FINAL TRANSCRIPT

Loblaw Companies Limited

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Loblaw Companies Limited Second Quarter 2023 results conference call. At this time, all lines are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. This call is being recorded on Wednesday, July 26, 2023.

I would now like to turn the conference over to Roy MacDonald. Please go ahead.

Roy MacDonald – Vice President Investor Relations, Loblaw Companies Limited

Thank you, Michelle. Good morning, everybody. Welcome to the Loblaw Companies Limited Second Quarter 2023 results call. As always, I'm joined this morning in the room with Galen Weston, our Chairman and President, and with Richard Dufresne, our Chief Financial Officer.

Before we begin the call, I want to 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. These statements are based on assumptions and reflect management's current expectations and as such 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 this morning.

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

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

With that, I will turn the call over to Richard.

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Thank you, Roy, and good morning, everyone.

I'm pleased to report that we continued to deliver consistent operational and financial results with solid top-line performance and strong earnings growth. We remained focused on delivering value to consumers and carefully managing our expenses, all part of retail excellence.

On a consolidated basis, revenue grew by 6.9 percent, and EBITDA increased by 9.4 percent. Adjusted earnings per share grew by 14.8 percent to $1.94 a share. On a GAAP basis, our earnings per share reflected a 36 percent increase. This was unusually high as we lap the hundred-million-dollar one-time charge last year specifically related to PC Bank.

In Drug retail, absolute sales increased 7.4 percent and same-store sales grew 5.7 percent. Front-store same-store sales grew by 5 percent on continued strength in cosmetics and health and beauty.

OTC performance remained strong but off its peak levels. Similarly, growth in our Drug business has moderated as it laps last year's post-pandemic reopening.

Pharmacy same-store sales grew 6.3 percent driven by growth in acute and chronic scripts partially offset by lower-cost COVID vaccines and testing. At the same time, we're pleased with the growth of services related to expanded scope of practice.

In Food retail, absolute sales increased 6.4 percent and same-store sales grew 6.1 percent. In Q2 our internal food inflation number was generally in line with the CPI. However, shoppers in our grocery stores actually beat inflation by taking advantage of our pricing, private brands, and hard discount stores. That means that our Loblaw shoppers experience a lower rate of inflation than CPI.

As we battle inflation, we remain highly concerned about ongoing cost increases, and I wanted to offer some facts. This year suppliers have raised the price we pay for products by more than $1 million. This is double what we would expect normally. We have received double-digit increases from the same suppliers who gave us double-digit increases last year. That's why you see products that are noticeably more expensive than they were just a couple of years ago.

While cost increases are coming in from all tiers of our supplier base, the largest global brands stand out. Let me give you an example. Since inflation began, one of our largest vendors has submitted price increases totaling 50 percent, or a quarter billion dollars. That's just one supplier.

Here's another good illustration. In Q2 the average price for meat, fruit, and vegetables purchased in our stores were up in the mid-single digits, but the average purchase in the center of store where you find the biggest brands was up in the double digits. At the same time, our food profit margins have declined as our costs have grown faster than our prices. The math is very simple. Cost increases from big brands were well above Canada's food inflation and our food margin declined, suggesting that grocer profiteering just don't add up.

Food inflation is a global problem. The causes range from climate change to war. We know that some cost increases are justified, but many are not. The price of transportation, wheat, flour, paper, and plastic are all well off 2022 highs. Our teams are actively reaching out to our largest suppliers, pressing for cost decreases based on these facts. With lowered costs we will lower prices.

Returning to our performance, our ability to deliver value was reflected across our Food business. Our hard discount banners continued to outperform the overall discount channel, delivering strong traffic and item count growth as customers continue to focus on value offerings.

In Quebec our discount position continues to grow. We converted 10 Provigo stores to Maxi in the quarter, and we'll convert another 10 stores in Q3. We continue to be very pleased with the sales growth being generated from these converted stores. Our market banners remain healthy despite the ongoing shift to discount stores. Having the right customer offer in all our stores remains a key focus.

Right (inaudible) posted a solid quarter with all major categories delivering positive same-store sales and apparel outpacing food same-store sales. That said, net-net it remains a drag on our same-store sale performance to the tune of 60 basis points in the quarter. We remain comfortable with our inventory levels.

