

## Management's Discussion and Analysis

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## Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") for Loblaw Companies Limited and its subsidiaries (collectively, the "Company" or "Loblaw") should be read in conjunction with the Company's third quarter 2019 unaudited interim period condensed consolidated financial statements and the accompanying notes included in this Quarterly Report, the audited annual consolidated financial statements and the accompanying notes for the year ended December 29, 2018 and the related annual MD&A included in the Company's 2018 Annual Report – Financial Review ("2018 Annual Report").

The Company's third quarter 2019 unaudited interim period condensed consolidated financial statements and the accompanying notes have been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP"). These unaudited interim period condensed consolidated financial statements include the accounts of the Company and other entities that the Company controls and are reported in Canadian dollars.

Management uses non-GAAP financial measures to exclude the impact of certain expenses and income that must be recognized under GAAP when analyzing consolidated and segment underlying operating performance, as the excluded items are not necessarily reflective of the Company's underlying operating performance and make comparisons of underlying financial performance between periods difficult. The Company excludes additional items if it believes doing so would result in a more effective analysis of underlying operating performance. The exclusion of certain items does not imply that they are non-recurring. See Section 12 "Non-GAAP Financial Measures" for more information on the Company's non-GAAP financial measures.

A glossary of terms used throughout this Quarterly Report can be found on page 140 of the Company's 2018 Annual Report.

The information in this MD&A is current to November 12, 2019, unless otherwise noted.

On December 30, 2018, the Company implemented IFRS 16, "Leases" ("IFRS 16"), replacing International Accounting Standard ("IAS") 17, "Leases" ("IAS 17") and related interpretations. The standard introduced a single, on-balance sheet recognition and measurement model for lessees, eliminating the distinction between operating and finance leases. The Company implemented the standard using the modified retrospective approach. As a result, the Company's 2019 results incorporate lease accounting under IFRS 16. Under IFRS 16, the depreciation expense on right-of-use assets and interest expense on lease liabilities replaces rent expense, which was previously recognized on a straight-line basis in operating income under IAS 17 over the term of a lease. Prior year results have not been restated.

On November 1, 2018, the Company and its parent George Weston Limited ("Weston") completed a reorganization under which the Company distributed its approximate 61.6% effective interest in Choice Properties Real Estate Investment Trust ("Choice Properties") to Weston on a tax-free basis to the Company and its Canadian shareholders ("the reorganization" or "the spin-out"). The Company's interest in Choice Properties is presented separately as Discontinued Operations in the Company's current and comparative results. As a result of the spin-out, buildings owned by Choice Properties and leased by the Company are accounted for as leases and no longer accounted for as owned property. The building components associated with these leases post spin-out are classified as leasehold improvements resulting in incremental depreciation expense.

See Section 3 Consolidated Results of Operations "Other Business Matters" of this MD&A for more information on the implementation of IFRS 16 and the spin-out related incremental depreciation.

### 1. Forward-Looking Statements

This Quarterly Report, including this MD&A, contains forward-looking statements about the Company's objectives, plans, goals, aspirations, strategies, financial condition, results of operations, cash flows, performance, prospects, opportunities and legal and regulatory matters. Specific forward-looking statements in this Quarterly Report include, but are not limited to, statements with respect to the Company's anticipated future results, events and plans, strategic initiatives and restructuring, regulatory changes including further healthcare reform, future liquidity, planned capital investments, and the status and impact of information technology ("IT") systems implementations. These specific forward-looking statements are contained throughout this Quarterly Report including, without limitation, in Section 3 "Consolidated Results of Operations", "Section 4.1 "Retail Segment" Other Retail Business Matters, Section 5 "Liquidity and Capital Resources", Section 11 "Outlook" and Section 12 "Non-GAAP Financial Measures" of this MD&A. Forward-looking statements are typically identified by words such as "expect", "anticipate", "believe", "foresee", "could", "estimate", "goal", "intend", "plan", "seek", "strive", "will", "may", "should" and similar expressions, as they relate to the Company and its management.

Forward-looking statements reflect the Company's estimates, beliefs and assumptions, which are based on management's perception of historical trends, current conditions and expected future developments, as well as other factors it believes are appropriate in the circumstances. The Company's expectation of operating and financial performance in 2019 is based on certain assumptions including assumptions about healthcare reform impacts, anticipated cost savings and operating efficiencies from Process and Efficiency initiatives and anticipated benefits from strategic initiatives. The Company's estimates, beliefs and assumptions are inherently subject to significant business, economic, competitive and other uncertainties and contingencies regarding future events, and as such, are subject to change. The Company can give no assurance that such estimates, beliefs and assumptions will prove to be correct.

Numerous risks and uncertainties could cause the Company's actual results to differ materially from those expressed, implied or projected in the forward-looking statements, including those described in Section 12 "Enterprise Risks and Risk Management" of the Company's 2018 Annual Report, and the Company's 2018 Annual Information Form ("AIF") (for the year ended December 29, 2018). Such risks and uncertainties include:

- changes to the regulation of generic prescription drug prices, the reduction of reimbursements under public drug benefit plans and the elimination or reduction of professional allowances paid by drug manufacturers;
- the inability of the Company's IT infrastructure to support the requirements of the Company's business, or the occurrence of any internal or external security breaches, denial of service attacks, viruses, worms and other known or unknown cybersecurity or data breaches;
- failure to realize benefits from investments in the Company's new IT systems;
- failure to realize the anticipated benefits associated with the Company's strategic priorities and major initiatives, including revenue growth, anticipated cost savings and operating efficiencies or organizational changes that may impact the relationships with franchisees and associates;
- failure to effectively respond to consumer trends or heightened competition, whether from current competitors or new entrants to the marketplace;
- failure to maintain an effective supply chain and consequently an appropriate assortment of available product at store level;
- failure to execute the Company's e-commerce initiatives or to adapt its business model to the shifts in the retail landscape caused by digital advances;
- public health events including those related to food and drug safety;
- errors made through medication dispensing or errors related to patient services or consultation;
- adverse outcomes of legal and regulatory proceedings and related matters;
- changes to any of the laws, rules, regulations or policies applicable to the Company's business;
- failure to achieve desired results in labour negotiations, including the terms of future collective bargaining agreements; and
- changes in economic conditions, including economic recession or changes in the rate of inflation or deflation, employment rates and household debt, political uncertainty, interest rates, currency exchange rates or derivative and commodity prices.

This is not an exhaustive list of the factors that may affect the Company's forward-looking statements. Other risks and uncertainties not presently known to the Company or that the Company presently believes are not material could also cause actual results or events to differ materially from those expressed in its forward-looking statements. Additional risks and uncertainties are discussed in the Company's materials filed with the Canadian securities regulatory authorities ("securities regulators") from time to time, including, without limitation, the section entitled "Risks" in the Company's 2018 AIF (for the year ended December 29, 2018). Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect the Company's expectations only as of the date of this MD&A. Except as required by law, the Company does not undertake to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

## 2. Key Financial Performance Indicators

The Company's interest in Choice Properties is presented separately as Discontinued Operations in the Company's current and comparative results. Unless otherwise indicated, all financial information reflects the Company's results from Continuing Operations and includes the impacts of spin-out related incremental depreciation, the implementation of IFRS 16 and the consolidation of franchises.

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

As at or for the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019 (16 weeks)	2018 <sup>(4)</sup> (16 weeks)
<b>Consolidated:</b>		
Revenue growth	2.3%	1.1%
Operating income	\$ 690	\$ 592
Adjusted EBITDA <sup>(2)</sup>	1,492	1,060
Adjusted EBITDA margin <sup>(2)</sup>	10.2%	7.4%
Net earnings (loss)	\$ 353	\$ 117
Continuing Operations	353	(15)
Discontinued Operations	—	132
Net earnings (loss) attributable to shareholders of the Company from Continuing Operations	334	(23)
Net earnings (loss) available to common shareholders of the Company <sup>(i)</sup>	331	106
Continuing Operations	331	(26)
Discontinued Operations	—	132
Adjusted net earnings available to common shareholders of the Company <sup>(2)</sup>	458	562
Continuing Operations	458	466
Discontinued Operations	—	96
Diluted net earnings (loss) per common share (\$)	\$ 0.90	\$ 0.28
Continuing Operations	\$ 0.90	\$ (0.07)
Discontinued Operations	\$ —	\$ 0.35
Adjusted diluted net earnings per common share <sup>(2)</sup> (\$)	\$ 1.25	\$ 1.49
Continuing Operations	\$ 1.25	\$ 1.24
Discontinued Operations	\$ —	\$ 0.25
Cash and cash equivalents and short term investments	\$ 1,022	\$ 1,426
Cash flows from operating activities <sup>(iii)</sup>	1,061	1,162
Free cash flow <sup>(2)(iii)</sup>	186	318
<b>Financial Measures:</b>		
Retail debt to rolling year retail adjusted EBITDA <sup>(2)</sup>	3.0x	1.7x
Rolling year adjusted return on equity <sup>(2)</sup>	13.4%	12.3%
Rolling year adjusted return on capital <sup>(2)</sup>	7.8%	9.6%
<b>Retail Segment:</b>		
Food retail same-store sales growth	0.1%	0.9%
Drug retail same-store sales growth	4.1%	2.5%
Operating income	\$ 655	\$ 551
Adjusted gross profit <sup>(2)</sup>	4,262	4,108
Adjusted gross profit % <sup>(2)</sup>	29.6%	29.1%
Adjusted EBITDA <sup>(2)</sup>	\$ 1,452	\$ 1,017
Adjusted EBITDA margin <sup>(2)</sup>	10.1%	7.2%
<b>Financial Services Segment:</b>		
Earnings before income taxes	\$ 15	\$ 22
Annualized yield on average quarterly gross credit card receivables	13.7%	13.2%
Annualized credit loss rate on average quarterly gross credit card receivables	3.4%	3.2%

(i) Net earnings available to common shareholders of the Company are net earnings attributable to shareholders of the Company net of dividends declared on the Company's Second Preferred Shares, Series B.

(ii) Includes amounts from Continuing and Discontinued Operations.

### 3. Consolidated Results of Operations

The Company's interest in Choice Properties is presented separately as Discontinued Operations in the Company's current and comparative results. Unless otherwise indicated, all financial information reflects the Company's results from Continuing Operations and includes the impacts of spin-out related incremental depreciation, the implementation of IFRS 16 and the consolidation of franchises.

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019				2018 <sup>(4)</sup>			
	(16 weeks)	(16 weeks)	\$ Change	% Change	(40 weeks)	(40 weeks)	\$ Change	% Change
<b>Revenue</b>	<b>\$ 14,655</b>	\$ 14,319	\$ 336	2.3 %	<b>\$ 36,447</b>	\$ 35,475	\$ 972	2.7 %
<b>Operating income</b>	<b>690</b>	592	98	16.6 %	<b>1,729</b>	1,478	251	17.0 %
Adjusted EBITDA <sup>(2)</sup>	<b>1,492</b>	1,060	432	40.8 %	<b>3,707</b>	2,633	1,074	40.8 %
Adjusted EBITDA margin <sup>(2)</sup>	<b>10.2%</b>	7.4%			<b>10.2%</b>	7.4%		
<b>Depreciation and amortization</b>	<b>\$ 775</b>	\$ 459	\$ 316	68.8 %	<b>\$ 1,935</b>	\$ 1,141	\$ 794	69.6 %
<b>Net interest expense and other financing charges</b>	<b>223</b>	292	(69)	(23.6)%	<b>571</b>	469	102	21.7 %
Adjusted net interest expense and other financing charges <sup>(2)</sup>	<b>223</b>	116	107	92.2 %	<b>571</b>	293	278	94.9 %
<b>Income taxes</b>	<b>114</b>	315	(201)	(63.8)%	<b>293</b>	506	(213)	(42.1)%
Adjusted income taxes <sup>(2)</sup>	<b>171</b>	169	2	1.2 %	<b>422</b>	425	(3)	(0.7)%
Adjusted income tax rate <sup>(2)</sup>	<b>26.3%</b>	26.2%			<b>26.5%</b>	26.6%		
<b>Net earnings (loss) attributable to shareholders of the Company from Continuing Operations</b>	<b>\$ 334</b>	\$ (23)	\$ 357	1,552.2 %	<b>\$ 824</b>	\$ 488	\$ 336	68.9 %
<b>Net earnings (loss) available to common shareholders of the Company<sup>(i)</sup></b>	<b>331</b>	106	225	212.3 %	<b>815</b>	533	282	52.9 %
Continuing Operations	<b>331</b>	(26)	357	1,373.1 %	<b>815</b>	479	336	70.1 %
Discontinued Operations	<b>—</b>	132	(132)	(100.0)%	<b>—</b>	54	(54)	(100.0)%
Adjusted net earnings available to common shareholders of the Company <sup>(2)</sup>	<b>\$ 458</b>	\$ 562	\$ (104)	(18.5)%	<b>\$ 1,121</b>	\$ 1,344	\$ (223)	(16.6)%
Continuing Operations	<b>458</b>	466	(8)	(1.7)%	<b>1,121</b>	1,151	(30)	(2.6)%
Discontinued Operations	<b>—</b>	96	(96)	(100.0)%	<b>—</b>	193	(193)	(100.0)%
<b>Diluted net earnings (loss) per common share (\$)</b>	<b>\$ 0.90</b>	\$ 0.28	\$ 0.62	221.4 %	<b>\$ 2.20</b>	\$ 1.40	\$ 0.80	57.1 %
Continuing Operations	<b>\$ 0.90</b>	\$ (0.07)	\$ 0.97	1,385.7 %	<b>\$ 2.20</b>	\$ 1.26	\$ 0.94	74.6 %
Discontinued Operations	<b>\$ —</b>	\$ 0.35	\$ (0.35)	(100.0)%	<b>\$ —</b>	\$ 0.14	\$ (0.14)	(100.0)%
Adjusted diluted net earnings per common share <sup>(2)</sup> (\$)	<b>\$ 1.25</b>	\$ 1.49	\$ (0.24)	(16.1)%	<b>\$ 3.03</b>	\$ 3.54	\$ (0.51)	(14.4)%
Continuing Operations	<b>\$ 1.25</b>	\$ 1.24	\$ 0.01	0.8 %	<b>\$ 3.03</b>	\$ 3.03	\$ —	— %
Discontinued Operations	<b>\$ —</b>	\$ 0.25	\$ (0.25)	(100.0)%	<b>\$ —</b>	\$ 0.51	\$ (0.51)	(100.0)%
Diluted weighted average common shares outstanding (in millions)	<b>366.2</b>	376.3			<b>369.7</b>	380.0		

(i) Net earnings available to common shareholders of the Company are net earnings attributable to shareholders of the Company net of dividends declared on the Company's Second Preferred Shares, Series B.

