ 11,908	\$ 3,853	\$ 8,055

The following items were recognized in operating income during 2007: fixed asset impairment charge of \$33 (2006 – \$27), accelerated depreciation charge of \$3 (2006 – charge of \$5) and restructuring and other charges of a nominal amount (2006 – charge of \$27) (see note 4).

Note 13. Other Assets

	2007	2006
Unrealized cross currency basis swaps receivable (note 22)	\$ 270	\$ 165
Franchise investments and other receivables	186	195
Accrued benefit plan asset (note 14)	181	182
Deferred charges and other	185	147
	\$ 822	\$ 689

Included in deferred charges and other above are \$9 (2006 – nil) of unrealized interest rate swap receivable and \$5 (2006 – nil) related to an electricity forward contract (see note 22).

Note 14. Employee Future Benefits

Pension and Other Benefit Plans

The Company sponsors a number of pension plans, including registered funded defined benefit pension plans, defined contribution pension plans and supplemental unfunded arrangements providing pension benefits in excess of statutory limits. Certain obligations of the Company to these supplemental pension arrangements are secured by a standby letter of credit issued by a major Canadian chartered bank. The Company's defined benefit pension plans are predominantly non-contributory and these benefits are, in general, based on career average earnings.

A new national defined contribution pension plan for salaried employees was introduced by the Company during 2006. All eligible salaried employees were given the option to join this new plan and convert their past accrued pension benefits or to remain in their existing defined benefit pension plans. All new salaried employees participate only in the new national defined contribution pension plan.

The Company also offers certain employee post-retirement and post-employment benefit plans and a long term disability benefit plan. Post-retirement and post-employment benefit plans are generally not funded, are mainly non-contributory and include health care, life insurance and dental benefits. Employees eligible for post-retirement benefits are those who retire at certain retirement ages and employees eligible for post-employment benefits are those on long term disability leave. The majority of post-retirement health care plans for current and future retirees include a limit on the total benefits payable by the Company.

The Company also contributes to various multi-employer pension plans that provide pension benefits.

The accrued benefit plan obligations and the fair value of the benefit plan assets were determined using a September 30 measurement date for accounting purposes.

Funding of Pension and Other Benefit Plans

The most recent actuarial valuations of the defined benefit pension plans for funding purposes ("funding valuations") were performed as at December 31, 2006 for all plans, except two plans for which funding valuations are to be performed as at December 31, 2007 and were last performed as at December 31, 2004. The Company is required to file funding valuations at least every three years; accordingly, the next required funding valuations for the above mentioned plans will be performed no later than December 31, 2009 and 2010, respectively.

Total cash payments made by the Company during 2007, consisting of contributions to funded defined benefit pension plans, defined contribution pension plans, multi-employer pension plans, long term disability benefit plan and benefits paid directly to beneficiaries of the unfunded defined benefit pension plans and other benefit plans, were \$183 (2006 – \$166). In 2006, the Company accrued \$36 relating to a one-time contribution to a multi-employer pension plan which was paid in 2007 (see note 5).

During 2008, the Company expects to contribute approximately \$76 to its registered funded defined benefit pension plans. This estimate may vary subject to the completion of actuarial valuations, market performance and regulatory requirements. The Company also expects to make contributions in 2008 to defined contribution pension plans and multi-employer pension plans as well as benefit payments to the beneficiaries of the unfunded defined benefit pension plans and other benefit plans.

Notes to the Consolidated Financial Statements

Pension and Other Benefit Plans Status

Information on the Company's defined benefit pension plans and other benefit plans, in aggregate, was as follows:

	2007			2006		
	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾	Total	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾	Total
Benefit Plan Assets						
Fair value, beginning of year	\$ 1,052	\$ 44	\$ 1,096	\$ 944	\$ 42	\$ 986
Actual return (loss) on plan assets	91	1	92	74	(1)	73
Employer contributions	77	10	87	90	21	111
Employee contributions	2	2	4	2	-	2
Benefits paid	(61)	(23)	(84)	(58)	(18)	(76)
Other	-	(1)	(1)	-	-	-
Fair value, end of year	\$ 1,161	\$ 33	\$ 1,194	\$ 1,052	\$ 44	\$ 1,096
Accrued Benefit Plan Obligations						
Balance, beginning of year	\$ 1,262	\$ 308	\$ 1,570	\$ 1,155	\$ 243	\$ 1,398
Current service cost	52	44	96	50	9	59
Interest cost	65	16	81	62	13	75
Benefits paid	(61)	(23)	(84)	(58)	(18)	(76)
Actuarial (gain) / loss	(87)	(22)	(109)	55	61	116
Contractual termination benefits ⁽²⁾	7	-	7	-	-	-
Special termination benefits ⁽²⁾	6	-	6	-	-	-
Curtailment gains ⁽³⁾	(11)	(2)	(13)	-	-	-
Other	(1)	(2)	(3)	(2)	-	(2)
Balance, end of year	\$ 1,232	\$ 319	\$ 1,551	\$ 1,262	\$ 308	\$ 1,570
Deficit of Plan Assets Versus Plan Obligations						
Unamortized past service costs	\$ (71)	\$ (286)	\$ (357)	\$ (210)	\$ (264)	\$ (474)
Unamortized net actuarial loss	2	(6)	(4)	5	(7)	(2)
	193	137	330	313	172	485
Net accrued benefit plan asset (liability)	\$ 124	\$ (155)	\$ (31)	\$ 108	\$ (99)	\$ 9
Recorded in the consolidated balance sheets as follows:						
Other assets (note 13)	\$ 170	\$ 11	\$ 181	\$ 145	\$ 37	\$ 182
Other liabilities (note 17)	(46)	(166)	(212)	(37)	(136)	(173)
Net accrued benefit plan asset (liability)	\$ 124	\$ (155)	\$ (31)	\$ 108	\$ (99)	\$ 9

(1) Other benefit plans include post-retirement, post-employment and long term disability benefit plans.

(2) Contractual and special termination benefits resulted from the 2007 Project Simplify, which involves the restructuring and streamlining of the Company's merchandising and store operations, were recorded in restructuring and other charges in 2007 (see note 4).

(3) Certain defined benefit pension plans and other benefit plans affected by the 2007 Project Simplify to restructure and streamline the Company's merchandising and store operations were remeasured as at March 31, 2007 and costs subsequent to April 1, 2007 were determined using a discount rate of 5.0%. This resulted in a nominal impact to 2007 net earnings and curtailment gains which were offset against unamortized net actuarial losses for those plans.

Funded Status of Plans in a Deficit

Included in the accrued benefit plan obligations and the fair value of benefit plan assets at year end are the following amounts in respect of plans with accrued benefit plan obligations in excess of benefit plan assets:

	2007		2006	
	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾
Fair Value of Benefit Plan Assets	\$ 326	\$ 33	\$ 1,052	\$ 44
Accrued Benefit Plan Obligations	424	319	1,262	308
Deficit of Plan Assets versus Plan Obligations	\$ (98)	\$ (286)	\$ (210)	\$ (264)

(1) Other benefit plans include post-retirement, post-employment and long term disability benefit plans.