Online sales in the quarter increased 13.9 percent, reflecting the strength of our digital businesses as we lap our first post-COVID quarter. Growth was led by PCX delivery and online pharmacy. We continued to enhance our customer experience and differentiate ourselves by offering more choice and flexibility.

Retail gross margin was 31.1 percent, down 30 basis points compared to last year. The driving factor was higher shrink in Drug, where we also saw pressure from lower services revenue. In Food we controlled costs well, investing our savings into lower prices.

Across our Retail segment, another quarter of careful cost management resulted in an improvement of 60 basis points in our SG&A rate as a percentage of sales. Adjusted Retail EBITDA increased by $142 million, or 9.8 percent in the quarter, yielding a margin of 11.8 percent, up 40 basis points compared to last year.

PC Financial adjusted earnings before tax declined by $22 million, largely a function of increased net credit losses and loss provisions and higher interest rates this year. The top-line business performance remains in line with our expectations with revenue up $51 million driven by higher interest income and an increase in consumer spending. On a consolidated basis, Adjusted EBITDA margin was 11.9 percent in the quarter, up 20 basis points compared to last year.

Our Retail free cash flow was $600 million in Q1 reflecting higher CAPEX spend and lapping one-time tax recoveries from last year. In the quarter we repurchased $500 million worth of common shares. Looking ahead, our second half same-store sales will reflect comparisons against our very strong sales performance last year in both Food and Drug.

At the Bank, we expect continued revenue growth from the growth in our portfolio, and we expect to see ongoing pressure on credit loss provisions given the current economic forecast. However, we remain confident in our ability to deliver our full year outlook.

I will now turn the call over to Galen.

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Thank you, Richard, and good morning. I was pleased with another quarter of consistent performance. The business charted strong core results, providing continued confidence that we are delivering retail excellence and serving our customers well.

In our Drug business, we returned to a more normal growth rate. In our front store, elevated sales of cough and cold meds subsided, while beauty remained brisk. Although COVID services have declined nationwide, we are increasing our range of patient care. In fact, it feels like every month another province moves to expand and fund services that pharmacists can provide to plug growing gaps in primary care systems.

Just this morning, New Brunswick announced its first six pharmacy primary care clinics, following an innovative recent rollout of 26 in Nova Scotia. Yesterday in Ontario, we unveiled two pharmacy sites redesigned to provide more clinical services and a better patient experience. We'll invest in a total of 72 of these clinics this year, another step towards the pharmacy of the future and our journey to improving Canadians' access to primary care.

In our Food business, market stores continue to perform well, lifted in part by the customer response to our President's Choice summer product lineup, including new customer favorites like frozen mochi and Ube Boba Pie. The ongoing shift to discount continued to pick up steam, driving high growth in our stores. Our hard discount locations have never been busier with our highest ever customer counts, double-digit growth, and No Frills was recently named the most trusted store for low prices. We'll add 25 more [discount stores] to the network this year [through conversion from Provigo to Maxi].

As customers focus on value, sales in our private brands continue to outpace national brands, delivering an average savings as high as 25 percent. More Canadians are turning to PC Optimum points to fill their carts with redemption rates climbing. We were delighted to see a recent survey that said Canadians are paying more attention to loyalty programs and that PC Optimum is by far their favourite, used an incredible nine out of 10 times.

As has been the case since this period of inflation began climbing, our Food gross margins declined. The business was highly efficient in the quarter, and we invested those savings in promotions. Once again, our product costs increased more than our prices. Despite Canada having one of the lowest food inflation rates in the world, we continue to face historic cost increases.

As our business moves forward, so do our efforts to manage our impact on the environment. It was a busy quarter in this regard. Shortly after our first electric truck hit the road, we announced that five hydrogen fuel cell electric trucks will join the fleet, allowing zero emission deliveries, and we announced that electricity purchased for Alberta supermarkets, drug stores, offices, and distribution centres will soon come entirely from wind, sun, and water. The impact will be the equivalent of taking all the homes in a city the size of Lethbridge off the grid, and we'll cut our national carbon footprint by 17 percent. We continue to execute well against our business plans and our purpose of helping Canadians live life well.

I'll now open the call for questions.

Roy MacDonald – Vice President Investor Relations, Loblaw Companies Limited

Thank you, Galen. Michelle, if you'd please introduce the Q&A process.