**Net Earnings Available to Common Shareholders of the Company and Diluted Net Earnings Per Common Share from Continuing Operations**

Net earnings available to common shareholders of the Company from Continuing Operations in the third quarter of 2019 were \$331 million (\$0.90 per common share). When compared to the third quarter of 2018, this represented an increase of \$357 million (\$0.97 per common share). The increase included the unfavourable impact of spin-out related incremental depreciation of approximately \$21 million (\$0.06 per common share) and the unfavourable impact of the implementation of IFRS 16 of approximately \$2 million (nil per common share). When normalized for these impacts, net earnings available to common shareholders of the Company from Continuing Operations increased by \$380 million (\$1.03 per common share). This increase included an improvement in underlying operating performance of \$15 million and the favourable change in adjusting items totaling \$365 million, as described below:

- the improvement in underlying operating performance of \$15 million (\$0.03 per common share) was primarily due to the following:
  - an improvement in underlying operating performance in the Retail segment (excluding the impact of the consolidation of franchises), driven by an increase in adjusted gross profit<sup>(2)</sup>, partially offset by an increase in selling, general and administrative expenses ("SG&A") and an increase in depreciation and amortization.
- the favourable change in adjusting items totaling \$365 million (\$0.96 per common share) was primarily due to the following:
  - the favourable impact of the prior year charge related to Glenhuron Bank Limited ("Glenhuron") of \$367 million (\$0.98 per common share); and
  - the favourable impact of the reversal of certain tax reserves following the completion of a tax audit that included a review of the Shoppers Drug Mart Corporation acquisition costs incurred in 2014 of \$8 million (\$0.02 per common share);
 partially offset by,
  - the year-over-year unfavourable impact of restructuring and other related costs of \$11 million (\$0.03 per common share).
- diluted net earnings per common share from Continuing Operations also included the favourable impact of the repurchase of common shares (\$0.04 per common share).

Adjusted net earnings available to common shareholders of the Company<sup>(2)</sup> from Continuing Operations in the third quarter of 2019 were \$458 million. When compared to the third quarter of 2018, this represented a decrease of \$8 million. When normalized for the year-over-year impact of spin-out related incremental depreciation and the implementation of IFRS 16, adjusted net earnings available to common shareholders of the Company<sup>(2)</sup> increased by \$15 million. Adjusted net earnings per common share<sup>(2)</sup> were \$1.25. When compared to the third quarter of 2018, this represented an increase of \$0.01, or 0.8%. When normalized for the impact of spin-out related incremental depreciation, adjusted diluted net earnings per common share<sup>(2)</sup> was \$1.31. This represented an increase of approximately 5.6% or \$0.07 per common share. The increase included the favourable impact of the repurchase of common shares. IFRS 16 had a nominal impact on net earnings per share in the third quarter of 2019.

Year-to-date net earnings available to common shareholders of the Company from Continuing Operations were \$815 million (\$2.20 per common share). When compared to the same period in 2018, this represented an increase of \$336 million (\$0.94 per common share). The increase included the unfavourable impact of spin-out related incremental depreciation of approximately \$52 million (\$0.14 per common share) and the unfavourable impact of the implementation of IFRS 16 of approximately \$8 million (\$0.02 per common share). When normalized for these impacts, net earnings available to common shareholders of the Company from Continuing Operations increased by \$396 million (\$1.10 per common share). This increase included the improvement in underlying operating performance of \$30 million and the favourable change in adjusting items totaling \$366 million, as described below:

- the improvement in underlying operating performance of \$30 million (\$0.07 per common share) was primarily due to the following:
  - an improvement in the underlying operating performance in the Retail segment (excluding the impact of the consolidation of franchises). This was driven by an increase in adjusted gross profit<sup>(2)</sup> which was partially offset by an increase in SG&A and an increase in depreciation and amortization;
 partially offset by,
  - the Financial Services segment, primarily due to an increase in loyalty program costs driven by the growth in the credit card portfolio and higher operating costs including investments in digital strategy.
- the favourable change in adjusting items totaling \$366 million (\$0.94 per common share) was primarily due to the following:
  - the favourable impact of the prior year charge related to Glenhuron of \$367 million (\$0.97 per common share);
  - the favourable impact of the prior year inventory provision related to healthcare reform of \$14 million (\$0.04 per common share); and
  - the favourable impact associated with a prior period regulatory matter of \$11 million (\$0.03 per common share);
 partially offset by,
  - the year-over-year unfavourable impact of restructuring and other related costs of \$27 million (\$0.07 per common share).

- diluted net earnings per common share from Continuing Operations also included the favourable impact of the repurchase of common shares (\$0.09 per common share).

Year-to-date adjusted net earnings available to common shareholders of the Company<sup>(2)</sup> from Continuing Operations were \$1,121 million. When compared to the same period in 2018, this represented a decrease of \$30 million. When normalized for the year-over-year impact of spin-out related incremental depreciation and the implementation of IFRS 16, adjusted net earnings available to common shareholders of the Company<sup>(2)</sup> increased by approximately \$30 million.

Year-to-date adjusted net earnings per common share<sup>(2)</sup> from Continuing Operations were \$3.03, flat compared to the same period in 2018. When normalized for the year-over-year impact of spin-out related incremental depreciation and the implementation of IFRS 16, adjusted diluted net earnings per common share<sup>(2)</sup> were \$3.19, an increase of approximately 5.3% or \$0.16 per common share. The increase included the favourable impact of the repurchase of common shares.

**Discontinued Operations** Net earnings available to common shareholders of the Company from Discontinued Operations were nil in the third quarter of 2019. When compared to the third quarter of 2018, this represented a decrease of \$132 million (\$0.35 per common share). Year-to-date net earnings available to common shareholders of the Company from Discontinued Operations were nil in 2019. When compared to the same period in 2018, this represented a decrease of \$54 million (\$0.14 per common share).

## Revenue

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019				2018 <sup>(4)</sup>			
	(16 weeks)	(16 weeks)	\$ Change	% Change	(40 weeks)	(40 weeks)	\$ Change	% Change
Retail	\$ 14,420	\$ 14,105	\$ 315	2.2 %	\$ 35,778	\$ 34,860	\$ 918	2.6 %
Financial Services	309	274	35	12.8 %	859	746	113	15.1 %
Consolidation and Eliminations	(74)	(60)	(14)	(23.3)%	(190)	(131)	(59)	(45.0)%
Revenue from Continuing Operations	\$ 14,655	\$ 14,319	\$ 336	2.3 %	\$ 36,447	\$ 35,475	\$ 972	2.7 %

In the third quarter of 2019, revenue was \$14,655 million. When compared to the third quarter of 2018, this represented an increase of \$336 million, or 2.3%. The increase was primarily due to an increase in the Retail segment sales of \$315 million. After excluding the consolidation of franchises, Retail segment sales increased by \$226 million, or 1.6%, due to positive same-store sales growth and a net increase in Retail square footage. The increase was also due to an improvement in Financial Services segment sales of \$35 million which was driven by higher interest and interchange income and higher sales attributable to *The Mobile Shop*.

In 2019, year-to-date revenue was \$36,447 million. When compared to the same period in 2018, this represented an increase of \$972 million, or 2.7%. The increase was primarily due to an improvement in Retail segment sales of \$918 million. After excluding the consolidation of franchises, Retail segment sales increased by \$682 million, or 2.0%, due to positive same-store sales growth and a net increase in Retail square footage. The increase was also due to an improvement in Financial Services segment sales of \$113 million which was driven by higher interest and interchange income and higher sales attributable to *The Mobile Shop*.

**Operating Income** Operating income was \$690 million in the third quarter of 2019. When compared to the third quarter of 2018, this represented an increase of \$98 million. The increase included the favourable impact of IFRS 16 of approximately \$104 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$28 million. When normalized for these impacts, operating income increased by \$22 million, or 3.7%, due to improvements in underlying operating performance of \$36 million, and was partially offset by the unfavourable change in adjusting items totaling \$14 million, as described below:

- the improvement in underlying operating performance of \$36 million was primarily due to the Retail segment, including the favourable contribution from the consolidation of franchises of \$15 million, partially offset by the decline in underlying operating performance of the Financial Services segment;
- the unfavourable change in adjusting items totaling \$14 million which was primarily due to the following:
  - the year-over-year unfavourable impact of restructuring and other related costs of \$15 million; and
  - the unfavourable impact of a prior year adjustment related to the Loblaw Card Program of \$4 million;
partially offset by,
  - the favourable impact of the prior year transaction and other related costs in connection with the spin-out of Choice Properties of \$6 million.

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Year-to-date operating income was \$1,729 million. When compared to the same period in 2018, this represented an increase of \$251 million. The increase included the favourable impact of IFRS 16 of approximately \$261 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$70 million. When normalized for these impacts, operating income increased by \$60 million, or 4.1%, due to improvements in underlying operating performance of \$80 million, and was partially offset by the unfavourable change in adjusting items totaling \$20 million, as described below:

- the improvement in underlying operating performance of \$80 million was primarily due to the Retail segment, including the favourable contribution from the consolidation of franchises of \$36 million, partially offset by the decline in underlying operating performance of the Financial Services segment;
- the unfavourable change in adjusting items totaling \$20 million which was primarily due to the following:
  - the year-over-year unfavourable impact of restructuring and other related costs of \$36 million; and
  - the unfavourable impact of income earned in the prior year from the wind-down of *PC Financial* banking services of \$20 million; partially offset by,
  - the favourable impact of reversing a prior year inventory provision related to healthcare reform of \$19 million; and
  - the favourable impact associated with a prior period regulatory matter of \$15 million.

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

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019				2018 <sup>(4)</sup>			
	(16 weeks)	(16 weeks)	\$ Change	% Change	(40 weeks)	(40 weeks)	\$ Change	% Change
Retail	\$ 1,452	\$ 1,017	\$ 435	42.8 %	\$ 3,565	\$ 2,477	\$ 1,088	43.9 %
Financial Services	40	43	(3)	(7.0)%	142	156	(14)	(9.0)%
Adjusted EBITDA <sup>(2)</sup>	\$ 1,492	\$ 1,060	\$ 432	40.8 %	\$ 3,707	\$ 2,633	\$ 1,074	40.8 %

In the third quarter of 2019, adjusted EBITDA<sup>(2)</sup> was \$1,492 million. When compared to the third quarter of 2018, this represented an increase of \$432 million. The increase included the year-over-year favourable impact of IFRS 16 of approximately \$382 million. When normalized for the impact of IFRS 16, adjusted EBITDA<sup>(2)</sup> in the third quarter of 2019 increased by \$50 million, or 4.7%. The increase in adjusted EBITDA<sup>(2)</sup> of \$50 million was primarily due to improvements in the Retail segment, partially offset by the Financial Services segment.

In 2019, year-to-date adjusted EBITDA<sup>(2)</sup> was \$3,707 million. When compared to the same period in 2018, this represented an increase of \$1,074 million. The increase included the year-over-year favourable impact of IFRS 16 of approximately \$954 million. When normalized for the impact of IFRS 16, adjusted EBITDA<sup>(2)</sup> increased by \$120 million, or 4.6%. The year-to-date increase in adjusted EBITDA<sup>(2)</sup> was primarily due to improvements in the Retail segment, partially offset by the Financial Services segment.

**Depreciation and Amortization** In the third quarter of 2019, depreciation and amortization was \$775 million. When compared to the third quarter of 2018, this represented an increase of \$316 million. The increase included the unfavourable impact of IFRS 16 of approximately \$278 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$28 million. When normalized for these impacts, the increase in depreciation and amortization was \$10 million, or 2.2%, primarily driven by the consolidation of franchises and an increase in IT assets.

Year-to-date depreciation and amortization was \$1,935 million. When compared to the same period of 2018, this represented an increase of \$794 million. The increase included the unfavourable impact of IFRS 16 of approximately \$693 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$70 million. When normalized for these impacts, the increase in depreciation and amortization was \$31 million, or 2.7%, primarily driven by the consolidation of franchises and an increase in IT assets.

Depreciation and amortization both for the third quarter of 2019 and year-to-date period included the amortization of intangible assets related to the acquisition of Shoppers Drug Mart Corporation ("Shoppers Drug Mart") of \$157 million (2018 – \$161 million) and \$392 million (2018 – \$401 million), respectively.

**Net Interest Expense and Other Financing Charges** In the third quarter of 2019, net interest expense and other financing charges were \$223 million. When compared to the third quarter of 2018, this represented a decrease of \$69 million. The decrease included the unfavourable impact of IFRS 16 of approximately \$106 million. When normalized for this impact, the decrease in net interest expense and other financing charges was \$175 million, or 59.9%, primarily driven by the prior year interest charge related to Glenhuron of \$176 million.

Year-to-date net interest expense and other financing charges were \$571 million. When compared to the same period in 2018, this represented an increase of \$102 million. The year-to-date increase included the unfavourable impact of IFRS 16 of approximately \$270 million. When normalized for this impact, the decrease in net interest expense and other financing charges was \$168 million, or 35.8%, primarily driven by the prior year interest charge related to Glenhuron of \$176 million, partially offset by higher interest expense in the Financial Services segment.