Asset Allocations

The benefit plan assets are held in trust and at September 30 consisted of the following asset categories:

Percentage of Plan Assets	2007		2006	
	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾
Asset Category				
Equity securities	63%	– %	63%	–%
Debt securities	35%	91%	36%	93%
Cash and cash equivalents	2%	9%	1%	7%
Total	100%	100%	100%	100%

(1) Other benefit plans include post-retirement, post-employment and long term disability benefit plans.

Pension benefit plan assets include securities issued by the Company's majority shareholder, George Weston Limited ("Weston"), and by Loblaw having a fair value of \$5 and \$1 (2006 – \$3 and nil), respectively, as at September 30, 2007. Other benefit plan assets do not include any Weston or Loblaw securities.

Notes to the Consolidated Financial Statements

Pension and Other Benefit Plans Cost

The total net cost for the Company's benefit plans and multi-employer pension plans was as follows:

	2007		2006	
	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾
Current service cost, net of employee contributions	\$ 50	\$ 42	\$ 48	\$ 9
Interest cost on plan obligations	65	16	62	13
Actual (return) loss on plan assets	(91)	(1)	(74)	1
Actuarial (gain) loss	(87)	(22)	55	61
Contractual termination benefits ⁽²⁾	7	-	-	-
Special termination benefits ⁽²⁾	6	-	-	-
Curtailment loss ⁽²⁾	2	-	-	-
Defined benefit plan (income) cost, before adjustments to recognize the long term nature of employee future benefit costs	(48)	35	91	84
Excess (shortfall) of actual return over expected return on plan assets	9	(1)	(1)	(4)
Excess (shortfall) of amortized net actuarial loss over actual actuarial loss on accrued benefit obligation	99	34	(43)	(40)
(Shortfall) excess of amortized past service costs over actual past service costs	-	(1)	1	-
Net defined benefit plan cost	60	67	48	40
Defined contribution plan cost	10	-	6	-
Multi-employer pension plan cost ⁽³⁾	50	-	85	-
Net benefit plan cost	\$ 120	\$ 67	\$ 139	\$ 40
Recognized in the consolidated statements of earnings as follows:				
Pension and other benefit plan costs	\$ 105	\$ 67	\$ 139	\$ 40
Restructuring and other charges ⁽²⁾	15	-	-	-
Net benefit plan cost	\$ 120	\$ 67	\$ 139	\$ 40

(1) Other benefit plans include post-retirement, post-employment and long term disability benefit plans.

(2) Contractual and special termination benefits and curtailment losses resulted from the 2007 Project Simplify, which involves the restructuring and streamlining of the Company's merchandising and store operations, were recorded in restructuring and other charges in 2007 (see note 4).

(3) Included in 2006 is a \$36 amount relating to a one-time contribution to a multi-employer pension plan which was paid in 2007 (see note 5).

Plan Assumptions

The significant annual weighted average actuarial assumptions used in calculating the Company's accrued benefit plan obligations as at the measurement date of September 30 and the net defined benefit plan cost for the year were as follows:

	2007		2006	
	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾	Pension Benefit Plans	Other Benefit Plans ⁽¹⁾
Accrued Benefit Plan Obligations				
Discount rate	5.5%	5.3%	5.0%	5.0%
Rate of compensation increase	3.5%		3.5%	
Net Defined Benefit Plan Cost				
Discount rate ⁽²⁾	5.0%	5.0%	5.25%	5.2%
Expected long term rate of return on plan assets	7.75%	5.0%	8.0%	5.0%
Rate of compensation increase	3.5%		3.5%	

(1) Other benefit plans include post-retirement, post-employment and long term disability benefit plans.

(2) Certain defined benefit pension plans and other benefit plans affected by the 2007 Project Simplify to restructure and streamline the Company's merchandising and store operations were remeasured as at March 31, 2007 and costs subsequent to April 1, 2007 were determined using a discount rate of 5.0%. This resulted in a nominal impact to 2007 net earnings and curtailment gains which were offset against unamortized net actuarial losses for those plans.

The growth rate of health care costs, primarily drug and other medical costs for other benefit plans, was estimated at 10.0% (2006 – 10.0%) and is assumed to gradually decrease to 5.0% by 2015 (2006 – 5.0% by 2014), remaining at that level thereafter.

Sensitivity of Key Assumptions

The following table outlines the key assumptions for 2007 and the sensitivity of a 1% change in each of these assumptions on the accrued benefit plan obligations and on the benefit plan cost for defined benefit pension plans and other benefit plans. The table reflects the impact on the current service and interest cost components for the discount rate and expected growth rate of health care costs assumptions.

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.

	Pension Benefit Plans		Other Benefit Plans ⁽¹⁾	
	Accrued Benefit Plan Obligations	Benefit Plan Cost ⁽²⁾	Accrued Benefit Plan Obligations	Benefit Plan Cost ⁽²⁾
Expected long term rate of return on plan assets		7.75%		5.0%
Impact of: 1% increase	n/a	\$ (11)	n/a	\$ -
1% decrease	n/a	\$ 11	n/a	\$ -
Discount rate	5.5%	5.0%	5.3%	5.0%
Impact of: 1% increase	\$ (174)	\$ (9)	\$ (37)	\$ (4)
1% decrease	\$ 203	\$ 10	\$ 42	\$ 4
Expected growth rate of health care costs ⁽³⁾			10.0%	10.0%
Impact of: 1% increase	n/a	n/a	\$ 31	\$ 5
1% decrease	n/a	n/a	\$ (27)	\$ (5)

n/a – not applicable

(1) Other benefit plans include post-retirement, post-employment and long term disability benefit plans.

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

(3) Gradually decreasing to 5.0% by 2015 for the accrued benefit plan obligation and the benefit plan cost, and remaining at that level thereafter.

Notes to the Consolidated Financial Statements

Note 15. Short Term Debt

During 2007, the Company entered into a 364-day revolving committed credit facility of \$500 million, which matures in March 2008 and has no financial covenants. Borrowings are based on short term floating interest rates. At December 29, 2007, nil was drawn on this facility. Subsequent to December 29, 2007, the Company obtained a 60-day extension of the facility extending the maturity date to May 2008.

Note 16. Long Term Debt

	2007	2006
Loblaw Companies Limited Notes		
6.00%, due 2008	\$ 390	\$ 390
5.75%, due 2009	125	125
7.10%, due 2010	300	300
6.50%, due 2011	350	350
5.40%, due 2013	200	200
6.00%, due 2014	100	100
7.10%, due 2016	300	300
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	(44)	(34)
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
Other at a weighted average interest rate of 9.57%, due 2008 to 2043	17	21
VIE loans payable (i) (see note 26)	153	124
Capital lease obligations (i) (see note 18)	62	32
Total long term debt	4,284	4,239
Less amount due within one year	432	27
	\$ 3,852	\$ 4,212

(i) Pursuant to the requirements of AcG 15, the consolidated balance sheet as at December 29, 2007 includes \$183 (2006 – \$156) of loans payable and capital lease obligations of VIEs consolidated by the Company, \$32 (2006 – \$23) of which is due within one year.

The schedule of repayment of long term debt, inclusive of VIE and other debt, based on maturity is as follows: 2008 – \$432; 2009 – \$149; 2010 – \$326; 2011 – \$376; 2012 – \$24; thereafter – \$2,977.