Q & A

Operator

Thank you. Your first question comes from George Doumet, Scotiabank. Please go ahead.

George Doumet – Scotiabank

Yes, good morning. Thanks for taking my questions. Richard, I believe last call you mentioned a 6 percent Q1 exit in food same-store sales. Just wondering if you can talk to the trends that happened kind of inter quarter in Q2. Was it stable, how was the exit, and any general comments you can have on market share for the market banners?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

You're right, that's what we sort of guided towards. I think the key perspective to take into consideration is you look at our sales trajectory in dollars, and that has continued, okay, and that's what generated our 6 percent same-store performance in Q2. But you need to take into consideration then that last year, Q3 in Food was 7 percent same-store sale and Q4 was 8 percent. Okay, so we're going to be cycling that versus—like, this quarter we cycled 1 percent. So, while sales trajectory will continue, we're going to be cycling against those figures. So, you're going to see same-store sales growth rate decline because of that, but that doesn't mean our sales are dropping.

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You're going to see the same for Drug. Drug has been 6 percent this quarter. It was 6 percent last year. But if you look at Q3 and Q4 of last year, Q3 was 8 percent same-store sales and Q4 was 9 percent. We're going to be facing into that as we go forward. But this is part of our plan, and we still remain very good regarding our outlook.

George Doumet – Scotiabank

Okay, and just market share comments you have maybe for the market banners?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes, market share, like a positive trajectory in the quarter, and that's what I'd say.

George Doumet – Scotiabank

Okay. Can you talk a little bit to shrink, what areas of the business is it most prevalent in and what impact that had on gross margins? Maybe what we're doing to fix it and just how confident you are in kind of maintaining the gross margins flat, I guess, (multiple speakers).

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes, a very good question. I think that's everybody's question this morning. So yes, so our gross margin is down 30 basis points. In Food it's a combination of shrink, but also what we call trading margin, okay, being the fact that our costs have gone up a little bit more than our price. In Shoppers it's essentially all shrink.

We've been talking about shrink for a few quarters now. I think the key point on shrink is that we've been investing capital and labour in store for close to a year now. Our view right now, it's early though, is we see it peaking. We've got indicators that are telling us that that it is peaking and in certain instances is getting a little bit better. But we will comment on that in the next quarter because we're going to be recounting a significant number of stores in this quarter, so we'll be able to affirm this with confidence when we release Q3. It's important for us as we plan for 2024. I don't know if that's helpful.

George Doumet – Scotiabank

Okay, thanks.

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Other than that, we feel good about our gross margin performance going forward.

George Doumet – Scotiabank

Okay. No, thanks for that. Just one last one, if I may. One of your competitors observed promotional penetration is exceeding pre-pandemic levels. Just wondering how you guys see that and perhaps any commentary you can share to that. Thanks.

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, we have commented on pre-pandemic promotional penetration. What we realize also in our own approach to our business we took out a lot of inefficient promotions, as you'll remember in 2020. So, we're pretty much at what we'd call a normalized level of promotional penetration at the moment, and so we're not going to comment too much on that in the future. Just think about us being back there now.

George Doumet – Scotiabank

Okay, thanks for your comments.

Operator

Thank you. The next question comes from Irene Nattel of RBC Capital Markets. Please go ahead.

Irene Nattel – RBC Capital Markets

Thanks, and good morning, everyone. I guess what we're all struggling with is the interplay between the tougher comps a year ago, so slowing same-store sales, but also your ability to get some margin catch-up which was so challenging when we were facing that almost double-digit inflation. Can you talk through a little bit some of the puts and takes there and how we should be thinking about that?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Okay, Irene, good question. I think for us, like, we've been focused on stability of gross margin, and we still feel we're stable, like down 30 basis points for us; we're in the zone. But what we spend most time focused on is the growth rate of our SG&A. Because if we can manage our SG&A growth rate as a percentage versus the year before, that's what will allow us to land on our financial framework. If you look at the performance we've had so far this year, and if I look ahead for the second half, I feel good about my SG&A cost curve. Therefore, that gives us confidence in our ability to deliver on our plan.