### Income Taxes

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019				2018 <sup>(4)</sup>			
	(16 weeks)	(16 weeks)	\$ Change	% Change	(40 weeks)	(40 weeks)	\$ Change	% Change
Income taxes	\$ 114	\$ 315	\$ (201)	(63.8)%	\$ 293	\$ 506	\$ (213)	(42.1)%
Add (deduct) impact of the following:								
Tax impact of items included in adjusted earnings before taxes	49	45	4	8.9 %	117	110	7	6.4 %
Reserve release related to 2014 tax audit	8	—	8	100.0 %	8	—	8	100.0 %
Statutory corporate income tax rate change	—	—	—	— %	4	—	4	100.0 %
Charge related to Glenhuron	—	(191)	191	100.0 %	—	(191)	191	100.0 %
Adjusted income taxes <sup>(2)</sup>	\$ 171	\$ 169	\$ 2	1.2 %	\$ 422	\$ 425	\$ (3)	(0.7)%
Effective tax rate	24.4%	105.0%			25.3%	50.1%		
Adjusted income tax rate <sup>(2)</sup>	26.3%	26.2%			26.5%	26.6%		

Income tax expense in the third quarter of 2019 was \$114 million (2018 – \$315 million) and the effective income tax rate was 24.4% (2018 – 105.0%). Year-to-date income tax expense was \$293 million (2018 – \$506 million) and the effective income tax rate was 25.3% (2018 – 50.1%). The decrease in the income tax expense and effective tax rate was primarily attributable to a charge of \$191 million in the third quarter of 2018 related to Glenhuron, the reversal of certain tax reserves following the completion of a tax audit that included a review of the Shoppers Drug Mart acquisition costs incurred in 2014, as well as the impact of other non-deductible items.

Adjusted income tax expense<sup>(2)</sup> in the third quarter of 2019 was \$171 million (2018 – \$169 million) and the adjusted income tax rate<sup>(2)</sup> was 26.3% (2018 – 26.2%). The increases were primarily attributable to an increase in certain non-deductible items. Year-to-date adjusted income tax expense<sup>(2)</sup> was \$422 million (2018 – \$425 million) and the adjusted income tax rate<sup>(2)</sup> was 26.5% (2018 – 26.6%). The decreases were primarily attributable to a decrease in certain non-deductible items.

**Other Business Matters**

**IFRS 16 Implementation** In 2016, the International Accounting Standards Board ("IASB") issued IFRS 16, replacing IAS 17 and related interpretations. The standard introduced a single, on-balance sheet recognition and measurement model for lessees, eliminating the distinction between operating and finance leases. The Company implemented the standard on December 30, 2018 using the modified retrospective approach. As a result, the Company's 2019 results incorporate lease accounting under IFRS 16. Prior year results have not been restated. See Section 10, "Accounting Standards", of this MD&A for more information on the implementation of IFRS 16.

The implementation of IFRS 16 significantly increased the assets and liabilities on the Company's Condensed Consolidated Balance Sheet and changed the timing and presentation of lease-related expenses in the Company's Retail segment results. The Company recorded a right-of-use asset of \$7.6 billion and a lease liability of \$9.2 billion under the new standard. Under IFRS 16, the depreciation expense on right-of-use assets and interest expense on lease liabilities replaced rent expense, which was previously recognized on a straight-line basis in operating income under IAS 17 over the term of a lease.

The following table provides the year-over-year impacts of the implementation of IFRS 16 on the consolidated results of the Company in the third quarter of 2019:

(millions of Canadian dollars unless where otherwise indicated)

Favourable/(unfavourable)

	\$ Change	
	(16 weeks)	(40 weeks)
Operating income	\$ 104	\$ 261
Adjusted EBITDA <sup>(2)</sup>	382	954
Net interest expense and other financing charges	(106)	(270)
Depreciation and amortization	(278)	(693)
Net earnings available to common shareholders of the Company	(2)	(8)
Diluted net earnings per common share (\$)	\$ —	\$ (0.02)

**Spin-out of Choice Properties** On November 1, 2018, the Company and its parent Weston completed a reorganization under which the Company distributed its approximate 61.6% effective interest in Choice Properties to Weston on a tax-free basis to the Company and its Canadian shareholders. The Company no longer retains its interest in Choice Properties and ceased to consolidate its equity interest in Choice Properties in its consolidated financial statements as at October 31, 2018. The reorganization is reflected separately as Discontinued Operations in the current and comparative results. Unless otherwise noted, all comparisons of operating results exclude the results of Choice Properties.

**Impact on Retail Segment Results** As a result of the spin-out, buildings owned by Choice Properties and leased by the Company are accounted for as leases and no longer accounted for as owned property. The building components associated with these leases post spin-out are classified as leasehold improvements and depreciated over the lesser of the lease term and useful life up to 25 years. The remaining average lease term on the leases related to these leasehold improvements is approximately 10 years. The impact of this change in 2019 is expected to be an increase in annual depreciation and amortization of approximately \$85 million compared to 2018. The Company's 2019 third quarter financial results included incremental depreciation and amortization of \$28 million (\$0.06 per common share) and \$70 million (\$0.14 per common share) year-to-date.

**Process and Efficiency** The Company continues to execute on a multi-year plan, initiated in 2018, that focuses on improving processes and generating efficiencies across administrative, store, and distribution network infrastructure. Many initiatives are underway to reduce the complexity and cost of business operations, ensuring a low cost operating structure that allows for continued investments in the Company's strategic growth areas. Management anticipates investing capital as well as recording restructuring and other charges related to these initiatives in 2019 and beyond. In the third quarter of 2019, the Company recorded approximately \$22 million of restructuring and other related charges, primarily related to Process and Efficiency initiatives (\$50 million year-to-date).

#### 4. Reportable Operating Segments Results of Operations

The Company has two reportable operating segments, with all material operations carried out in Canada:

- The Retail segment consists primarily of corporate and franchise-owned retail food and Associate-owned drug stores. The Retail segment also includes in-store pharmacies and other health and beauty products, apparel and other general merchandise and supports the *PC Optimum* Program. This segment is comprised of several operating segments that are aggregated primarily due to similarities in the nature of products and services offered for sale in the retail operations and the customer base; and
- The Financial Services segment provides credit card services, the *PC Optimum* Program, insurance brokerage services, deposit taking services and telecommunication services. As a result of the wind-down of *PC Financial* personal banking services, the Financial Services segment no longer offers personal banking services.

##### 4.1 Retail Segment

Unless otherwise indicated, the following financial information represents the Retail segment's results from Continuing Operations and includes the impacts of spin-out related incremental depreciation, the implementation of IFRS 16 and the consolidation of franchises.

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019				2018 <sup>(4)</sup>			
	(16 weeks)	(16 weeks)	\$ Change	% Change	(40 weeks)	(40 weeks)	\$ Change	% Change
Sales	\$ 14,420	\$ 14,105	\$ 315	2.2%	\$ 35,778	\$ 34,860	\$ 918	2.6%
Operating income	655	551	104	18.9%	1,602	1,309	293	22.4%
Adjusted gross profit <sup>(2)</sup>	4,262	4,108	154	3.7%	10,622	10,231	391	3.8%
Adjusted gross profit % <sup>(2)</sup>	29.6%	29.1%			29.7%	29.3%		
Adjusted EBITDA <sup>(2)</sup>	\$ 1,452	\$ 1,017	\$ 435	42.8%	\$ 3,565	\$ 2,477	\$ 1,088	43.9%
Adjusted EBITDA margin <sup>(2)</sup>	10.1%	7.2%			10.0%	7.1%		
Depreciation and amortization	\$ 771	\$ 457	\$ 314	68.7%	\$ 1,921	\$ 1,134	\$ 787	69.4%

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019		2018		2019		2018	
	(16 weeks)	(16 weeks)	(16 weeks)	(16 weeks)	(40 weeks)	(40 weeks)	(40 weeks)	(40 weeks)
	Sales	Same-store sales						
Food retail	\$ 10,423	0.1%	\$ 10,272	0.9%	\$ 25,796	0.8%	\$ 25,219	1.1%
Drug retail	3,997	4.1%	3,833	2.5%	9,982	3.5%	9,641	2.6%
Pharmacy	1,929	5.3%	1,828	0.5%	4,790	3.9%	4,604	1.3%
Front store	2,068	3.1%	2,005	4.3%	5,192	3.2%	5,037	3.8%

**Sales** In the third quarter of 2019, retail segment sales were \$14,420 million. When compared to the third quarter of 2018, this represented an increase of \$315 million, or 2.2%. After excluding the consolidation of franchises, Retail segment sales increased by \$226 million, or 1.6%, primarily driven by the following factors:

- Food retail same-store sales growth was 0.1% (2018 – 0.9%) for the quarter. After excluding the unfavourable impact of the timing of Thanksgiving, Food retail same-store sales growth was approximately 1.0%.
  - Sales growth in food was modest;
  - Sales growth in pharmacy was modest;
  - The Company's Food retail average quarterly internal food price index was moderately lower than (2018 – was marginally lower than) the average quarterly national food price inflation of 4.1% (2018 – inflation of 0.3%), as measured by The Consumer Price Index for Food Purchased from Stores ("CPI"). CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in the Company's stores; and
  - Food retail basket size increased and traffic decreased in the quarter.
- Drug retail same-store sales growth was 4.1% (2018 – 2.5%). The timing of Thanksgiving had a nominal impact on the Drug retail same-store sales growth in the third quarter of 2019.
  - Pharmacy same-store sales growth was 5.3% (2018 – 0.5%). The number of prescriptions dispensed increased by 3.1% (2018 – 3.3%). On a same-store basis, the number of prescriptions dispensed increased by 2.9% (2018 – 3.2%) and the average prescription value increased by 1.6% (2018 – decreased by 3.0%).
  - Front store same-store sales growth was 3.1% (2018 – 4.3%).

In the last 12 months, 20 food and drug stores were opened, and 9 food and drug stores were closed, resulting in a net increase in Retail square footage of 0.4 million square feet, or 0.6%.

Year-to-date retail sales were \$35,778 million. When compared to the same period in 2018, this represented an increase of \$918 million, or 2.6%. After excluding the consolidation of franchises, Retail segment sales increased by \$682 million, or 2.0%. Year-to-date Food retail sales of \$25,796 million were higher by \$577 million, or 2.3%. The increase was primarily due to positive year-to-date same-store sales growth of 0.8% (2018 – 1.1%) After excluding the unfavourable impact of the timing of Thanksgiving, Food retail year-to-date same-store sales growth was approximately 1.2% in 2019. Drug retail sales were \$9,982 million. When compared to the same period in 2018, this represented an increase of \$341 million, or 3.5%. Year-to-date Drug retail same-store sales growth was 3.5% (2018 – 2.6%). Pharmacy same-store sales growth was 3.9% (2018 – 1.3%), which included the negative impact of incremental healthcare reform. Front store same-store sales growth was 3.2% (2018 – 3.8%). The timing of Thanksgiving had a nominal impact on the Drug retail year-to-date same-store sales growth in 2019.

The redemption of Loblaw Cards resulted in the delivery of approximately \$1 million of free products to customers in the third quarter of 2019 and \$4 million year-to-date, which was provided for in the fourth quarter of 2017. The redemptions did not benefit sales or the Company's financial performance and Management does not believe it had a significant impact on Food retail same-store sales.

**Operating Income** In the third quarter of 2019, operating income was \$655 million. When compared to the third quarter of 2018, this represented an increase of \$104 million. The increase included the favourable impact of IFRS 16 of approximately \$104 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$28 million. When normalized for these impacts, operating income increased by \$28 million, or 5.1%. This was driven by improvements in underlying operating performance of \$41 million, and was partially offset by the unfavourable change in adjusting items totaling \$13 million as described below:

- the improvements in underlying operating performance of \$41 million were driven by an increase in adjusted gross profit<sup>(2)</sup>, partially offset by an increase in SG&A and an increase in depreciation and amortization. The improvements in underlying operating performance included the favourable year-over-year contribution from consolidation of franchises of \$15 million;
- partially offset by,
- the unfavourable change in adjusting items totaling \$13 million which was primarily due to the following:
    - the year-over-year unfavourable impact of restructuring and other related costs of \$14 million; and
    - the change in fair value adjustment on fuel and foreign currency contracts of \$3 million;
- partially offset by,
- the favourable impact of the prior year transaction and other related costs in connection with the spin-out of Choice Properties of \$6 million.

Year-to-date operating income was \$1,602 million. When compared to the same period in 2018, this represented an increase of \$293 million. The increase included the favourable impact of IFRS 16 of approximately \$261 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$70 million. When normalized for these impacts, operating income increased by \$102 million, or 7.8%, driven by improvements in underlying operating performance of \$101 million and the favourable change in adjusting items totaling \$1 million, as described below:

- the improvements in underlying operating performance of \$101 million, was driven by an increase in adjusted gross profit<sup>(2)</sup>, partially offset by an increase in SG&A and an increase in depreciation and amortization. The improvements in underlying operating performance included the favourable contribution from the consolidation of franchises of \$36 million; and
- the favourable change in adjusting items totaling \$1 million, primarily due to the following:
  - the favourable impact of the prior year inventory provision related to healthcare reform of \$19 million;
  - the favourable impact associated with a prior period regulatory matter of \$15 million; and
  - the favourable impact of the prior year transaction and other related costs in connection with the spin-out of Choice Properties of \$6 million;partially offset by,
  - the year-over-year unfavourable impact of restructuring and other related costs of \$35 million.

**Adjusted Gross Profit<sup>(2)</sup>** Adjusted gross profit<sup>(2)</sup> in the third quarter of 2019 was \$4,262 million. When compared to the third quarter of 2018, this represented an increase of \$154 million. Adjusted gross profit percentage<sup>(2)</sup> of 29.6% increased by 50 basis points compared to the third quarter of 2018. Adjusted gross profit percentage<sup>(2)</sup>, excluding the consolidation of franchises, was 27.4%, flat compared to the third quarter of 2018. Margins were negatively impacted by Drug retail, while Food retail margins were stable.

Year-to-date adjusted gross profit<sup>(2)</sup> was \$10,622 million. When compared to the same period of 2018, this represented an increase of \$391 million. Adjusted gross profit percentage<sup>(2)</sup> of 29.7% increased by 40 basis points compared to 2018. Excluding the consolidation of franchises, adjusted gross profit<sup>(2)</sup> increased by \$155 million. Adjusted gross profit percentage<sup>(2)</sup>, excluding the consolidation of franchises, was 27.6%, a decrease of 10 basis points compared to the same period of 2018. Margins were negatively impacted by Drug retail, while Food retail margins were stable.

