

## **Management's Discussion and Analysis**

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## Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") for George Weston Limited ("GWL" or the "Company") should be read in conjunction with the Company's second quarter 2018 unaudited interim period condensed consolidated financial statements and the accompanying notes on pages 47 to 83 of this Quarterly Report, the audited annual consolidated financial statements and the accompanying notes for the year ended December 31, 2017 and the related annual MD&A included in the Company's 2017 Annual Report. In addition, the following MD&A should be read in conjunction with the Company's "Forward-Looking Statements" beginning on page 2 of this Quarterly Report.

The Company's second quarter 2018 unaudited interim period condensed consolidated financial statements and the accompanying notes have been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP") as issued by the International Accounting Standards Board ("IASB"). 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, except where otherwise noted.

The Company has two reportable operating segments, Loblaw Companies Limited ("Loblaw") and Weston Foods. The Company also holds cash, short term investments and a direct interest in Choice Properties Real Estate Investment Trust ("Choice Properties") of approximately 3.8% (2017 – 6.0%). Loblaw has three reportable operating segments: Retail, Financial Services and Choice Properties. Loblaw provides Canadians with grocery, pharmacy, health and beauty, apparel, general merchandise, financial services, and wireless mobile products and services. Loblaw also holds approximately 61.7% (2017 – 82.5%) effective interest in Choice Properties, which owns, manages and develops a high quality portfolio of commercial retail, industrial, office and residential properties across Canada. Weston Foods is a leading North American bakery that offers packaged bread and rolls in Canada as well as frozen and artisan bread and rolls, cakes, donuts, pies, biscuits and alternatives throughout Canada and the U.S.

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

A glossary of terms and ratios used throughout this Quarterly Report can be found beginning on page 146 of the Company's 2017 Annual Report.

The information in this MD&A is current to July 30, 2018, unless otherwise noted.

During the second quarter of 2018, Choice Properties completed the acquisition of Canadian Real Estate Investment Trust ("CREIT"), as described in "Loblaw Other Business Matters" under "Loblaw Segment Results" section of this MD&A.

### FORWARD-LOOKING STATEMENTS

This Quarterly Report, including this MD&A, for the Company 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 minimum wage increases and 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 the "Loblaw Segment Results, Loblaw Other Business Matters", "Liquidity and Capital Resources", "Outlook" and "Non-GAAP Financial Measures" sections 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", "maintain", "achieve", "grow", "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 2018 is based on certain assumptions including assumptions about sales and volume growth, anticipated cost savings, operating efficiencies, anticipated benefits from strategic initiatives, anticipated minimum wage increases and healthcare reform impacts. 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 the "Enterprise Risks and Risk Management" section of the Company's 2017 Annual Report and the Company's Annual Information Form ("AIF") for the year ended December 31, 2017. 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;
- failure to effectively manage Loblaw's loyalty program;
- 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 execute Loblaw's e-commerce initiative or to adapt its business model to the shifts in the retail landscape caused by digital advances;
- failure to realize benefits from investments in the Company's new IT systems;
- failure to effectively respond to consumer trends or heightened competition, whether from current competitors or new entrants to the marketplace;
- changes to any of the laws, rules, regulations or policies applicable to the Company's business, including increases to minimum wage;
- public health events including those related to food and drug safety;
- failure to realize the anticipated benefits, including revenue growth, anticipated cost savings or operating efficiencies, associated with the Company's investment in major initiatives that support its strategic priorities, including Choice Properties' failure to realize the anticipated benefits from the acquisition of CREIT;
- adverse outcomes of legal and regulatory proceedings and related matters;
- reliance on the performance and retention of third party service providers, including those associated with the Company's supply chain and Loblaw's apparel business, including issues with vendors in both advanced and developing markets;
- failure to achieve desired results in labour negotiations, including the terms of future collective bargaining agreements;
- the inability of the Company to manage inventory to minimize the impact of obsolete or excess inventory and to control shrink;
- changes in economic conditions, including economic recession or changes in the rate of inflation or deflation, employment rates and household debt, political uncertainty, tariff disputes, which may include newly imposed surtaxes, interest rates, currency exchange rates or derivative and commodity prices;
- the inability of the Company to effectively develop and execute its strategy; and
- the inability of the Company to anticipate, identify and react to consumer and retail trends.

## Management's Discussion and Analysis

This is not an exhaustive list of the factors that may affect the Company's forward-looking statements. Other risks and uncertainties not presently known to the Company or that the Company presently believes are not material could also cause actual results or events to differ materially from those expressed in its forward-looking statements. Additional risks and uncertainties are discussed in the Company's materials filed with the Canadian securities regulatory authorities from time to time, including without limitation, the section entitled "Operating and Financial Risks and Risk Management" in the Company's AIF for the year ended December 31, 2017. 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 Quarterly Report. Except as required by law, the Company does not undertake to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

### KEY FINANCIAL PERFORMANCE INDICATORS

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

(\$ millions except where otherwise indicated)  
As at or for the periods ended as indicated

	12 Weeks Ended	
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>
Sales	\$ 11,245	\$ 11,436
Operating income	589	640
Adjusted EBITDA <sup>(1)</sup>	1,073	1,038
Adjusted EBITDA margin <sup>(1)</sup>	9.5%	9.1%
Net earnings attributable to shareholders of the Company	\$ 38	\$ 170
Net earnings available to common shareholders of the Company	28	160
Adjusted net earnings available to common shareholders of the Company <sup>(1)</sup>	210	216
Diluted net earnings per common share (\$)	\$ 0.21	\$ 1.23
Adjusted diluted net earnings per common share <sup>(1)</sup> (\$)	\$ 1.63	\$ 1.67
Cash and cash equivalents, short term investments and security deposits	\$ 2,410	\$ 2,651
Cash flows from operating activities	601	916
Free cash flow <sup>(1)</sup>	213	543
Total debt	16,587	12,975
Rolling year adjusted return on average equity attributable to common shareholders of the Company <sup>(1)</sup>	12.7%	12.7%
Rolling year adjusted return on capital <sup>(1)</sup>	11.5%	12.6%

## CONSOLIDATED RESULTS OF OPERATIONS

(\$ millions except where otherwise indicated) For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change
<b>Sales</b>	\$ 11,245	\$ 11,436	\$ (191)	(1.7)%	\$ 21,989	\$ 22,239	\$ (250)	(1.1)%
<b>Operating income</b>	589	640	(51)	(8.0)%	1,091	1,153	(62)	(5.4)%
Adjusted EBITDA <sup>(1)</sup>	1,073	1,038	35	3.4 %	1,991	1,965	26	1.3 %
Adjusted EBITDA margin <sup>(1)</sup>	9.5%	9.1%			9.1%	8.8%		
<b>Depreciation and amortization<sup>(i)</sup></b>	\$ 400	\$ 385	\$ 15	3.9 %	\$ 800	\$ 769	\$ 31	4.0 %
<b>Net interest expense and other financing charges</b>	385	135	250	185.2 %	403	305	98	32.1 %
Adjusted net interest expense and other financing charges <sup>(1)</sup>	182	134	48	35.8 %	323	263	60	22.8 %
Income taxes	126	140	(14)	(10.0)%	232	241	(9)	(3.7)%
Adjusted income taxes <sup>(1)</sup>	164	173	(9)	(5.2)%	299	319	(20)	(6.3)%
Adjusted income tax rate <sup>(1)</sup>	26.9%	27.0%			26.9%	27.1%		
<b>Net earnings attributable to shareholders of the Company</b>	\$ 38	\$ 170	\$ (132)	(77.6)%	\$ 228	\$ 288	\$ (60)	(20.8)%
<b>Net earnings available to common shareholders of the Company</b>	28	160	(132)	(82.5)%	208	268	(60)	(22.4)%
Adjusted net earnings available to common shareholders of the Company <sup>(1)</sup>	210	216	(6)	(2.8)%	388	400	(12)	(3.0)%
<b>Diluted net earnings per common share (\$)</b>	\$ 0.21	\$ 1.23	\$ (1.02)	(82.9)%	\$ 1.61	\$ 2.08	\$ (0.47)	(22.6)%
Adjusted diluted net earnings per common share <sup>(1)</sup> (\$)	\$ 1.63	\$ 1.67	\$ (0.04)	(2.4)%	\$ 3.01	\$ 3.10	\$ (0.09)	(2.9)%

- (i) Depreciation and amortization includes \$119 million (2017 – \$121 million) in the second quarter of 2018 and \$240 million (2017 – \$242 million) year-to-date of amortization of intangible assets, acquired with Shoppers Drug Mart Corporation, recorded by Loblaw and \$4 million (2017 – nil) year-to-date of accelerated depreciation recorded by Weston Foods, related to restructuring and other related costs.

### Net Earnings Available to Common Shareholders of the Company

Net earnings available to common shareholders of the Company in the second quarter of 2018 were \$28 million (\$0.21 per common share), a decrease of \$132 million (\$1.02 per common share) compared to the same period in 2017. The decrease included the decline in the underlying operating performance of \$6 million (\$0.04 per common share) and the unfavourable year-over-year net impact of adjusting items totaling \$126 million (\$0.98 per common share), as described below.

- The decline in underlying operating performance of \$6 million (\$0.04 per common share) was primarily due to:
  - the unfavourable underlying operating performance of Weston Foods;
  - the unfavourable underlying operating performance of Loblaw's Retail segment, which as previously announced, the year-over-year performance was expected to be negatively impacted by minimum wage increases, incremental healthcare reform, and the disposition of Loblaw's gas bar operations in the third quarter of 2017; and
  - the unfavourable impact of an increase in depreciation and amortization, as described below; partially offset by,
  - the favourable underlying operating performance of Loblaw's Financial Services segment.

## Management's Discussion and Analysis

In the second quarter of 2018, Loblaw's Choice Properties segment completed the acquisition of CREIT. The impact of the acquisition of CREIT to net earnings available to common shareholders of the Company for the second quarter of 2018 was nominal, as set out in "Loblaw Segment Results" section of this MD&A.

- The unfavourable year-over-year net impact of adjusting items totaling \$126 million (\$0.98 per common share) was primarily due to:
  - the fair value adjustment of the Trust Unit liability of \$86 million (\$0.68 per common share);
  - the unfavourable impact of acquisition and other costs related to Choice Properties' acquisition of CREIT of \$51 million (\$0.39 per common share); and
  - the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares of \$15 million (\$0.12 per common share);partially offset by,
  - the foreign currency translation of \$14 million (\$0.12 per common share);
  - the fair value adjustment of derivatives of \$6 million (\$0.05 per common share); and
  - the favourable impact of the reversal of provisions related to the Loblaw Card Program of \$4 million (\$0.03 per common share).
- Net earnings available to common shareholders of the Company also included the positive contribution from the increase in the Company's ownership interest in Loblaw, as a result of Loblaw's share repurchases for cancellation.

Adjusted net earnings available to common shareholders of the Company<sup>(1)</sup> decreased by \$6 million (\$0.04 per common share) to \$210 million (\$1.63 per common share) in the second quarter of 2018 compared to the same period in 2017. Adjusted diluted net earnings per common share<sup>(1)</sup> also included the positive contribution from the increase in the Company's ownership interest in Loblaw (\$0.09 per common share). Normalized for the disposition of Loblaw's gas bar operations, adjusted net earnings available to common shareholders of the Company<sup>(1)</sup> were relatively flat (increased by \$0.01 per common share, or 0.6%) compared to the same period in 2017.

Year-to-date net earnings available to common shareholders of the Company was \$208 million (\$1.61 per common share), a decrease of \$60 million (\$0.47 per common share) compared to the same period in 2017. The decrease was primarily due to the decline in the underlying operating performance of \$12 million (\$0.09 per common share) and the unfavourable year-over-year net impact of adjusting items totaling \$48 million (\$0.38 per common share), as described below.

- The decline in underlying operating performance of \$12 million (\$0.09 per common share) was primarily due to:
  - the unfavourable underlying operating performance of Weston Foods;
  - the unfavourable underlying operating performance of Loblaw's Retail segment, which as previously announced, the year-over-year performance was expected to be negatively impacted by minimum wage increases, incremental healthcare reform, and the disposition of Loblaw's gas bar operations in the third quarter of 2017;
  - the unfavourable impact of an increase in adjusted net interest expenses and other financing charges<sup>(1)</sup>, excluding the acquisition of CREIT, as described below; and
  - the unfavourable impact of an increase in depreciation and amortization, as described below;partially offset by,
  - the favourable underlying operating performance of Loblaw's Choice Properties segment net of consolidation and eliminations, excluding the acquisition of CREIT; and
  - the favourable underlying operating performance of Loblaw's Financial Services segment.

- The unfavourable year-over-year net impact of adjusting items totaling \$48 million (\$0.38 per common share) was primarily due to:
  - the fair value adjustment of the Trust Unit liability of \$62 million (\$0.48 per common share); and
  - the unfavourable impact of acquisition and other costs related to Choice Properties' acquisition of CREIT of \$55 million (\$0.43 per common share);
 partially offset by,
  - the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares of \$28 million (\$0.22 per common share);
  - the foreign currency translation of \$28 million (\$0.22 per common share); and
  - the fair value adjustment of derivatives of \$20 million (\$0.15 per common share).
- Net earnings available to common shareholders of the Company also included the positive contribution from the increase in the Company's ownership interest in Loblaw, as a result of Loblaw's share repurchases for cancellation.