Irene Nattel – RBC Capital Markets

That's really helpful, thank you. How should we be thinking also about the interplay between the consumer trade down activity, promotional intensity? Like, where does that all kind of shake out in terms of gross margin? Is it a tailwind, is it a headwind? How does all that come together?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

It's noise at the margin, obviously, because we have two large businesses, like a big conventional business, a big discount business. Obviously, discount is a lower gross margin rate than market, but like the—and the growth in discount, like, is markedly higher; same-store sale and discount is markedly higher than market, so you're seeing that at play. But more sales get more dollars, so it's like for us, we're managing on a consolidated basis, and when we look at it on a consolidated, what we lose from one, we get from the other. That's what we've experienced so far, and that's what we expect going forward, also.

Irene Nattel – RBC Capital Markets

Richard, what I'm hearing you say is that we should be slightly less focused on the gross margin sort of change, 30 basis points up, 20 basis points down, whatever it is, and focus on the growth in the gross margin dollars relative to the top line? Or (multiple speakers) relative to the top line?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes, Irene, but we also look at both. There's been a significant effort on shrink that started a year ago because we were starting to see it creep up, and it was not much noticeable. Now, it's noticeable, so we talk about it. But we've taken actions a year ago, and we're starting to see the benefits from that. We're not done in our actions. With that plateauing and with what we see ahead together, that allows us to feel decent about our performance for the second half.

By the way, we're thinking about that as we're planning for '24, so we're already well advanced in our planning cycle for '24, and all of these factors are in play as we prepare for next year.

Irene Nattel – RBC Capital Markets

That's great, thank you. Finally, just one last question. You brought back a fair amount of stock in Q2. How should we be thinking about the aggregate NCIB in 2023?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes, Irene, if you look at it and you compare it to last year, we're more or less at the same place. I think we're ahead by, I don't know, maybe $50 million. So for us, like, we're on plan.

Irene Nattel – RBC Capital Markets

That's great, thank you.

Operator

Thank you. The next question comes from Mark Petrie of CIBC. Please go ahead.

Mark Petrie – CIBC

Yes, thanks. Good morning. I wanted to just follow up on a couple topics. First, it's Shoppers. I know you spoke about shrink. You're no longer (inaudible) it out, Shoppers overall, as a margin tailwind. How much of that would you say is its own performance, and how much is just that the growth rate is now normalizing and no longer materially exceeding the Food growth?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

If you were to exclude shrink, gross margin in Shoppers would have been up in the quarter. It was a factor. That's an area where we spent a lot of effort. Like, if you go in stores, you'll see what we refer to as fragrance lockups. That's where the professional (inaudible) have been focused on, so we've locked up many of these fragrances, and you're going to see more of those over the coming months. Those are high-priced items which, when they go, it hurts the bottom line. As we put that behind, it'll definitely help shrink.

Interestingly, we're not losing sales. That was a big fear as we were locking up fragrances, that we'd be losing sales, but we're not losing sales. That's going to start to yield benefits over the coming months.

Mark Petrie – CIBC

Yes. Okay, helpful. On the Pharmacy services, Galen, I know you talked about it in your comments, but I'm just sort of curious. You're lapping some of the big COVID-driven services, but also expanding these clinics. Where are we at in terms of the progression of that in terms of headwind versus tailwind? Obviously, it's a headwind right now, but is it more of a headwind now than it was a couple quarters ago, and when does that sort of normalize, do you think?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, so it is a headwind entirely because we're cycling those extraordinary COVID vaccination and COVID test numbers. We really focus on what's happening with the underlying growth rate of the other expanded scope of practice services, and we see very encouraging growth trajectories underneath it all. It'll take until we've cycled through the last of that COVID period before we see, call it, meaningful growth in the business on an absolute basis.

Remember, the way to think about our expanded scope of practice initiative, which includes the pharmacy-led clinics and the expanded scope of practice across all these provinces, think about it as a fast growing, accretive contributor to the business that will drive, or will help us drive our financial framework. It's not going to deliver a step change in growth in sales or in profitability, but it will give us that long-term tailwind that will allow us to continue to perform as we have for the last number of years in that business.