**Adjusted EBITDA<sup>(2)</sup>** In the third quarter of 2019, adjusted EBITDA<sup>(2)</sup> was \$1,452 million. When compared to the third quarter of 2018, this represented an increase of \$435 million. The increase included the year-over-year favourable impact of IFRS 16 of approximately \$382 million and the favourable impact of the consolidation of franchises of \$20 million. When normalized for the impact of IFRS 16, adjusted EBITDA<sup>(2)</sup> increased by \$53 million, or 5.2%. This was driven by an increase in adjusted gross profit<sup>(2)</sup> described above, partially offset by an increase in SG&A of \$100 million. When normalized for the impact of IFRS 16 and the consolidation of franchises, SG&A increased \$33 million, and SG&A as a percentage of sales, was 20.1%, an improvement of 10 basis points compared to the third quarter of 2018. The improvement was primarily driven by Process and Efficiency initiatives.

Year-to-date adjusted EBITDA<sup>(2)</sup> was \$3,565 million. When compared to the same period of 2018, this represented an increase of \$1,088 million. The increase included the year-over-year favourable impact of IFRS 16 of approximately \$954 million and the favourable impact of the consolidation of franchises of \$50 million. When normalized for the impact of IFRS 16, adjusted EBITDA<sup>(2)</sup> increased by \$134 million, or 5.4%, driven by an increase in adjusted gross profit<sup>(2)</sup> described above, partially offset by an increase in SG&A of \$257 million. Normalized for the impact of IFRS 16 and the consolidation of franchises, SG&A increased \$71 million, and SG&A as a percentage of sales, was 20.4%, an improvement of 20 basis points compared to 2018. The improvement was primarily driven by Process and Efficiency initiatives.

In the third quarter of 2019, adjusted EBITDA<sup>(2)</sup> included gains of \$2 million (2018 – loss of \$2 million) and \$7 million year-to-date (2018 – loss of \$2 million) related to the sale and leaseback of properties to Choice Properties.

**Depreciation and Amortization** In the third quarter of 2019, depreciation and amortization was \$771 million. When compared to the third quarter of 2018, this represented an increase of \$314 million. The increase included the unfavourable impact of IFRS 16 of approximately \$278 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$28 million. When normalized for these impacts, the increase in depreciation and amortization was \$8 million, or 1.8%, primarily driven by the consolidation of franchises and an increase in IT assets.

Year-to-date depreciation and amortization was \$1,921 million. When compared to the same period of 2018, this represented an increase of \$787 million. The increase included the unfavourable impact of IFRS 16 of approximately \$693 million and the unfavourable impact of spin-out related incremental depreciation of approximately \$70 million. When normalized for these impacts, the increase in depreciation and amortization was \$24 million, or 2.1%, primarily driven by the consolidation of franchises and an increase in IT assets.

Depreciation and amortization in the third quarter of 2019 and year-to-date included the amortization of intangibles assets related to the acquisition of Shoppers Drug Mart of \$157 million (2018 – \$161 million) and \$392 million (2018 – \$401 million), respectively.

### Other Retail Business Matters

**Consolidation of Franchises** The Company has more than 500 franchise food retail stores in its network. As at the end of the third quarter of 2019, 444 of these stores were consolidated for accounting purposes under a simplified franchise agreement ("Franchise Agreement") implemented in 2015.

The Company will convert franchises to the Franchise Agreement as existing agreements expire, at the end of which all franchises will be consolidated. The following table provides the total impact of the consolidation of franchises included in the consolidated results of the Company.

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars unless where otherwise indicated)	2019 (16 weeks)	2018 (16 weeks)	2019 (40 weeks)	2018 (40 weeks)
Number of consolidated franchise stores, beginning of period	424	352	400	310
Add: Net number of consolidated franchise stores in the period	20	27	44	69
Number of consolidated franchise stores, end of period	444	379	444	379
Sales	\$ 420	\$ 331	\$ 1,020	\$ 784
Adjusted gross profit <sup>(2)</sup>	429	341	1,022	786
Adjusted EBITDA <sup>(2)</sup>	45	25	107	57
Depreciation and amortization	24	19	58	44
Operating income	21	6	49	13
Net income attributable to non-controlling interests	19	8	41	15

Operating income that is included in the table above does not significantly impact net earnings available to common shareholders of the Company as the related income is largely attributable to non-controlling interests.

The Company expects that the estimated annual impact in 2019 of new and current consolidated franchises will be revenue of approximately \$1,345 million, adjusted EBITDA<sup>(2)</sup> of approximately \$135 million, depreciation and amortization of approximately \$80 million and net earnings attributable to non-controlling interests of approximately \$45 million.

### 4.2 Financial Services Segment

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019 (16 weeks)	2018 (16 weeks)	\$ Change	% Change	2019 (40 weeks)	2018 (40 weeks)	\$ Change	% Change
Revenue	\$ 309	\$ 274	\$ 35	12.8 %	\$ 859	\$ 746	\$ 113	15.1 %
Earnings before income taxes	15	22	(7)	(31.8)%	67	119	(52)	(43.7)%

(millions of Canadian dollars except where otherwise indicated)	<b>As at October 5, 2019</b>	As at October 6, 2018 <sup>(4)</sup>	\$ Change	% Change
Average quarterly net credit card receivables	<b>\$ 3,217</b>	\$ 2,973	\$ 244	8.2%
Credit card receivables	<b>3,263</b>	3,023	240	7.9%
Allowance for credit card receivables	<b>188</b>	163	25	15.3%
Annualized yield on average quarterly gross credit card receivables	<b>13.7%</b>	13.2%		
Annualized credit loss rate on average quarterly gross credit card receivables	<b>3.4%</b>	3.2%		

**Revenue** In the third quarter of 2019, revenue was \$309 million. When compared to the third quarter of 2018, this represented an increase of \$35 million. Year-to-date revenue was \$859 million. When compared to the same period in 2018, this represented an increase of \$113 million. The increase was primarily driven by:

- higher interest and interchange income attributable to the growth in the credit card portfolio; and
- higher sales attributable to *The Mobile Shop*.

**Earnings before income taxes** In the third quarter of 2019, earnings before income taxes were \$15 million. When compared to the third quarter of 2018, this represented a decrease of \$7 million, primarily driven by:

- higher operating costs including investments in digital strategy;
- higher interest expense and credit losses driven by the growth in the credit card portfolio;
- an increase in loyalty program costs driven by the growth in credit card portfolio;

partially offset by,

- revenue growth, as described above.

Year-to-date earnings before income taxes were \$67 million. When compared to the same period in 2018, this represented a decrease of \$52 million. The decrease in year-to-date earnings before income taxes in the third quarter of 2019 was primarily driven by:

- an increase in loyalty program costs driven by the growth in credit card portfolio;
- higher operating costs including investments in digital strategy;
- higher interest expense and credit losses driven by the growth in the credit card portfolio; and
- prior year recognition of income of \$20 million, net of certain costs incurred, relating to President's Choice Bank's agreement to end its business relationship with a major Canadian chartered bank, which represented the personal banking services offered under the *PC Financial* brand;

partially offset by,

- revenue growth, as described above; and
- lower customer acquisition costs.

**Credit Card Receivables** As at October 5, 2019, credit card receivables were \$3,263 million. When compared to October 6, 2018, this represented an increase of \$240 million. This increase was primarily driven by growth in the average customer balance and active customer base as a result of continued investments in customer acquisition, marketing and product initiatives. For the same reasons, the allowance for credit card receivables increased to \$188 million, an increase of \$25 million compared to October 6, 2018.

#### **Other Financial Services Business Matters**

**Wind-down of PC Financial personal banking services** In the third quarter of 2017, President's Choice Bank ("PC Bank") entered into an agreement to end its business relationship with a major Canadian chartered bank, which represented the personal banking services offered under the *PC Financial* brand. As a result of this agreement, PC Bank received a payment of approximately \$44 million, net of certain costs incurred, \$20 million of which was recognized in the first half of 2018 and \$24 million which was recognized in 2017.

## 5. Liquidity and Capital Resources

The Company's interest in Choice Properties has been presented separately as Discontinued Operations in the Company's current and comparative results. Unless otherwise indicated, all financial information represents the Company's results from Continuing Operations.

### 5.1 Cash Flows

The following Major Cash Flow Components are presented on a Total Company basis, inclusive of Continuing and Discontinued Operations.

#### Major Cash Flow Components

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019				2018 <sup>(4)</sup>			
	(16 weeks)	(16 weeks)	\$ Change	% Change	(40 weeks)	(40 weeks)	\$ Change	% Change
Cash and cash equivalents, beginning of period	\$ 1,151	\$ 1,187	\$ (36)	(3.0)%	\$ 1,065	\$ 1,798	\$ (733)	(40.8)%
Cash flows from (used in):								
Operating activities	\$ 1,061	\$ 1,162	\$ (101)	(8.7)%	\$ 2,972	\$ 2,187	\$ 785	35.9 %
Investing activities	(423)	(536)	113	21.1 %	49	(2,500)	2,549	102.0 %
Financing activities	(846)	(501)	(345)	(68.9)%	(3,144)	(169)	(2,975)	(1,760.4)%
Effect of foreign currency exchange rate changes on cash and cash equivalents	1	2	(1)	(50.0)%	2	(2)	4	200.0 %
Change in cash and cash equivalents	\$ (207)	\$ 127	\$ (334)	(263.0)%	\$ (121)	\$ (484)	\$ 363	75.0 %
Cash and cash equivalents, end of period	\$ 944	\$ 1,314	\$ (370)	(28.2)%	\$ 944	\$ 1,314	\$ (370)	(28.2)%

**Cash Flows from Operating Activities** Cash flows from operating activities were \$1,061 million in the third quarter of 2019, a decrease of \$101 million compared to the third quarter of 2018. The decrease in cash flows from operating activities included a favourable impact attributable to the implementation of IFRS 16 with an offsetting impact in cash flows used in financing activities. Normalized for the impact of IFRS 16, the decrease in cash flows from operating activities was primarily due to lower cash earnings, an unfavourable change in non-cash working capital and an increase in income taxes paid.

Year-to-date cash flows from operating activities were \$2,972 million in 2019, an increase of \$785 million compared to the same period in 2018. The increase in cash flows from operating activities included a favourable impact attributable to the implementation of IFRS 16 with an offsetting impact in cash flows used in financing activities. Normalized for the impact of IFRS 16, the decrease in cash flows from operating activities was primarily due to lower cash earnings, partially offset by favourable changes in non-cash working capital and provisions.

**Cash Flows from (used in) Investing Activities** Cash flows used in investing activities were \$423 million in the third quarter of 2019, a decrease of \$113 million compared to the third quarter of 2018. The decrease in cash flows used in investing activities was primarily due to a favourable change in security deposits, partially offset by an unfavourable change in short term investments.

Year-to-date cash flows from investing activities were \$49 million in 2019, an increase of \$2,549 million compared to the same period in 2018. The increase in cash flows from investing activities was primarily due to prior year's cash used in the acquisition of Canadian Real Estate Investment Trust ("CREIT") and the repayment of the Company's \$1,200 million debentures, which were classified as security deposits, partially offset by an unfavourable change in short term investments.

## Capital Investments and Store Activity

As at or for the periods ended October 5, 2019 and October 6, 2018	<b>2019</b> <b>(40 weeks)</b>	2018 (40 weeks)	% Change
Capital investments from Continuing Operations (millions of Canadian dollars)	<b>\$ 780</b>	\$ 656	18.9 %
Corporate square footage (in millions)	<b>35.6</b>	35.5	0.3 %
Franchise square footage (in millions)	<b>16.4</b>	16.2	1.2 %
Associate-owned drug store square footage (in millions)	<b>18.6</b>	18.5	0.5 %
Total retail square footage (in millions)	<b>70.6</b>	70.2	0.6 %
Number of corporate stores	<b>548</b>	550	(0.4)%
Number of franchise stores	<b>539</b>	532	1.3 %
Number of Associate-owned drug stores	<b>1,341</b>	1,335	0.4 %
Total number of stores	<b>2,428</b>	2,417	0.5 %
Percentage of corporate real estate owned	<b>8%</b>	72%	
Percentage of franchise real estate owned	<b>4%</b>	49%	
Percentage of Associate-owned drug store real estate owned	<b>1%</b>	1%	
Average store size (square feet)			
Corporate	<b>65,000</b>	64,500	0.8 %
Franchise	<b>30,400</b>	30,500	(0.3)%
Associate-owned drug store	<b>13,900</b>	13,900	— %

**Cash Flows used in Financing Activities** Cash flows used in financing activities were \$846 million in the third quarter of 2019, an increase of \$345 million compared to the third quarter of 2018. Normalized for the impact of IFRS 16, the decrease in cash flows used in financing activities was due to higher net issuances of long term debt, partially offset by higher repurchases of common shares.

Year-to-date cash flows used in financing activities were \$3,144 million in 2019, an increase of \$2,975 million compared to the same period in 2018. Normalized for the impact of IFRS 16, the increase in cash flows used in financing activities was due to prior year's higher net issuances of debt, partially offset by lower interest paid and lower repurchases of common shares.

The Company's significant long term debt transactions are set out in Section "5.3 Components of Total Debt".

## Management's Discussion and Analysis

**Free Cash Flow<sup>(2)</sup>** The definition of free cash flow<sup>(2)</sup> was changed in the first quarter of 2019 to normalize for the impact of the implementation of IFRS 16. Lease payments were deducted from the calculation, which resulted in no IFRS 16 impact on the metric.