During 2006, the Company repaid its \$125 of 8.70% Series 1996 Provigo Inc. Debenture as it matured.

The VIE loans payable of \$153 (2006 – \$124) represent financing obtained by eligible independent franchisees through a structure involving independent trusts to facilitate the purchase of the majority of their inventory and fixed assets, consisting mainly of fixtures and equipment. The loans payable, which have an average term to maturity of 7 years (2006 – 8 years), are due and payable on demand under certain predetermined circumstances and are secured through a general security agreement made by the independent franchisees in favour of the independent funding trust. Interest is charged on a floating rate basis and prepayment of the loans may be made without penalty. The independent funding trust within the structure finances its activities through the issuance of short term asset-backed commercial paper (“ABCP”) to third-party investors. The independent funding trust has a global style liquidity agreement from a major Canadian chartered bank in the event that it is unable to issue short term ABCP. As disclosed in note 23, a standby letter of credit has been provided by a major Canadian chartered bank for the benefit of the independent funding trust equal to approximately 10% of the total principal amount of the loans outstanding at any point in time. The Company has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit. In the event of a default by an independent franchisee and the Company has not, within a specified time period assumed the loan, or the default is not otherwise remedied, the independent funding trust shall assign the loan to the Company and draw upon the standby letter of credit (see note 26).

The fair value of long term debt issues at year end 2007 is \$4,216 (2006 – \$4,798). The fair values were estimated based on the discounted cash flows of the debt at the Company’s estimated incremental borrowing rates for debt of the same remaining maturities.

Note 17. Other Liabilities

	2007	2006
Accrued benefit plan liability (note 14)	\$ 212	\$ 173
Unrealized equity forwards payable (note 22)	91	13
Unrealized interest rate swap liability (note 22)	28	–
Goods and services tax and provincial sales tax	23	14
Restructuring and other charges (note 4)	21	21
Stock-based compensation (note 21)	10	17
Other	74	76
	\$ 459	\$ 314

Note 18. Leases

As Lessee

Future minimum lease payments relating to the Company’s operating leases are as follows:

	Payments due by year						2007 Total	2006 Total
	2008	2009	2010	2011	2012	Thereafter to 2046		
Operating lease payments	\$ 192	\$ 172	\$ 150	\$ 128	\$ 108	\$ 673	\$ 1,423	\$ 1,492
Expected sub-lease income	(37)	(31)	(26)	(20)	(16)	(42)	(172)	(188)
Net operating lease payments	\$ 155	\$ 141	\$ 124	\$ 108	\$ 92	\$ 631	\$ 1,251	\$ 1,304

Notes to the Consolidated Financial Statements

Capital Leases

Capital lease obligations of \$62 (2006 – \$32) are included in the consolidated balance sheet as at year end (see note 16). The capital lease obligations are related primarily to equipment of the third-party VIE that provides distribution and warehousing services. The amount due within one year is \$9 (2006 – \$4).

Sale-Leaseback

In 2007, the Company completed a sale-leaseback transaction of property and a partially constructed building (“Property”) for a total purchase price of \$109, subject to a vendor take back mortgage of \$27 which bears interest at 6% due in 2009. There was no gain or loss recorded on the sale of the Property. The Company has leased back the Property for a term of 20 years, with options to renew for an additional 20 years, and in turn subleased the Property to a third-party logistics provider. The leaseback was accounted for as an operating lease and commences in 2008. The Company also entered into a warehousing and distribution agreement with the third-party logistics provider, which will use this Property to provide services to Loblaw.

Note 19. Common Share Capital (authorized – unlimited)

The changes in the common shares issued and outstanding during the year were as follows:

	2007		2006	
	Number of Common Shares	Common Share Capital	Number of Common Shares	Common Share Capital
Issued and outstanding, beginning of year	274,173,564	\$ 1,196	274,054,814	\$ 1,192
Stock options exercised for shares (note 21)	–	–	118,750	4
Issued and outstanding, end of year	274,173,564	\$ 1,196	274,173,564	\$ 1,196
Weighted average outstanding	274,173,564		274,066,885	

Normal Course Issuer Bids (“NCIB”) The Company intends to renew its NCIB to purchase on the Toronto Stock Exchange or enter into equity forwards to purchase up to 5% of its common shares outstanding. The Company, in accordance with the rules and by-laws of the Toronto Stock Exchange, may purchase its shares at the then market price of such shares. The Company did not purchase any shares under its NCIB during 2007 or 2006.

Note 20. Accumulated Other Comprehensive Income

The following table provides further detail regarding the composition of accumulated other comprehensive income for the year ended December 29, 2007:

	Cash Flow Hedges	Available- for-sale Assets	Total
Balance, beginning of year	\$ -	\$ -	\$ -
Cumulative impact of implementing new accounting standards (net of income taxes of \$1) (note 2)	(4)	20	16
Net unrealized loss on available-for-sale financial assets (net of income taxes of \$5)	-	(56)	(56)
Reclassification of loss on available-for-sale financial assets (net of income taxes of nil)	-	33	33
Net gain on derivatives designated as cash flow hedges (net of income taxes of \$2)	57	-	57
Reclassification of gain on derivatives designated as cash flow hedges (net of income taxes of \$1)	(31)	-	(31)
Balance, end of year	\$ 22	\$ (3)	\$ 19

An estimated net gain of \$18 recorded in accumulated other comprehensive income related to the cash flow hedges as at December 29, 2007, is expected to be reclassified to net earnings during the next 12 months. This will be offset by the estimated loss on available-for-sale financial assets that are hedged. Remaining amounts will be reclassified to net earnings over periods up to 4 years.

Note 21. Stock-Based Compensation (\$, except where otherwise indicated)

The Company maintains various types of stock-based compensation plans, which are described below.

The Company's net stock-based compensation cost recognized in operating income related to its stock option plan and the associated equity forwards and the restricted share unit plan was as follows:

(\$ millions)	2007	2006
Stock option plan income	\$ -	\$ (11)
Equity forwards loss (note 22)	67	32
Restricted share unit plan expense	5	16
Net stock-based compensation cost	\$ 72	\$ 37

Stock Option Plan The Company maintains a stock option plan for certain employees. Under this plan, the Company may grant options for up to 20.4 million common shares; however, the Company has set a guideline which limits the number of stock option grants to a maximum of 5% of outstanding common shares at any time. Stock options have up to a seven-year term, vest 20% cumulatively on each anniversary date of the grant and are exercisable at the designated common share price, which is 100% of the market price of the Company's common shares on the last trading day prior to the effective date of the grant. Each stock option is exercisable into one common share of the Company at the price specified in the terms of the option, or option holders may elect to receive in cash the share appreciation value equal to the excess of the market price at the date of exercise over the specified option price.

During 2007, the Company granted 4,368,980 (2006 – 189,354) stock options with a weighted average exercise price of \$47.28 (2006 – \$55.30) per common share under its existing stock option plan, which allows for settlement in shares or in the share appreciation value in cash at the option of the employee.

Notes to the Consolidated Financial Statements

In 2007, the share appreciation value of a nominal amount (2006 – \$11 million) was paid on the exercise of 108,000 (2006 – 815,403) stock options. The Company issued nil (2006 – 118,750) common shares on the exercise of stock options and received cash consideration of nil (2006 – \$4 million) for which it had recorded a stock-based compensation liability of nil (2006 – \$0.1 million).