Mark Petrie – CIBC

Yes, understood. Maybe just to follow up on that, are these pharmacy care clinics, like, how do the economics on these sort of stack up versus other investment opportunities in the store network? I'm sort of thinking of just regular store renovations or new stores. What do the paybacks look like for those care clinics?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

So, it depends. There's a pharmacist-led clinic inside a pharmacy, and that has a very high payback relative to what you would consider, say, a new store. Think about it as an incremental renovation with meaningful sales upside. That would be superior to the sort of regular return rate. Then you have the standalones, which are far less in number than the in-stores, and they have what I'd describe as slightly pressured core returns until you add the pharmacy prescription on top of it, which has always been a major amplifier for any investment that we've made in medical clinics. Then it delivers a very healthy return that would be in line with or above return rates we get for Shoppers Drug Mart.

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes, Mark, just to give you some order of magnitude, like, we've built two of these and it's our first two, so we didn't spend much time focused on the return. But, like, we're talking a few hundred thousand dollars. This is not millions of dollars, and I can tell you the first two, I'm sure they will look amazing because they want to make it look good for us. But the next ones that are coming, once we know that the concept is working, we're going to tighten the screws on the costs. But it's not a big cost, so it's not something that you should worry about from a big CAPEX standpoint.

Mark Petrie – CIBC

Yes, understood. Appreciate the comments. All the best.

Operator

Thank you. The next question comes from Tammy Chen of BMO Capital Markets. Please go ahead.

Tammy Chen – BMO Capital Markets

Yes, thanks for the questions. First, I wanted to go back to the SG&A. Richard, could you maybe elaborate a little bit more on this quarter, in particular, you were able to get pretty good leverage. What were some of the areas that this came from, and how should we think about that going forward when it seems like right on the gross margin side, whether it's Shoppers or also the Food side, there's limitations to which you can pass through your costs?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes. Obviously, when your top line goes up 7 percent, it's definitely helping your SG&A rate, okay? But that's not typical of the growth we get normally in our business. We don't look at it as a percentage of sales. We look at it at a percentage growth versus the year before. If you want to drive operating leverage, you need to have your SG&A grow at the lower rate than your top line. That's what we focused on, and we've laid out plans that allow us to deliver on that. Our plans for ‘23 are quite robust, and based on what we see coming ahead, that gives us confidence that we should be able to deliver on our framework.

As I was mentioning earlier, right now we're working on 2024, and we're adopting the same approach. We need to make sure that the growth in our SG&A in dollars doesn't grow too fast because then we won't be able to deliver on 2024. We're taking actions now to make sure that this happens, and that's how again, in 2024, we should be able to continue to deliver on our framework. The plan is laid out. It's not like we're going to take more initiatives now. We have our plan laid out, and if we just deliver on our plan, we should deliver on our framework.

Tammy Chen – BMO Capital Markets

Okay. Within that, I'm curious specifically on the whole labour and wage environment. I think last quarter you had said the number of ratified agreements over the last few months were at the higher end of the normal range. I'm just wanting to understand if you think at this point there might be still some incremental catch-up for you and your labour costs with respect to broader market wage inflation that we've seen over the last two or so years, or are you largely through that?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

So, we know always what's coming. Like, we know when negotiations happen, and so we budget that in our plan, as like everything else. We’ve budgeted what's to come. As we've answered that question, Galen has answered that question a few times recently, and we talk about, like, we've been at the higher end of the range, but it's at the high end of a range that we're planning for, so that's how we're thinking about it. Right now, based on what we see, we should be within our plans on what we see ahead.

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

To your question about catch-up, no, we don't have any substantial catch-up issues that we're facing. Think about them more as normal course negotiations. Then the thing that we try and be careful of is locking in growth rates that would not be in line with the long-term inflation rate. That's where we try and land these agreements.

Tammy Chen – BMO Capital Markets

Okay, thank you.

Operator

Thank you. The next question comes from Michael Van Aelst of TD Securities. Please go ahead.

Michael Van Aelst – TD Securities

Thank you. You mentioned about some of the costs coming down, or vendor costs coming down, but not necessarily showing up in the cost of goods sold yet. Can you talk about what—give us some insight as to what some of the pushback is from vendors as to why they aren't pushing it down and why they're still trying to push through price increases?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, so I mean, a couple of things. First of all, we're seeing meaningful shifts in a whole line of commodities that are core ingredients in these products. That's why we expect products that are heavy in these ingredients to start to slow and ultimately turn the other way. You'll have to ask the packaged goods manufacturers what their perspective is on why they're not bringing retail prices down. They have a litany of explanations for us, but the fundamentals are that if the cost of the inputs are starting to slow and reverse, then ultimately, we should see some component of that show up in cost increases.

