FINAL TRANSCRIPT

Loblaw Companies Limited

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Loblaw Companies Limited Q3 2020 Earnings Call. At this time, all participants are in a listen-only mode.

After the speakers' presentation, there will be a question-and-answer session. To ask a question during the session, you will need to press *, 1 on your telephone.

Please be advised that today's conference is being recorded.

If you require any further assistance, please press *, 0. Thank you.

It is now my pleasure to hand the conference over to your moderator for today. Roy MacDonald, Vice President, Investor Relations, please go ahead.

Roy MacDonald — VP Investor Relations, Loblaw Companies Limited

Good morning, everybody. Thank you, Jack. Welcome to the Loblaw Limited Third Quarter 2020 Results Conference Call. This morning I'm joined by Galen Weston, our Executive Chairman; Sarah Davis, our President; and Darren Myers, our Chief Financial Officer.

And before we begin the call, I'll remind you that today's discussion will include forward-looking statements, which may include, but are not limited to, statements with respect to Loblaw's anticipated future results and the impact of the COVID-19 pandemic. These statements are based on assumptions and reflect management's current expectations and are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from our expectations. These risks and uncertainties are discussed in the Company's materials filed with the Canadian securities regulators.

And any forward-looking statements speak only as of the date that they are made. The Company disclaims any intention or obligation to update or revise any of the forward-looking statements, whether as a result of new information, future events, or otherwise, other than what's required by law.

Also, certain non-GAAP financial measures may be discussed or referred to today. Please refer to our annual report and other materials filed with the Canadian securities regulators for a reconciliation of each of these measures to the most directly comparable GAAP financial measure.

And with that, I'll turn the call over to Darren.

Darren Myers — Chief Financial Officer, Loblaw Companies Limited

Thank you, Roy, and good morning, everyone. The third quarter represented an improvement in our results in what continues to be a challenging, dynamic time. The pandemic continues to influence consumer behaviour, impacting sales mix and elevating associated costs.

On an adjusted consolidated basis, our reported revenue grew by 6.9 percent; adjusted EBITDA was up 2.1 percent; adjusted net earnings were up 1.3 percent; and adjusted earnings per share increased by 4 percent.

Our same-store sales and drug retail increased 6.1 percent. Front store same-store sales grew 2.4 percent while pharmacy same-store sales grew by 10.3 percent. Front store sales mix was driven by strong performance in food, HABA, and household products. While we continue to experience pressure in cosmetics and OTC, cosmetics showed an improvement in the rate of decline relative to our second quarter.

In pharmacy, we delivered strong sales, in part due to the demand for 90-day prescription refills following the lift of government restrictions. We expect some negative impact from the timing of these changes on our Q4 prescription business.

Food Retail same-store sales grew 6.9 percent in the quarter. Food sales growth included changes within the category mix and the benefit from strong demand for essential food categories. Demand across our formats remained strong, with 9.7 percent growth in our Market division and 4.7 percent in our Discount division.

Our average article price was 5.3 percent for the quarter. The average article price increase reflects a change in our sales mix, including consumers buying larger-format items. The increase is not indicative of inflation, which, using CPI as a reference, would have been closer to the 1.8 percent for the quarter.

For the quarter, our Food Retail basket size remained elevated while traffic continued to be negative. We did see traffic starting to improve and the basket not quite as high; however, we remain well outside pre-COVID rates.

Total retail gross margin was 26.7 percent, excluding the consolidation of franchises, a decline of 60 basis points compared to last year. Our margins were negatively impacted by declines in Food and Drug rates. In Food, our rate was negatively impacted by sales mix and targeted pricing investments. In Drug, we were negatively impacted by mix.

Retail SG&A as a percentage of sales was 17.2 percent, excluding the benefit from franchise consolidation, an improvement of 10 basis points. The improvement reflects the benefit of sales leverage, process efficiencies, and continuing to delay discretionary spending. This was partially offset by higher COVID-related costs and higher costs associated with the growth in e-commerce. During the quarter, COVID-related costs increased our spending by an estimated $85 million.

Retail EBITDA increased $22 million and EBITDA margin came in at 9.5 percent, a decrease of 60 basis points compared to last year.

Moving to PC Financial, revenue was $278 million, down $31 million in the quarter, driven primarily by lower credit card spending, partially offset by strength in our Mobile sales. Adjusted EBITDA contributions increased by $10 million year over year as a result of timing of investments and adjustments to our ECL provision.

Adjusted consolidated EBITDA margin was 9.7 percent in the quarter. Normalized for the consolidation of franchises, EBITDA margin declined 40 basis points compared to last year.

In the quarter, IFRS net earnings available to common shareholders was $345 million, an increase of 3.3 percent, and fully diluted earnings per share were $1.30, an increase of 4 percent.

Moving to cash flow, the Company generated a $121 million of free cash flow in the quarter. We repurchased 5 million common shares during the quarter, and today we announced a $0.02 or 6.3 percent increase in our quarterly dividend. This marks our ninth consecutive annual increase.

In September, we received an upgrade by DBRS to BBB (high). This reflects the strength and stability of our business and the ability to continue to generate strong cash flows.