At year end, a total of 6,532,756 (2006 – 4,084,646) stock options were outstanding, and represented approximately 2.4% (2006 – 1.5%) of the Company's issued and outstanding common shares, which was within the Company's guideline of 5%. Of the 6,532,756 (2006 – 4,084,646) outstanding options, 6,491,516 (2006 – 4,043,406) relate to stock option grants that allow for settlement in shares or in the share appreciation value in cash at the option of the employee and 41,240 (2006 – 41,240) relate to stock option grants, issued prior to December 30, 2001 that will be settled by issuing common shares.

A summary of the status of the Company's stock option plan and activity was as follows:

	2007		2006	
	Options (number of shares)	Weighted Average Exercise Price/Share	Options (number of shares)	Weighted Average Exercise Price/Share
Outstanding options, beginning of year	4,084,646	\$ 61.36	5,305,422	\$ 56.98
Granted	4,368,980	\$ 47.28	189,354	\$ 55.30
Exercised	(108,000)	\$ 48.75	(934,153)	\$ 35.18
Forfeited/cancelled	(1,812,870)	\$ 60.69	(475,977)	\$ 61.56
Outstanding options, end of year	6,532,756	\$ 52.34	4,084,646	\$ 61.36
Options exercisable, end of year	1,314,278	\$ 59.00	1,544,232	\$ 57.37

Range of Exercise Prices	2007 Outstanding Options			2007 Exercisable Options	
	Number of Options Outstanding	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price/Share	Number of Exercisable Options	Weighted Average Exercise Price/Share
\$ 33.03 – \$ 49.11	4,077,233	6	\$ 47.16	47,240	\$ 48.50
\$ 50.80 – \$ 55.50	1,332,112	3	\$ 53.56	817,675	\$ 53.73
\$ 69.63 – \$ 72.95	1,123,411	4	\$ 69.69	449,363	\$ 69.69

Restricted Share Unit ("RSU") Plan The Company maintains a RSU plan for certain senior employees. The RSUs entitle employees to a cash payment after the end of each performance period, of up to 3 years, following the date of award. The RSU payment will be an amount equal to the weighted average price of a Loblaw common share on the last three trading days preceding the end of the performance period for the RSUs multiplied by the number of RSUs held by the employee.

During 2007, the Company granted 335,056 (2006 – 691,001) RSUs to 349 (2006 – 238) employees, 161,621 (2006 – 211,526) RSUs were cancelled and 154,700 (2006 – 112,707) were paid out in the amount of \$8 million (2006 – \$6 million). At year end, a total of 768,687 (2006 – 749,952) RSUs were outstanding.

Employee Share Ownership Plan (“ESOP”) The Company maintains an ESOP which allows employees to acquire the Company's common shares through regular payroll deductions of up to 5% of their gross regular earnings. The Company contributes an additional 25% (2006 – 25%) of each employee's contribution to the plan. The ESOP is administered through a trust which purchases the Company's common shares on the open market on behalf of employees. A compensation cost of \$6 million (2006 – \$6 million) related to this plan was recognized in operating income.

Deferred Share Units (“DSUs”) Plan Members of the Company's Board of Directors, who are not management of the Company, may elect annually to receive all or a portion of their annual retainer(s) and fees in the form of DSUs, the value of which is determined by the market price of the Company's common shares at the time the director's annual retainer(s) or fees are earned. Upon termination of Board service, the common shares due to the director, as represented by the DSUs, will be purchased on the open market on the director's behalf. At year end, 56,082 (2006 – 44,397) DSUs were outstanding. The year-over-year change in the deferred share unit compensation liability was minimal and was recognized in operating income.

Note 22. Financial Instruments

A summary of the Company's outstanding financial derivative instruments is as follows:

	Notional Amounts Maturing						2007	2006
	2008	2009	2010	2011	2012	Thereafter	Total	Total
Cross currency basis swaps	\$ 140	\$ 31	\$ 174	\$ 56	\$ 166	\$ 533	\$ 1,100	\$ 1,060
Interest rate swaps receivable	\$ 240	\$ 140	\$ 50	\$ 200	\$ –	\$ –	\$ 630	\$ 630
Interest rate swaps payable	\$ –	\$ –	\$ –	\$ –	\$ –	\$ 150	\$ 150	\$ 150
Equity forwards	\$ –	\$ –	\$ 124	\$ 35	\$ 25	\$ 70	\$ 254	\$ 247
Electricity forward contract	\$ 9	\$ 8	\$ 8	\$ 8	\$ –	\$ –	\$ 33	\$ 42

Notional amounts do not represent assets or liabilities and are therefore not recorded on the consolidated balance sheet. The notional amounts are used in order to calculate the payments to be exchanged under the contracts.

Cross Currency Basis Swaps The Company enters into cross currency basis swaps to manage its exposure to fluctuations in the foreign currency exchange rate on a portion of its United States dollar denominated cash, cash equivalents and short term investments.

The Company entered into cross currency basis swaps to exchange United States dollars for \$1.1 billion (2006 – \$1.1 billion) Canadian dollars, which mature by 2017. Cross currency basis swaps totalling \$590 are designated in a cash flow hedge and the remaining undesignated \$510 are classified as held-for-trading financial assets. Currency adjustments receivable or payable arising from these swaps are settled in cash on maturity. A cumulative unrealized foreign currency exchange rate receivable of \$270 (2006 – \$165) was recorded in other assets.

Interest Rate Swaps The Company enters into interest rate swaps to manage a portion of its exposure to fluctuations in interest rates. The Company's interest rate swaps convert a notional \$630 (2006 – \$630) of its floating rate available-for-sale cash equivalents and short term investments to average fixed rate investments at 5.60% (2006 – 5.60%), which mature by 2011. At year end, the fair value of these interest rate swaps of \$9 was recorded in other assets and the unrealized fair value gain of \$9 is deferred, net of tax, in accumulated other comprehensive income. When realized, these unrealized gains are reclassified to net earnings. Prior to December 31, 2006, these unrealized gains or losses were not recognized on the Company's balance sheet.

Notes to the Consolidated Financial Statements

During 2007, the Company terminated hedge accounting for its interest rate swaps previously designated as a cash flow hedge of the variable interest rate exposure on commercial paper. These interest rate swaps converted a notional \$150 (2006 – \$150) of floating rate commercial paper debt to an average fixed rate debt of 8.37% (2006 – 8.37%) which matures by 2013. As a result of this termination, the cumulative loss of \$2, net of income taxes, in accumulated other comprehensive income was reclassified to net earnings. At year end, the fair value of these interest rate swaps of \$28 was recorded in other liabilities. Prior to December 31, 2006, these unrealized gains or losses were not recognized on the Company's balance sheet.