Look, we operate—as you know, we source a lot of controlled brand product, and so we have pretty good visibility into how this should evolve. Having said that, I don't think it's reasonable to expect an aggressive reversion or a shift into a deflationary environment. The reductions that we're seeing in commodities are moderate. They're notable, meaningful, but it's not at this point headed towards a cost reversal.

Michael Van Aelst – TD Securities

All right. On your private label sourcing, is that cost plus?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

No, it's negotiated differently depending on the vendor.

Michael Van Aelst – TD Securities

Does that mean you're not necessarily getting cost reductions on your private label either?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

No, all I'm saying is that we negotiate them on a case-by-case basis, and we are seeing reductions in some cases with a couple of national brands and with control brand vendors as well.

Michael Van Aelst – TD Securities

Okay. Because I'm trying to see how the cost environment is influencing your private label penetration. It seems like it's still growing. I'm wondering how close you think we are to peak levels in private label. Then, I know in the past you've talked about CPG companies are eventually going to try to push back and get some volume back, but it seems like it's tough for them to do if they're still taking double-digit increases. Where do you see private label penetration peaking out, I guess, or how soon, and what are you expecting over the next year, let's call it?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, you're right. We have talked about this a few times, that we would expect, again, the larger brands to start investing to drive volume. We're seeing some signs of it, but it's emerging more slowly than probably we expected earlier in the year, and that's benefiting our control brands. Today our control brands are still growing faster than national brands. We do think that that will rebalance itself at some point in the relatively near future, but that really is up to the big brands to determine when and how.

Michael Van Aelst – TD Securities

Okay, and can you just comment to whether you're being—holding onto your margins in private label, or are you seeing any erosion there?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

No, we're holding onto our margins.

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes, we are. I think (inaudible), I think Galen made the point, like, we're still growing faster than national brand, but because of the environment we're in, if you actually go one level down and you look at no name versus PC, no name is still growing high double-digit. In today's environment, we expect that to continue just because of the nature of what we're in right now.

Michael Van Aelst – TD Securities

Okay, all right. Then just on the tonnage, I know people like to try and infer (phon) tonnage out of your inflation and your same-store sales, but what are you seeing in your tonnage numbers, and how do they—what do you believe is happening with your market share?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

I can take tonnage (inaudible), give you a sense of tonnage. It's clearly positive in discount, it's somewhat negative in conventional. Net-net (inaudible), it's about flat. That's where we are right now, which is a significant improvement from where we were at this time last year. But you're now clearly seeing discount being positive territory, and it's been the case for a few quarters now. That should help you figure out how we're doing on share. We feel we're progressing on share, and so yes, so that's where we stand right now.

Michael Van Aelst – TD Securities

All right, thank you.

Operator

Thank you. The next question comes from Vishal Shreedhar of National Bank. Please go ahead.

Vishal Shreedhar – National Bank

Hi. I was hoping you could update us on some of your adjacent value drivers like freight as a service and media. I know you've installed some screens in your stores, and maybe where those businesses are and how much you think they can grow in the near term?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, so they're all progressing nicely. We don't have a new frame for you, Vishal. Third-party transport, it's a meaningful contributor now in terms of its size and scale. We're investing a little bit of capital in it to continue that growth trajectory and remain optimistic about its potential.

Media is much smaller. As we mentioned the last quarter, we've just completed—well, last quarter we completed a big infrastructure, a technical infrastructure project, which we call RMP, which is essentially the tool that allows advertisers easier access to our customer audiences and to advertise with us. We're getting really terrific responses back from the industry in regards to that tool. We're delivering on all our financial targets in relation to media now, but it remains small. It's yet to sort of ramp up at a level where it would be relevant to comment to you on its size and scope.

But with both of these, just keep in mind that our goal is to use these adjacencies to drive that long-term financial framework. In the same way that pharmacy services are going to do that, that's what transport helps us do, that's what media helps us do. You need to look at it as all enablers of us delivering that long-term growth rate rather than any of them contributing to an outsize or step-up in terms of earnings growth. Does that make sense?