Looking ahead, there continues to be a high degree of uncertainty about the duration and the impacts of the COVID-19 pandemic on the Canadian economy. We expect continued volatility in our business as shopping behaviours continue to evolve, as does the demand for the types of products and services we provide.

In the four weeks following the end of the third quarter, volatility continued. Food Retail sales and COVID-related costs have continued on a similar trajectory to Q3, while Drug retail sales have seen a deceleration of growth, primarily due to the impact of the timing of the prescription volumes related to the change in fill rates. Given the volatility and continued uncertainty, it is too early to extrapolate a trend.

In conclusion, we are focused on delivering value to our customers. Incremental sales volumes and ongoing benefits from our process and efficiency initiatives allowed us to offset cost inflation and invest in our strategic initiatives while generating earnings growth.

I will now turn the call over to Sarah.

Sarah Davis — President, Loblaw Companies Limited

Good morning. COVID-19 remains important context for our day-to-day operations and our performance in the third quarter. You will remember that in the early part of the year, it was the dominant factor and a substantial drag on our profitability. We saw significant channel, format, and store switching, favouring conventional over discounts. There were significant fluctuations in buying patterns away from discretionary items to necessary items, and we are investing heavily to keep our colleagues and our customers safe.

Today, we continue to maneuver through these challenging times but with our feet squarely beneath us. Our Q3 results show our sequentially improving performance, including tonnage, market share, margin, and profit improvements, while we continue to invest in the safety of our people and our stores. We have also made considerable progress on our strategic pillars.

On a consolidated basis, our revenue grew 6.9 percent in the quarter. At Shoppers, front store sales grew 2.4 percent and Rx was up 10.3 percent. Underlying these results, there were some extremes in major categories. Prescription counts were strong, up 5 percent, as government restrictions on fill rates unwound. There has been a surge in demand for flu shots, and we have administered more to date than we did in all of last year. On the other hand, our beauty and our cough-and-cold businesses remain soft. These categories improved over Q2 but continue to trend down year over year. In summary, Shoppers performance remains complex, with signs of strength and irregularities that are normalizing.

I want to take a minute to applaud our pharmacists. They have played a huge part in the Canadian healthcare response for months now, rapidly expanding their scope and even ramping up to conduct almost 155,000 asymptomatic COVID tests in recent months. I think their response has been exceptional. These are important examples that demonstrate the strength of our pharmacy assets and our ability to leverage those assets to provide Canadians with essential family healthcare services.

Turning now to grocery. In Q3, our Market division continued with its 2020 winning streak. With same-store sales of 9.7 percent, we posted another quarter of share gains, we delivered market-leading value in Fresh, and continued to see customer satisfaction scores that were well ahead of past years.

In Discount, we are seeing a slow but certain resurgence, following well-explained relative softness early in the pandemic. In the quarter, sales grew 4.7 percent, with Food sales even higher. We invested in price and maintained strong promotions.

Banner by banner, our food stores are well positioned to meet the challenges of the pandemic, while we continue to provide customers with the everyday values that have always been important to them.

During the quarter, we made good progress on our strategy and our new customer behaviours confirmed that we are on the right path. More specifically, as the early pandemic panic settled, customers told us what really matters to them now. They care about convenience, health, and brands they can trust. These customer priorities align beautifully with our strategy.

Our Everyday Digital retail strategy continues to deliver convenience. We have an unmatched network and a first-mover advantage. In Q3, we expanded our digital offering with Shoppers front store offer online, adding to the strong existing beauty offer which was up nearly 200 percent in the quarter.

We also created some great e-commerce excitement. Our Shoppers beauty team had a hashtag challenge on TikTok that drew over 800 million views. And our Joe Fresh team had overwhelming success with our exclusive Jilly Jacket, based on a social media influencer program.

Turning to health and wellness. 2020 will be remembered as a foundational year for our Connected Healthcare Network strategy. As mentioned earlier, patients and governments are turning to pharmacists for a greater range of services and we're finding new ways to serve them. During the quarter, we opened the first of our medical clinics. We made a strategic investment in Maple, which now supports 160 in-store, virtual care sites in our British Columbia pharmacies. And we launched PC Health, a consumer app that provides everything from help navigating the medical system, to live access to care providers, to programs and rewards for healthier behaviours.

Finally, you're aware of our Payments & Rewards strategy, based on the growing loyalty loop we have established with millions of Canadians through PC Optimum. In September, we launched the PC Money Account, which is a return to banking for us. But it's different; we have found ways to give customers more rewards for more activities as they spend, save, or transfer their money day to day. Over 50 percent of our customers use cash or debit when shopping in our stores. This new product gives them unmatched reward and it gives them another reason to shop with us.

With all that is going on in retail today, it was a tricky quarter to maneuver. We continued to invest heavily to keep people safe, but we are rising above the challenges and finding ways to improve day by day. As we look forward, many pieces of our strategy are falling into place in ways that clearly make sense for our customers. I am very encouraged.

And I will now turn the call over to Galen.