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019		2018 <sup>(4)</sup>		2019		2018 <sup>(4)</sup>	
	(16 weeks)	(16 weeks)	\$ Change	% Change	(40 weeks)	(40 weeks)	\$ Change	% Change
Cash flows from operating activities	\$ 1,061	\$ 1,162	\$ (101)	(8.7)%	\$ 2,972	\$ 2,187	\$ 785	35.9 %
Less: Cash flows from operating activities from Discontinued Operations <sup>(i)</sup>	—	112	(112)	(100.0)%	—	248	(248)	(100.0)%
Cash flows from operating activities from Continuing Operations <sup>(i)</sup>	\$ 1,061	\$ 1,050	\$ 11	1.0 %	\$ 2,972	\$ 1,939	\$ 1,033	53.3 %
Less:								
Capital investments	397	300	97	32.3 %	780	656	124	18.9 %
Interest paid	104	303	(199)	(65.7)%	275	451	(176)	(39.0)%
Lease payments, net <sup>(ii)</sup>	374	—	374	100.0 %	979	—	979	100.0 %
Free cash flow <sup>(2)</sup> from Continuing Operations	\$ 186	\$ 447	\$ (261)	(58.4)%	\$ 938	\$ 832	\$ 106	12.7 %

(i) Cash flows from operating activities from Continuing Operations include distributions received in 2018 and the payment related to the conversion of Class C LP Units in 2018 from Discontinued Operations. Cash flows from Discontinued Operations include the outflow of these items.

(ii) Includes cash rent paid on lease liabilities, net of lease payments received from finance leases.

Free cash flow<sup>(2)</sup> from Continuing Operations was \$186 million in the third quarter of 2019, a decrease of \$261 million compared to the third quarter of 2018. The decrease in free cash flow<sup>(2)</sup> was primarily due to an unfavourable change in non-cash working capital, an increase in income taxes paid and higher capital investments, partially offset by higher cash earnings and a decrease in interest paid.

Year-to-date free cash flow<sup>(2)</sup> was \$938 million in 2019, an increase of \$106 million compared to the same period in 2018. The increase in free cash flow<sup>(2)</sup> was primarily due to a decrease in interest paid, higher cash earnings and a favourable change in provisions, partially offset by higher capital investments and an increase in income taxes paid.

### 5.2 Liquidity and Capital Structure

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

PC Bank expects to obtain long term financing for its credit card portfolio through the issuance of *Eagle Credit Card Trust*<sup>®</sup> ("Eagle") notes and Guaranteed Investment Certificates.

The Company manages its capital structure on a segmented basis to ensure that each of the reportable operating segments is employing a capital structure that is appropriate for the industry in which it operates. The following table presents total debt from Continuing Operations, as monitored by management, by reportable operating segment:

(millions of Canadian dollars)	As at October 5, 2019			As at October 6, 2018			As at December 29, 2018		
	Retail	Financial Services	Total	Retail	Financial Services	Total	Retail	Financial Services	Total
Bank indebtedness	\$ 152	\$ —	\$ 152	\$ 266	\$ —	\$ 266	\$ 56	\$ —	\$ 56
Short term debt	—	550	550	—	690	690	—	915	915
Long term debt due within one year	350	644	994	1,386	609	1,995	1,373	274	1,647
Long term debt <sup>(i)</sup>	4,422	1,683	6,105	3,960	1,522	5,482	4,762	1,617	6,379
Certain other liabilities	56	—	56	48	—	48	48	—	48
Total debt excluding lease liabilities	\$ 4,980	\$ 2,877	\$ 7,857	\$ 5,660	\$ 2,821	\$ 8,481	\$ 6,239	\$ 2,806	\$ 9,045
Lease liabilities due within one year	\$ 1,306	\$ —	\$ 1,306	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Lease liabilities	7,706	—	7,706	—	—	—	—	—	—
Total debt including total lease liabilities	\$ 13,992	\$ 2,877	\$ 16,869	\$ 5,660	\$ 2,821	\$ 8,481	\$ 6,239	\$ 2,806	\$ 9,045

(i) Finance lease obligations of \$546 million and \$535 million were included in long term debt as at October 6, 2018 and December 29, 2018, respectively, prior to the implementation of IFRS 16.

**Retail** The Company manages its capital structure with the objective of maintaining Retail segment credit metrics consistent with those of investment grade retailers. The Company monitors the Retail segment's debt to rolling year retail adjusted EBITDA<sup>(2)</sup> ratio as a measure of the leverage being employed.

	As at October 5, 2019 <sup>(i)</sup>	As at October 6, 2018 <sup>(4)</sup>	As at December 29, 2018
Retail debt to rolling year retail adjusted EBITDA <sup>(2)</sup>	3.0x	1.7x	1.9x

(i) Includes the annualized impact of IFRS 16. Rolling year retail adjusted EBITDA<sup>(2)</sup> is expected to be approximately \$1.2 billion higher on an annualized basis due to the change in presentation of the Company's rent expense.

The Retail debt to rolling year retail adjusted EBITDA<sup>(2)</sup> ratio as at October 5, 2019 increased compared to October 6, 2018 and December 29, 2018 primarily due to an increase in Retail debt driven by the increase in lease liabilities as a result of the implementation of IFRS 16. This increase was partially offset by the improvement in adjusted EBITDA<sup>(2)</sup> also as a result of the implementation of IFRS 16.

**President's Choice Bank** PC Bank's capital management objectives are to maintain a consistently strong capital position while considering the economic risks generated by its credit card receivables portfolio and to meet all regulatory requirements as defined by the Office of the Superintendent of Financial Institutions ("OSFI").

**Covenants and Regulatory Requirements** The Company is required to comply with certain financial covenants for various debt instruments. As at October 5, 2019 and throughout the third quarter, the Company was in compliance with such covenants. As at October 5, 2019 and throughout the third quarter, PC Bank has met all applicable regulatory requirements.

### 5.3 Components of Total Debt

**Debentures** There were no debentures repaid in the third quarter of 2019. On a year-to-date basis in 2019, the Company redeemed, at par, \$800 million of 3.75% debentures with an original maturity date of March 12, 2019.

During the third quarter of 2018, the Company repaid two unsecured term loan facilities totaling \$298 million bearing variable interest rates. On a year-to-date basis in 2018, the Company also repaid the \$275 million Shoppers Drug Mart Notes at maturity. The notes bore an interest rate of 2.36%.

**Committed Credit Facilities** The Company has a \$1.0 billion committed credit facility with a maturity date of June 10, 2021. This committed credit facility contains certain financial covenants. As at October 5, 2019, there were no amounts drawn (October 6, 2018 and December 29, 2018 – nil) under this facility.

**Independent Securitization Trusts** The Company, through PC Bank, participates in various securitization programs that provide a source of funds for the operation of its credit card business. PC Bank maintains and monitors a co-ownership interest in credit card receivables with independent securitization trusts, including *Eagle* and Other Independent Securitization Trusts, in accordance with its financing requirements.

The following table summarizes the amounts securitized to independent securitization trusts:

(millions of Canadian dollars)	As at October 5, 2019	As at October 6, 2018	As at December 29, 2018
Securitized to independent securitization trusts:			
Securitized to <i>Eagle Credit Card Trust</i> <sup>®</sup>	\$ 1,000	\$ 1,150	\$ 750
Securitized to other independent securitization trusts	550	690	915
<b>Total securitized to independent securitization trusts</b>	<b>\$ 1,550</b>	<b>\$ 1,840</b>	<b>\$ 1,665</b>

Under its securitization programs, PC Bank is required to maintain, at all times, a credit card receivable pool balance equal to a minimum of 107% of the outstanding securitized liability. PC Bank was in compliance with this requirement as at October 5, 2019 and throughout the third quarter of 2019.

During the third quarter of 2019, *Eagle* issued \$250 million of senior and subordinated term notes with a maturity date of July 17, 2024 at a weighted average interest rate of 2.28%. In connection with this issuance, \$250 million of bond forward agreements were settled, resulting in a realized fair value loss of \$8 million before income taxes recorded in other comprehensive loss and a net effective interest rate of 2.94% on the *Eagle* note issued.

During the third quarter of 2018, *Eagle* issued \$250 million of senior and subordinated term notes with a maturity date of July 17, 2023 at a weighted average interest rate of 3.10%. In connection with this issuance, \$250 million of bond forward agreements were settled, resulting in a realized fair value loss of \$1 million before income taxes recorded in other comprehensive income and a net effective interest rate of 3.15% on the *Eagle* notes issued.

**Independent Funding Trusts** As at October 5, 2019, the independent funding trust had drawn \$501 million (October 6, 2018 – \$545 million; December 29, 2018 – \$536 million) from the revolving committed credit facility that is the source of funding to the independent funding trusts. The Company provides credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trusts. As at October 5, 2019, the Company provided a credit enhancement of \$64 million (October 6, 2018 and December 29, 2018 – \$64 million) for the benefit of the independent funding trusts representing not less than 10% (2018 – not less than 10%) of the principal amount of loans outstanding.

During the second quarter of 2019, the Company renewed the revolving committed credit facility relating to the independent funding trusts until May 27, 2022.

#### 5.4 Financial Condition

##### Rolling Year Adjusted Return on Equity<sup>(2)</sup> and Rolling Year Adjusted Return on Capital<sup>(2)</sup>

	As at October 5, 2019 <sup>(ii)</sup>	As at October 6, 2018 <sup>(4)</sup>	As at December 29, 2018
Rolling year adjusted return on equity <sup>(2)</sup>	13.4%	12.3%	12.6%
Rolling year adjusted return on capital <sup>(2)(i)</sup>	7.8%	9.6%	9.8%

(i) Includes the annualized impact of IFRS 16. Tax-effected adjusted operating income<sup>(2)</sup> is expected to be approximately \$0.2 billion higher on an annualized basis due to the change in presentation of the Company's rent expense.

(ii) Opening equity and opening capital include the implementation impacts of IFRS 16 when calculating the average of equity and average of capital, respectively.

Rolling year adjusted return on equity<sup>(2)</sup> as at October 5, 2019 increased compared to October 6, 2018 and December 29, 2018 primarily due to the decrease in retained earnings as a result of the implementation of IFRS 16 and common share repurchases.

Rolling year adjusted return on capital<sup>(2)</sup> as at October 5, 2019 decreased compared to October 6, 2018 and December 29, 2018 primarily due to an increase in total debt driven by the increase in lease liabilities as a result of the implementation of IFRS 16. The increase in debt was partially offset by the improvement in tax-effected adjusted operating income<sup>(2)</sup> also as a result of IFRS 16.

## 5.5 Credit Ratings

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

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

In the third quarter of 2019, Standard and Poor's reaffirmed the credit ratings and outlook of the Company. Subsequent to the third quarter of 2019, Dominion Bond Rating Service reaffirmed the credit ratings of the Company and changed the trend from Stable to Positive.

## 5.6 Share Capital

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

(millions of Canadian dollars except where otherwise indicated)	October 5, 2019 (16 weeks)		October 6, 2018 (16 weeks)		October 5, 2019 (40 weeks)		October 6, 2018 (40 weeks)	
	Number of Common Shares	Common Share Capital	Number of Common Shares	Common Share Capital	Number of Common Shares	Common Share Capital	Number of Common Shares	Common Share Capital
Issued and outstanding, beginning of period	366,100,437	\$ 7,163	374,582,150	\$ 7,260	371,790,967	\$ 7,177	386,293,941	\$ 7,460
Issued for settlement of stock options	519,984	28	666,171	34	1,836,381	91	1,621,089	80
Purchased and cancelled	(4,313,300)	(84)	—	—	(11,320,227)	(161)	(12,666,709)	(246)
Issued and outstanding, end of period	362,307,121	\$ 7,107	375,248,321	\$ 7,294	362,307,121	\$ 7,107	375,248,321	\$ 7,294
Shares held in trust, beginning of period	(555,455)	\$ (10)	(271,777)	\$ (5)	(734,727)	\$ (15)	(780,938)	\$ (15)
Purchased for future settlement of RSUs and PSUs	—	—	—	—	(300,000)	(5)	—	—
Released for settlement of RSUs and PSUs	23,798	—	33,726	—	503,070	10	542,887	10
Shares held in trust, end of period	(531,657)	\$ (10)	(238,051)	\$ (5)	(531,657)	\$ (10)	(238,051)	\$ (5)
Issued and outstanding, net of shares held in trust, end of period	361,775,464	\$ 7,097	375,010,270	\$ 7,289	361,775,464	\$ 7,097	375,010,270	\$ 7,289
Weighted average outstanding, net of shares held in trust	364,201,921		374,608,772		366,718,947		377,587,465	

**Dividends** The following table summarizes the Company's cash dividends declared for the periods as indicated:

	October 5, 2019 <sup>(i)</sup> (16 weeks)	October 6, 2018 (16 weeks)	October 5, 2019 (40 weeks)	October 6, 2018 (40 weeks)
Dividends declared per share (\$):				
Common Share	\$ 0.315	\$ 0.295	\$ 0.925	\$ 0.860
Second Preferred Share, Series B	\$ 0.33125	\$ 0.33125	\$ 0.99375	\$ 0.99375

(i) The third quarter dividends for 2019 of \$0.315 per share declared on common shares had a payment date of October 1, 2019. The third quarter dividends for 2019 of \$0.33125 per share declared on Second Preferred Shares, Series B had a payment date of September 30, 2019.

(millions of Canadian dollars)	October 5, 2019 (16 weeks)	October 6, 2018 (16 weeks)	October 5, 2019 (40 weeks)	October 6, 2018 (40 weeks)
Dividends declared:				
Common Share	\$ 117	\$ 109	\$ 341	\$ 322
Second Preferred Share, Series B	3	3	9	9
Total dividends declared	\$ 120	\$ 112	\$ 350	\$ 331

Subsequent to the end of third quarter of 2019, the Company's Board of Directors declared a quarterly dividend of \$0.315 per common share, payable on December 30, 2019 to shareholders of record on December 15, 2019 and a quarterly dividend of \$0.33125 per share on the Second Preferred Shares, Series B, payable on December 31, 2019 to shareholders of record on December 15, 2019. At the time such dividends are declared, the Company identifies on its website, [loblaw.ca](http://loblaw.ca), the designation of eligible and ineligible dividends in accordance with the administrative position of the Canada Revenue Agency.