Vishal Shreedhar – National Bank

Thank you for that colour. Just changing topics here, on Lifemark. How’s the integration progressing, and how should we think about Loblaw’s appetite for further acquisitions? What kind of sphere should we think them being in, if that’s in fact being contemplated?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, so start with primary care delivery, which is the foundation of our—sort of adjacent to pharmacy healthcare strategy. That is driven by pharmacists in the manner that we’ve just discussed on this call over the last few minutes. Then think about another adjacency, which is other forms of care delivery that would be complementary to that experience. That’s where Lifemark sits, and that was the driver behind that acquisition. It has good economics in that it’s accretive. It has a good market tailwind, so it should grow on its own at a sales rate that is higher than the rest of our core business. On a standalone basis, its long-term capacity to contribute is accretive and attractive.

But the reason that we bought it was because we thought that we could grow that business faster than others by linking it to our existing healthcare customer in a more integrated way. That’s really the prize. I would say that we are making steady progress testing that thesis and the value of that integration, and we'll continue to report on progress. But we're not going to make any more material acquisitions in adjacent healthcare delivery spaces until we are absolutely certain that we are a good owner for these kinds of assets, that there's a synergy within the enterprise from owning them. We've still got work to do to convince ourselves that that is in fact the case, and you won't see any incremental M&A until we're certain that it is.

Vishal Shreedhar – National Bank

Okay, and maybe a last one for me, just on the population growth and the disparate levels of growth across the country. Are you seeing the impact of that as you look at your business and saying, hey, these regions are benefiting more from population growth and we're seeing that in our stores and maybe some less so, and so maybe some areas are more competitive or less growth as a result?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Oh, yes. I mean, we see it every day, the changing demographics in markets all across the country. You see demographic shifts. You see cultural shifts. There are markets where customers are—where Canadians are moving to small towns. There are small towns on the periphery of big cities that are growing faster today than they were at any point in the last 20 years. That constitutes a new opportunity perhaps for an incremental store. You've heard us talk about T&T and the extraordinary success that we continue to experience when we open new T&T stores almost anywhere in the country. That is a reflection of immigration and the heavy weighting of Asian immigrants coming into the country.

We’ve been refining our No Frills business to better serve the South Asian customer, and we’ve seen fantastic results coming from our work on that front.

Then there’s the other tailwind, which is you want to add square footage that’s in line with accelerating population growth. As you’ve heard Richard describe on a number of occasions, we are continuing to build our pipeline of new stores so that we can meet that demand and make sure that we’re getting our fair share of the population growth in the country.

So, it’s a big and important driver, and it’s one of the reasons to have long-term optimism about Loblaw, is that population growth tailwind and knowing that everybody needs to eat and that we have formats that meet effectively just about every demographic and every culture.

Vishal Shreedhar – National Bank

Thank you.

Operator

Thank you. The next question comes from Chris Li of Desjardins. Please go ahead.

Chris Li – Desjardins

Hi, good morning. Maybe I’ll just start off with a couple of quick clarification questions. Richard, in the beginning, I think you mentioned that you expect food sales to drop in the second half because of tough comps. I just want to clarify. I think you meant sales growth to maybe moderate and not necessarily decline in the second half. Is that (multiple speakers).

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

No, I did not say sales are going to drop.

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

You did. But you meant—the growth rate's going to slow [NTD: original comment corrected in this update]. That's what he meant.

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

It's going to slow. Yes, sorry. You're not going to see the same same-store sales because we're going to be cycling higher comps. Okay, correction made. Thanks, Galen.

Chris Li -- Desjardins

Okay. Sorry, guys. I just wanted to make sure. Okay, that's great. Then just on the shrink, and again, just wanted to clarify. So, the shrink you saw in Drug is predominantly because of theft in the beauty category, and so you put a measure in place, so that should correct itself in due time.

Then on the Food side, I just want to clarify what's driving that? Is it because of the new store growth and being more precise with inventory count? Is that what's been causing higher shrink on the food side?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

No, it’s still organized crime in grocery also, albeit not at the same extent as we witness in Shoppers as a rate.

Chris Li – Desjardins

Okay, so in both instances, it’s mainly theft that’s causing that higher shrink?