Year-to-date adjusted net earnings available to common shareholders of the Company<sup>(1)</sup> decreased by \$12 million (\$0.09 per common share) to \$388 million (\$3.01 per common share) compared to the same period in 2017. Adjusted diluted net earnings per common share<sup>(1)</sup> also included the positive contribution from the increase in the Company's ownership interest in Loblaw (\$0.16 per common share). Normalized for the disposition of Loblaw's gas bar operations, adjusted net earnings available to common shareholders of the Company<sup>(1)</sup> decreased by approximately \$1 million or 0.3% (nominal impact to adjusted diluted net earnings per common share<sup>(1)</sup>).

## Sales

(\$ millions except where otherwise indicated)

For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change
Weston Foods	\$ 468	\$ 509	\$ (41)	(8.1)%	\$ 985	\$ 1,048	\$ (63)	(6.0)%
Loblaw	\$ 10,923	\$ 11,080	\$ (157)	(1.4)%	\$ 21,290	\$ 21,484	\$ (194)	(0.9)%
Intersegment	\$ (146)	\$ (153)			\$ (286)	\$ (293)		
Consolidated	\$ 11,245	\$ 11,436	\$ (191)	(1.7)%	\$ 21,989	\$ 22,239	\$ (250)	(1.1)%

Sales in the second quarter of 2018 were \$11,245 million, a decrease of \$191 million, or 1.7% compared to the same period in 2017. The decrease in sales was impacted by each of the Company's reportable operating segments as follows:

- Negatively by 0.3% due to sales decline of 8.1% at Weston Foods. Sales included the unfavourable impact of foreign currency translation of approximately 2.4%. Excluding the unfavourable impact of foreign currency translation, sales decreased by 5.7% mainly due to a decrease in volume, including the impact of product rationalization, and the negative impact of changes in sales mix.
- Negatively by 1.4% due to sales decline of 1.4% at Loblaw, primarily driven by the Retail segment, partially offset by the Choice Properties segment net of consolidation and eliminations, driven by the acquisition of CREIT. Retail sales decreased by \$271 million, or 2.5%, compared to the same period in 2017. Excluding the consolidation of franchises, Retail sales decreased by \$370 million, or 3.5%. The decrease was primarily due to the impact of the disposition of Loblaw's gas bar operations of \$376 million, partially offset by same-store sales growth. Food retail same-store sales growth was 0.8% after excluding gas bar operations. Loblaw's food retail average quarterly internal food price index was marginally lower than the average quarterly national food price inflation of 0.1% 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 Loblaw stores. Drug retail same-store sales growth was 1.7%.

## Management's Discussion and Analysis

Year-to-date sales were \$21,989 million, a decrease of \$250 million, or 1.1% compared to the same period in 2017. The decrease in sales was impacted by each of the Company's reportable operating segments as follows:

- Negatively by 0.3% due to sales decline of 6.0% at Weston Foods. Sales included the unfavourable impact of foreign currency translation of approximately 2.6%. Excluding the unfavourable impact of foreign currency translation, sales decreased by 3.4% mainly due to a decrease in volume, including the impact of product rationalization, and the negative impact of changes in sales mix.
- Negatively by 0.8% due to sales decline of 0.9% at Loblaw, primarily driven by the Retail segment, partially offset by the Choice Properties segment net of consolidation and eliminations, driven by the acquisition of CREIT, and the Financial Services segment. Retail sales decreased by \$324 million, or 1.5%, compared to the same period in 2017. Excluding the consolidation of franchises, Retail sales decreased by \$481 million, or 2.3%. The decrease was primarily due to the impact of the disposition of Loblaw's gas bar operations of \$720 million, partially offset by same-store sales growth and a net increase in Retail square footage. Food retail same-store sales growth was 1.3%, after excluding gas bar operations, and drug retail same-store sales growth was 2.7%.

### Operating Income

(\$ millions except where otherwise indicated)

For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change
Weston Foods	\$ 21	\$ 24	\$ (3)	(12.5)%	\$ 31	\$ 47	\$ (16)	(34.0)%
Loblaw	\$ 559	\$ 625	\$ (66)	(10.6)%	\$ 1,037	\$ 1,118	\$ (81)	(7.2)%
Intersegment	\$ 9	\$ (9)			\$ 23	\$ (12)		
Consolidated	\$ 589	\$ 640	\$ (51)	(8.0)%	\$ 1,091	\$ 1,153	\$ (62)	(5.4)%

Operating income in the second quarter of 2018 was \$589 million, a decrease of \$51 million, or 8.0% compared to the same period in 2017. The decrease included improvements in the underlying operating performance of \$18 million which were more than offset by the unfavourable year-over-year net impact of adjusting items totaling \$69 million, as described below:

- the improvement in underlying operating performance of \$18 million was primarily due to:
  - the favourable underlying operating performance of Loblaw's Choice Properties segment net of consolidation and eliminations, driven by the acquisition of CREIT; and
  - the favourable underlying operating performance of Loblaw's Financial Services segment; partially offset by,
  - the underlying operating performance of Weston Foods; and
  - the underlying operating performance of Loblaw's Retail segment, which as previously announced, the year-over-year performance was expected to be negatively impacted by minimum wage increases, incremental healthcare reform, and the disposition of Loblaw's gas bar operations in the third quarter of 2017.

- the unfavourable year-over-year net impact of adjusting items totaling \$69 million was primarily due to:
  - the unfavourable impact of acquisition and other costs related to Choice Properties' acquisition of CREIT of \$108 million;
 partially offset by,
  - the foreign currency translation of \$15 million;
  - the fair value adjustment of derivatives of \$11 million; and
  - the favourable impact of the reversal of provisions related to the Loblaw Card Program of \$11 million.

Year-to-date operating income decreased by \$62 million, or 5.4%, to \$1,091 million compared to the same period in 2017. The decrease included the decline in underlying operating performance of \$3 million, and the unfavourable year-over-year net impact of adjusting items totaling \$59 million, as described below:

- the decline in underlying operating performance of \$3 million was primarily due to:
  - the underlying operating performance of Weston Foods; and
  - the underlying operating performance of Loblaw's Retail segment, which as previously announced, the year-over-year performance was expected to be negatively impacted by minimum wage increases, incremental healthcare reform, and the disposition of Loblaw's gas bar operations in the third quarter of 2017;
 partially offset by,
  - the favourable underlying operating performance of Loblaw's Choice Properties segment net of consolidation and eliminations, driven by the acquisition of CREIT; and
  - the favourable underlying operating performance of Loblaw's Financial Services segment.
- the unfavourable year-over-year net impact of adjusting items totaling \$59 million was primarily due to:
  - the unfavourable impact of acquisition and other costs related to Choice Properties' acquisition of CREIT of \$120 million;
  - the unfavourable impact of healthcare reform on inventory balances of \$19 million;
  - the change in the fair value adjustment to investment properties at Loblaw of \$10 million; and
  - the unfavourable net charges related to the Loblaw Card Program of \$8 million;
 partially offset by,
  - the fair value adjustment of derivatives of \$35 million;
  - the foreign currency translation of \$32 million; and
  - the favourable impact of income earned, net of certain costs incurred, from the wind-down of PC Financial banking services of \$20 million.

## Management's Discussion and Analysis

### Adjusted EBITDA<sup>(1)</sup>

(\$ millions except where otherwise indicated)

For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change
Weston Foods	\$ 48	\$ 54	\$ (6)	(11.1)%	\$ 92	\$ 115	\$ (23)	(20.0)%
Loblaw	\$ 1,025	\$ 984	\$ 41	4.2 %	\$ 1,899	\$ 1,850	\$ 49	2.6 %
Consolidated	\$ 1,073	\$ 1,038	\$ 35	3.4 %	\$ 1,991	\$ 1,965	\$ 26	1.3 %

Adjusted EBITDA<sup>(1)</sup> in the second quarter of 2018 was \$1,073 million, an increase of \$35 million, or 3.4% compared to the same period in 2017. The increase in adjusted EBITDA<sup>(1)</sup> was impacted by each of the Company's reportable operating segments as follows:

- Negatively by 0.6% due to a decrease of 11.1% in adjusted EBITDA<sup>(1)</sup> at Weston Foods driven by the decline in sales and higher input and distribution costs, partially offset by productivity improvements and benefits realized from the transformation program, net of costs.
- Positively by 4.0% due to an increase of 4.2% in adjusted EBITDA<sup>(1)</sup> at Loblaw, primarily driven by Loblaw's Choice Properties segment net of consolidation and eliminations, driven by the acquisition of CREIT, and Loblaw's Financial Services segment, partially offset by Loblaw's Retail segment which included the disposition of Loblaw's gas bar operations of \$20 million. The decline in Retail adjusted EBITDA<sup>(1)</sup> was primarily driven by an increase in Retail selling, general and administrative expenses ("SG&A"), partially offset by an increase in Retail gross profit. Retail's year-over-year second quarter performance was negatively impacted by minimum wage increases and incremental healthcare reform.

Year-to-date adjusted EBITDA<sup>(1)</sup> increased by \$26 million, or 1.3%, to \$1,991 million compared to the same period in 2017. The increase in adjusted EBITDA<sup>(1)</sup> was impacted by each of the Company's reportable operating segments as follows:

- Negatively by 1.2% due to a decrease of 20.0% in adjusted EBITDA<sup>(1)</sup> at Weston Foods driven by the decline in sales and higher input and distribution costs, partially offset by productivity improvements and benefits realized from the transformation program, net of costs.
- Positively by 2.5% due to an increase of 2.6% in adjusted EBITDA<sup>(1)</sup> at Loblaw, primarily driven by Loblaw's Choice Properties segment net of consolidation and eliminations, driven by the acquisition of CREIT, and Loblaw's Financial Services segment, partially offset by Loblaw's Retail segment, which included the disposition of Loblaw's gas bar operations of \$30 million. The decline in Retail adjusted EBITDA<sup>(1)</sup> was primarily driven by an increase in Retail SG&A, partially offset by an increase in Retail gross profit. Retail segment's year-over-year performance was negatively impacted by minimum wage increases and incremental healthcare reform.

## Depreciation and Amortization

(\$ millions except where otherwise indicated)

For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017	\$ Change	% Change
Weston Foods	\$ 28	\$ 25	\$ 3	12.0%	\$ 59	\$ 49	\$ 10	20.4%
Loblaw	\$ 372	\$ 360	\$ 12	3.3%	\$ 741	\$ 720	\$ 21	2.9%
Consolidated	\$ 400	\$ 385	\$ 15	3.9%	\$ 800	\$ 769	\$ 31	4.0%

Depreciation and amortization in the second quarter of 2018 was \$400 million, an increase of \$15 million, or 3.9% compared to the same period in 2017. Year-to-date depreciation and amortization was \$800 million, an increase of \$31 million, or 4.0% compared to the same period in 2017. Depreciation and amortization in the second quarter and year-to date included \$119 million (2017 – \$121 million) and \$240 million (2017 – \$242 million), respectively, of amortization of intangible assets related to the acquisition of Shoppers Drug Mart Corporation (“Shoppers Drug Mart”) and year-to-date included \$4 million (2017 – nil) of accelerated depreciation incurred by Weston Foods. Excluding these amounts, depreciation and amortization increased in the second quarter and year-to-date by \$17 million and \$29 million, respectively, driven by:

- an increase in depreciation from the consolidation of Loblaw franchises;
- an increase in Loblaw’s IT assets; and
- an increase in depreciation due to investments in capital at Weston Foods.

## Net Interest Expense and Other Financing Charges

(\$ millions)

For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017	\$ Change	% Change
Net interest expense and other financing charges	\$ 385	\$ 135	\$ 250	185.2 %	\$ 403	\$ 305	\$ 98	32.1 %
Add: Fair value adjustment of the Trust Unit liability	(180)	1	(181)	(18,100.0)%	(99)	(23)	(76)	(330.4)%
Fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares	(23)	(2)	(21)	(1,050.0)%	19	(19)	38	200.0 %
Adjusted net interest expense and other financing charges <sup>(1)</sup>	\$ 182	\$ 134	\$ 48	35.8 %	\$ 323	\$ 263	\$ 60	22.8 %

Net interest expense and other financing charges in the second quarter of 2018 were \$385 million, an increase of \$250 million, or 185.2% compared to the same period in 2017. The increase was primarily due to the year-over-year impact of the change in the fair value adjustment of the Trust Unit liability and the change in the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares.

Adjusted net interest expense and other financing charges<sup>(1)</sup> in the second quarter of 2018 were \$182 million, an increase of \$48 million, or 35.8% compared to the same period in 2017, primarily driven by higher interest expense in Loblaw’s Choice Properties segment as a result of the issuance of new unsecured senior debentures, higher distributions from newly issued Trust Units to former CREIT unitholders as part of the acquisition consideration, higher interest expense on debt assumed in connection with the acquisition of CREIT, partially offset by the early redemption of the Series A senior unsecured debenture.

## Management's Discussion and Analysis

Year-to-date net interest expense and other financing charges were \$403 million, an increase of \$98 million, or 32.1% compared to the same period in 2017. The increase was primarily due to the year-over-year impact of the change in the fair value adjustment of the Trust Unit liability, partially offset by the change in the fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares.

Year-to-date adjusted net interest expense and other financing charges<sup>(1)</sup> were \$323 million, an increase of \$60 million, or 22.8% compared to the same period in 2017, primarily driven by the following:

- higher interest expense in Loblaw's Choice Properties segment as a result of the issuance of new unsecured senior debentures and higher distributions from newly issued Trust Units to former CREIT unitholders as part of the acquisition consideration, and the call premium for the early redemption of the Series A senior unsecured debenture;
- higher interest expense in the Loblaw's Financial Services segment due to an increase in borrowings related to credit card receivables; and
- higher interest expense in the Loblaw's Retail segment due to higher interest rates on variable rate debt.