Equity Forwards (\$, except where otherwise indicated) The Company enters into equity forwards to manage its exposure to fluctuations in its stock-based compensation cost as a result of changes in the market price of its common shares. At year end 2007, the Company had cumulative equity forwards to buy 4.8 million (2006 – 4.8 million) of its common shares at a cumulative average forward price of \$53.14 (2006 – \$51.43) including \$8.27 (2006 – \$6.56) per common share of interest expense net of dividends that has been recognized in net earnings and will be paid at termination. The equity forwards allow for settlement in cash, common shares or net settlement. They change in value as the market price of the Company's common shares changes and provide a partial offset to fluctuations in Loblaw's stock-based compensation cost, including RSU plan expense. The partial offset between the Company's stock-based compensation costs, including RSU plan expense, and the equity forwards is effective when the market price of the Company's common shares exceed the exercise price of the related employee stock options. When the market price of the common shares is lower than the exercise price of the related employee stock options, only RSUs will provide a partial offset to these equity forwards. The amount of net stock-based compensation cost recorded in operating income is mainly dependent upon the number of unexercised stock options and RSUs and their vesting schedules relative to the number of underlying common shares on the equity forwards and the level of and fluctuations in the market price of the underlying common shares. The Company has included a cumulative unrealized market loss, interest and dividends of \$91 million (2006 – \$13 million) in other liabilities relating to these equity forwards.

Electricity Forward Contract The Company entered into an electricity forward contract to minimize price volatility and to maintain a portion of the Company's electricity costs in Alberta, Canada at approximately 2006 rates. This electricity forward contract has an initial term of five years and expires in December 2011. Commencing December 31, 2006, Loblaw is required to measure its electricity forward contract at fair value in accordance with Section 3855. At year end, the fair value of this forward contract of \$5 was recorded in other assets. During 2007, a loss in value of \$2 was recorded in operating income. Prior to December 31, 2006, this non-financial derivative instrument was not recognized on the comparative period consolidated balance sheet and therefore gains and losses due to fair value changes in the contract were also not recognized in the Company's statement of earnings.

Fair Value of Derivative Instruments The fair value of derivative instruments is the estimated amount that the Company would receive or pay to terminate the instrument agreement at the reporting date. The fair values have been determined by reference to prices available from the markets on which the instruments trade and prices provided by counterparties. Commencing December 31, 2006, the fair value of all derivative instruments approximated their carrying value and are recorded in other assets or other liabilities. Prior to December 31, 2006, the interest rate swaps were not recorded on the comparative consolidated balance sheet. The unrecorded unrealized interest rate swap receivable was \$17, as at December 30, 2006.

The following table summarizes the change in fair value of financial assets and financial liabilities, including non-financial derivatives, classified as held-for-trading, recognized in net earnings in 2007, before income taxes and minority interest.

	52 Weeks Ended December 29, 2007	
	Designated as held-for-trading	Required to be classified as held-for-trading
Cash equivalents and short term investments	\$ 76	\$ –
Electricity forward	–	2
Interest rate swaps	–	5
Cross currency basis swaps	–	(79)
Equity forwards associated with stock-based compensation	–	79
Fair value loss	\$ 76	\$ 7

Fair Value of Other Financial Instruments The fair values of accounts receivable, bank indebtedness, commercial paper, accounts payable and accrued liabilities and short term debt approximate their carrying values given their short term maturities. See note 16 for carrying and fair values of long term debt.

The equity investment in franchises is measured at cost because there is no quoted market prices in an active market and these investments are classified as available-for-sale.

Foreign Currency Exchange Rate Risk The Company is exposed to foreign currency exchange rate variability on its cash, cash equivalents and short term investments. At year end, the Company had \$801 (2006 – \$864) in cash, cash equivalents and short term investments held by Glenhuron. To manage this risk, the company designates a portion of its cross currency basis swaps in a cash flow hedge of the exposure to fluctuations in the foreign currency exchange rate on a portion of its United States dollar denominated cash equivalents and short term investments. The remaining undesignated cross currency basis swaps economically hedge exposure to fluctuations in the foreign currency exchange rate on the remaining United States dollar denominated cash, cash equivalents and short term investments.

During the year, the unrealized foreign currency exchange loss of \$79, related to the cash equivalents and short term investments classified as available-for-sale is recognized in other comprehensive income and was partially offset by the unrealized foreign currency exchange rate gain of \$72 before income taxes relating to the designated cross currency basis swaps also deferred in other comprehensive income. The unrealized foreign currency exchange loss of \$76 on the designated held-for-trading cash, cash equivalents and short term investments is partially offset in operating income by the unrealized foreign currency exchange rate gain of \$79 relating to the cross currency basis swaps which are not designated in a cash flow hedge. During the year, the Company realized a foreign currency exchange gain of \$46 relating to cross currency basis swaps that matured or were terminated.

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

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

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

Credit risk from *PC* Bank's credit card receivables and receivables from independent franchisees, associates and independent accounts results from the possibility that customers may default on their payment obligation. *PC* Bank manages the credit card receivable risk by employing stringent credit scoring techniques and 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.

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

Notes to the Consolidated Financial Statements

Note 23. Contingencies, Commitments and Guarantees

The Company is involved in and potentially subject to various claims by third parties arising out of the normal course and conduct of its business including, but not limited to, product liability, labour and employment, regulatory and environmental claims. In addition, the Company is involved in and potentially subject to regular audits from federal and provincial tax authorities relating to income, capital and commodity taxes and as a result of these audits may receive assessments and reassessments.

Although such matters cannot be predicted with certainty, management currently considers the Company's exposure to such claims and litigation, to the extent not covered by the Company's insurance policies or otherwise provided for, not to be material to these consolidated financial statements, with the exception of the items disclosed in legal proceedings below.

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

The Company establishes standby letters of credit used in connection with certain obligations mainly related to real estate transactions and benefit programs. The aggregate gross potential liability related to these standby letters of credit is approximately \$221 (2006 – \$221). Other standby letters of credit related to the financing program for the Company's independent franchisees and securitization of PC Bank's credit card receivables have been identified as guarantees and are discussed further in the Guarantees section below.

Guarantees The Company has provided to third parties the following significant guarantees as defined pursuant to AcG 14, "Disclosure of Guarantees":

Independent Funding Trust Independent franchisees of the Company may obtain financing through a structure involving independent trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. These trusts are administered by a major Canadian chartered bank. The independent funding trust within the structure finances its activities through the issuance of short term ABCP to third-party investors. The independent funding trust has a global style liquidity agreement from a major Canadian chartered bank in the event that it is unable to issue short term ABCP. The gross principal amount of loans issued to the Company's independent franchisees outstanding as of December 29, 2007 was \$418 (2006 – \$419) including \$153 (2006 – \$124) of loans payable by VIEs consolidated by the Company in 2007 (see note 26). Based on a formula, the Company has agreed to provide credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trust equal to approximately 10% of the principal amount of the loans outstanding at any point in time, \$44 (2006 – \$44) as of December 29, 2007 (see note 26). This credit enhancement allows the independent funding trust to provide favorable financing terms to the Company's independent franchisees. As well, each independent franchisee provides security to the independent funding trust for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and the Company has not, within a specified time period, assumed the loan or the default is not otherwise remedied, the independent funding trust shall assign the loan to the Company and draw upon this standby letter of credit. The Company has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit. As a result of implementing Section 3855 (see note 2), a liability of \$7 related to the fair value of this standby letter of credit was recognized.