Richard Dufresne – Chief Financial Officer, Loblaw Companies Limited

Yes.

Chris Li – Desjardins

Okay, that’s great. Then just on e-commerce, are you seeing any notable increase in adoption either at Loblaw or the industry? Or has the adoption remained largely stagnant because of high inflation and the shift to discount?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, so you saw that our numbers, I think, were up 13 percent in terms of overall e-commerce volume. It’s important to note that a disproportionate part of that is the Pharmacy business, so digital prescription filling, and so I’ll just focus on PC Express as a good proxy for sort of consumer product online adoption. That’s in and around flat is kind of the way to, to think about it, maybe a little bit better than that, with substantial growth on the delivery side of the equation and a little bit of decline on the pickup side. You blend it out and you get essentially to flat.

We are still waiting to see what the normalized post-COVID growth rate is for e-commerce. But it's certainly not going backwards, and we expect it to continue to grow as we look forward.

A couple of interesting updates I can provide. Between last quarter and now, we launched the PC Pass, which is our subscription product for PC Express for pickup and delivery. We've seen fantastic adoption of that product. It's now up to about 10 percent of the total sales in PC Express.

Then, of course, we continue to work away on improving the overall value proposition. I'm delighted to say we're at all-time highs in terms of our service levels and our fill rates for our customers. The service just gets better and better, and we continue to have high conviction that that is a really valuable service for our best customers and that it will continue to grow.

Chris Li – Desjardins

Okay, that's super helpful because I was going to ask you—one of the large discounting competitors recently launched a subscription program for e-commerce, and you guys obviously have a strong one as well. I was just going to ask, among the many tools that Loblaw has at your disposal, how effective is the subscription program to retaining customers? I think you just sort of answered my question there.

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, it's really been quite powerful. Probably the most encouraging insight is that we've acquired many more new customers with the subscription service than we expected. We thought, as you would, that it would be primarily a retention tool. It is serving that function, but it's also been a way for us to acquire new customers that have surprised us on the upside.

Chris Li – Desjardins

That's great. Then maybe finally, I know I ask this almost every quarter, but just any new updates on any potential changes in generic drug prices?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

No updates on that. I think we've actually got some certainty with the—I can't remember now what the organization is called. I think we have clarity on generics and branded for the next couple of years. We'll follow up with you to make sure I'm giving you the right insight on that. But no, nothing on the horizon that would constitute a meaningful risk.

Chris Li – Desjardins

That's great. Thanks very much.

Operator

Thank you. The next question comes from Irene Nattel of RBC Capital Markets. Please go ahead.

Irene Nattel – RBC Capital Markets

Thanks. Just one follow-up question, if I might, on Shoppers and beauty. What are you seeing now in terms of demand run rates? As consumer wallets are being squeezed, are you seeing any pressure there? How successful are the promotions that you're running using PC Optimum, for beauty specifically?

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes, beauty continues to be robust, and I think there's two forces at work. The first one is, beauty on the kind of the luxury spectrum of spend on myself, it's actually relatively low priced. The alternative of buying a high-end cosmetic product or fragrance versus buying an expensive handbag or a dress. It tends to be a lot more recession proof than perhaps other categories, and we are certainly seeing that continue in our business.

The second one, which is important to remember, is we've had a big retailer exit the market in Nordstrom's in recent months, and that volume—they were a big beauty retailer, and that volume needs to go back out into the market. We would be a disproportionate beneficiary of that in the local geographies where we would be competing with them, so that's also helpful for a business like ours.

Irene Nattel – RBC Capital Markets

That's great, so the lipstick index lives.

Galen Weston – Executive Chairman and President, Loblaw Companies Limited

Yes.

Irene Nattel – RBC Capital Markets

Thanks, Galen.

Operator

Thank you. There are no further questions at this time. Please continue with closing remarks.

Roy MacDonald – Vice President Investor Relations, Loblaw Companies Limited

Great. Well, thank you everybody for your time this morning. Please reach out to me if you have any questions. I'll ask you to mark your calendars for Wednesday, November 15 at 10:00 AM when we will reconvene to discuss our Q3 results. Thanks, everybody, and have a great day.

Operator

Ladies and gentlemen, this does conclude the conference call for today. We thank you for your participation and ask that you please disconnect your lines.