### Income Taxes

(\$ millions except where otherwise indicated) For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change
Income taxes	\$ 126	\$ 140	\$ (14)	(10.0)%	\$ 232	\$ 241	\$ (9)	(3.7)%
Add: Tax impact of items excluded from adjusted earnings before taxes <sup>(1) (i)</sup>	38	33	5	15.2 %	67	78	(11)	(14.1)%
Adjusted income taxes <sup>(1)</sup>	\$ 164	\$ 173	\$ (9)	(5.2)%	\$ 299	\$ 319	\$ (20)	(6.3)%
Effective income tax rate applicable to earnings before taxes	61.8%	27.7%			33.7%	28.4%		
Adjusted income tax rate applicable to adjusted earnings before taxes <sup>(1)</sup>	26.9%	27.0%			26.9%	27.1%		

(i) See the adjusted EBITDA<sup>(1)</sup> table and the adjusted net interest expense and other financing charges<sup>(1)</sup> table included in the "Non-GAAP Financial Measures" section of this MD&A for a complete list of items excluded from adjusted earnings before taxes<sup>(1)</sup>.

The effective tax rate in the second quarter of 2018 was 61.8%, compared to 27.7% in the same period in 2017. The increase in the effective income tax rate was primarily attributable to the impact of non-deductible items including costs related to the acquisition of CREIT and an increase in the non-deductible fair value adjustment to the Trust Unit liability.

The adjusted income tax rate<sup>(1)</sup> for the second quarter of 2018 was 26.9%, compared to 27.0% in the same period in 2017. The decrease in the adjusted income tax rate<sup>(1)</sup> was primarily attributable to the decrease in the U.S. federal statutory corporate income tax rate from 35.0% to 21.0%, enacted in the fourth quarter of 2017, and the impact of certain non-deductible items.

The year-to-date effective tax rate was 33.7%, compared to 28.4% in the same period in 2017. The increase in the effective income tax rate was primarily attributable to the impact of non-deductible items including costs related to the acquisition of CREIT and an increase in the non-deductible fair value adjustment to the Trust Unit liability.

The year-to-date adjusted income tax rate<sup>(1)</sup> was 26.9%, compared to 27.1% in the same period in 2017. The decrease in the adjusted income tax rate<sup>(1)</sup> was primarily attributable to the decrease in the U.S. federal statutory corporate income tax rate from 35.0% to 21.0%, enacted in the fourth quarter of 2017, and the impact of certain non-deductible items.

## REPORTABLE OPERATING SEGMENTS

### WESTON FOODS SEGMENT RESULTS

(\$ millions except where otherwise indicated)

For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017	\$ Change	% Change
Sales	\$ 468	\$ 509	\$ (41)	(8.1)%	\$ 985	\$ 1,048	\$ (63)	(6.0)%
Operating income	\$ 21	\$ 24	\$ (3)	(12.5)%	\$ 31	\$ 47	\$ (16)	(34.0)%
Adjusted EBITDA <sup>(1)</sup>	\$ 48	\$ 54	\$ (6)	(11.1)%	\$ 92	\$ 115	\$ (23)	(20.0)%
Adjusted EBITDA margin <sup>(1)</sup>	10.3%	10.6%			9.3%	11.0%		
Depreciation and amortization <sup>(i)</sup>	\$ 28	\$ 25	\$ 3	12.0 %	\$ 59	\$ 49	\$ 10	20.4 %

(i) Depreciation and amortization includes \$4 million year-to-date of accelerated depreciation related to restructuring and other related costs recorded in the first quarter of 2018.

**Sales** Weston Foods sales in the second quarter of 2018 were \$468 million, a decrease of \$41 million, or 8.1%, compared to the same period in 2017. Sales included the unfavourable impact of foreign currency translation of approximately 2.4%. Excluding the unfavourable impact of foreign currency translation, sales decreased by 5.7% mainly due to a decrease in volume, including the impact of product rationalization, and the negative impact of changes in sales mix.

On a year-to-date basis, sales were \$985 million, a decrease of \$63 million, or 6.0%, compared to the same period in 2017. Sales included the unfavourable impact of foreign currency translation of approximately 2.6%. Excluding the unfavourable impact of foreign currency translation, sales decreased by 3.4% mainly due to a decrease in volume, including the impact of product rationalization, and the negative impact of changes in sales mix.

**Operating Income** Weston Foods operating income in the second quarter of 2018 was \$21 million, a decrease of \$3 million, or 12.5%, compared to the same period in 2017. The decrease was primarily due to the decline in underlying operating performance of \$9 million, partially offset by the favourable year-over-year net impact of adjusting items totaling \$6 million, as described below:

- the fair value adjustment of derivatives of \$6 million; and
  - the impact of restructuring and other related costs of \$3 million;
- partially offset by,
- the unfavourable year-over-year impact of the net proceeds from insurance claims of \$3 million.

Year-to-date operating income in 2018 was \$31 million, a decrease of \$16 million, or 34.0%, compared to the same period in 2017. The decrease was primarily due to the decline in underlying operating performance of \$29 million, partially offset by the favourable year-over-year net impact of adjusting items totaling \$13 million, as described below:

- the fair value adjustment of derivatives of \$19 million;
- partially offset by,
- the unfavourable impact of restructuring and other related costs of \$3 million; and
  - the unfavourable year-over-year impact of the net proceeds from insurance claims of \$3 million.

## Management's Discussion and Analysis

**Adjusted EBITDA<sup>(1)</sup>** Weston Foods adjusted EBITDA<sup>(1)</sup> in the second quarter of 2018 was \$48 million, a decrease of \$6 million, or 11.1%, compared to the same period in 2017. The decrease was driven by the decline in sales and higher input and distribution costs, partially offset by productivity improvements and benefits realized from the transformation program, net of costs.

Year-to-date adjusted EBITDA<sup>(1)</sup> was \$92 million, a decrease of \$23 million, or 20.0%, compared to the same period in 2017. The decrease was driven by the decline in sales and higher input and distribution costs, partially offset by productivity improvements and benefits realized from the transformation program, net of costs.

Weston Foods adjusted EBITDA margin<sup>(1)</sup> in the second quarter of 2018 decreased to 10.3% compared to 10.6% in the same period in 2017. Year-to-date adjusted EBITDA margin<sup>(1)</sup> was 9.3% compared to 11.0% in the same period in 2017. The decline in adjusted EBITDA margin<sup>(1)</sup> in the second quarter of 2018 and year-to-date was driven by the factors as described above.

**Depreciation and Amortization** Weston Foods depreciation and amortization in the second quarter of 2018 was \$28 million and \$59 million year-to-date, an increase of \$3 million and \$10 million, respectively, compared to the same period in 2017. Depreciation and amortization included \$4 million year-to-date of accelerated depreciation recorded in the first quarter of 2018, related to the previously announced closure of an unprofitable manufacturing facility in the U.S. Excluding this amount, depreciation and amortization increased in the second quarter of 2018 and year-to-date by \$3 million and \$6 million, respectively, due to investments in capital.

### Weston Foods Other Business Matters

**Restructuring and other related costs** Weston Foods continuously evaluates strategic and cost reduction initiatives related to its manufacturing assets, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. In the second quarter of 2018 and year-to-date, Weston Foods recorded restructuring and other related costs of \$2 million (2017 – \$5 million) and \$17 million (2017 – \$14 million), respectively, which were primarily related to the reorganization costs from the transformation program and the previously announced closure of an unprofitable manufacturing facility in the U.S. that was completed in the first quarter of 2018. Restructuring and other related costs recorded in the second quarter of 2018 and year-to-date included \$2 million and \$13 million, respectively, of severance and exit costs and \$4 million year-to-date of accelerated depreciation.

### LOBLAW SEGMENT RESULTS

(\$ millions except where otherwise indicated)

For the periods ended as indicated	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	\$ Change	% Change
Sales	\$ 10,923	\$ 11,080	\$ (157)	(1.4)%	\$ 21,290	\$ 21,484	\$ (194)	(0.9)%
Operating income	\$ 559	\$ 625	\$ (66)	(10.6)%	\$ 1,037	\$ 1,118	\$ (81)	(7.2)%
Adjusted EBITDA <sup>(1)</sup>	\$ 1,025	\$ 984	\$ 41	4.2 %	\$ 1,899	\$ 1,850	\$ 49	2.6 %
Adjusted EBITDA margin <sup>(1)</sup>	9.4%	8.9%			8.9%	8.6%		
Depreciation and amortization <sup>(i)</sup>	\$ 372	\$ 360	\$ 12	3.3 %	\$ 741	\$ 720	\$ 21	2.9 %

(i) Depreciation and amortization in the second quarter of 2018 includes \$119 million (2017 – \$121 million) and \$240 million (2017 – \$242 million) year-to-date of amortization of intangible assets acquired with Shoppers Drug Mart.

As previously announced, Loblaw's year-over-year financial performance was negatively impacted by minimum wage increases and incremental healthcare reform. In addition, the disposition of Loblaw's gas bar operations, in the third quarter of 2017, had a negative year-over-year impact on financial performance.

In addition, sales, operating income and adjusted EBITDA<sup>(1)</sup> in the second quarter of 2018 and year-to-date included the impacts of Choice Properties' acquisition of CREIT, as described below, and the consolidation of franchises as set out in "Loblaw Other Business Matters".

In the second quarter of 2018, Choice Properties completed the acquisition of CREIT. The impact of the CREIT acquisition on consolidated results was an increase in revenue of \$69 million, adjusted EBITDA<sup>(1)</sup> of approximately \$48 million and net interest expense and other financing charges of \$48 million in the second quarter of 2018. The acquisition had a nominal impact on adjusted net earnings available to common shareholders of the Company<sup>(1)</sup> in the second quarter of 2018. On a year-to-date basis net interest expense and other financing charges included an additional \$2 million which was recorded in the first quarter of 2018.

**Sales** Loblaw sales in the second quarter of 2018 were \$10,923 million, a decrease of \$157 million, or 1.4%, compared to the same period in 2017. The decrease was primarily driven by Retail, partially offset by Choice Properties net of consolidation and eliminations, driven by the acquisition of CREIT. Retail sales decreased by \$271 million, or 2.5%, compared to the same period in 2017 and included food retail sales of \$7,676 million (2017 – \$7,988 million) and drug retail sales of \$2,924 million (2017 – \$2,883 million).

Excluding the consolidation of franchises, Retail sales decreased by \$370 million, or 3.5%, primarily driven by the following factors:

- the impact of the disposition of gas bar operations of \$376 million; and
  - the impact of incremental healthcare reform on drug retail;
- partially offset by,
- food retail same-store sales growth was 0.8% for the quarter after excluding gas bar operations. Including gas bar operations, food retail same-store sales growth was 0.8%. The timing of Easter had a nominal impact on food retail same-store sales growth in the second quarter of 2018. In the second quarter of 2017, food retail sales were relatively flat excluding the favourable impact of Easter. Loblaw's food retail average quarterly internal food price index was marginally lower than the average quarterly national food price inflation of 0.1% as measured by CPI. CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores;
  - drug retail same-store sales growth was 1.7%, including pharmacy same-store sales growth of 0.3% and front store same-store sales growth of 3.0%; and
  - 16 food and drug stores were opened and 23 food and drug stores were closed in the last 12 months, resulting in a net increase in Retail square footage of 0.1 million square feet, or 0.1%.

On a year-to-date basis, Loblaw sales were \$21,290 million, a decrease of \$194 million, or 0.9%, compared to the same period in 2017, primarily driven by Retail, partially offset by Choice Properties net of consolidation and eliminations, driven by the acquisition of CREIT, and Financial Services. Retail sales decreased by \$324 million, or 1.5%, compared to the same period in 2017 and included food retail sales of \$14,947 million (2017 – \$15,423 million) and drug retail sales of \$5,808 million (2017 – \$5,656 million). The decrease was primarily due to the impact of the disposition of gas bar operations of \$720 million.

Year-to-date food retail same-store sales growth was 1.3%, after excluding gas bar operations. Year-to-date drug retail same-store sales growth was 2.7%, including pharmacy same-store sales growth of 1.9% and front store same-store sales growth of 3.4%.

The redemption of Loblaw Cards resulted in the delivery of approximately \$36 million of free products to customers in the second quarter of 2018 and \$53 million year-to-date, which was provided for in the fourth quarter of 2017. The redemptions did not benefit sales or Loblaw's financial performance and Loblaw's management does not believe it had a significant impact on food retail same-store sales.

## Management's Discussion and Analysis

**Operating Income** Loblaw operating income in the second quarter of 2018 was \$559 million, a decrease of \$66 million, or 10.6% compared to the same period in 2017. The decrease in operating income included the improvements in underlying operating performance of \$27 million, which was more than offset by the unfavourable year-over-year net impact of certain adjusting items totaling \$93 million, as described below:

- the improvement in underlying operating performance of \$27 million was primarily due to Choice Properties net of consolidation and eliminations driven by the acquisition of CREIT, and Financial Services. The improvement was partially offset by Retail which included the unfavourable impact of the disposition of gas bar operations. Retail's year-over-year second quarter performance was negatively impacted by minimum wage increases and incremental healthcare reform. The decline in underlying operating performance also included the favourable year-over-year contribution from the consolidation of franchises in the second quarter of 2018; and
- the unfavourable year-over-year net impact of certain adjusting items totaling \$93 million was primarily due to the following:
  - the impact of acquisition and other costs related to Choice Properties' acquisition of CREIT of \$108 million; and
  - the change in the fair value adjustment to investment properties of \$10 million;partially offset by,
  - the impact of the reversal of provisions related to the Loblaw Card Program of \$11 million;
  - the fair value adjustment of derivatives of \$5 million; and
  - the favourable impact of income earned, net of certain costs incurred, from the wind-down of PC Financial banking services of \$3 million.