**Normal Course Issuer Bid** Activity under the Company's Normal Course Issuer Bid ("NCIB") during the periods was as follows:

(millions of Canadian dollars except where otherwise indicated)	October 5, 2019 (16 weeks)	October 6, 2018 (16 weeks)	October 5, 2019 (40 weeks)	October 6, 2018 (40 weeks)
Common shares repurchased under the NCIB for cancellation (number of shares)	4,313,300	—	11,320,227	12,666,709
Cash consideration paid <sup>(i)</sup>	\$ 309	\$ —	\$ 774	\$ 844
Premium charged to retained earnings	225	—	428	598
Reduction in common share capital	84	—	161	246
Common shares repurchased under the NCIB and held in trust (number of shares)	—	—	300,000	—
Cash consideration paid	\$ —	\$ —	\$ 20	\$ —
Premium charged to retained earnings	—	—	15	—
Reduction in common share capital	—	—	5	—

(i) Includes \$185 million paid for common shares related to the automatic share purchase plan, as described below.

In the first quarter of 2019, the Company completed an automatic share purchase plan ("ASPP") that was initiated in the fourth quarter of 2018 to facilitate the repurchase of the Company's common shares under its NCIB. Under the ASPP, the Company's broker purchased 2,927,733 common shares for approximately \$185 million.

In the second quarter of 2019, the Company renewed its NCIB to purchase on the Toronto Stock Exchange ("TSX") or through alternative trading systems up to 18,455,884 of the Company's common shares, representing approximately 5% of issued and outstanding common shares. In accordance with the rules of the TSX, the Company may purchase its common shares from time to time at the then market price of such shares. As of October 5, 2019, the Company had purchased 7,924,470 common shares under its current NCIB for cancellation.

## 5.7 Off-Balance Sheet Arrangements

The Company uses off-balance sheet arrangements including letters of credit, guarantees and cash collateralization in connection with certain obligations. There were no significant changes to these off-balance sheet arrangements during the third quarter of 2019. For a discussion of the Company's significant off-balance sheet arrangements see Section 7.7 "Off-Balance Sheet Arrangements" of the Company's 2018 Annual Report.

## 6. Financial Derivative Instruments

The Company uses derivative instruments to offset certain of its financial risks. The Company uses bond forwards and interest rate swaps, to manage its anticipated exposure to fluctuations in interest rates on future debt issuances. The Company did not enter into any significant bond forwards or interest rate swaps in the third quarter of 2019.

The Company also uses futures, options and forward contracts to manage its anticipated exposure to fluctuations in commodity prices and exchange rates in its underlying operations. For further details on the impact of these instruments during the third quarter of 2019 see Section 12 "Non-GAAP Financial Measures" of the MD&A.

## 7. Results by Quarter

The Company follows a 52-week reporting cycle which periodically necessitates a fiscal year of 53 weeks due to an accounting convention. Fiscal years 2018 and 2017 were 52 weeks. The next 53 week year will occur in 2020. The 52-week reporting cycle is divided into four quarters of 12 weeks each except for the third quarter, which is 16 weeks in duration.

The Company's interest in Choice Properties is presented separately as Discontinued Operations in the Company's current and comparative results. Unless otherwise indicated, all financial information reflects the Company's results from Continuing Operations and includes the impacts of spin-out related incremental depreciation, the implementation of IFRS 16 and the consolidation of franchises.

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

	Third Quarter		Second Quarter		First Quarter		Fourth Quarter	
	2019 (16 weeks)	2018 <sup>(4)</sup> (16 weeks)	2019 (12 weeks)	2018 <sup>(4)</sup> (12 weeks)	2019 (12 weeks)	2018 <sup>(4)</sup> (12 weeks)	2018 <sup>(4)</sup> (12 weeks)	2017 <sup>(4)</sup> (12 weeks)
(millions of Canadian dollars except where otherwise indicated)								
<b>Revenue</b>	<b>\$ 14,655</b>	<b>\$ 14,319</b>	\$ 11,133	\$ 10,821	\$ 10,659	\$ 10,335	\$ 11,218	\$ 10,992
<b>Adjusted EBITDA<sup>(2)</sup></b>	<b>1,492</b>	<b>1,060</b>	1,175	840	1,040	733	895	882
<b>Net earnings (loss) available to common shareholders of the Company</b>	<b>331</b>	<b>106</b>	286	50	198	377	221	31
Continuing Operations	331	(26)	286	293	198	212	228	(24)
Discontinued Operations	—	132	—	(243)	—	165	(7)	55
Adjusted net earnings available to common shareholders of the Company <sup>(2)</sup>	<b>\$ 458</b>	<b>\$ 562</b>	\$ 373	\$ 421	\$ 290	\$ 361	\$ 402	\$ 436
Continuing Operations	458	466	373	373	290	312	388	398
Discontinued Operations	—	96	—	48	—	49	14	38
<b>Net earnings (losses) per common share:</b>								
<b>Basic (\$)</b>	<b>\$ 0.91</b>	<b>\$ 0.28</b>	\$ 0.78	\$ 0.13	\$ 0.54	\$ 0.99	\$ 0.59	\$ 0.08
Continuing Operations	\$ 0.91	\$ (0.07)	\$ 0.78	\$ 0.77	\$ 0.54	\$ 0.55	\$ 0.61	\$ (0.06)
Discontinued Operations	\$ —	\$ 0.35	\$ —	\$ (0.64)	\$ —	\$ 0.44	\$ (0.02)	\$ 0.14
<b>Diluted (\$)</b>	<b>\$ 0.90</b>	<b>\$ 0.28</b>	\$ 0.77	\$ 0.13	\$ 0.53	\$ 0.98	\$ 0.59	\$ 0.08
Continuing Operations	\$ 0.90	\$ (0.07)	\$ 0.77	\$ 0.77	\$ 0.53	\$ 0.55	\$ 0.61	\$ (0.06)
Discontinued Operations	\$ —	\$ 0.35	\$ —	\$ (0.64)	\$ —	\$ 0.43	\$ (0.02)	\$ 0.14
Adjusted diluted net earnings per common share <sup>(2)</sup> (\$)	<b>\$ 1.25</b>	<b>\$ 1.49</b>	\$ 1.01	\$ 1.11	\$ 0.78	\$ 0.94	\$ 1.07	\$ 1.12
Continuing Operations	\$ 1.25	\$ 1.24	\$ 1.01	\$ 0.98	\$ 0.78	\$ 0.81	\$ 1.03	\$ 1.02
Discontinued Operations	\$ —	\$ 0.25	\$ —	\$ 0.13	\$ —	\$ 0.13	\$ 0.04	\$ 0.10
Average national food price inflation (as measured by CPI)	<b>4.1%</b>	<b>0.3%</b>	3.6%	0.1%	3.3%	1.2%	1.7%	1.0%
Food retail same-store sales growth	<b>0.1%</b>	<b>0.9%</b>	0.6%	0.8%	2.0%	1.9%	0.8%	0.5%
Drug retail same-store sales growth	<b>4.1%</b>	<b>2.5%</b>	4.0%	1.7%	2.2%	3.7%	1.9%	3.6%

**Revenue** Revenue for the last eight quarters was impacted by various factors including the following:

- seasonality, which was greatest in the fourth quarter and least in the first quarter;
- the timing of holidays;
- macro-economic conditions impacting food and drug retail prices;
- consolidation of franchises; and
- changes in net retail square footage. Over the past eight quarters, net retail square footage increased by 0.4 million square feet to 70.6 million square feet.

**Net Earnings Available to Common Shareholders of the Company from Continuing Operations and Diluted Net Earnings Per Common Share from Continuing Operations** Net earnings available to common shareholders of the Company from continuing operations and diluted net earnings per common share from continuing operations for the last eight quarters were impacted by the following items:

- seasonality, which was greatest in the fourth quarter and least in the first quarter;
- the timing of holidays;
- minimum wage increases and incremental healthcare reform;
- cost savings and operating efficiencies from Process and Efficiency initiatives and benefits from strategic initiatives;
- changes in the underlying operating performance of the Company;
- the favourable impact of the repurchase of common shares for cancellation; and
- the impact of certain adjusting items, as set out in Section 12 "Non-GAAP Financial Measures", including:
  - the charge related to Glenhuron;
  - the *PC Optimum* Program;
  - the Loblaw Card Program;
  - restructuring and other related charges;
  - the wind-down of *PC Financial* personal banking services;
  - the impact of healthcare reform on inventory balances;
  - the remeasurement of deferred tax balances;
  - asset impairments, net of recoveries;
  - the gain or loss on sale of non-operating properties; and
  - certain prior period items.

The consolidation of franchises does not significantly impact net earnings available to common shareholders of the Company as the related earnings are largely attributable to non-controlling interests.

## 8. Internal Control over Financial Reporting

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

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

In designing such controls, it should be recognized that due to inherent limitations, any control, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and may not prevent or detect misstatements. Additionally, management is required to use judgment in evaluating controls and procedures.

**Changes in Internal Control over Financial Reporting** There were no changes in the Company's internal control over financial reporting in the third quarter of 2019 that materially affected or are reasonably likely to materially affect the Company's internal control over financial reporting.

## 9. Enterprise Risks and Risk Management

A detailed full set of risks inherent in the Company's business are included in the Company's AIF for the year ended December 29, 2018 and the Company's MD&A in the Company's 2018 Annual Report, which are hereby incorporated by reference. The Company's 2018 Annual Report and AIF are available online on [www.sedar.com](http://www.sedar.com). Those risks and risk management strategies remain unchanged.

## 10. Accounting Standards

### Accounting Standard Implemented in 2019

**IFRS 16** In 2016, the IASB issued IFRS 16, replacing IAS 17 and related interpretations. The standard introduces a single, on-balance sheet recognition and measurement model for lessees, eliminating the distinction between operating and finance leases. Lessees recognize a right-of-use asset representing its control of and right to use the underlying asset and a lease liability representing its obligation to make future lease payments. Lessor accounting remains similar to IAS 17.

IFRS 16 became effective for annual periods beginning on or after January 1, 2019. For leases where the Company is the lessee, it had the option of adopting a fully retrospective approach or a modified retrospective approach on transition to IFRS 16. The Company adopted the standard on December 30, 2018 using the modified retrospective approach. The Company applied the requirements of the standard retrospectively with the cumulative effects of initial application recorded in opening retained earnings as at December 30, 2018, and no restatement of the comparative period. Under the modified retrospective approach, the Company chose to measure all right-of-use assets retrospectively as if the standard had been applied since lease commencement dates.

Substantially all of the Company's operating leases are real estate leases for retail stores, distribution centers and corporate offices. Other leased assets include passenger vehicles, trucks and IT equipment. The Company recognized right-of-use assets and lease liabilities for its operating leases except for certain classes of underlying assets in which the lease terms are 12 months or less. The depreciation expense on right-of-use assets and interest expense on lease liabilities replaced rent expense, which was previously recognized on a straight-line basis under IAS 17 over the term of a lease. There are no significant impacts to the Company's existing finance leases under IAS 17 as a lessee.

The Company also has owned and leased properties which are leased and subleased to third parties, respectively. The subleases are mainly related to non-consolidated franchisees, ancillary tenants and gas bar land. As an intermediate lessor, the Company reassessed the classification of its subleases by reference to the right-of-use assets arising from the head lease and recognized a corresponding finance lease receivable when the reassessment concluded that the subleases were finance leases.

IFRS 16 permits the use of recognition exemptions and practical expedients. The Company applied the following recognition exemptions and practical expedients:

- grandfathered the definition of leases for existing contracts at the date of initial application;
- excluded certain short-term leases from IFRS 16 lease accounting;
- used portfolio application for leases with similar characteristics, such as vehicle and equipment leases;
- applied a single discount rate to a portfolio of leases with reasonably similar characteristics at the date of initial application;
- excluded initial direct costs from the measurement of right-of-use assets at the date of initial application; and
- used hindsight in determining lease term at the date of initial application.

The Company did not exercise the practical expedient wherein a lessee may rely on its assessment of whether leases are onerous applying IAS 37, "Provisions, Contingent Liabilities and Contingent Assets" immediately before the date of initial application as an alternative to performing an impairment review. On the date of initial application, the Company applied the requirements of IAS 36, "Impairment of Assets" and recorded an impairment of \$94 million on right-of-use assets in opening retained earnings, which represents an incremental \$46 million to the previous onerous lease provision.

## Management's Discussion and Analysis

The impact of adopting IFRS 16 on the Company's balance sheet as at December 30, 2018 was as follows:

Condensed Consolidated Balance Sheet (millions of Canadian Dollars) / Increase (Decrease)	As at December 30, 2018
<b>Current assets</b>	
Prepaid expenses and other assets	\$ (104)
<b>Total current assets</b>	\$ (104)
<b>Fixed assets<sup>(i)</sup></b>	<b>(435)</b>
Right-of-use assets <sup>(i)</sup>	7,602
Intangible assets	(82)
Deferred income tax assets	34
Other assets	128
<b>Total assets</b>	<b>\$ 7,143</b>
<b>Current liabilities</b>	
Trade payables and other liabilities	\$ (11)
Provisions	(4)
Long term debt due within one year <sup>(i)</sup>	(37)
Lease liabilities due within one year <sup>(i)(ii)</sup>	1,192
<b>Total current liabilities</b>	<b>\$ 1,140</b>
Provisions	(51)
Long term debt <sup>(i)</sup>	(498)
Lease liabilities <sup>(i)(ii)</sup>	7,985
Deferred income tax liabilities	(256)
Other liabilities	(379)
Retained earnings	(798)
<b>Total liabilities and equity</b>	<b>\$ 7,143</b>

(i) Leases previously classified as finance lease arrangements under IAS 17 were presented within fixed assets, long term debt due within one year and long term debt. Effective December 30, 2018, these balances are included in right-of-use assets and lease liabilities.

(ii) Leases that are short-term or where the lease payments are variable and do not depend on an index or rate are not included in the calculation of lease liabilities. These lease expenses are recognized in selling, general and administrative expenses on the most systematic basis.

The Company used its incremental borrowing rates as at December 30, 2018 to measure lease liabilities. The weighted average incremental borrowing rate was 4.36%. The weighted average lease term remaining as at December 30, 2018 was approximately 10 years.