Galen Weston — Chairman and Chief Executive Officer, Loblaw Companies Limited

Thank you, Sarah, and good morning. Loblaw delivered better results in a complex quarter. The Company remains steadfast in its commitment to put customers and colleagues first, as we sustained investments in safety measures at store level while resisting pressure to raise prices at a time when Canadians need value more than ever.

Colleague engagement and customer satisfaction scores remained at all-time highs in the quarter, and as performance in our Discount and Drug segments began to come back, our Market division maintained its positive momentum. This is reflective of a great team effort, and I want to thank the 200,000 colleagues at all levels of our organization who enabled us to keep Canadians fed and well during the quarter.

As Sarah described, we did this while also advancing our strategic pillars with decisive steps forward in Everyday Digital retail, Payments & Rewards, and Connected Healthcare. In the face of extraordinary circumstances, Loblaw effectively balanced operating a strong colleague- and customer-focused core business, made forward-thinking investments in its digital future, and delivered earnings growth. We continue to do so with conviction that this will create value over the long-term. Thank you.

I'll now turn the call over for questions.

Roy MacDonald

Thank you, Galen.

Jack, if you don't mind introducing the Q&A process, please?

Q&A

Operator

Certainly. At this time, if you'd like to ask a question, please press *, 1 on your telephone keypad.

Karen Short with Barclays, your line is open.

Karen Short — Barclays

Hi. Thanks very much. Just wanted to ask a couple of questions on Discount generally. So it seems like you've invested more in Discount and that obviously impacted the gross margin side of things. But wondering why you think you need to do that and whether the Canadian consumer is actually focused on discount right now. Or maybe if it's not the best timing on something like that because there really isn't such a focus on discount. And then I had a follow-up.

Sarah Davis

Okay. Hi. It's Sarah. I'll start. I would say that from a discount perspective, we actually find it's actually quite competitive out there in terms of the intensity that we're seeing. So we did feel that it was important to make some investments in price through this time.

Different scenario in our Market division, where we also resisted the urge to raise prices and have, as a result, seen some share gains.

Karen Short

Okay. And then maybe a little bit more colour on PC Health. I know we talked about this in the past offline, but now seems the right time to do that. But wondering if you could just give a little bit more colour on how you see that unfolding just broadly. And it seems like a very strong position that you have to actually gain share and leverage the relationships that you have.

Sarah Davis

Okay. So I would say on PC Health, it's still very early days. We have that (phon) launched it. We only launched it in the Atlantic provinces of Canada. We plan to launch in Ontario in the fourth quarter.

But the idea is that it's an app that helps Canadians maneuver the health system. And as I mentioned in my remarks, it does anything from helping them find points of care as well as rewarding them for healthy behaviour.

So that's sort of the short place where we are right now in the short term. Long term, we're looking for ways to expand across the country. We do plan to roll it out across the country in 2021.

And I don't know, Darren, if there's anything you want to add on in the health space to that.

Darren Myers

No. I think, Sarah, you characterized it well. I mean it is still early days but it's got a lot of exciting potential for us, in particular when you think of the velocity we can bring to an app like that and the kind of ecosystem we can build around it. So we're excited by its potential but its early days and it will take time before it's kind of ramping and probably moving the numbers in any major way.

Sarah Davis

Okay. Maybe I'll just add, if I could, on how in a different part of the country, in BC, where our investment in Maple has allowed us to provide in-pharmacy virtual care to customers. So you would go into a pharmacy, you would be able to see a virtual doctor for a minor ailment that you may have, and you would be able to get your prescription prescribed at that time.

And what we've seen in those pharmacies—it's in 160 pharmacies right now in British Columbia—is that there's a 93 percent in-pharmacy fill rate after the virtual doctor's appointment. So we think that's a nice add-on which would contribute to the PC Health app at some point as well.

Karen Short

Okay. And sorry, just last question. I mean obviously, there's been a lot of volatility on top-line growth versus EBIT or EBITDA growth over the last several quarters for obvious reasons. But this quarter seems like we may be kind of at a new level of “normal”, and there was about a call it 500-ish basis-point gap on EBITDA growth versus sales growth. Do you think that’s kind of the right way to think about it until we get into whatever the new normal may be? Is that a reasonable kind of gap to think of?

Darren Myers

That’s a great question, Karen, and one that I’m hesitant to answer just given I don’t want to provide guidance. I think that, while we have these COVID costs, and I don’t see a reason that they’re going to go away, it’s a reasonable assumption that you’re just not going to get the flowthrough. So yes, the profit rate growth will be less than the revenue growth.

I think from us, we’re looking and expect to continue to see some gross margin improvements over time. Having said that, on the SG&A side, this was a really good quarter with a lot of good things going away so we’ll probably see a little bit of pressure on the SG&A relative to this quarter. So I think you’re probably thinking about it right, but of course, it’s hard for me to give you a good guidance on that.

Karen Short

Great. Thanks very much.

Operator

Mark Petrie with CIBC, your line is open.

Mark Petrie — CIBC Capital Markets

Yeah. Good morning. I wanted to ask about the gross margin performance specifically and looking for some more commentary with regards to the relative materiality of the biggest factors in each of Food and Drug. I mean, I know you’re not going to give specifics, and mix is the biggest factor. But some more colour just in terms of which mix shifts are the most material, whether it’s channel, reg promo, category, brand versus owned brands, that kind of thing.