Year-to-date Loblaw operating income was \$1,037 million, a decrease of \$81 million, or 7.2% compared to the same period in 2017. The decrease in operating income included an improvement in underlying operating performance of \$26 million, which was more than offset by the unfavourable year-over-year net impact of certain adjusting items totaling \$107 million, as described below:

- the improvement in underlying operating performance of \$26 million was primarily due to Choice Properties net of consolidation and eliminations driven by the acquisition of CREIT, and Financial Services. The improvement was partially offset by Retail which included the unfavourable impact of the disposition of gas bar operations. Retail's year-over-year performance was negatively impacted by minimum wage increases and incremental healthcare reform and included the favourable year-over-year contribution from the consolidation of franchises in the first quarter of 2018; and
- the unfavourable year-over-year net impact of certain adjusting items totaling \$107 million was primarily due to the following:
  - the impact of acquisition and other costs related to Choice Properties' acquisition of CREIT of \$120 million;
  - the impact of healthcare reform on inventory balances of \$19 million; and
  - the change in the fair value adjustment to investment properties of \$10 million;partially offset by,
  - the favourable impact of income earned, net of certain costs incurred, from the wind-down of PC Financial banking services of \$20 million;
  - the fair value adjustment of derivatives of \$16 million; and
  - the pension annuities and buy-outs in the prior year of \$6 million.

**Adjusted EBITDA<sup>(1)</sup>** Loblaw adjusted EBITDA<sup>(1)</sup> in the second quarter of 2018 was \$1,025 million, an increase of \$41 million, or 4.2% compared to the same period in 2017. The increase was driven by Choice Properties net of consolidation and eliminations driven by the acquisition of CREIT, and Financial Services, partially offset by Retail. Retail adjusted EBITDA<sup>(1)</sup> decreased \$19 million driven by an increase in Retail SG&A, partially offset by an increase in Retail gross profit. The decrease in Retail adjusted EBITDA<sup>(1)</sup> included the unfavourable impact of the disposition of Loblaw's gas bar operations of approximately \$20 million and the favourable contribution from the consolidation of franchises of \$13 million.

- Retail gross profit percentage was 29.5%, an increase of 140 basis points compared to the same period in 2017. Excluding the consolidation of franchises, Retail gross profit decreased by \$7 million. Retail gross profit percentage, excluding the consolidation of franchises, was 27.9%, an increase of 90 basis points compared to the second quarter of 2017. The increase in Retail gross profit percentage was primarily due to the favourable impact from the disposition of gas bar operations of approximately 70 basis points. Margins were positively impacted by food retail and negatively impacted by healthcare reform.
- Retail SG&A as a percentage of sales was 20.9%, an unfavourable increase of 140 basis points compared to the second quarter of 2017. Excluding the consolidation of franchises, Retail SG&A increased by \$25 million. SG&A as a percentage of sales, excluding the consolidation of franchises, was 19.3%, an unfavourable increase of 90 basis points compared to the second quarter of 2017, mainly driven by:
  - the unfavourable impact from the disposition of gas bar operations of approximately 60 basis points;
  - higher store costs driven by minimum wage increases; and
  - the unfavourable impact of foreign exchange;partially offset by,
  - previously announced cost saving initiatives.

Loblaw adjusted EBITDA<sup>(1)</sup> included an increase in Choice Properties adjusted EBITDA<sup>(1)</sup>, net of consolidations and eliminations, of \$50 million, primarily due to the contribution from the investment properties included in the acquisition of CREIT, as well as the expansion of the portfolio through other acquisitions and development of properties and an increase in base rent and operating cost recoveries from existing properties; and an increase in Financial Services adjusted EBITDA<sup>(1)</sup> of \$10 million, primarily driven by higher year-over-year interchange income due to an industry-wide reduction in interchange rates imposed on MasterCard International Incorporated<sup>®</sup> ("MasterCard<sup>®</sup>") issuers affecting the first half of 2017 and growth in credit card receivables.

Year-to-date Loblaw adjusted EBITDA<sup>(1)</sup> was \$1,899 million, an increase of \$49 million, or 2.6% compared to the same period in 2017, primarily driven by Choice Properties net of consolidation and elimination, which included the favourable contribution from the acquisition of CREIT, and Financial Services, partially offset by Retail. Retail adjusted EBITDA<sup>(1)</sup> decreased \$38 million driven by an increase in Retail SG&A, partially offset by an increase in Retail gross profit. The decrease in Retail adjusted EBITDA<sup>(1)</sup> included the unfavourable impact of the disposition of Loblaw's gas bar operations of approximately \$30 million and the favourable contribution from the consolidation of franchises of \$13 million.

- Retail gross profit percentage was 29.4%, an increase of 120 basis points compared to the same period in 2017. Excluding the consolidation of franchises, Retail gross profit increased by \$23 million. Retail gross profit percentage, excluding the consolidation of franchises, was 27.9%, an increase of 80 basis points compared to the first quarter of 2017. The increase in Retail gross profit percentage was primarily due to the favourable impact from the disposition of gas bar operations of approximately 80 basis points. Margins were positively impacted by food retail and negatively impacted by healthcare reform.

## Management's Discussion and Analysis

- Retail SG&A as a percentage of sales was 21.2%, an unfavourable increase of 130 basis points compared to the first quarter of 2017. Excluding the consolidation of franchises, Retail SG&A increased by \$74 million. SG&A as a percentage of sales, excluding the consolidation of franchises, was 19.7%, an unfavourable increase of 90 basis points compared to the first quarter of 2017, mainly driven by:
  - the unfavourable impact from the disposition of gas bar operations of approximately 60 basis points;
  - higher store costs driven by minimum wage increases and the launch of *PC Optimum*; and
  - the unfavourable impact of foreign exchange;
 partially offset by,
  - previously announced cost saving initiatives.

Loblaw adjusted EBITDA<sup>(1)</sup> included an increase in Choice Properties adjusted EBITDA<sup>(1)</sup>, net of consolidations and eliminations, of \$61 million, primarily due to the contribution from the investment properties acquired as part of the acquisition of CREIT, as well as the expansion of the portfolio through other acquisitions and development of properties and an increase in base rent and operating cost recoveries from existing properties; and an increase in Financial Services adjusted EBITDA<sup>(1)</sup> of \$26 million, primarily driven by higher year-over-year interchange income due to an industry-wide reduction in interchange rates imposed on MasterCard<sup>®</sup> issuers affecting the first half of 2017 and growth in credit card receivables.

**Depreciation and Amortization** Loblaw's depreciation and amortization was \$372 million in the second quarter of 2018, an increase of \$12 million, or 3.3% compared to the same period in 2017, primarily driven by the consolidation of franchises and an increase in IT assets.

Year-to-date depreciation and amortization was \$741 million, an increase of \$21 million, or 2.9% compared to the same period in 2017, primarily driven by the consolidation of franchises and an increase in IT assets.

Depreciation and amortization included \$119 million (2017 – \$121 million) in the second quarter of 2018 and \$240 million (2017 – \$242 million) year-to-date of amortization of intangible assets related to the acquisition of Shoppers Drug Mart.

### Loblaw Other Business Matters

**Consolidation of Franchises** Loblaw has more than 500 franchise food retail stores in its network. As at the end of the second quarter of 2018, 352 of these stores were consolidated for accounting purposes under a new, simplified franchise agreement ("Franchise Agreement") implemented in 2015.

Loblaw will convert the remaining franchises to the Franchise Agreement as existing agreements expire, at the end of which all franchises will be consolidated. The following table presents the number of franchises consolidated in the second quarter of 2018 and year-to-date, and the total impact of the consolidation of franchises included in the consolidated results of the Company.

(\$ millions except where otherwise indicated)

For the periods ended as indicated	12 Weeks Ended		24 Weeks Ended	
	Jun. 16, 2018	Jun. 17, 2017	Jun. 16, 2018	Jun. 17, 2017
Number of Consolidated Franchise stores, beginning of period	331	225	310	200
Add: Net Number of Consolidated Franchise stores in the period	21	16	42	41
Number of Consolidated Franchise stores, end of period	352	241	352	241
Sales	\$ 254	\$ 155	\$ 453	\$ 296
Operating income	12	2	7	—
Adjusted EBITDA <sup>(1)</sup>	25	12	32	19
Depreciation and amortization	13	10	25	19
Net income attributable to Non-Controlling Interests	12	3	7	2

Operating income 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.

Loblaw expects<sup>(2)</sup> that the estimated annual impact in 2018 of new and current consolidated franchises will be revenue of approximately \$1,000 million, adjusted EBITDA<sup>(1)</sup> of approximately \$80 million, depreciation and amortization of approximately \$60 million and net earnings attributable to non-controlling interests of approximately \$22 million.

**Wind-down of PC Financial 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, \$3 million of which was recognized in the second quarter of 2018, and \$24 million of which was recognized in 2017.

PC Bank will continue to operate the PC MasterCard<sup>®</sup> program and customers will earn *PC Optimum* points. PC Bank remains committed to providing payment products to its customers and continues to strengthen its credit card services and loyalty program.

**Acquisition of Investment Properties** In the second quarter of 2018, in addition to the acquisition of CREIT, Choice Properties acquired one investment property from third-party vendors for an aggregate purchase price of \$2 million, excluding acquisition costs, which was fully settled in cash.

**Choice Properties' Acquisition of Canadian Real Estate Investment Trust** On May 4, 2018, Choice Properties acquired all the assets and assumed all the liabilities, including outstanding debt, of CREIT for total consideration of \$3,708 million. The consideration was comprised of \$1,652 million of cash and the issuance of 182,836,481 Trust Units.

In anticipation of the acquisition, Choice Properties arranged a new \$1,500 million committed revolving credit facility. Concurrent with the closing of the acquisition of CREIT, Choice Properties repaid and cancelled its existing credit facilities prior to the acquisition and those acquired from CREIT.

Also, concurrent with the closing of the acquisition, Loblaw, Choice Properties' controlling unitholder, converted all of its outstanding Class C LP Units with the face value of \$925 million into Class B LP Units of Choice Properties Limited Partnership. Choice Properties issued to Loblaw 70,881,226 Class B LP Units upon the conversion and the shortfall in value of approximately \$99 million was paid in cash. In connection with this conversion, the Company recognized capital gains income tax expense of approximately \$4 million in contributed surplus and \$4 million in non-controlling interest.

The cash portion of the acquisition and other transactions in relation to CREIT was financed as follows:

- \$1,300 million of proceeds from the issuance of senior unsecured debentures Series K and L; and
- \$800 million was obtained through two unsecured term loan facilities, of which \$175 million is due in four years and \$625 million is due in five years.

## Management's Discussion and Analysis

The preliminary purchase equation is based on management's best estimate of fair value. The actual amount allocated to certain identifiable net assets could vary as the purchase equation is finalized. The preliminary purchase price allocation at the acquisition date is as follows:

(\$ millions)	As at May 4, 2018
<b>Net Assets Acquired:</b>	
Cash and cash equivalents	\$ 28
Accounts receivable and other assets	45
Mortgages, loans and notes receivable	204
Equity accounted joint ventures	683
Investment properties	4,730
Intangible assets	30
Goodwill	381
Trade payables and other liabilities	(171)
Long term debt	(1,841)
Deferred income tax liabilities	(381)
<b>Total Net Assets Acquired</b>	<b>\$ 3,708</b>

Choice Properties has one year to finalize the fair value of the assets acquired and the liabilities assumed.

The goodwill is generated on consolidation of Choice Properties and is attributable to deferred income tax recorded on temporary differences arising between the fair value of the investment properties acquired and their respective income tax bases for the Company's effective ownership interest in Choice Properties. The goodwill arising from this acquisition is not deductible for tax purposes. Management has allocated this goodwill to Loblaw segment for impairment testing.

As at June 16, 2018, on a year-to-date basis, Loblaw, through Choice Properties incurred costs totaling to \$120 million related to the acquisition of CREIT which were recorded in SG&A. Of this amount, \$108 million was recognized during the second quarter of 2018.

Included in the unaudited interim period condensed consolidated financial statements for the second quarter of 2018 are approximately \$69 million in revenue and \$48 million of operating income related to CREIT since the date of acquisition, excluding the impact of acquisition transaction costs and any adjustment to the fair value of the investment properties acquired.

On a year-to-date pro forma basis, the impact of the CREIT acquisition on Choice Properties revenue and net income in the first half of 2018 would have amounted to approximately \$210 million and \$75 million, respectively, excluding the impact of acquisition transaction costs and any adjustment to the fair value of the investment properties acquired. This pro forma information incorporates the effect of the preliminary purchase equation as if the acquisition had been effective January 1, 2018.

The following table provides the impacts of the acquisition of CREIT on the consolidated results of the Company in the second quarter of 2018:

(\$ millions unless where otherwise indicated)	12 Weeks Ended Jun. 16, 2018
Revenue	\$ 69
Adjusted EBITDA <sup>(1)</sup>	48
Adjusted net interest expense and other financing charges <sup>(1)</sup>	48
Adjusted net earnings available to common shareholders of the Company <sup>(1)</sup>	—
Adjusted diluted net earnings per common share <sup>(1)</sup> (\$)	—

On a year-to-date pro forma basis, the impact of the CREIT acquisition on the Company's revenue and net income attributable to shareholders of the Company in the first half of 2018 would have amounted to approximately \$207 million and \$5 million, respectively, excluding the impact in the quarter of acquisition transaction costs and any adjustment to the fair value of the investment properties acquired. This pro forma information incorporates the effect of the preliminary purchase equation as if the acquisition had been effective January 1, 2018.