Neither the independent funding trust nor the Company can voluntarily terminate the agreement prior to December 2009, and following that date only upon six months' prior notice. Automatic termination of the agreement can only occur if specific, predetermined events occur and are not remedied within the time periods required including downgrades of the Company below a long term credit rating of "A (low)" or a short term credit rating of "R-1 (low)" as issued by Dominion Bond Rating Service ("DBRS"). On February 7, 2008, DBRS downgraded the Company's long term credit rating to "BBB (high)" from "A (low)" and also lowered the Company's short term credit rating to "R-2 (high)" from "R-1 (low)". Subsequent to the DBRS downgrades, the Company was notified that an Event of Termination of the independent funding trust agreement for the Company's franchisees had occurred as a result of the credit rating downgrades. The \$44 (2006 – \$44) standby letter of credit provided to the independent funding trust by the Company has not been drawn upon. If such an event were to occur, long term debt in the amount of \$126 would need to be reclassified to short term liabilities. This amount relates to certain franchisees that are VIEs that the Company currently consolidates. The Company is currently in the process of securing alternative financing with a syndicate of banks in the form of a 364-day committed credit facility for the benefit of its franchisees to address this issue. Any new alternative financing structure, which

might be implemented, would need to be reviewed to determine if there are any implications with respect to the consolidation of VIEs. In accordance with Canadian GAAP, the financial statements of the independent funding trust are not consolidated with those of the Company.

Standby Letter of Credit A standby letter of credit for the benefit of an independent trust with respect to the credit card receivables securitization program of *PC* Bank has been issued by a major Canadian chartered bank. This standby letter of credit could be drawn upon in the event of a major decline in the income flow from or in the value of the securitized credit card receivables. The Company has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit. The aggregate gross potential liability under this arrangement, which represents 9% (2006 – 9%) on a portion of the securitized credit card receivables amount, is approximately \$89 (2006 – \$68) (see note 10).

Lease Obligations In connection with historical dispositions of certain of its assets, the Company has assigned leases to third parties. The Company remains contingently liable for these lease obligations in the event any of the assignees are in default of their lease obligations. The estimated amount for minimum rent, which does not include other lease related expenses such as property tax and common area maintenance charges, is in aggregate \$79 (2006 – \$111).

Indemnification Provisions The Company from time to time enters into agreements in the normal course of its business, such as service and outsourcing arrangements and leases, in connection with business or asset acquisitions or dispositions. These agreements by their nature may provide for indemnification of counterparties. These indemnification provisions may be in connection with breaches of representation and warranty or with future claims for certain liabilities, including liabilities related to tax and environmental matters. The terms of these indemnification provisions vary in duration and may extend for an unlimited period of time. Given the nature of such indemnification provisions, the Company is unable to reasonably estimate its total maximum potential liability as certain indemnification provisions do not provide for a maximum potential amount and the amounts are dependent on the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time. Historically, the Company has not made any significant payments in connection with these indemnification provisions.

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

In addition to the claim described above, 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 is uncertain. However, based on information currently available, these claims, individually and in the aggregate, are not expected to have a material impact on the Company.

Note 24. Variable Interest Entities (“VIEs”)

Pursuant to AcG 15, the Company consolidates all VIEs for which it is the primary beneficiary. AcG 15 defines a VIE as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. AcG 15 requires the primary beneficiary to consolidate VIEs and considers an entity to be the primary beneficiary of a VIE if it holds variable interests that expose it to a majority of the VIE's expected losses or that entitle it to receive a majority of the VIE's expected residual returns or both. The Company has identified the following significant VIEs:

Independent Franchisees The Company enters into various forms of franchise agreements that generally require the independent franchisee to purchase inventory from the Company and pay certain fees in exchange for services provided by the Company and for the right to use certain trademarks and licenses owned by the Company. Independent franchisees generally lease the land and building from

Notes to the Consolidated Financial Statements

the Company, and when eligible, may obtain financing through a structure involving independent trusts to facilitate the purchase of the majority of their inventory and fixed assets, consisting mainly of fixtures and equipment. These trusts are administered by a major Canadian chartered bank. Under the terms of certain franchise agreements, the Company may also lease equipment to independent franchisees. Independent franchisees may also obtain financing through operating lines of credit with traditional financial institutions or through issuing preferred shares or notes payable to the Company. The Company monitors the financial condition of its independent franchisees and provides for estimated losses or write-downs on its accounts and notes receivable or investments when appropriate.

As at year end 2007, 137 (2006 – 123) of the Company's independent franchise stores met the criteria for a VIE and were consolidated pursuant to AcG 15.

Warehouse and Distribution Agreement The Company has warehouse and distribution agreements with third-party entities to provide to the Company distribution and warehousing services from dedicated facilities. The Company has no equity interest in these third-party entities; however, the terms of the agreement with the third-party entities are such that the Company has determined that the third-party entities meet the criteria for a VIE that requires consolidation by the Company. The impact of the consolidation of the warehouse and distribution entities were not material.

Accordingly, the Company has included the results of these independent franchisees and these third-party entities that provide distribution and warehousing services in its consolidated financial statements. The consolidation of these VIEs by the Company does not result in any change to its tax, legal or credit risks, nor does it result in the Company assuming any obligations of these third parties.

Independent Trust The Company has also identified that it holds a variable interest, by way of a standby letter of credit, in an independent trust which is used to securitize credit card receivables for PC Bank. In these securitizations, PC Bank sells a portion of its credit card receivables to the independent trust in exchange for cash. Although this independent trust has been identified as a VIE, it was determined that the Company is not the primary beneficiary and therefore this VIE is not subject to consolidation by the Company. The Company's maximum exposure to loss as a result of its involvement with this independent trust is disclosed in notes 10 and 23.

In 2006, PC Bank restructured its credit card securitization program. Eagle Credit Card Trust ("Eagle"), a previously established independent trust, issued \$500 of five year senior notes and subordinated notes due in 2011 at a weighted average rate of 4.5% to finance the purchase of credit card receivables previously securitized by PC Bank through an independent trust. The subordinated notes provide credit support to those notes which are more senior. PC Bank will continue to service the credit card receivables on behalf of Eagle, but will not receive any fee for its servicing obligations and has a retained interest in the securitized receivables represented by the right to future cash flows after obligations to investors have been met. In accordance with Canadian GAAP, the financial statements of Eagle are not consolidated with those of the Company. The restructuring of the portfolio yielded a nominal net loss.

Note 25. Related Party Transactions

The Company's majority shareholder, George Weston Limited and its affiliates other than Loblaw ("Weston"), are related parties. It is the Company's policy to conduct all transactions and settle all balances with related parties on market terms and conditions. Related party transactions include:

Inventory Purchases Purchases of inventory from related parties for resale in the distribution network represented approximately 3% (2006 – 3%) of the cost of sales, selling and administrative expenses.

Cost Sharing Agreements Weston has entered into certain contracts with third parties for administrative and corporate services, including telecommunication services and information technology related matters on behalf of the Company. Through cost sharing agreements that have been established between the Company and Weston concerning these costs, the Company has agreed to be responsible to Weston for its proportionate share of the costs incurred on its behalf. Payments by the Company pursuant to these cost sharing agreements in 2007 were approximately \$27 (2006 – \$25).

Real Estate Matters The Company leases certain properties from an affiliate of Weston, namely office space for approximately \$2 (2006 – \$4). During 2006, the Company purchased from an affiliate of Weston, a property designated for future development for consideration of \$8, which was prepaid in accordance with a former ground lease between the parties.