Darren Myers

Hey, Mark. Let me start. And I think it's probably best just to step back again and think about Q2, which I know you know well. But when we think about Q2, we were impacted right off the bat with COVID from a product mix perspective and we were down 90 basis points. So we're pleased that we saw an improvement in that decline. So we had a 30-basis-point improvement in our decline. But we still saw declines in both Food and Drug.

On the Drug side, I will say that certainly, it's predominantly or all mix. So you think about discretion areas like cosmetics or beauty, those are the areas that have certainly impacted us.

And then on the Food side, it's a bit of a combination. Sarah said there is increased intensity that we are seeing in Discount, so we have been a bit more intensive in terms of our relative investments. And so it's a mix of both investing and mix of category. So think about things like HMR which tends to be a high-margin category that is down year over year. So there's lots of things that play within the mix, but it's a combination of the two things.

Mark Petrie

Okay. Thanks. Sarah, you mentioned that you saw positive signs on customer satisfaction, specifically in the Market division. And I think, Galen, maybe you mentioned it for the business overall. I wanted to ask specifically about e-commerce. And as you've seen demand rise so materially, can you just talk about customer satisfaction and feedback with that offer specifically? And as you understand the pain points, what steps can you take to help address those? And I guess two topics I'm interested in specifically would be product substitutions and wait times at customer pickup.

Sarah Davis

So from Q2 to Q3, we saw a significant improvement in customer satisfaction in our e-commerce business. As you can imagine, at the height of the pandemic, the wait times were longer than customers were expecting. And certainly, we had to do a lot of work in order to improve and increase the capacity in order to get all of that increased demand. So during Q2, I think we mentioned that we saw basically triple the demand in e-commerce, and so there was a factor there.

But we quickly ramped it up. So I would say Q3, significant improvements in our customer satisfaction related to e-commerce. But the two areas that continued to be raised as areas of focus for us are the two that you mentioned. So it is product substitutions and it would be wait times. And we've got a lot of initiatives in place to improve on both of those two areas and making sure that we provide customers with the best service that we can.

Mark Petrie

And are those initiatives—

Darren Myers

I will say, Mark. Sorry. I was just going to add. I mean, and Sarah said it, our fill rates have improved from Q2 to Q3. And like she said, there's a lot of initiatives. One example is now if you go onto the app, you can see where there's low stock on an item, so it helps people with things like, well, you should pick your own substitution, and, of course, we're going to continue to improve our substitutions as well. So there's enhancements that are happening that we think will continue to improve the performance here.

Mark Petrie

Okay. Okay. Great. That's helpful colour. And I guess just one last one. I mean, obviously there's been a tremendous amount of shift in consumer behaviour and preferences. But I wanted to ask specifically about your prepared foods business and just the category kind of holistically, and at a high level, sort of all variations, including in-store, HMR, delivery, meal kits, all that kind of stuff. I guess, big picture, do you think this can continue to be a growth area for you over the next few years? And I guess, what are you doing differently or do you need to do differently in order to kind of address the market opportunity and the shifting consumer needs?

Sarah Davis

That's a great question. So I've always believed in solving meals for Canadians. And I think this pandemic has just made it more, even more relevant than it ever has been. So yes. Absolutely.

So we've got a bunch of different tests going on with a few different things. So we've got the meal—so we've got different versions—so we have meal kits where it's raw ingredients that you put together that you can purchase in our stores or online. We've got ready-to-cook meals where it's all prepared for you and all you need to do is put it into the oven, which can also be bought in our stores or online or delivered to your home.

We now have meal solutions in about 240 stores, where we've got 80 of them in Shoppers as well. So 80 of our Shoppers stores have them as well where it makes sense there. So we expanded our offer in Q3 to have one-pan meals, ready meals, and slow cooker meal kits that you can use with an instapot. So I would say–and the other thing that we are piloting is we started offering kits from a meal from 12 GTA restaurants. So we've got a few different areas in order to solve meals for Canadians in a few different ways.

So good traction there. We've seen high growth but it's still on a relatively small base for us. But yes, we do see a lot of potential in this area.

Mark Petrie

Okay. Appreciate all the comments. All the best.

Operator

Irene Nattel with RBC Capital Markets, your line is open.

Irene Nattel — RBC Capital Markets

Thanks and good morning, everyone. A couple of follow-ups if I may. You mentioned competitive intensity, particularly in Discount. Is that in western—can you talk about where we might be seeing that? Is it in Western Canada in reaction to some of the FreshCo conversions? Where are we seeing the greatest intensity?

Sarah Davis

That’s a good question. I would say we’re seeing it across the country in some of the national players. And then, of course, we are specifically impacted by some of the conversions in Western Canada as well, but I would say it would be a national intensity.

Irene Nattel

That’s great. Thank you. And just sticking sort of on the same kind of theme, you said that you’re seeing market share gains. Who do you think or which channel do you think that these gains are—at the expense of who or whom?