## LIQUIDITY AND CAPITAL RESOURCES

### CASH FLOWS

(\$ millions) For the periods ended as indicated	12 Weeks Ended			24 Weeks Ended		
	Jun. 16, 2018	Jun. 17, 2017	Change	Jun. 16, 2018	Jun. 17, 2017	Change
Cash and cash equivalents, beginning of period	\$ 1,575	\$ 1,324	\$ 251	\$ 2,034	\$ 1,560	\$ 474
Cash flows from operating activities	601	916	(315)	1,059	1,300	(241)
Cash flows used in investing activities	(532)	(374)	(158)	(1,903)	(511)	(1,392)
Cash flows (used in) from financing activities	(159)	(337)	178	294	(821)	1,115
Effect of foreign currency exchange rate changes on cash and cash equivalents	2	(3)	5	3	(2)	5
Cash and cash equivalents, end of period	\$ 1,487	\$ 1,526	\$ (39)	\$ 1,487	\$ 1,526	\$ (39)

**Cash Flows from Operating Activities** The decrease in cash inflows in the second quarter of 2018 was \$315 million, primarily driven by:

- unfavourable changes in non-cash working capital;
- a decrease in provision balances;
- lower cash earnings; and
- an increase in income taxes paid.

The year-over-year decrease in cash inflows in the second quarter of 2018 was \$241 million, primarily driven by:

- unfavourable changes in non-cash working capital;
- a decrease in provision balances; and
- lower cash earnings;

partially offset by,

- a decrease in income taxes paid.

**Cash Flows used in Investing Activities** Cash flows used in the second quarter of 2018 was \$532 million, an increase of \$158 million, compared to the second quarter of 2017, driven by cash paid in connection to the acquisition of CREIT, partially offset by the decrease in security deposits.

Year-to-date cash flows used in investing activities was \$1,903 million, an increase of \$1,392 million compared to the same period in 2017. The increase in cash flows used in the quarter was driven by cash paid related to the acquisition of CREIT and a decrease in security deposits. The year-to-date cash flows used was primarily driven by cash paid related to the acquisition of CREIT.

The following table summarizes the Company's capital investments by each of its reportable operating segments:

(\$ millions) For the periods ended as indicated	12 Weeks Ended			24 Weeks Ended		
	Jun. 16, 2018	Jun. 17, 2017	Change	Jun. 16, 2018	Jun. 17, 2017	Change
Weston Foods	\$ 38	\$ 33	\$ 5	\$ 60	\$ 66	\$ (6)
Loblaw	246	254	(8)	468	408	60
Total capital investments	\$ 284	\$ 287	\$ (3)	\$ 528	\$ 474	\$ 54

## Management's Discussion and Analysis

**Cash Flows (used in) from Financing Activities** The cash used in financing activities in the second quarter of 2018 was \$159 million, a decrease of \$178 million compared to the second quarter of 2017, driven by Loblaw's higher net issuances of long term debt primarily related to the acquisition of CREIT, partially offset by a decrease in bank indebtedness and higher repurchases of Loblaw's common shares.

Year-to-date cash inflows from financing activities was \$294 million, an increase of \$1,115 million compared to the same period in 2017. The increase in year-to-date cash inflows from financing activities was driven by Loblaw's higher net issuances of long term debt primarily related to the acquisition of CREIT, partially offset by higher repurchases of Loblaw's common shares and the timing of Loblaw's dividends paid.

The Company's significant long term debt transactions are set out in the "Components of Total Debt" section of this MD&A.

### Free Cash Flow<sup>(1)</sup>

(\$ millions) For the periods ended as indicated	12 Weeks Ended			24 Weeks Ended		
	Jun. 16, 2018	Jun. 17, 2017	Change	Jun. 16, 2018	Jun. 17, 2017	Change
Cash flows from operating activities	\$ 601	\$ 916	\$ (315)	\$ 1,059	\$ 1,300	\$ (241)
Less: Interest paid	104	86	18	283	257	26
Fixed asset purchases	210	207	3	368	340	28
Intangible asset additions	74	80	(6)	160	134	26
Free cash flow <sup>(1)</sup>	\$ 213	\$ 543	\$ (330)	\$ 248	\$ 569	\$ (321)

The year-over-year free cash flow<sup>(1)</sup> in the second quarter of 2018 was \$213 million, a decrease of \$330 million compared to the second quarter of 2017. The decrease in free cash flow<sup>(1)</sup> was primarily due to lower cash flow from operating activities and higher interest paid.

On a year-to-date basis, the free cash flow<sup>(1)</sup> was \$248 million, a decrease of \$321 million compared to the same period in 2017. The decrease in free cash flow<sup>(1)</sup> was primarily driven by lower cash flow from operating activities, an increase in capital investments and higher interest paid.

### LIQUIDITY

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

Loblaw expects that cash and cash equivalents, short term investments, future operating cash flows and the amounts available to be drawn against committed credit facilities will enable it to finance its capital investment program and fund its ongoing business requirements, including working capital, pension plan funding requirements and financial obligations, over the next 12 months. Financial Services expects to obtain long term financing for the growth of its credit card receivables through the issuance of *Eagle Credit Card Trust*<sup>®</sup> ("Eagle") notes and Guaranteed Investment Certificates ("GICs"). Choice Properties expects to obtain long term financing for the acquisition of properties primarily through the issuance of equity and unsecured debentures.

For details on the Company's cash flows, see the "Cash Flows" section of this MD&A.

**Total Debt** The following table presents total debt, as monitored by management:

(\$ millions)	Jun. 16, 2018	As at	
		Jun. 17, 2017	Dec. 31, 2017
Bank indebtedness	\$ 248	\$ 320	\$ 110
Short term debt	1,230	1,156	1,258
Long term debt due within one year	2,623	581	1,635
Long term debt	12,918	11,253	10,457
Certain other liabilities	43	33	41
Fair value of financial derivatives related to the above debt	(475)	(368)	(435)
<b>Total debt</b>	<b>\$ 16,587</b>	<b>\$ 12,975</b>	<b>\$ 13,066</b>

Management targets credit metrics consistent with those of an investment grade profile. The Company (excluding Loblaw) holds significant cash and cash equivalents and short term investments and as a result monitors its leverage on a net debt basis. The Company (excluding Loblaw) has total debt of \$1,080 million (June 17, 2017 – \$1,143 million; December 31, 2017 – \$1,098 million) and cash and cash equivalents and short term investments of \$770 million (June 17, 2017 – \$891 million; December 31, 2017 – \$803 million), resulting in a \$310 million net debt position (June 17, 2017 – \$252 million net debt position; December 31, 2017 – \$295 million net debt position).

Loblaw’s management is focused on managing its capital structure on a segmented basis to ensure that each of its operating segments is employing a capital structure that is appropriate for the industry in which it operates.

- Loblaw targets maintaining Retail credit metrics consistent with those of investment grade retailers. Loblaw monitors the Retail segment’s debt to rolling year adjusted EBITDA<sup>(1)</sup> ratio as a measure of the leverage being employed. The Retail segment’s debt to rolling year adjusted EBITDA<sup>(1)</sup> ratio as at the end of the second quarter of 2018 was decreased compared to the second quarter of 2017 and flat compared to year end 2017. The decrease in the Loblaw Retail segment’s debt to rolling year adjusted EBITDA<sup>(1)</sup> ratio compared to the second quarter of 2017 was primarily as a result of a decrease in Retail segment’s debt.
- PC Bank 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.
- Choice Properties targets maintaining credit metrics consistent with those of investment grade Real Estate Investment Trusts (“REIT”). Choice Properties monitors metrics relevant to the REIT industry including targeting an appropriate debt to total assets ratio. In connection with the acquisition of CREIT, Choice Properties entered into \$1.3 billion of senior unsecured debentures in the first quarter of 2018 and obtained \$800 million through two unsecured term loan facilities in the second quarter of 2018.

**Covenants and Regulatory Requirements** The Company, Loblaw and Choice Properties are required to comply with certain financial covenants for various debt instruments. As at the end of the second quarter of 2018 and throughout the first half of 2018, the Company, Loblaw and Choice Properties were in compliance with their respective covenants. As at the end of the second quarter of 2018 and throughout the second quarter, PC Bank and Choice Properties have met all applicable regulatory requirements.

**Short Form Base Shelf Prospectus** In the first quarter of 2018, Choice Properties filed a Short Form Base Shelf Prospectus, which allows for the potential issuance of up to \$2 billion of Trust Units and debt securities, or any combination thereof, over a 25-month period. Under this prospectus, Choice Properties issued \$650 million of senior unsecured debentures.

In the first quarter of 2018, GWL filed a Short Form Base Shelf Prospectus allowing for the issuance of up to \$1 billion of senior and subordinated debt securities, and preferred shares, or any combination thereof over a 25-month period.

## Management's Discussion and Analysis

### COMPONENTS OF TOTAL DEBT

**Debentures and Medium Term Notes ("MTNs")** The following table summarizes the debentures and MTNs issued or assumed in the periods ended as indicated:

(\$ millions)	Interest Rate	Maturity Date	12 Weeks Ended	24 Weeks Ended
			Jun. 16, 2018	Jun. 16, 2018
			Principal Amount	Principal Amount
Choice Properties senior unsecured debentures				
– Series I <sup>(i)</sup>	3.01%	March 21, 2022	\$ —	\$ 300
– Series J <sup>(i)</sup>	3.55%	January 10, 2025	—	350
– Series K <sup>(ii)</sup>	3.56%	September 9, 2024	—	550
– Series L <sup>(ii)</sup>	4.18%	March 8, 2028	—	750
– Series A-C <sup>(iii)</sup>	3.68%	July 24, 2018	125	125
– Series B-C <sup>(iii)</sup>	4.32%	January 15, 2021	100	100
– Series C-C <sup>(iii)</sup>	2.56%	November 30, 2019	100	100
– Series D-C <sup>(iii)</sup>	2.95%	January 18, 2023	125	125
<b>Total debentures and MTNs issued</b>			<b>\$ 450</b>	<b>\$ 2,400</b>

(i) Offerings were made under the Choice Properties' Short Form Base Shelf Prospectus filed in the first quarter of 2018.

(ii) The net proceeds from the issuance of Series K and L were held in escrow as a part of the financing for the acquisition of CREIT.

During the second quarter of 2018, the Company completed the acquisition of CREIT and the proceeds were released from escrow.

(iii) Assumed by Loblaw in connection with the acquisition of CREIT.

There were no MTNs issued in the comparative periods in 2017.

The following table summarizes the debentures and MTNs repaid in the periods ended as indicated:

(\$ millions)	Interest Rate	Maturity Date	12 Weeks Ended		24 Weeks Ended	
			Jun. 16, 2018	Jun. 17, 2017	Jun. 16, 2018	Jun. 17, 2017
			Principal Amount	Principal Amount	Principal Amount	Principal Amount
Shoppers Drug Mart Notes	2.36%	May 24, 2018	\$ 275	\$ —	\$ 275	\$ —
Choice Properties senior unsecured debentures						
– Series A	3.55%	July 5, 2018 <sup>(i)</sup>	—	—	400	—
– Series 6	3.00%	April 20, 2017 <sup>(ii)</sup>	—	—	—	200
<b>Total debentures and MTNs repaid</b>			<b>\$ 275</b>	<b>\$ —</b>	<b>\$ 675</b>	<b>\$ 200</b>

(i) Redeemed on February 12, 2018.

(ii) Redeemed on January 23, 2017.

**Unsecured Term Loan Facilities** In the second quarter of 2018, Choice Properties obtained \$800 million through two unsecured term loan facilities, one \$175 million 4-year unsecured term loan provided by syndicate of lenders maturing May 4, 2022 and one \$625 million 5-year unsecured term loan provided by a syndicate of lenders maturing May 4, 2023. The term loans bear interest at variable rates of either Prime plus 0.45% or bankers' acceptance rate plus 1.45%. The pricing of these term loans is contingent on Choice Properties credit ratings from DBRS and S&P remaining at "BBB".

**Committed Credit Facilities** The components of the committed lines of credit available were as follows:

(\$ millions)	Maturity Date	Jun. 16, 2018		As at			
		Available Credit	Drawn	Jun. 17, 2017		Dec. 31, 2017	
				Available Credit	Drawn	Available Credit	Drawn
Loblaw committed credit facility	June 10, 2021	\$ 1,000	\$ —	\$ 1,000	\$ —	\$ 1,000	\$ —
Choice Properties committed bi-lateral credit facility	December 21, 2018	—	—	250	250	250	250
Choice Properties committed syndicated credit facility	July 5, 2022	—	—	500	214	500	311
Choice Properties committed syndicated credit facility	May 4, 2023	1,500	182	—	—	—	—
Total committed lines of credit		\$ 2,500	\$ 182	\$ 1,750	\$ 464	\$ 1,750	\$ 561

In the first half of 2018, Choice Properties repaid and cancelled the \$250 million committed bi-lateral credit facility and the \$500 million committed syndicated credit facility.