The following reconciliation is between lease liabilities recognized on December 30, 2018 and operating lease commitments disclosed under IAS 17 as at December 29, 2018 discounted using the weighted average incremental borrowing rate as at the date of initial application:

(millions of Canadian Dollars)	As at December 30, 2018
Operating lease commitment as at December 29, 2018 as disclosed in the Company's notes to the consolidated financial statements	\$ 9,987
Discounted using the weighted average incremental borrowing rate as at December 30, 2018	\$ 8,048
Finance lease obligations recognized as at December 29, 2018	535
Extension and termination options reasonably certain to be exercised	594
<b>Lease liabilities recognized as at December 30, 2018</b>	<b>\$ 9,177</b>
Lease liabilities due within one year	\$ 1,192
Lease liabilities	7,985
<b>Total lease liabilities</b>	<b>\$ 9,177</b>

### Critical Accounting Estimates and Judgments for Leases

**Judgments Made in Relation to Accounting Policies Applied** Management exercises judgment in determining the appropriate lease term on a lease by lease basis. Management considers all facts and circumstances that create an economic incentive to exercise a renewal option or to not exercise a termination option including investments in major leaseholds, store performances and past business practice. The periods covered by renewal options are only included in the lease term if management is reasonably certain to renew. Management considers reasonably certain to be a high threshold. Changes in the economic environment or changes in the retail industry may impact management's assessment of lease term, and any changes in management's estimate of lease terms may have a material impact on the Company's balance sheet and statement of earnings.

**Key Sources of Estimation** In determining the carrying amount of right-of-use assets and lease liabilities, the Company is required to estimate the incremental borrowing rate specific to each leased asset or portfolio of leased assets if the interest rate implicit in the lease is not readily determined. Management determines the incremental borrowing rate of each leased asset or portfolio of leased assets by incorporating the Company's creditworthiness, the security, term and value of the underlying leased asset, and the economic environment in which the leased asset operates. The incremental borrowing rates are subject to change mainly due to macroeconomic changes in the environment.

### 11. Outlook<sup>(3)</sup>

Loblaw is focused on its strategic framework, delivering best in food and health and beauty, using data driven insights underpinned by process and efficiency excellence. This framework is supported by the Company's financial plan of maintaining a stable trading environment that targets positive same-store sales and stable gross margin, creating efficiencies to deliver operating leverage, investing for the future and returning capital to shareholders.

The Company will remain focused on delivering Process and Efficiency improvements to offset increasing costs and to fund continued incremental investments in its strategic growth areas of Everyday Digital Retail, Connected Healthcare and Payments & Rewards.

In 2019, on a full-year comparative basis, excluding the impact of the spin-out of Choice Properties, we expect to:

- deliver positive same-store sales and stable gross margin in the Retail segment in a highly competitive market;
- deliver positive adjusted net earnings growth;
- invest approximately \$1.1 billion in capital expenditures, net of proceeds from property disposals; and
- return capital to shareholders by allocating a significant portion of free cash flow to share repurchases.

## 12. Non-GAAP Financial Measures

The Company uses the following non-GAAP financial measures: Retail segment gross profit; Retail segment adjusted gross profit; Retail segment adjusted gross profit percentage; adjusted earnings before income taxes, net interest expense and other financing charges and depreciation and amortization ("adjusted EBITDA"); adjusted EBITDA margin; adjusted operating income; adjusted net interest expense and other financing charges; adjusted income taxes; adjusted income tax rate; adjusted net earnings available to common shareholders; adjusted diluted net earnings per common share, free cash flow; retail debt to rolling year retail adjusted EBITDA; rolling year adjusted return on equity; and rolling year adjusted return on capital. The Company believes these non-GAAP financial measures provide useful information to both management and investors in measuring the financial performance and financial condition of the Company for the reasons outlined below.

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

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

The Company's interest in Choice Properties has been presented separately as Discontinued Operations in the Company's current and comparative results. Unless otherwise indicated, all financial information represents the Company's results from Continuing Operations.

**Retail Segment Gross Profit, Retail Segment Adjusted Gross Profit and Retail Segment Adjusted Gross Profit Percentage** The following tables reconcile adjusted gross profit by segment to gross profit by segment, which is reconciled to revenue and cost of merchandise inventories sold measures as reported in the condensed consolidated statements of earnings for the periods ended as indicated. The Company believes that Retail segment gross profit and Retail segment adjusted gross profit are useful in assessing the Retail segment's underlying operating performance and in making decisions regarding the ongoing operations of the business.

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

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars)	2019 (16 weeks)				2018 <sup>(4)</sup> (16 weeks)			
	Retail	Financial Services	Eliminations	Total	Retail	Financial Services	Eliminations	Total
Revenue	\$ 14,420	\$ 309	\$ (74)	\$ 14,655	\$ 14,105	\$ 274	\$ (60)	\$ 14,319
Cost of merchandise inventories sold	10,158	47	—	10,205	9,997	35	—	10,032
Gross profit	\$ 4,262	\$ 262	\$ (74)	\$ 4,450	\$ 4,108	\$ 239	\$ (60)	\$ 4,287
Adjusted gross profit	\$ 4,262	\$ 262	\$ (74)	\$ 4,450	\$ 4,108	\$ 239	\$ (60)	\$ 4,287

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars)	2019 (40 weeks)				2018 <sup>(4)</sup> (40 weeks)			
	Retail	Financial Services	Eliminations	Total	Retail	Financial Services	Eliminations	Total
Revenue	\$ 35,778	\$ 859	\$ (190)	\$ 36,447	\$ 34,860	\$ 746	\$ (131)	\$ 35,475
Cost of merchandise inventories sold	25,156	117	—	25,273	24,648	83	—	24,731
Gross profit	\$ 10,622	\$ 742	\$ (190)	\$ 11,174	\$ 10,212	\$ 663	\$ (131)	\$ 10,744
Add impact of the following:								
Impact of health care reform on inventory balances	—	—	—	—	19	—	—	19
Adjusted gross profit	\$ 10,622	\$ 742	\$ (190)	\$ 11,174	\$ 10,231	\$ 663	\$ (131)	\$ 10,763

**Impact of healthcare reform on inventory balances** In the first quarter of 2018, the Company recorded an inventory provision for the write-down of inventories below cost to net realizable value, related to its generic drug inventory, as a result of healthcare reform announced in the first quarter of 2018, effective April 1, 2018.

**Adjusted Operating Income, Adjusted EBITDA and Adjusted EBITDA Margin** The following tables reconcile adjusted operating income and adjusted EBITDA to operating income, which is reconciled to net earnings attributable to shareholders of the Company as reported in the condensed consolidated statements of earnings for the periods ended as indicated. The Company believes that adjusted EBITDA is useful in assessing the performance of its ongoing operations and its ability to generate cash flows to fund its cash requirements, including the Company's capital investment program.

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

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars)	2019 (16 weeks)			2018 <sup>(4)</sup> (16 weeks)		
	Retail	Financial Services	Consolidated	Retail	Financial Services	Consolidated
Net earnings (loss) attributable to shareholders of the Company			\$ 334			\$ (23)
Add impact of the following:						
Non-controlling interests			19			8
Net interest expense and other financing charges			223			292
Income taxes			114			315
Operating income	\$ 655	\$ 35	\$ 690	\$ 551	\$ 41	\$ 592
Add (deduct) impact of the following:						
Amortization of intangible assets acquired with Shoppers Drug Mart	\$ 157	\$ —	\$ 157	\$ 161	\$ —	\$ 161
Restructuring and other related costs	21	1	22	7	—	7
Fair value adjustment on fuel and foreign currency contracts	3	—	3	—	—	—
Loss on sale of non-operating properties	2	—	2	—	—	—
Spin-out of Choice Properties	—	—	—	6	—	6
Loblaw Card Program	—	—	—	(4)	—	(4)
Adjusting Items	\$ 183	\$ 1	\$ 184	\$ 170	\$ —	\$ 170
Adjusted operating income	\$ 838	\$ 36	\$ 874	\$ 721	\$ 41	\$ 762
Depreciation and amortization	771	4	775	457	2	459
Less: Amortization of intangible assets acquired with Shoppers Drug Mart	(157)	—	(157)	(161)	—	(161)
Adjusted EBITDA	\$ 1,452	\$ 40	\$ 1,492	\$ 1,017	\$ 43	\$ 1,060

## Management's Discussion and Analysis

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars)	2019 (40 weeks)			2018 <sup>(4)</sup> (40 weeks)		
	Retail	Financial Services	Consolidated	Retail	Financial Services	Consolidated
Net earnings attributable to shareholders of the Company			\$ 824			\$ 488
Add impact of the following:						
Non-controlling interests			41			15
Net interest expense and other financing charges			571			469
Income taxes			293			506
Operating income	\$ 1,602	\$ 127	\$ 1,729	\$ 1,309	\$ 169	\$ 1,478
Add (deduct) impact of the following:						
Amortization of intangible assets acquired with Shoppers Drug Mart	\$ 392	\$ —	\$ 392	\$ 401	\$ —	\$ 401
Restructuring and other related costs	49	1	50	14	—	14
Pension annuities and buy-outs	10	—	10	1	—	1
Fair value adjustment on fuel and foreign currency contracts	5	—	5	(11)	—	(11)
Impact of health care reform on inventory balances	—	—	—	19	—	19
Loblaw Card Program	—	—	—	4	—	4
Wind-down of <i>PC Financial</i> personal banking services	—	—	—	—	(20)	(20)
Spin-out of Choice Properties	—	—	—	6	—	6
Fair value adjustment on investment properties	(3)	—	(3)	1	—	1
Gain on sale of non-operating properties	(4)	—	(4)	—	—	—
Certain prior period items	(15)	—	(15)	—	—	—
Adjusting Items	\$ 434	\$ 1	\$ 435	\$ 435	\$ (20)	\$ 415
Adjusted operating income	\$ 2,036	\$ 128	\$ 2,164	\$ 1,744	\$ 149	\$ 1,893
Depreciation and amortization	1,921	14	1,935	1,134	7	1,141
Less: Amortization of intangible assets acquired with Shoppers Drug Mart	(392)	—	(392)	(401)	—	(401)
Adjusted EBITDA	\$ 3,565	\$ 142	\$ 3,707	\$ 2,477	\$ 156	\$ 2,633

In addition to the items described in the Retail segment adjusted gross profit section above, adjusted EBITDA was impacted by the following:

**Amortization of intangible assets acquired with Shoppers Drug Mart** The acquisition of Shoppers Drug Mart in 2014 included approximately \$6,050 million of definite life intangible assets, which are being amortized over their estimated useful lives. Annual amortization associated with the acquired intangibles will be approximately \$525 million until 2024 and will decrease thereafter.

**Restructuring and other related costs** The Company continuously evaluates strategic and cost reduction initiatives related to its store infrastructure, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. Restructuring activities related to these initiatives are ongoing.

**Fair value adjustment on fuel and foreign currency contracts** The Company is exposed to commodity price and U.S. dollar exchange rate fluctuations. In accordance with the Company's commodity risk management policy, the Company enters into exchange traded futures contracts and forward contracts to minimize cost volatility relating to fuel prices and the U.S. dollar exchange rate. These derivatives are not acquired for trading or speculative purposes. Pursuant to the Company's derivative instruments accounting policy, changes in the fair value of these instruments, which include realized and unrealized gains and losses, are recorded in operating income. Despite the impact of accounting for these commodity and foreign currency derivatives on the Company's reported results, the derivatives have the economic impact of largely mitigating the associated risks arising from price and exchange rate fluctuations in the underlying commodities and U.S. dollar commitments.

**Gain/loss on sale of non-operating properties** In the third quarter of 2019, the Company disposed of vacant land to a third party and recorded a loss of \$2 million related to the sale.

**Spin-out of Choice Properties** In the third quarter of 2018, the Company recorded transaction and other related costs in connection with the spin-out of its interest in Choice Properties.

**Loblaw Card Program** In the fourth quarter of 2017, the Company and Weston acknowledged their involvement in an industry wide price-fixing arrangement involving certain packaged bread products. In connection with the arrangement, the Company offered customers a \$25 Loblaw Card, which can be used to purchase items sold in Loblaw grocery stores across Canada. The Company recorded a charge of \$107 million associated with the Loblaw Card Program in the fourth quarter of 2017. In 2018, the Company recorded total charge of \$4 million year-to-date, of which \$4 million of reversal was recorded in the third quarter of 2018.

**Pension annuities and buy-outs** The Company has and continues to undertake annuity purchases and pension buy-outs in respect of former employees to reduce its defined benefit pension plan obligation and decrease future pension volatility and risks.

**Wind-down of PC Financial personal banking services** In the third quarter of 2017, PC Bank entered into an agreement to end its business relationship with a major Canadian chartered bank, which represented the personal banking services offered under the PC Financial brand. As a result of this agreement, PC Bank received a payment of approximately \$44 million, net of certain costs incurred, \$20 million of which was recognized in the first half of 2018 and \$24 million which was recognized in 2017.

**Fair value adjustment on investment properties** The Company elected to change the measurement of investment properties from cost model to fair value model. Prior to the second quarter of 2018, the Company recognized investment properties at cost less accumulated depreciation and any accumulated impairment losses. Under the fair value model, investment properties are initially measured at cost and subsequently measured at fair value. Fair value is determined based on available market evidence. If market evidence is not readily available in less active markets, the Company uses alternative valuation methods such as discounted cash flow projections or recent transaction prices. Gains and losses on fair value are recognized in operating income in the period in which they are incurred. Gains and losses from disposal of investment properties are determined by comparing the fair value of disposal proceeds and the carrying amount and are recognized in operating income.

**Certain prior period items** In the second quarter of 2019, the Company revised its estimate of the amount owed associated with a prior period regulatory matter.

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

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars)	2019 (16 weeks)	2018 <sup>(4)</sup> (16 weeks)	2019 (40 weeks)	2018 <sup>(4)</sup> (40 weeks)
Net interest expense and other financing charges	\$ 223	\$ 292	\$ 571	\$ 469
Deduct impact of the following:				
Charge related to Glenhuron	—	(176)	—	(176)
Adjusted net interest expense and other financing charges	\$ 223	\$ 116	\$ 571	\$ 293

**Charge related to Glenhuron** In the third quarter of 2018, the Company recorded a charge of \$367 million related to the Tax Court of Canada's decision on Glenhuron. Of the total charge, \$176 million was recorded in net interest and other financing charges and \$191 million was recorded in income taxes.