Sarah Davis

It’s difficult to know. I’m seeing market share gains in our conventional business, in our Market division. And so presumably, it would be against the conventional players, but it could be against others. It’s hard to know exactly who we’re winning against.

Irene Nattel

Okay. Thank you. And then just thinking about kind of the evolution over the next six months, it seems to me there's going to be a lot of puts and takes both from a demand and a margin perspective. I'm thinking about front store at Shoppers and perhaps lower sales of cosmetics and also, certain types of illnesses and the impact that that has. Thinking about the potential for rising e-commerce penetration as we move through these brutally cold winter months when no one wants to stand outside. I'm just wondering how you're thinking about it and how you're planning for some of the distortions that we may see more in the next couple of quarters.

Sarah Davis

That's a great question. I would say that what we have been doing is trying to be very agile. We've seen a lot of different changes in the way that our business has been operating. Certainly, looking at Shoppers, as I said in my opening remarks, that's very, very complex as they've got ups and downs across the business. So I think we'll just expect to see more of the same. Hopefully, I would say in some cases it's starting to normalize.

So I think we understand some of the trends in terms of what's happening in beauty. I think we understand the trends in happening in cough and cold, as people not been out as much, we have seen a decline there, and we're looking at ways to offset some of that. And we've seen great demand in flu vaccinations, in COVID testing. And if there's other potential areas that the pharmacists can take a bigger role, we would be happy to do that too.

So I think we are maneuvering that. I think in the grocery business, we've got a pretty good understanding of what happens when communities move into lockdown; what happens when it opens up again. We have been holding some extra inventory in case of some of these areas where there are lockdowns.

So I think we'll just continue with the agility we've been doing so far through the pandemic.

Irene Nattel

That's great. Thank you.

Sarah Davis

Oh, actually, one other mention, actually, if I could just say on your mention on e-commerce. I think what we've got that we like about the model that we have is it really can scale up and scale back down. So we did scale up as we went through the pandemic and we have the capacity for very high penetration now in e-commerce. And at the same time, it scaled back a little bit in Q3, so we have the ability to scale back there too. So we've got a fairly agile e-commerce model as well.

Operator

Michael Van Aelst with TD Securities, your line is open.

Michael Aelst — TD Securities

Thank you. Good morning. I wanted to continue on the e-commerce, actually. So you said it was up about 175 percent so I guess that's somewhere in that 4 percent to 4.5 percent penetration for food. Does that seem reasonable?

Sarah Davis

Yeah. That's around about the right area.

Michael Aelst

Okay. So when you look at the delivery versus click-and-collect, do you see any changes in behaviour of, say the relative growth the past few quarters?

Sarah Davis

Yeah. So what we saw in Q2 is that the click-and-collect or pickup is a much larger proportion of our e-commerce business. And so what we saw in Q2 was that delivery was increasing at a higher rate than click-and-collect. But of course, click-and-collect ended up being—it's still substantially higher.

In Q3, we actually saw a reversal where our click-and-collect business actually rose at a higher rate than delivery. So interesting trend. So as that, you know, it'll (unintelligible) we would have seen a change there. But both are growing significantly.

Michael Aelst

Okay. And then what percentage of the e-commerce business comes from PC Insiders?

Darren Myers

It'd be a relatively small percentage of it today. Obviously, we have plans for it better (phon) in the future.

Michael Aelst

Okay. And then so when we look at the gross margin contraction, you talked about some of the mix factors in that. But how much is e-commerce of that 60 basis points? Because we saw when your e-commerce penetration was higher in Q2, you had 30 basis points more compression than what we saw in this quarter. Is that delta mostly due to e-commerce?

Darren Myers

No. The nice thing with the e-commerce business is it's accretive on the gross margin. We see a nicer basket in it. So it's really not driven by the e-commerce. It's for the reasons that I already walked through.

Michael Aelst

Okay.

Sarah Davis

For e-commerce, it would be on the SG&A side. So it'd be the labour side where you'd actually see a dilution on gross profit. To Darren's point, it's actually accretive.

Michael Aelst

Okay. Great. And then I believe, at this point, you're the only grocer charging for click-and-collect for pick fees. How long do you think you can be the outlier here?

Sarah Davis

Well, I think for now we're pleased with our performance; we're seeing significant growth in it. So I don't know exactly what our plan for how long exactly, but it's something that we would monitor. And at some point, we know that we will likely not be charging those fees.

Darren Myers

Yeah. And I mean, and just to add, I mean, our customers so far are telling us they're happy to pay a fee for the service. It's a very good service that they're getting and it's a very nominal fee, and so our customers have been happy. But as you point out, Mike, it's something we've got to keep watching.

Michael Aelst

Okay. Great. And then on the same-store sales side, in your outlook statements, you did talk about, I guess, continued performance in Food in Q4. But if you look at October compared to September and zero in a little bit closer, have you seen a material pickup as the restaurants started to close down again?

Darren Myers

I would say, I mean, we want to be careful how much we give. We're seeing still volatility even week to week. Some weeks there's a bit of a pickup; some there aren't. So I want to be careful not to give you a false trend. I think overall, to the comment, we said we were on the similar trajectory from what we see at this point to the quarter.