During the second quarter of 2018, Choice Properties entered into a new syndicated \$1.5 billion senior unsecured committed revolving credit facility maturing May 4, 2023. The credit facility bears interest at variable rates of either: Prime plus 0.45% or bankers' acceptance rate plus 1.45%. The pricing of this credit facility is contingent on Choice Properties' credit ratings from DBRS and S&P remaining at "BBB".

**Independent Securitization Trusts** Loblaw, 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 the 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)	As at		
	Jun. 16, 2018	Jun. 17, 2017	Dec. 31, 2017
Securitized to independent securitization trusts:			
Securitized to <i>Eagle</i>	\$ 900	\$ 650	\$ 900
Securitized to Other Independent Securitization Trusts	590	560	640
Total securitized to independent securitization trusts	\$ 1,490	\$ 1,210	\$ 1,540

Subsequent to the second 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 the issuance, \$250 million of bond forward agreements were settled after the quarter, resulting in a realized fair value loss of \$1 million and a net effective interest rate of 3.15% on the *Eagle* note issued.

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 the end of the second quarter of 2018 and throughout the first half of 2018.

**Independent Funding Trusts** As at the end of the second quarter of 2018, the independent funding trusts had drawn \$549 million (June 17, 2017 – \$555 million; December 31, 2017 – \$551 million) from the revolving committed credit facility that is the source of funding to the independent funding trusts. Loblaw provides credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trusts in the amount of \$64 million (June 17, 2017 and December 31, 2017 – \$64 million), representing not less than 10% (June 17, 2017 and December 31, 2017 – not less than 10%) of the principal amount of loans outstanding.

## Management's Discussion and Analysis

### FINANCIAL CONDITION

	Jun. 16, 2018	As at	
		Jun. 17, 2017	Dec. 31, 2017
Rolling year adjusted return on average equity attributable to common shareholders of the Company <sup>(1)</sup>	12.7%	12.7%	12.8%
Rolling year adjusted return on capital <sup>(1)</sup>	11.5%	12.6%	12.9%

The rolling year adjusted return on average equity attributable to common shareholders of the Company<sup>(1)</sup> remained flat as at the end of the second quarter of 2018 compared to the end of the second quarter of 2017, and slightly decreased compared to year end 2017.

The rolling year adjusted return on capital<sup>(1)</sup> decreased as at the end of the second quarter of 2018 compared to the end of the second quarter of 2017 and year end 2017, primarily due to increase in long term debt and Loblaw's earnings, partially offset by Loblaw's shares repurchased for cancellation.

### CREDIT RATINGS

Subsequent to the second quarter of 2018, Standard & Poor's reaffirmed credit ratings and outlook for GWL and Loblaw.

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

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

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

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

The following table sets out the current credit ratings of Choice Properties:

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

## SHARE CAPITAL

**Common Share Capital** The following table summarizes the activity in the Company's common shares issued and outstanding for the periods ended as indicated:

(\$ millions except where otherwise indicated)	12 Weeks Ended				24 Weeks Ended			
	Jun. 16, 2018		Jun. 17, 2017		Jun. 16, 2018		Jun. 17, 2017	
	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	127,956,198	\$ 226	127,903,707	\$ 195	127,905,581	\$ 221	127,898,582	\$ 195
Issued for settlement of stock options	48,053	4	15,125	1	100,298	9	20,250	1
Purchased and cancelled	—	—	—	—	(1,628)	—	—	—
Issued and outstanding, end of period	128,004,251	\$ 230	127,918,832	\$ 196	128,004,251	\$ 230	127,918,832	\$ 196
Shares held in trusts, beginning of period	(134,128)	—	(264,296)	—	(228,803)	—	(266,999)	—
Released for settlement of RSUs and PSUs	4,332	—	95,530	—	99,007	—	98,233	—
Shares held in trusts, end of period	(129,796)	—	(168,766)	—	(129,796)	—	(168,766)	—
Issued and outstanding net of shares held in trusts, end of period	127,874,455	\$ 230	127,750,066	\$ 196	127,874,455	\$ 230	127,750,066	\$ 196
Weighted average outstanding, net of shares held in trusts	127,838,376		127,732,859		127,776,173		127,683,476	

### Normal Course Issuer Bid ("NCIB") Program

There was no NCIB activity under its NCIB program in the second quarter of 2018 and 2017.

In the second quarter of 2018, GWL renewed its NCIB program to purchase on the Toronto Stock Exchange ("TSX") or through alternative trading systems up to 6,398,134 of its common shares, representing approximately 5% of the common shares outstanding. In accordance with the rules and regulations of the TSX, any purchases must be at the then market price of such shares. As of June 16, 2018, the Company did not purchase any common shares under its current NCIB program.

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

(\$)	12 Weeks Ended		24 Weeks Ended	
	Jun. 16, 2018	Jun. 17, 2017	Jun. 16, 2018	Jun. 17, 2017
Dividends declared per share <sup>(i)</sup> :				
Common share	\$ 0.490	\$ 0.455	\$ 0.945	\$ 0.895
Preferred share:				
Series I	\$ 0.3625	\$ 0.3625	\$ 0.7250	\$ 0.7250
Series III	\$ 0.3250	\$ 0.3250	\$ 0.6500	\$ 0.6500
Series IV	\$ 0.3250	\$ 0.3250	\$ 0.6500	\$ 0.6500
Series V	\$ 0.296875	\$ 0.296875	\$ 0.593750	\$ 0.593750

(i) Dividends declared on common shares and Preferred Shares, Series III, Series IV and Series V were paid on July 1, 2018. Dividends declared on Preferred Shares, Series I were paid on June 15, 2018.

## Management's Discussion and Analysis

The following table summarizes the Company's cash dividends declared subsequent to the end of the second quarter of 2018:

(\$)

Dividends declared per share <sup>(i)</sup> – Common share	\$	<b>0.49</b>
– Preferred share:		
Series I	\$	<b>0.3625</b>
Series III	\$	<b>0.3250</b>
Series IV	\$	<b>0.3250</b>
Series V	\$	<b>0.296875</b>

(i) Dividends declared on common shares and Preferred Shares, Series III, Series IV and Series V are payable on October 1, 2018. Dividends declared on Preferred Shares, Series I are payable on September 15, 2018.

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

### 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 the Company's off-balance sheet arrangements during the second quarter of 2018. For a discussion of the Company's significant off-balance sheet arrangements see Section 7.7, "Off-Balance Sheet Arrangements", of the Company's 2017 Annual Report.

## QUARTERLY RESULTS OF OPERATIONS

The Company's year end is December 31. Activities are reported on a fiscal year ending on the Saturday closest to December 31. As a result, the Company's fiscal year is usually 52 weeks in duration but includes a 53rd week every five to six years. Each of the years ended December 31, 2017 and December 31, 2016 contained 52 weeks. 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. When a fiscal year contains 53 weeks, the fourth quarter is 13 weeks in duration.

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.

### Selected Quarterly Information

(\$ millions except where otherwise indicated)	Second Quarter		First Quarter		Fourth Quarter		Third Quarter	
	2018 (12 weeks)	2017 <sup>(3)</sup> (12 weeks)	2018 (12 weeks)	2017 <sup>(3)</sup> (12 weeks)	2017 <sup>(3)</sup> (12 weeks)	2016 (12 weeks)	2017 <sup>(3)</sup> (16 weeks)	2016 (16 weeks)
Sales	\$ 11,245	\$ 11,436	\$ 10,744	\$ 10,803	\$ 11,402	\$ 11,519	\$ 14,648	\$ 14,605
Operating income	589	640	502	513	164	491	1,244	782
Adjusted EBITDA <sup>(1)</sup>	1,073	1,038	918	927	1,065	1,027	1,307	1,242
Depreciation and amortization <sup>(i)</sup>	400	385	400	384	407	392	509	497
Net earnings	78	365	378	242	78	231	904	487
Net earnings attributable to shareholders of the Company	38	170	190	118	44	92	434	268
Net earnings available to common shareholders of the Company	28	160	180	108	34	82	420	254
Net earnings per common share (\$) - basic	\$ 0.22	\$ 1.25	\$ 1.41	\$ 0.85	\$ 0.27	\$ 0.64	\$ 3.29	\$ 1.99
Net earnings per common share (\$) - diluted	\$ 0.21	\$ 1.23	\$ 1.40	\$ 0.84	\$ 0.27	\$ 0.64	\$ 3.25	\$ 1.97
Adjusted diluted net earnings per common share <sup>(1)</sup> (\$)	\$ 1.63	\$ 1.67	\$ 1.38	\$ 1.43	\$ 1.76	\$ 1.59	\$ 2.14	\$ 2.06
Weston Foods sales (decline) growth	(8.1)%	2.6 %	(4.1)%	(4.1)%	(1.9)%	1.9 %	(0.7)%	3.7%
Weston Foods sales (decline) growth excluding impact of foreign currency translation	(5.7)%	0.2 %	(1.5)%	(1.6)%	0.9 %	2.1 %	1.0 %	3.7%
Average quarterly national food price inflation (deflation) (as measured by CPI)	0.1 %	(1.4)%	1.2 %	(3.9)%	1.0 %	(2.3)%	0.3 %	0.2%
Food retail same-store sales growth (decline)	0.8 %	1.2 %	1.9 %	(1.2)%	0.5 %	1.1 %	1.4 %	0.8%
Drug retail same-store sales growth	1.7 %	3.7 %	3.7 %	0.9 %	3.6 %	3.4 %	3.3 %	2.8%

(i) Depreciation and amortization includes amortization of intangible assets acquired with Shoppers Drug Mart recorded by Loblaw and accelerated depreciation recorded by Weston Foods, related to restructuring and other related costs.

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

## Management's Discussion and Analysis

### Net Earnings Available to Common Shareholders of the Company and Diluted Net Earnings Per Common Share

Consolidated quarterly net earnings available to common shareholders of the Company and diluted net earnings per common share for the last eight quarters were impacted by the following items:

- underlying operating performance of each of the Company's reportable operating segments;
- the disposition of Loblaw's gas bar operations in the third quarter of 2017;
- net synergies associated with Loblaw's acquisition of Shoppers Drug Mart;
- the impact of Loblaw's store closure plan;
- the favourable impact of Loblaw's share repurchases for cancellation; and
- the impact of certain adjusting items as set out in the "Non-GAAP Financial Measures" section of this MD&A, including:
  - amortization of intangible assets acquired with Shoppers Drug Mart;
  - restructuring and other related costs;
  - the *PC Optimum* program;
  - asset impairments, net of recoveries;
  - the change in fair value adjustment to the Trust Unit liability;
  - the Loblaw Card Program;
  - CREIT acquisition and other related costs; and
  - the impact of healthcare reform on inventory balances;partially offset by,
  - gain on disposition of Loblaw's gas bar operations;
  - the statutory corporate tax rate change;
  - Loblaw's wind-down of PC Financial banking services; and
  - the change in fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares.

### 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 controls over financial reporting in the second quarter of 2018 that materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting, except as noted below:

As permitted by the provisions of National Instrument 52-109, "Certification of Disclosures in Issuers' Annual and Interim Filings", management, including the CEO and CFO, have limited the scope of their design of the Company's disclosure controls and procedures and internal control over financial reporting to exclude controls, policies and procedures of CREIT. Choice Properties acquired the assets and liabilities of CREIT and its subsidiaries on May 4, 2018.

CREIT's contribution to the Company's consolidated financial statements for the quarter ended June 17, 2018 was approximately 0.6% of revenue, approximately 8.1% of operating income, excluding the impact in the quarter of acquisition transaction costs and any adjustment to the fair value of the investment properties acquired, and approximately 95% of investment properties. CREIT had a nominal impact on net earnings available to common shareholders of the Company in the second quarter of 2018.

The scope limitation is primarily based on the time required to assess CREIT's disclosure controls and procedures and internal controls over financial reporting in a manner consistent with the Company's other operations. The assessment on CREIT's design effectiveness of disclosure controls and procedures and internal controls over financial reporting is expected to be completed by the first quarter of 2019. Further details related to the acquisition of CREIT are set out in Loblaw Segment Results and in Note 3 Business Acquisitions of the Company's unaudited interim period condensed consolidated financial statements for the second quarter of 2018.

## **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 31, 2017 and the MD&A included in the Company's 2017 Annual Report, which are hereby incorporated by reference. The Company's 2017 Annual Report and AIF are available online on [www.sedar.com](http://www.sedar.com). Those risks and risk management strategies remain unchanged, inclusive of the acquisition of CREIT.

## **ACCOUNTING STANDARDS**

### **Accounting Standards Implemented in 2018**

On January 1, 2018, the Company implemented IFRS 15, "Revenue from Contracts with Customers" ("IFRS 15") and IFRS 9, "Financial Instruments" ("IFRS 9"), in accordance with IAS 8, "Accounting Policies, Changes in Accounting Estimates and Errors". The impacts on implementation of IFRS 15 and IFRS 9 on the Company's condensed consolidated financial statements are described below.

**IFRS 15** In 2014, the IASB issued IFRS 15, "Revenue from Contracts with Customers", replacing IAS 18, "Revenue" ("IAS 18"), IAS 11, "Construction Contracts", and related interpretations. IFRS 15 provides a comprehensive framework for the recognition, measurement and disclosure of revenue from contracts with customers, excluding contracts within the scope of the accounting standards on leases, insurance contracts and financial instruments. IFRS 15 is effective for annual periods beginning on or after January 1, 2018.

The Company adopted the standard on January 1, 2018 and applied the requirements of the standard retrospectively with the cumulative effects of initial application recorded in opening retained earnings on January 1, 2017 and with the restatement of comparative periods. IFRS 15 permits the use of exemptions and practical expedients. The Company applied the practical expedient in which contracts that began and were completed within the same annual reporting period before December 31, 2017 or are completed on January 1, 2017 do not require restatement.