Borrowings/Lendings The Company, from time to time, may borrow funds from or may lend funds to Weston on a short term basis at short term market borrowing rates. There were no such amounts outstanding as at year end.

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

Management Agreements The Company has entered into an agreement with Weston to provide certain administrative services by each company to the other. The services to be provided under this agreement include those related to commodity management, pension and benefits, tax, medical, travel, information system, risk management, treasury and legal. Payments are made quarterly based on the actual costs of providing these services. Where services are provided on a joint basis for the benefit of the Company and Weston together, each party pays the appropriate proportion of such costs. Net payments under this agreement in 2007 were \$9. Fees paid under this agreement are reviewed each year by the Audit Committee.

The Company, through Glenhuron, manages certain United States cash, cash equivalents and short term investments for wholly owned non-Canadian subsidiaries of Weston and management fees earned are based on market rates. Glenhuron has an agreement with a subsidiary of Weston for the administration of a loan portfolio of third-party long term loans receivable.

Note 26. Subsequent Events

On February 7, 2008, the Company's Medium Term Notes, other notes and debentures, and commercial paper ratings were downgraded by DBRS and Standard & Poor's ("S&P"). DBRS downgraded the Company's long term credit rating to "BBB (high)" from "A (low)" and also lowered Loblaw's short term credit rating to "R-2 (high)" from "R-1 (low)". In addition, S&P downgraded Loblaw commercial paper rating to "A-2" from "A-1 (low)". As a result of the DBRS downgrade of the short term credit rating, the Company has limited access to commercial paper. The Company has entered into discussions, which have not yet been finalized, with a syndicate of banks to secure short term funding to replace its existing 364-day revolving committed credit facility of \$500, as described in note 15, with a new, longer term committed credit facility of a higher amount.

Subsequent to the DBRS downgrades, the Company was notified that an Event of Termination of the independent funding trust agreement for the Company's franchisees had occurred as a result of the credit rating downgrades. The \$44 standby letter of credit provided to the independent funding trust by the Company has not been drawn upon. If such an event were to occur, long term debt in the amount of \$126 would need to be reclassified to short term liabilities. This amount relates to certain franchisees that are VIEs that the Company currently consolidates. The gross principal amount of the franchisee loans outstanding at the end of 2007 was \$418 (2006 - \$419), including \$153 (2006 - \$124) of loans payable of VIEs consolidated by the Company in 2007. The Company is currently in the process of securing alternative financing with a syndicate of banks, in the form of a 364-day committed credit facility for the benefit of its franchisees to address this issue. Any new alternative financing structure which may be implemented would need to be reviewed to determine if there are any implications with respect to the consolidation of VIEs.

Note 27. Other Information

Segment Information The only reportable operating segment is merchandising, which includes primarily food as well as general merchandise and drugstore products and services. All sales to external parties were generated in Canada and all fixed assets and goodwill were attributable to Canadian operations.

Five Year Summary⁽¹⁾

Year ⁽²⁾ (\$ millions except where otherwise indicated)	2007	2006	2005	2004	2003
Operating Results					
Sales ⁽⁴⁾	29,384	28,640	27,627	26,030	25,066
Sales excluding the impact of tobacco sales and VIEs ⁽³⁾ ⁽⁴⁾	27,915	26,834	25,558	24,276	23,232
Operating expenses ⁽⁴⁾	28,648	28,351	26,226	24,378	23,599
Operating income	736	289	1,401	1,652	1,467
Adjusted operating income ⁽³⁾	1,034	1,326	1,600	1,652	1,488
Adjusted EBITDA ⁽³⁾	1,589	1,892	2,132	2,125	1,881
Interest expense	252	259	252	239	196
Net earnings (loss)	330	(219)	746	968	845
Financial Position					
Working capital	471	675	539	290	356
Fixed assets	7,953	8,055	7,785	7,113	6,390
Goodwill	807	794	1,587	1,621	1,607
Total assets	13,674	13,486	13,761	12,949	12,113
Net debt ⁽³⁾	3,728	3,891	3,901	3,828	3,707
Shareholders' equity	5,545	5,441	5,886	5,414	4,690
Cash Flow					
Cash flows from operating activities	1,245	1,180	1,489	1,443	1,032
Free cash flow ⁽³⁾	402	70	103	(24)	(437)
Capital investment	613	937	1,156	1,258	1,271
Per Common Share (\$)					
Basic net earnings (loss)	1.20	(.80)	2.72	3.53	3.07
Adjusted basic net earnings ⁽³⁾	2.05	2.72	3.35	3.48	3.10
Dividend rate at year end	.84	.84	.84	.76	.60
Cash flows from operating activities	4.55	4.31	5.43	5.26	3.75
Capital investment	2.24	3.42	4.22	4.59	4.62
Book value	20.22	19.85	21.48	19.74	17.07
Market price at year end	34.07	48.79	56.37	72.02	67.85
Financial Ratios					
Adjusted EBITDA margin (%) ⁽³⁾	5.7	7.1	8.3	8.8	8.1
Operating margin (%)	2.5	1.0	5.1	6.3	5.9
Adjusted operating margin (%) ⁽³⁾	3.7	4.9	6.3	6.8	6.4
Return on average total assets (%) ⁽³⁾	5.8	2.3	11.2	14.2	13.9
Return on average shareholders' equity (%)	6.0	(3.9)	13.2	19.2	19.3
Interest coverage	2.7	1.0	5.1	6.4	6.4
Net debt ⁽³⁾ to equity	.67	.72	.66	.71	.79
Cash flows from operating activities activities to net debt ⁽³⁾	.33	.30	.38	.38	.28
Price/net earnings ratio at year end	28.4	(61.0)	20.7	20.4	22.1
Market/book ratio at year end	1.7	2.5	2.6	3.6	4.0
Operating Statistics					
Retail square footage (in millions)	49.6	49.7	48.5	45.7	42.3
Average corporate store size (square feet)	60,800	57,400	56,100	53,600	50,500
Corporate stores sales per average square foot (\$)	591	585	579	592	605
Same-store sales growth ⁽⁴⁾	2.4%	0.8%	0.2%	1.5%	4.7%
Number of corporate stores	628	672	670	658	646
Number of franchised stores	408	405	402	400	397

(1) For financial definitions and ratios refer to the Glossary of Terms on page 85.

(2) 2003 was a 53 week year.

(3) See Non-GAAP Financial Measures on page 40.

(4) During 2006, the Company implemented Emerging Issues Committee Abstract 156, "Accounting by a Vendor for Consideration Given to a Customer (Including a Reseller of the Vendor's Products)" on a retroactive basis. Accordingly certain sales incentives paid to independent franchisees, associates and independent accounts for prior years have been reclassified between sales and cost of sales, selling and administrative expenses. For a further discussion, see the Accounting Standards Implemented in 2006 section in the Management's Discussion and Analysis of this Financial Report.