Sarah Davis

And just keep in mind that our business is a national one. So it's not weighed as heavily just to one jurisdiction where the markets might be closed as well.

Michael Aelst

Okay. And can you just comment on the impact of apparel in general merchandise on same-store sales trends in the quarter?

Darren Myers

Yes. The right-hand side overall was still a headwind, certainly to a lesser extent than Q1 and Q2 of this year. We saw growth in H&E. We've seen a nice pickup in that business, which is great. And then we continue to see some declines in apparel, cosmetics, and still tobacco.

Michael Aelst

Great. Thank you very much.

Darren Myers

Thanks, Mike.

Operator

Patricia Baker with Scotiabank, your line is open.

Patricia Baker — Scotiabank

Thank you. Good morning, everyone. Thanks for taking my questions. I have quite a few here. First of all, in your response to Karen Short's question about PC Health, and, Sarah, you referenced the 93 percent fill rate from the virtual doctor's visits. I'm just curious what that number would compare to in the past to what the fill rate would have been for fills in pharmacies where you have a medical clinic kind of on the premises, sort of in the same building. Do you have a rough idea whether that would be an equivalent number? Or whether these virtual visits are higher?

Sarah Davis

So virtual visits would be much higher than what we would get from a medical clinic in the same building.

Patricia Baker

Okay.

Sarah Davis

I mean, they would vary by medical clinic. But in general, the 93 percent is a very high rate.

Patricia Baker

Okay. Thank you. That's very helpful. Then secondly, you announced that you're now doing Shoppers Drug Mart front store online. Can you just talk about what the model is there? Are you picking from store? Are you shipping from store? What exactly are you doing?

Sarah Davis

It's basically, we're picking in store.

Patricia Baker

Okay. You just made a comment about the fact that, in Q3, you saw a reversal in terms of the relative rate of growth between click-and-collect and delivery, and with delivery, which was higher in Q2, but it's actually, click-and-collect is higher in Q3. I'm just curious whether that trend with delivery growth being lower than click-and-collect is consistent across all geographies, or if there's some geographical differences in those relative rates.

Sarah Davis

We've seen it pretty consistent right across the board. So certainly, GTA saw the same trend as what we would have seen in Western Canada.

Patricia Baker

Okay. And then, with respect to the price investments, you indicated from a channel perspective where you're making those investments. Can you talk about where you've seen the need from a category perspective to make price investments in Q3?

Sarah Davis

That's a great question. I'd prefer not to. It feels a bit competitive to say—

Patricia Baker

Okay. Fair enough.

Sarah Davis

—where we're making our category investments.

Patricia Baker

Okay. Fair enough. Then another trend in Q3 was, and it was explained very well in the introduction, but you had that average unit price of plus-5.3 percent, but you noticed that that doesn't really bear a direct relationship to inflation because it's really about people buying bigger packs. And so I'm just curious, when you think about that trend, what it's telling you or what you're anticipating from the perspective of household kind of replenishment and coming back that you'll probably have delay of replacement of some of those purchases.

Darren Myers

Well, I think it’s just a function of kind of that bigger basket, going to the store less often, so you buy a larger size of something versus thinking you’re going to go two or three times in a week. So it’s just a function of that. So I don’t expect major normalizations out of that.

Patricia Baker

Okay. So would that trend have been different in Q3 versus what we saw in Q2 or Q1, then? Just the way that you’ve called it out, it sounded like a different trend.

Darren Myers

Well, in Q3, we saw the average article price lift as well. I think it was just 50, maybe 50 basis points less; it was in the high 4s. So this trend was starting at that time certainly, in Q2.

Patricia Baker

Okay. Super. And—

Sarah Davis

I think maybe the differences, and certainly at the beginning, like the last week of the height of the pandemic, there would have been the panic buying and there would have been a let-up. Certainly, on pharmacy we saw the replenishment where they didn’t have to do the replenishment through Q2. But I would say now through Q2 and Q3, it stabilized to people just buying bigger-size packs, as Darren mentioned.

Patricia Baker

Okay. Super. And this is my last question, I promise. So you went through the holiday season, the Thanksgiving season. Can you just talk about what you might’ve learned from that? And is there any thinking to how that’s setting you up for the coming Christmas holiday season?

Sarah Davis

Yeah. It was very interesting. I would say that we were pretty pleased with how Thanksgiving as well as Halloween worked out for us. I think we didn't see a significant change in our performance in terms of it. I would say it was spread out a little bit more and I would say that people are still getting together and celebrating, just in smaller groups. But our sell-through for both Thanksgiving and Halloween was strong.

Patricia Baker

Okay. Thank you

Sarah Davis

So we expect the same—similar thing when you look forward to the holidays and what are we expecting, it's always hard to predict exactly during these volatile times but we are expecting a similar thing, that there will still be gatherings. People will still be eating meals in smaller groups. They likely won't be going out to as many restaurants and parties. And so it will be eating at home in small groups that we are anticipating for the holiday season.

Patricia Baker

Okay. Thank you very much.

Operator

Vishal Shreedhar with National Bank, your line is open.