The implementation of IFRS 15 did not have a significant impact on Weston Foods or Loblaw's segment revenue streams, including Loblaw's franchise arrangements with non-consolidated stores. IFRS 15 impacted the allocation of revenue that is deferred in relation to the Loblaw's customer loyalty award programs. Under IAS 18 and related interpretations, revenue was allocated to the customer loyalty awards using the residual fair value method. Under this method, a portion of the consideration equaling the fair value of the points was allocated to the loyalty awards and deferred until the points were ultimately redeemed. The residual consideration was allocated to the goods and services sold and recognized as revenue. Under IFRS 15, consideration will be allocated between the loyalty awards and the goods and services on which the awards were earned, based on their relative stand-alone selling prices. Using this relative fair value approach, the amount allocated to the loyalty points and recorded as deferred revenue will be, on average, lower than the amounts allocated under the residual value method. The majority of Loblaw's loyalty liability, which is a contract liability, is expected to be redeemed and recognized as revenue within one year of issuance.

## Management's Discussion and Analysis

In addition, in the fourth quarter of 2017, Loblaw recorded a charge of \$189 million under IAS 18 and related interpretations, related to the revaluation of the existing loyalty liability for outstanding points to reflect a higher anticipated redemption rate under the new *PC Optimum* program. Under IFRS 15, using the relative fair value approach, this revaluation of the loyalty liability decreases by \$24 million resulting in a charge before income taxes of \$165 million.

The impact of the above changes on equity as at January 1, 2017 and December 31, 2017 is as follows:

### Consolidated Balance Sheets

Increase (Decrease) (\$ millions)	As at January 1, 2017	As at December 31, 2017
Loyalty liability	\$ (43)	\$ (64)
Income taxes payable	12	11
Deferred income tax liabilities	—	7
Equity	31	46

The impact of this change on the comparative period as at June 17, 2017, and for 12 weeks and 24 weeks ended June 17, 2017 is as follows:

### Condensed Consolidated Balance Sheets

Increase (Decrease) (\$ millions)	As at June 17, 2017
Loyalty liability	\$ (47)
Income taxes payable	13
Equity	34

### Condensed Consolidated Statement of Earnings

Increase (Decrease) (\$ millions)	12 Weeks Ended June 17, 2017	24 Weeks Ended June 17, 2017
Revenue	\$ 1	\$ 4
Income taxes	—	1

The implementation of IFRS 15 had a nominal impact on earnings per share for the comparative periods.

The quarterly and annual impacts of this change in 2017 are as follows:

### Summary of Condensed Consolidated Quarterly Statement of Earnings

Increase (Decrease) (\$ millions)	March 25, 2017 (12 weeks)	June 17, 2017 (12 weeks)	October 7, 2017 (16 weeks)	December 31, 2017 (12 weeks)	December 31, 2017 (52 weeks)
Revenue	\$ 3	\$ 1	\$ —	\$ (7)	\$ (3)
SG&A	—	—	—	(24)	(24)
Income taxes	1	—	—	5	6
Net earnings	2	1	—	12	15

**IFRS 9** In 2014, the IASB issued IFRS 9, “Financial Instruments”, replacing IAS 39, “Financial Instruments: Recognition and Measurement” (“IAS 39”), and related interpretations. IFRS 9 includes revised guidance on the classification and measurement of financial assets, including impairment and a new general hedge accounting model. IFRS 9 is effective for annual periods beginning on or after January 1, 2018. The Company implemented the new requirements for classification and measurement, impairment and general hedging on December 31, 2017 by applying the requirements for classification and measurement, including impairment, retrospectively with the cumulative effects of initial application recorded in opening retained earnings as at December 31, 2017 with no restatement of comparative periods. The Company also applied related amendments to IFRS 7, “Financial Instruments: Disclosures”.

*Classification and measurement* IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics. Financial assets are classified and measured based on these categories: amortized cost, fair value through other comprehensive income, and fair value through profit and loss. Financial liabilities are classified and measured based on two categories: amortized cost or fair value through profit and loss. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are not separated, but the hybrid financial instrument as a whole is assessed for classification.

The following table summarizes the classification impacts upon adoption of IFRS 9. The adoption of the new classification requirements under IFRS 9 did not result in significant changes in measurement or the carrying amount of financial assets and liabilities, with the exception of credit card receivables as noted below.

<b>Asset/Liability</b>	<b>Classification under IAS 39</b>	<b>Classification under IFRS 9</b>
Cash and cash equivalents	Fair value through profit and loss <sup>(i)</sup>	Amortized cost
Short term investments	Fair value through profit and loss <sup>(i)</sup>	Amortized cost
Accounts receivable	Loans and receivables	Amortized cost
Credit card receivables	Loans and receivables	Amortized cost
Security deposits	Fair value through profit and loss <sup>(i)</sup>	Fair value through profit and loss
Franchise loans receivable	Loans and receivables	Amortized cost
Certain other assets <sup>(ii)</sup>	Loans and receivables	Amortized cost/fair value through profit and loss
Certain long term investments	Available-for-sale	Fair value through other comprehensive income
Bank indebtedness	Other liabilities	Amortized cost
Trade payables and other liabilities	Other liabilities	Amortized cost
Short term debt	Other liabilities	Amortized cost
Long term debt	Other liabilities	Amortized cost
Trust Unit liability	Fair value through profit and loss <sup>(iii)</sup>	Fair value through profit and loss
Certain other liabilities	Other liabilities	Amortized cost
Derivatives	Fair value through profit and loss <sup>(iii)</sup>	Fair value through profit and loss

(i) Financial instruments designated at fair value through profit and loss.

(ii) Certain other assets Include mortgages, loans and notes receivable which are classified as either amortized cost or fair value through profit and loss.

(iii) Financial instruments required to be classified at fair value through profit and loss.

Financial assets are not reclassified subsequent to their initial recognition, unless the Company identifies changes in its business model in managing financial assets.

*Impairment* IFRS 9 replaces the ‘incurred loss’ model in IAS 39 with a forward-looking ‘expected credit loss’ (“ECL”) model. The ECL model requires considerable judgment, including consideration of how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. The new impairment model is applied, at each balance sheet date, to financial assets measured at amortized cost or those measured at fair value through other comprehensive income, except for investments in equity instruments.

IFRS 9 outlines a three-stage approach to recognizing ECL which is intended to reflect the increase in credit risks of a financial instrument. The Company applies the ECL model to assess for impairment on its financial assets at each balance sheet date. Loblaw, through PC Bank, recognizes loss allowances based on ECL on credit card receivables, which are measured at amortized costs. Credit card receivables are assessed collectively for impairment, applying the three-stage approach on assessing the impairment on credit card receivables as described below.

- Stage 1 is comprised of all financial instruments that have not had a significant increase in credit risks since initial recognition or that have low credit risk at the reporting date. PC Bank is required to recognize impairment for Stage 1 financial instruments based on the expected losses over the expected life of the instrument arising from loss events that could occur during the 12 months following the reporting date.

## Management's Discussion and Analysis

- Stage 2 is comprised of all financial instruments that have had a significant increase in credit risks since initial recognition but that do not have objective evidence of a credit loss event. For Stage 2 financial instruments the impairment is recognized based on the expected losses over the expected life of the instrument arising from loss events that could occur over the expected life. PC Bank is required to recognize a lifetime ECL for Stage 2 financial instruments.
- Stage 3 is comprised of all financial instruments that have objective evidence of impairment at the reporting date. PC Bank is required to recognize impairment based on a lifetime ECL for Stage 3 financial instruments.

In each stage of the impairment model, impairment is determined based on the probability of default, loss given default, and expected exposures at default on drawn and undrawn exposures on credit card receivables, discounted using an average portfolio yield rate. The application of the ECL model required PC Bank to apply the following significant judgments, assumptions and estimations:

- Movement of impairment measurement between the three stages of the ECL model, based on the assessment of increase in credit risks on credit card receivables. The assessment of changes in credit risks includes qualitative and quantitative factors of the accounts, such as historical credit loss experience and external credit scores;
- Thresholds for significant increase in credit risks based on changes in probability of default over the expected life of the instrument relative to initial recognition; and
- Forecasts of future economic conditions.

The ECL model had a significant impact on PC Bank's impairment of credit card receivables. The Company revised certain inputs of the ECL model since the implementation of IFRS 9 in the first quarter of 2018 and has retrospectively applied the impact of these revisions with no impact to earnings in the first quarter of 2018. As a result of the refinements, the cumulative impact arising from the ECL model on the impairment of credit card receivables as at January 1, 2018 was as follows:

### Condensed Consolidated Balance Sheets

Increase (Decrease) (\$ millions)	As at January 1, 2018
Credit card receivables	\$ (98)
Deferred income tax assets	26
Income taxes payable	4
Deferred income tax liabilities	(4)
Equity	(72)

The Company also applied ECL models to the assessment of impairment on trade receivables and other financial assets of the Company. The Company adopted the practical expedient to determine ECL on trade receivables using a provision matrix based on historical credit loss experiences to estimate lifetime ECL. The ECL models applied to other financial assets also required judgment, assumptions and estimations on changes in credit risks, forecasts of future economic conditions and historical information on the credit quality of the financial asset. The provision matrix and ECL models applied do not have a material impact on trade receivables and other financial assets of the Company.

Impairment losses are recorded in the SG&A in the consolidated statement of earnings with the carrying amount of the financial asset or group of financial assets reduced through the use of impairment allowance accounts. In periods subsequent to the impairment where the impairment loss has decreased, and such decrease can be related objectively to conditions and changes in factors occurring after the impairment was initially recognized, the previously recognized impairment loss is reversed through the consolidated statement of earnings. The impairment reversal is limited to the lesser of the decrease in impairment or the extent that the carrying amount of the financial asset at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized, after the reversal.

*General hedging* IFRS 9 requires the Company to ensure that hedge accounting relationships are aligned with the Company's risk management objectives and strategy and to apply a more qualitative and forward-looking approach to assessing hedge effectiveness. The Company's risk management strategy and hedging activities are disclosed in the Company's 2017 Annual Report, Note 32 Financial Risk Management and in this Quarterly Report, Note 19 Financial Instruments.

### **Changes to Significant Accounting Policies**

The following significant accounting policies reflect certain impacts to the presentation of the Company's unaudited interim period condensed consolidated financial statements, resulting from the acquisition of CREIT. Upon closing of the acquisition, the significant accounting policies of CREIT were aligned to those of the Company.

**Investment Properties** Investment properties are properties owned by the Company that are held to either earn rental income, for capital appreciation, or both. The Company's investment properties include single tenant properties held to earn rental income and certain multiple tenant properties. Land and buildings leased to franchisees are not accounted for as investment properties as these properties are related to the Company's operating activities.

In conjunction with the acquisition of CREIT, the Company elects to change the measurement model of investment property assets from cost to fair value model retrospectively with restatement. Prior to the second quarter of 2018, the Company recognized investment property assets at costs 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. Under the discounted cash flow methodology, discount rates are applied to the projected annual operating cash flows, generally over a minimum term of ten years, including a terminal value of the investment properties based on a capitalization rate applied to the estimated net operating income, a non-GAAP measure, in the terminal year. 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.

The Company implemented the change retrospectively in the second quarter of 2018, and the impacts to comparative periods are as follow:

#### Consolidated Balance Sheets

Increase (Decrease) (\$ millions)	As at June 17, 2017	As at December 31, 2017	As at January 1, 2017
Investment Properties	\$ 41	\$ 41	\$ 41
Deferred income tax liabilities	5	5	5
Equity	36	36	36

The change in accounting policy had no impact on earnings per share for the comparative periods.

**Joint Arrangements** The Company, through Choice Properties, owned investment under joint arrangements. Joint arrangements are arrangements of which two or more parties have joint control. Joint control is the contractual sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control. Joint arrangements are classified as either joint operations or joint ventures depending on Choice Properties' rights and obligations in the arrangement based on factors such as the structure, legal form and contractual terms of the arrangement.

*Joint Ventures* A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint arrangement.

## Management's Discussion and Analysis

Choice Properties' investment in a joint venture is recorded using the equity method and is initially recognized in the consolidated balance sheet at cost and adjusted thereafter to recognize Choice Properties' share of the profit or loss and other comprehensive income of the joint venture. The Company's share of the joint venture's profit or loss is recognized in the Company's consolidated statements of income and other comprehensive income.

The financial statements of the equity-accounted investment are prepared for the same reporting period as the Company's. Where necessary, adjustments are made to bring the accounting policies in line with those of the Company's.

A joint venture is considered to be impaired if there is objective evidence of impairment, as a result of one or more events that occurred after initial recognition of the joint venture, and that event has a negative impact on the future cash flows of the joint venture that can be reliably estimated.

*Joint Operations* A joint operation is a joint arrangement whereby the parties that have joint control have rights to the assets and obligations for the liabilities relating to the arrangement.

The financial statements of the joint operations are prepared for the same reporting period as the Company's. Where necessary, adjustments are made to bring the accounting policies in line with those of the Company's.

The Company recognizes its proportionate share of assets, liabilities, revenues and expenses of joint operations.