Glossary of Terms

Term	Definition	Term	Definition
Adjusted basic net earnings per common share	Basic net earnings per common share adjusted for items that affect the comparability of the financial results and are not a result of ongoing operations (see Non-GAAP Financial Measures on page 40).	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.
Adjusted EBITDA	Adjusted operating income before depreciation and amortization (see Non-GAAP Financial Measures on page 40).	Market/book ratio at year end	Market price per common share at year end divided by book value per common share at year end.
Adjusted EBITDA margin	Adjusted EBITDA divided by sales excluding the impact of tobacco sales and VIEs (see Non-GAAP Financial Measures on page 40).	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.
Adjusted operating income	Operating income adjusted for items that affect the comparability of the financial results and are not a result of ongoing operations (see Non-GAAP Financial Measures on page 40).	Net debt	Bank indebtedness, commercial paper, long term debt due within one year, long term debt and debt equivalents less cash, cash equivalents and short term investments (see Non-GAAP Financial Measures on page 40).
Adjusted operating margin	Adjusted operating income divided by sales excluding the impact of tobacco sales and VIEs (see Non-GAAP Financial Measures on page 40).	Net debt to equity	Net debt divided by total shareholders' equity.
Annual Report	For 2007, the Annual Report consists of the Annual Summary and the Financial Report.	New store	A newly constructed store, conversion or major expansion.
Basic net (loss) earnings per common share	Net (loss) earnings available to common shareholders divided by the weighted average number of common shares outstanding during the year.	Operating income	Earnings before interest expense, income taxes and minority interest.
Book value per common share	Shareholders' equity divided by the number of common shares outstanding at year end.	Operating margin	Operating income divided by sales.
Capital investment	Fixed asset purchases.	Price/net (loss) earnings ratio at year end	Market price per common share at year end divided by basic net (loss) earnings per common share for the year.
Capital investment per common share	Capital investment divided by the weighted average number of common shares outstanding during the year.	Renovation	A capital investment in a store resulting in no change to the store square footage.
Cash flows from operating activities per common share	Cash flows from operating activities divided by the weighted average number of common shares outstanding during the year.	Retail sales	Combined sales of stores owned by the Company and those owned by the Company's independent franchisees.
Cash flows from operating activities to net debt	Cash flows from operating activities divided by net debt.	Retail square footage	Retail square footage includes corporate and independent franchised stores.
Control label	A brand and associated trademark that is owned by the Company for use in connection with its own products and services.	Return on average total assets	Operating income divided by average total assets excluding cash, cash equivalents and short term investments (see Non-GAAP Financial Measures on page 40).
Conversion	A store that changes from one Company banner to another Company banner.	Return on average shareholders' equity	Net (loss) earnings available to common shareholders divided by average total common shareholders' equity.
Corporate stores sales per average square foot	Sales by corporate stores divided by the average corporate stores' square footage at year end.	Sales excluding the impact of tobacco sales and VIEs	Total sales less sales attributable to tobacco sales and the consolidation of VIEs pursuant to AcG 15 (see Non-GAAP Financial Measures on page 40).
Diluted net (loss) earnings per common share	Net (loss) earnings available to common shareholders divided by the weighted average number of common shares outstanding during the period minus the dilutive impact of outstanding stock option grants at period end.	Same-store sales	Retail sales from the same physical location for stores in operation in that location in both periods being compared by excluding sales from a store that has undergone a conversion or major expansion in the period.
Dividend rate per common share at year end	Dividend per common share declared in the fourth quarter multiplied by four.	Variable interest entity ("VIE")	An entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest (see note 24 to the consolidated financial statements).
Free cash flow	Cash flows from operating activities less fixed asset purchases and dividends (see Non-GAAP Financial Measures on page 40).	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.
Gross margin	Sales less cost of sales and inventory shrinkage divided by sales.	Working capital	Total current assets less total current liabilities.
Interest coverage	Operating income divided by interest expense adding back interest capitalized to fixed assets.	Year	A fiscal year ends on the Saturday closest to December 31, usually 52 weeks in duration, but includes 53 weeks every 5 to 6 years. The year ended January 3, 2004 contained 53 weeks.

Shareholder and Corporate Information

National Head Office and Store Support Centre

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

Stock Exchange Listing and Symbol

The Company's common shares are listed on the Toronto Stock Exchange and trade under the symbol "L".

Common Shares

63% of the Company's common shares are owned beneficially by W. Galen Weston and George Weston Limited.

At year end 2007 there were 274,173,564 common shares issued and outstanding, 4,911 registered common shareholders and 100,823,829 common shares available for public trading.

The average daily trading volume of the Company's common shares for 2007 was 456,020.

Trademarks

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

Common Dividend Policy

The declaration and payment of dividends and the amount thereof are at the discretion of the Board which takes into account the Company's financial results, capital requirements, available cash flow and other factors the Board considers relevant from time to time. Over the long term, the Company's objective is for its dividend payment ratio to be in the range of 20% to 25% of the prior year's adjusted basic net earnings per common share⁽¹⁾.

Common Dividend Dates

The declaration and payment of quarterly dividends are made subject to approval by the Board of Directors. The anticipated record and payment dates for 2008 are:

Record Date	Payment Date
March 15	April 1
June 15	July 1
Sept. 15	Oct. 1
Dec. 15	Dec. 30

Normal Course Issuer Bid

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

Investor Relations

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

Value of Common Shares

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

Registrar and Transfer Agent

Computershare Investor Services Inc.
100 University Avenue
Toronto, Canada
M5J 2Y1
Tel: (416) 263-9200
Toll free: 1-800-663-9097
Fax: (416) 263-9394
Toll free fax: 1-888-453-0330

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

Additional financial information has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR) and with the Office of the Superintendent of Financial Institutions (OSFI) as the primary regulator for the Company's subsidiary, President's Choice Bank. The Company holds an analyst call shortly following the release of its quarterly results. These calls are archived in the Investor Zone section of the Company's website.

Independent Auditors

KPMG LLP
Chartered Accountants
Toronto, Canada

Annual Meeting

The 2008 Annual Meeting of Shareholders of Loblaw Companies Limited will be held on Wednesday, April 30, 2008 at 11:00 a.m. (EST), at the Metro Toronto Convention Centre, South Building, Hall G, 222 Bremner Boulevard, Toronto, Ontario, Canada.

(1) See Non-GAAP Financial Measures on page 40.

Additional Company reports are available online at www.loblaw.ca

For more information about our offerings, visit our web-sites at:



www.loblaw.ca



www.pc.ca

www.joe.ca

Business Review Report

Provides an update on achievements towards Making Loblaw the Best Again, plus outlines Loblaw's priorities for 2008, 2007 financial highlights, facts and statistics, corporate social responsibility summary, corporate governance practices, and corporate and shareholder information.

February 2008

2007 Annual Report

Contains Loblaw Companies Limited annual financial statements, report to shareholders, auditor's report, and management discussion and analysis.

March 2008

2007 Corporate Social Responsibility Report

Loblaw Companies Limited first Corporate Social Responsibility (CSR) report will outline the environmental and social achievements made in 2007 which support our five business pillars. It will describe the strategy and priorities, primarily for 2008, and how we will use this inaugural year to set long-term objectives.

Available April 2008

Ce rapport est disponible en français.

Loblaw is committed to making a positive contribution to our world by minimizing our impact on the environment. This 2007 Annual Report was printed in Canada on Rolland Enviro 100, which contains 100% post-consumer waste and is processed chlorine-free, using biogas energy.