Vishal Shreedhar — National Bank

Hi. Thanks for taking my questions. I just wanted to ask a little bit more about e-commerce, which is a popular topic over the last several quarters. Regarding your micro-fulfillment centres and the implementation of technology, I think you're using Takeoff Technology. Hoping you could provide us some perspective—I know its early days—on what you think about that. And is this something that you're going to roll out more broadly? And if you aren't prepared to give us that answer, then maybe you could tell us at what point you'd be prepared to make that conclusion.

Sarah Davis

That's a good question. So right now, we've got one automated micro-fulfillment centre that yes, you're right, we are working with Takeoff. We're pretty pleased with the performance that it's providing us.

And then on the other hand, we've got four manual fulfillment centres. And so we're currently just doing the comparison of the performance of the two versus the cost of implementing the two different versions. So we're not prepared to announce what it is that we're going to do going forward, but the tests continue, and likely in the new year, we'll have a better position on this.

Vishal Shreedhar

Okay. And with respect to Loblaw Media, my perception was, in the past, that was something that management was pretty excited about and I know the pandemic kind of slowed down the implementation of that. Wondering if that's a profitable program for Loblaw at this point? And what your suppliers are thinking about it?

Sarah Davis

Yeah. I would say early days on Media, and I would say that the pandemic did dampen that a little bit, but I would say we feel very optimistic about it. Our suppliers that who—some of the vendors who we have worked with on that on some programs are very pleased with the results that they see through it.

Right now, it's about neutral on an earnings perspective. And for 2021 is when we think that we can make some progress on Loblaw Media.

Vishal Shreedhar

Okay. And with respect to the efficiency initiatives, obviously, a ton of things going on at Loblaw, and sometimes the growth initiatives get a little bit more colour on the calls maybe due to analysts' questions. But the efficiency initiatives, management commented on that. It seemed like they were additive in this quarter as they were in prior. Wondering if you can give us a sense of what particular initiatives were the big drivers of efficiency this quarter and what we can look forward to in the quarters ahead.

Darren Myers

Yeah. Vishal, as we've talked before, I mean this program hasn't stopped. It is ingrained in our culture and how we're approaching every day. We've talked before about it's really in six buckets. There isn't a silver bullet. It's on every aspect of the business, whether you're in store support, whether it's in GNFR in the store. It's things like shelf labels. It's things like self-checkout. It's just improvements everywhere. So I wouldn't call out one specific item other than just to call out just our major focus continues here and will continue in this area.

Sarah Davis

And I think on the Shoppers side, if there is an area that probably had a biggest impact for them, it would be on the self-checkout, which has probably been helped a little bit by COVID as well, where people would like to prefer to not to be as close to people so they are choosing self-checkout. We did do some expansions in that in stores and I would say that the penetration is increasing significantly in Shoppers.

Vishal Shreedhar

Thanks.

Operator

Peter Sklar with BMO Capital Markets, your line is open.

Peter Sklar — BMO Capital Markets

Okay. Thank you. Sorry to belabour the point, but back on the Discount channel and the pressures that you've been having there, would you say that the reason you're facing those pressures, it's just largely the competitive promotional intensity of your competitors? Or have there been any Loblaw-specific issues you could call out? So for example, missing the price margin balance or merchandising tactics or whatever.

Sarah Davis

That's an interesting question. I would say that I think there's a couple of things happening. Certainly, in the early days of the pandemic, we would have said, structurally, it was more difficult to satisfy customer needs through certainly some of our hard discount stores where high volume, high traffic, low assortment, just very high sales penetration in a small store made it more difficult.

I would say, since then, we've sort of managed that and we've got sort of the—the consumer has changed their buying patterns and so that seems to have stabilized. And it has been more of pricing investments and keeping promotions going in order to make sure that we're competitive against our competitors, but also to make sure that we're offering great value to our customers when they need it more than ever.

Peter Sklar

Okay. On the $85 million of COVID costs that you disclosed you incurred during the quarter, is that what we should assume is the new quarterly level going forward, all else being equal, and you need to keep the same level of sanitation and protections for the customers and employees, et cetera? Is that what we should be looking for on a quarterly basis?

Darren Myers

Yeah. Peter, certainly for where we're at today in this pandemic, that's a good run rate to be using.

Sarah Davis

Just keep in mind that Q3 was a four-period quarter. That would be lower at the same run rate in Q4.

Peter Sklar

Right. Good point. And when we eventually get out of this, whether through vaccines or otherwise, is some of that cost going to stick? Is that now structural in your business, for whatever reason, customers demand cleaner stores or whatever? Or is most of that going to disappear?

Darren Myers

That's a good question. I think I mean, it's challenging to predict. I think there will be some elevated costs but certainly it would not be this kind of run-rate cost. A large part of this would fall off. But I think there's going to be—I think consumers are going to have different expectations, at least for a period of time after. So I don't think it goes to zero but it certainly wouldn't stay at this level.

Peter Sklar

Right. Okay. And then just lastly, on the normal course issuer bid, Darren, I noticed you bought back some stock during the quarter. Is this largely just anti-dilutive measures on your part? Or I'm just wondering what your philosophy is. Is the Company trying to reduce the share count at this point?