**Adjusted Income Taxes and Adjusted Income Tax Rate** The following table reconciles adjusted income taxes to income taxes as reported in the condensed consolidated statements of earnings for the periods ended as indicated. The Company believes that adjusted income taxes is useful in assessing the Company's underlying operating performance and in making decisions regarding the ongoing operations of its business.

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

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	2019 (16 weeks)	2018 <sup>(4)</sup> (16 weeks)	2019 (40 weeks)	2018 <sup>(4)</sup> (40 weeks)
Adjusted operating income <sup>(i)</sup>	\$ 874	\$ 762	\$ 2,164	\$ 1,893
Adjusted net interest expense and other financing charges <sup>(i)</sup>	223	116	571	293
Adjusted earnings before taxes	\$ 651	\$ 646	\$ 1,593	\$ 1,600
Income taxes	\$ 114	\$ 315	\$ 293	\$ 506
Add (deduct) impact of the following:				
Tax impact of items included in adjusted earnings before taxes <sup>(ii)</sup>	49	45	117	110
Reserve release related to 2014 tax audit	8	—	8	—
Statutory corporate income tax rate change	—	—	4	—
Charge related to Glenhuron	—	(191)	—	(191)
Adjusted income taxes	\$ 171	\$ 169	\$ 422	\$ 425
Effective tax rate	24.4%	105.0%	25.3%	50.1%
Adjusted income tax rate	26.3%	26.2%	26.5%	26.6%

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

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

**Reserve release related to 2014 tax audit** In the third quarter of 2019, the Company reversed certain tax reserves following the completion of a tax audit that included a review of the Shoppers Drug Mart acquisition costs incurred in 2014.

**Statutory corporate income tax rate change** The Company's deferred income tax assets and liabilities are impacted by changes to provincial statutory corporate income tax rates resulting in a charge or benefit to earnings. The Company implements changes in the statutory corporate income tax rate in the same period the change is substantively enacted by the legislative body.

In the second quarter of 2019, the Government of Alberta substantively enacted a gradual decrease in the provincial statutory corporate income tax rate from 12% to 8% by 2022. The Company recorded income of \$4 million in the second quarter of 2019 and year-to-date related to the remeasurement of its deferred income tax balances.

**Charge related to Glenhuron** In the third quarter of 2018, the Company recorded a charge of \$367 million related to the Tax Court of Canada's decision on Glenhuron. Of the total charge, \$176 million was recorded in net interest and other financing charges and \$191 million was recorded in income taxes.

**Adjusted Net Earnings Available to Common Shareholders and Adjusted Diluted Net Earnings Per Common Share** The following table reconciles adjusted net earnings available to common shareholders of the Company and adjusted net earnings attributable to shareholders of the Company to net earnings attributable to shareholders of the Company and then to net earnings available to common shareholders of the Company for the periods ended as indicated. The Company believes that adjusted net earnings available to common shareholders and adjusted diluted net earnings per common share are useful in assessing the Company's underlying operating performance and in making decisions regarding the ongoing operations of its business.

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars except where otherwise indicated)	<b>2019</b> <b>(16 weeks)</b>	2018 <sup>(4)</sup> (16 weeks)	<b>2019</b> <b>(40 weeks)</b>	2018 <sup>(4)</sup> (40 weeks)
Net earnings attributable to shareholders of the Company	\$ 334	\$ 109	\$ 824	\$ 542
Net earnings from Discontinued Operations	—	(132)	—	(54)
Net earnings (loss) attributable to shareholders of the Company from Continuing Operations	\$ 334	\$ (23)	\$ 824	\$ 488
Prescribed dividends on preferred shares in share capital	(3)	(3)	(9)	(9)
Net earnings (loss) available to common shareholders of the Company from Continuing Operations	\$ 331	\$ (26)	\$ 815	\$ 479
Net earnings (loss) attributable to shareholders of the Company from Continuing Operations	\$ 334	\$ (23)	\$ 824	\$ 488
Adjusting items (refer to the following table)	127	492	306	672
Adjusted net earnings attributable to shareholders of the Company from Continuing Operations	\$ 461	\$ 469	\$ 1,130	\$ 1,160
Prescribed dividends on preferred shares in share capital	(3)	(3)	(9)	(9)
Adjusted net earnings available to common shareholders of the Company from Continuing Operations	\$ 458	\$ 466	\$ 1,121	\$ 1,151
Diluted weighted average common shares outstanding (millions)	366.2	376.3	369.7	380.0

Management's Discussion and Analysis

The following table reconciles adjusted net earnings available to common shareholders of the Company and adjusted diluted net earnings per common share to net earnings available to common shareholders of the Company and diluted net earnings per common share for the periods ended as indicated.

	2019 (16 weeks)		2018 <sup>(4)</sup> (16 weeks)		2019 (40 weeks)		2018 <sup>(4)</sup> (40 weeks)	
	Net Earnings Available to Common Shareholders of the Company	Diluted Net Earnings Per Common Share	Net Earnings (Loss) Available to Common Shareholders of the Company	Diluted Net Earnings (Loss) Per Common Share	Net Earnings Available to Common Shareholders of the Company	Diluted Net Earnings Per Common Share	Net Earnings Available to Common Shareholders of the Company	Diluted Net Earnings Per Common Share
For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars/Canadian dollars)								
<b>Continuing Operations</b>	\$ 331	\$ 0.90	\$ (26)	\$ (0.07)	\$ 815	\$ 2.20	\$ 479	\$ 1.26
<b>Discontinued Operations</b>	—	—	132	0.35	—	—	54	0.14
<b>As reported</b>	\$ 331	\$ 0.90	\$ 106	\$ 0.28	\$ 815	\$ 2.20	\$ 533	\$ 1.40
<b>Continuing Operations</b>	\$ 331	\$ 0.90	\$ (26)	\$ (0.07)	\$ 815	\$ 2.20	\$ 479	\$ 1.26
Add (deduct) impact of the following:								
Amortization of intangible assets acquired with Shoppers Drug Mart	\$ 116	\$ 0.31	\$ 118	\$ 0.31	\$ 287	\$ 0.78	\$ 294	\$ 0.76
Restructuring and other related costs	15	0.04	4	0.01	36	0.10	9	0.03
Fair value adjustment on fuel and foreign currency contracts	2	0.01	—	—	4	0.01	(8)	(0.02)
Loss (gain) on sale of non-operating properties	2	0.01	—	—	(3)	(0.01)	—	—
Pension annuities and buy-outs	—	—	—	—	7	0.02	1	—
Loblaw Card Program	—	—	(3)	(0.01)	—	—	3	0.01
Wind-down of PC Financial personal banking services	—	—	—	—	—	—	(15)	(0.04)
Impact of health care reform on inventory balances	—	—	—	—	—	—	14	0.04
Fair value adjustment on investment properties	—	—	—	—	(2)	(0.01)	1	—
Statutory corporate income tax rate change	—	—	—	—	(4)	(0.01)	—	—
Spin-out of Choice Properties	—	—	6	0.02	—	—	6	0.02
Charge related to Glenhuron	—	—	367	0.98	—	—	367	0.97
Certain prior period items	—	—	—	—	(11)	(0.03)	—	—
Reserve release related to 2014 tax audit	(8)	(0.02)	—	—	(8)	(0.02)	—	—
Adjusting items from Continuing Operations	\$ 127	\$ 0.35	\$ 492	\$ 1.31	\$ 306	\$ 0.83	\$ 672	\$ 1.77
<b>Adjusted Continuing Operations</b>	\$ 458	\$ 1.25	\$ 466	\$ 1.24	\$ 1,121	\$ 3.03	\$ 1,151	\$ 3.03
<b>Discontinued Operations</b>	\$ —	\$ —	\$ 132	\$ 0.35	\$ —	\$ —	\$ 54	\$ 0.14
Add (deduct) impact of the following:								
Fair value adjustment on investment properties	\$ —	\$ —	\$ 29	\$ 0.07	\$ —	\$ —	\$ 36	\$ 0.10
CREIT acquisition and other related costs	—	—	9	0.02	—	—	118	0.31
Restructuring and other related costs	—	—	(1)	—	—	—	(10)	(0.03)
Gain of sale of air rights	—	—	(11)	(0.03)	—	—	(11)	(0.03)
Fair value adjustment on Trust Unit ("Units") liability <sup>(i)</sup>	—	—	(62)	(0.16)	—	—	6	0.02
Adjusting items from Discontinued Operations	\$ —	\$ —	\$ (36)	\$ (0.10)	\$ —	\$ —	\$ 139	\$ 0.37
<b>Adjusted Discontinued Operations</b>	\$ —	\$ —	\$ 96	\$ 0.25	\$ —	\$ —	\$ 193	\$ 0.51
<b>Adjusted Total Company</b>	\$ 458	\$ 1.25	\$ 562	\$ 1.49	\$ 1,121	\$ 3.03	\$ 1,344	\$ 3.54

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

In addition to the items described in the adjusted gross profit<sup>(2)</sup>, and adjusted EBITDA<sup>(2)</sup> and adjusted net interest expense and other financing charges<sup>(2)</sup> section above, discontinued operations adjusted net earnings available to common shareholders of the Company was impacted by the following:

**CREIT acquisition and other related costs** The Company recorded acquisition and other related costs in connection with Choice Properties' acquisition of CREIT in discontinued operations in the first quarter of 2018.

**Gain on sale of air rights** In the third quarter of 2018, a joint venture owned by Choice Properties completed the sale of air rights on one of its properties. The Company recorded a gain in discontinued operations of \$11 million in the third quarter related to the sale.

**Fair value adjustment to the Trust Unit Liability** Prior to the spin-out of Choice Properties, the Company was exposed to market price fluctuations as a result of the Units held by unitholders other than the Company and on the basis the Company consolidated Choice Properties. These Units were presented as a liability on the Company's consolidated balance sheets as they were redeemable for cash at the option of the holder, subject to certain restrictions. The liability was recorded at fair value at each reporting date based on the market price of Units at the end of each period. An increase (decrease) in the market price of Units resulted in a charge (reduction) to net interest expense and other financing charges.

**Free Cash Flow** The following table reconciles free cash flow to cash flows from operating activities as reported in the condensed consolidated statements of cash flows for the periods ended as indicated. The Company believes that free cash flow is the appropriate measure in assessing the Company's cash available for additional financing and investing activities.

The definition of free cash flow<sup>(2)</sup> was changed in the first quarter of 2019 to normalize for the impact of the implementation of IFRS 16. Lease payments were deducted from the calculation, which resulted in no IFRS 16 impact on the metric.

For the periods ended October 5, 2019 and October 6, 2018 (millions of Canadian dollars)	2019 (16 weeks)	2018 <sup>(4)</sup> (16 weeks)	2019 (40 weeks)	2018 <sup>(4)</sup> (40 weeks)
Cash flows from operating activities from Continuing Operations <sup>(i)</sup>	\$ 1,061	\$ 1,050	\$ 2,972	\$ 1,939
Cash flows from operating activities from Discontinued Operations <sup>(i)</sup>	—	112	—	248
<b>Cash flows from operating activities Total Company</b>	<b>\$ 1,061</b>	<b>\$ 1,162</b>	<b>\$ 2,972</b>	<b>\$ 2,187</b>
Cash flows from operating activities from Continuing Operations <sup>(i)</sup>	\$ 1,061	\$ 1,050	\$ 2,972	\$ 1,939
Less:				
Capital investments	397	300	780	656
Interest paid	104	303	275	451
Lease payments, net <sup>(ii)</sup>	374	—	979	—
<b>Free cash flow from Continuing Operations</b>	<b>\$ 186</b>	<b>\$ 447</b>	<b>\$ 938</b>	<b>\$ 832</b>
Cash flows from operating activities from Discontinued Operations <sup>(i)</sup>	\$ —	\$ 112	\$ —	\$ 248
Less:				
Capital investments	—	84	—	196
Interest paid	—	157	—	261
<b>Free cash flow from Discontinued Operations</b>	<b>\$ —</b>	<b>\$ (129)</b>	<b>\$ —</b>	<b>\$ (209)</b>
<b>Free cash flow from Total Company</b>	<b>\$ 186</b>	<b>\$ 318</b>	<b>\$ 938</b>	<b>\$ 623</b>

(i) Cash flows from operating activities from Continuing Operations include distributions received in 2018 and the payment related to the conversion of Class C LP Units in 2018 from Discontinued Operations. Cash flows from Discontinued Operations include the outflow of these items.

(ii) Includes cash rent paid on lease liabilities, net of lease payments received from finance leases.

**Retail Debt to Rolling Year Retail Adjusted EBITDA, Rolling Year Adjusted Return on Equity and Rolling Year Adjusted Return on Capital** The Company uses the following metrics to measure its leverage and profitability. The definitions of these ratios are presented below.

- **Retail Debt to Rolling Year Retail Adjusted EBITDA** Retail segment total debt divided by Retail segment adjusted EBITDA for the last four quarters.
- **Rolling Year Adjusted Return on Equity** Adjusted net earnings available to common shareholders of the Company for the last four quarters divided by average total equity attributable to common shareholders of the Company.
- **Rolling Year Adjusted Return on Capital** Tax-effected adjusted operating income for the last four quarters divided by average capital where capital is defined as total debt, plus equity attributable to shareholders of the Company, less cash and cash equivalents, and short term investments.

### 13. Additional Information

Additional information about the Company has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR) and is available online at [sedar.com](http://sedar.com) and with OSFI as the primary regulator for the Company's subsidiary, PC Bank.

November 12, 2019  
Toronto, Canada

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#### MD&A Endnotes

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- (1) For financial definitions and ratios refer to the Glossary of Terms on page 140 of the Company's 2018 Annual Report.
  - (2) See Section 12 "Non-GAAP Financial Measures", which includes the reconciliation of such non-GAAP measures to the most directly comparable GAAP measures.
  - (3) To be read in conjunction with Section 1 "Forward-Looking Statements".
  - (4) Comparative figures have been restated. See note 4 in the Company's 2019 third quarter unaudited interim period condensed consolidated financial statements. Certain figures have been restated to conform with current year presentation.
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