Darren Myers

It’s part of our financial framework. It hasn’t changed. We see it as a great way, with our strong cash flow, to give back to shareholders. So it hasn’t changed. We resumed it in the quarter, and we can plan to continue to do buybacks.

Peter Sklar

Okay. Thank you.

Darren Myers

Okay. Thanks, Peter.

Operator

Chris Li with Desjardins. Your line is open.

Chris Li — Desjardins

Good morning, everyone. Sarah, just wondering, have you had discussions with the government in terms of what role Shoppers might play in the distribution of the COVID vaccine? And it seems like it will be a very large undertaking but with potential benefits, not only financially, but obviously, from a social good perspective. And just wondering if you do participate, what type of investment will Shoppers need to make to make sure that they’re well prepared?

Sarah Davis

We always have ongoing conversations with the many different governments across Canada. We would love to be part of the solution for providing a vaccine to Canadians. So we would definitely feel like we would be well suited for it. We have all of the protocols in place that we think would be required, and we’ll continue to have those conversations.

So I would say, in terms of preparing, I wouldn’t say—we are prepared to be able to do it through appointment only or through walk-in. I think we’re prepared to be able to do it any way that we can think of that it might be rolled out. I think it would just be a question of having the right labour in the right store as the vaccine becomes available and as we understand the rules of who will be getting the vaccine first and those types of protocols. But we feel well prepared to be able to do this.

Chris Li

Great. That's very helpful. And you mentioned cosmetic sales improved sequentially. Just wondering how much of the cosmetic sales have recovered versus last year during the quarter. Can you give us a sense of is it 70 percent, 80 percent, just some rough idea?

Sarah Davis

So we're still down. We were down in Q2 significantly, as it really wasn't the focus of customers at the height of the pandemic. We're still down in Q3 but we're starting to see an improvement, but it wouldn't be as down as much as—we would have more than 70 percent of last year's sales. It wouldn't be down that much.

Chris Li

Okay. That's helpful. And then just on the Discount side, I think you mentioned that the Food sales were higher if we exclude the right-hand side. And I think it will be helpful if you can maybe quantify for us what was the drag so we can get a true sense of this underlying strength of the food sales and discounts.

Darren Myers

Chris, I don't think we're going to give that number today. Like I said before, the right-hand side impact was a little bit less than the second quarter; well, it was quite a bit less than the second quarter. But I don't think we're going to give the number by division today. Sorry.

Chris Li

Okay. No problem. And then, Darren, just maybe a quick one on gross margin. If we assume the Market division has a higher gross margin rate than Discount, just wondering, did the strength from the Market division so far this year, did it have a meaningful impact on gross margin? On the gross margin rate?

Darren Myers

I mean, it certainly would have helped the margin rate. Yes.

Chris Li

Okay. And my last question. Do you expect the changes in the branded prescription drug prices starting Jan 1st of next year to have any material impact? I know in the past, you've always said you budget above $70 million to $80 million for drug reforming pack (phon). Is that sort of within that budgeting that you have for next year?

Darren Myers

I would say, I want to, again, careful to give colour for next year. But it would be within the kind of regular reform that we would expect. Nothing higher at this point in time from what we know.

Chris Li

Perfect. Thank you. And hope you have a strong finish to the year.

Darren Myers

Thanks, Chris.

Operator

Michael Van Aelst with TD Securities, your line is open.

Michael Van Aelst

Yes. Just a follow-up question on financial services actually. You might've mentioned it, but I missed it. Can you explain the big increase in the margin in the financial service side, given that you had lower revenues in COVID?

Darren Myers

Yeah, Mike. It's really a function of two things. One is timing of investments, and we called them out last year as a hurt in this quarter, so it's kind of normalizing of that.

And the second was just adjustments to our ECL provision. We are seeing some moderate improvement in the economic outlook, at least relative to the second quarter and the first quarter when we put the ECL provision there. So it's just more of a true-up on that.

Michael Van Aelst

So 18 is a more normalized level, then, is what you're suggesting.

Darren Myers

Yes.

Michael Van Aelst

Okay. And as you look into Q4, it's usually a big quarter seasonally for financial services. But given the lockdowns and people probably spending a little bit less and maybe fewer people in store, do you see any risk to the performance of the mobile shop or the credit card in general?

Darren Myers

Yeah. Listen. It's difficult to predict how things are going to go, depending on lockdowns and what. I'd say the underlying portfolio is still doing well. People are paying their bills. The loss rate year to date's relatively in line with last year. So the portfolio is quite healthy and people are still spending.

If there's further lockdowns, how that will play out is a question. I'd say we still expect a seasonal pickup into the fourth quarter. I just don't know the degree of the impact of things like lockdowns at this point. Too hard to predict.

Michael Van Aelst

All right. Thank you.

Operator

There are no further questions at this time. I'd now like to turn the call back over to the Loblaw team for final remarks.

Roy MacDonald

Thank you, and thanks everybody for your time this morning. If you have any follow-up questions, please give me a call or drop me a note. And mark your calendars for February 25th when we'll be discussing our full year 2020 results. Have a great day.

Operator

This concludes today's call. We thank you for your participation. You may now disconnect.