**Cash-Settled Share-Based Compensation Plans** Transferred Restricted Units ("TRUs") issued by Choice Properties represent the unvested restricted unit plan acquired in connection with the acquisition of CREIT and are accounted for as cash-settled awards. The TRUs entitle certain employees of Choice Properties to receive the value of the TRU award in Trust Units at the end of the applicable vesting period, which is usually three years in length. The TRUs are subject to vesting conditions and disposition restrictions. The TRUs remain subject to forfeiture until the employee has remained employed with Choice Properties for a specified period of time. Depending on the nature of the grant, the TRUs are subject to a six- or seven-year holding period during which the TRUs cannot be disposed.

The fair value of each unvested TRU is measured based on the market value of a Trust Unit, less a discount to account for the vesting and holding period restriction placed on the TRUs, while taking into account expected forfeitures.

### Critical Accounting Estimates and Judgments

The following critical accounting estimate and judgment reflects the Company's election to change the measurement of investment properties from the cost model to the fair value model.

#### Investment Properties

**Judgments Made in Relation to Accounting Policies Applied** Judgment is applied in determining whether certain costs are additions to the carrying value of investment properties, identifying the point at which substantial completion of the property occurs, and identifying the directly attributable borrowing costs to be included in the carrying value of the development property.

The Company, through Choice Properties also applies judgment in determining whether the properties it acquires are considered to be asset acquisitions or business combinations.

**Key Sources of Estimation** The fair value of investment properties is dependent on available comparable transactions, future cash flows over the holding period and discount rates and capitalization rates applicable to those assets. The review of anticipated cash flows involves assumptions relating to occupancy, rental rates and residual value. In addition to reviewing anticipated cash flows, management assesses changes in the business climate and other factors, which may affect the ultimate value of the property. These assumptions may not ultimately be achieved.

## OUTLOOK<sup>(2)</sup>

In the second half of 2018, Weston Foods expects:

- Sales will trend in a similar fashion to the first half of 2018, when compared to last year. Sales are expected to be negatively impacted by volume declines, including the loss of sales from key customers and product rationalization;
- Adjusted EBITDA<sup>(1)</sup> will trend in similar fashion to the first half of 2018, when compared to last year. Adjusted EBITDA<sup>(1)</sup> will be impacted by sales trends as described above, headwinds from higher input and distribution costs in an inflationary environment and minimum wage increases, partially offset by improvements from the transformation program and productivity;
- Investment in capital expenditures of approximately \$230 million for 2018, related to growth, regulatory and maintenance; and
- Depreciation will increase.

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 Loblaw'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.

Headwinds from minimum wage increases and healthcare reform will negatively impact Loblaw's financial performance in 2018. The first half of the year was characterized by incremental cost headwinds and a very competitive retail market. In the second half, management expects cost pressures to increase, including from the newly imposed surtax on certain U.S. imports. Management continues to focus on overcoming these headwinds.

In 2018, on a full-year comparative basis, normalized for the disposition of Loblaw's gas bar business and the impact of the CREIT acquisition, Loblaw expects to:

- deliver positive same-store sales and stable gross margin in its Retail segment in a highly competitive market;
- deliver essentially flat adjusted net earnings<sup>(1)</sup> growth with positive adjusted earnings per share<sup>(1)</sup> growth based on our share buyback program;
- invest approximately \$1.3 billion in capital expenditures, including \$1.0 billion in its Retail segment; and
- return capital to shareholders by allocating a significant portion of free cash flow<sup>(1)</sup> to share repurchases.

For 2018, the Company expects adjusted net earnings<sup>(1)</sup> to be lower when compared to prior year due to the results of Weston Foods and Loblaw, as described above.

### NON-GAAP FINANCIAL MEASURES

The Company uses the following non-GAAP financial measures: adjusted EBITDA and adjusted EBITDA margin, adjusted net earnings attributable to shareholders of the Company, adjusted net earnings available to common shareholders of the Company, adjusted diluted net earnings per common share, rolling year adjusted return on average equity attributable to common shareholders of the Company, rolling year adjusted return on capital and free cash flow. In addition to these items, the following measures are used by management in calculating adjusted diluted net earnings per common share: adjusted operating income, adjusted net interest expense and other financing charges, adjusted income taxes and adjusted income tax rate. The Company believes these non-GAAP financial measures provide useful information to both management and investors in measuring the financial performance and financial condition of the Company for the reasons outlined below.

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

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

## Management's Discussion and Analysis

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

The following table reconciles adjusted EBITDA to operating income, which is reconciled to GAAP net earnings attributable to shareholders of the Company reported for the periods ended as indicated.

(unaudited) (\$ millions)	12 Weeks Ended				Jun. 17, 2017 <sup>(3)</sup>			
	Jun. 16, 2018				Weston Foods	Loblaw	Other	Consolidated
Net earnings attributable to shareholders of the Company				\$ 38				\$ 170
Add impact of the following:								
Non-controlling interests				40				195
Income taxes				126				140
Net interest expense and other financing charges				385				135
Operating income	\$ 21	\$ 559	\$ 9	\$ 589	\$ 24	\$ 625	\$ (9)	\$ 640
Add impact of the following:								
Amortization of intangible assets acquired with Shoppers Drug Mart	\$ —	\$ 119	\$ —	\$ 119	\$ —	\$ 121	\$ —	\$ 121
CREIT acquisition and other related costs	—	108	—	108	—	—	—	—
Fair value adjustment on investment properties	—	10	—	10	—	—	—	—
Loblaw Card Program	—	(11)	—	(11)	—	—	—	—
Pension annuities and buy-outs	—	1	—	1	—	—	—	—
Restructuring and other related costs	2	(5)	—	(3)	5	—	—	5
Fair value adjustment of derivatives	(2)	(6)	—	(8)	4	(1)	—	3
Wind-down of PC Financial banking services	—	(3)	—	(3)	—	—	—	—
Inventory loss, net of recoveries	(1)	—	—	(1)	(4)	—	—	(4)
Asset impairments, net of recoveries	—	—	—	—	—	—	3	3
Foreign currency translation <sup>(i)</sup>	—	—	(9)	(9)	—	—	6	6
Adjusting items	\$ (1)	\$ 213	\$ (9)	\$ 203	\$ 5	\$ 120	\$ 9	\$ 134
Adjusted operating income	\$ 20	\$ 772	\$ —	\$ 792	\$ 29	\$ 745	\$ —	\$ 774
Depreciation and amortization excluding the impact of the above adjustments <sup>(ii)</sup>	28	253	—	281	25	239	—	264
Adjusted EBITDA	\$ 48	\$ 1,025	\$ —	\$ 1,073	\$ 54	\$ 984	\$ —	\$ 1,038

(i) Represents the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and cash equivalents and short term investments held by foreign operations.

(ii) Depreciation and amortization for the calculation of adjusted EBITDA excludes \$119 million (2017 – \$121 million) of amortization of intangible assets, acquired with Shoppers Drug Mart, recorded by Loblaw.

(unaudited) (\$ millions)	24 Weeks Ended				Jun. 17, 2017 <sup>(3)</sup>			
	Jun. 16, 2018				Weston Foods	Loblaw	Other	Consolidated
Net earnings attributable to shareholders of the Company				\$ 228			\$	288
Add impact of the following:								
Non-controlling interests				228				319
Income taxes				232				241
Net interest expense and other financing charges				403				305
Operating income	\$ 31	\$ 1,037	\$ 23	\$ 1,091	\$ 47	\$ 1,118	\$ (12)	\$ 1,153
Add impact of the following:								
Amortization of intangible assets acquired with Shoppers Drug Mart	\$ —	\$ 240	\$ —	\$ 240	\$ —	\$ 242	\$ —	\$ 242
CREIT acquisition and other related costs	—	120	—	120	—	—	—	—
Impact of healthcare reform on inventory balances	—	19	—	19	—	—	—	—
Fair value adjustment on investment properties	—	10	—	10	—	—	—	—
Loblaw Card Program	—	8	—	8	—	—	—	—
Pension annuities and buy-outs	—	1	—	1	—	7	—	7
Restructuring and other related costs	17	(6)	—	11	14	—	—	14
Fair value adjustment of derivatives	(10)	(11)	—	(21)	9	5	—	14
Wind-down of PC Financial banking services	—	(20)	—	(20)	—	—	—	—
Inventory loss, net of recoveries	(1)	—	—	(1)	(4)	—	—	(4)
Asset impairments, net of recoveries	—	—	—	—	—	—	3	3
Foreign currency translation <sup>(i)</sup>	—	—	(23)	(23)	—	—	9	9
Adjusting items	\$ 6	\$ 361	\$ (23)	\$ 344	\$ 19	\$ 254	\$ 12	\$ 285
Adjusted operating income	\$ 37	\$ 1,398	\$ —	\$ 1,435	\$ 66	\$ 1,372	\$ —	\$ 1,438
Depreciation and amortization excluding the impact of the above adjustments <sup>(ii)</sup>	55	501	—	556	49	478	—	527
Adjusted EBITDA	\$ 92	\$ 1,899	\$ —	\$ 1,991	\$ 115	\$ 1,850	\$ —	\$ 1,965

- (i) Represents the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and cash equivalents and short term investments held by foreign operations.
- (ii) Depreciation and amortization for the calculation of adjusted EBITDA excludes \$240 million (2017 – \$242 million) of amortization of intangible assets, acquired with Shoppers Drug Mart, recorded by Loblaw and \$4 million (2017 – nil) of accelerated depreciation recorded by Weston Foods, related to restructuring and other related costs.

The following items impacted operating income in the second quarters of 2018 and 2017, and on a year-to-date basis:

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

**CREIT acquisition and other related costs** In the first half of 2018, Loblaw recorded acquisition and other related costs in connection with the acquisition of CREIT.

**Impact of healthcare reform on inventory balances** In the first quarter of 2018, Loblaw 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.

## Management's Discussion and Analysis

**Fair value adjustment to investment properties** In conjunction with the acquisition of CREIT, 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.

**Loblaw Card Program** In the fourth quarter of 2017, the Company and Loblaw acknowledged their involvement in an industry wide price-fixing arrangement. In connection with the arrangement, Loblaw is offering customers a \$25 Loblaw Card, which can be used to purchase items sold in Loblaw grocery stores across Canada. Loblaw has recorded a charge of \$107 million associated with the Loblaw Card Program in the fourth quarter of 2017. In the first quarter of 2018, Loblaw recorded an additional charge of \$19 million, and in the second quarter of 2018, Loblaw recorded a reversal of \$11 million.

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

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

**Fair value adjustment of derivatives** The Company is exposed to commodity price and U.S. dollar exchange rate fluctuations primarily as a result of purchases of certain raw materials, fuels and utilities. In accordance with the Company's commodity risk management policy, the Company enters into commodity and foreign currency derivatives to reduce the impact of price fluctuations in forecasted raw material and fuel purchases over a specified period of time. These derivatives are not acquired for trading or speculative purposes. Pursuant to the Company's derivative instruments accounting policy, certain changes in fair value, which include realized and unrealized gains and losses related to future purchases of raw materials and fuel, 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.

**Wind-down of PC Financial 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 payments of approximately \$44 million, net of related costs, which was recognized between the third quarter of 2017 and the second quarter of 2018.

**Inventory loss, net of recoveries** In 2016, Weston Foods' damaged inventory of \$11 million (U.S. \$9 million) was written-off and was recorded in SG&A in the Company's consolidated statement of earnings. The Company received partial proceeds from the insurance claim in 2018 and 2017. The insurance claim remains in progress and further proceeds are expected to be recorded as the claim progresses.

**Asset impairments, net of recoveries** At each balance sheet date, the Company assesses and, when required, records impairments and recoveries of previous impairments related to the carrying value of its fixed assets, investment properties, intangible and other assets.

**Foreign currency translation** The Company's consolidated financial statements are expressed in Canadian dollars. A portion of the Company's (excluding Loblaw's) net assets are denominated in U.S. dollars and as a result, the Company is exposed to foreign currency translation gains and losses. The impact of foreign currency translation on a portion of the U.S. dollar denominated net assets, primarily cash and cash equivalents and short term investments held by foreign operations, is recorded in SG&A and the associated tax, if any, is recorded in income taxes. In the second quarter of 2018, a foreign currency translation gain of \$9 million (2017 – loss of \$6 million) was recorded in SG&A as a result of the appreciation (2017 – depreciation) of the U.S. dollar relative to the Canadian dollar. Year-to-date, a foreign currency translation loss of \$23 million (2017 – gain of \$9 million) was recorded in SG&A as a results of the depreciation (2017 – appreciation) of the U.S. dollar relative to the Canadian dollar.

**Adjusted Net Interest Expense and Other Financing Charges** The Company believes adjusted net interest expense and other financing charges is useful in assessing the ongoing net financing costs of the Company.

The following table reconciles adjusted net interest expense and other financing charges to GAAP net interest expense and other financing charges reported for the periods ended as indicated.

(\$ millions)	12 Weeks Ended		24 Weeks Ended	
	Jun. 16, 2018	Jun. 17, 2017	Jun. 16, 2018	Jun. 17, 2017
Net interest expense and other financing charges	\$ 385	\$ 135	\$ 403	\$ 305
Add: Fair value adjustment of the Trust Unit liability	(180)	1	(99)	(23)
Fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares	(23)	(2)	19	(19)
Adjusted net interest expense and other financing charges	\$ 182	\$ 134	\$ 323	\$ 263

In addition to certain items described in the "Adjusted EBITDA" section above, the following items impacted net interest expense and other financing charges in the second quarters of 2018 and 2017, and on a year-to-date basis:

**Fair value adjustment of the Trust Unit liability** The Company is exposed to market price fluctuations as a result of the Choice Properties Trust Units held by unitholders other than the Company. These Trust Units are presented as a liability on the Company's unaudited interim period condensed consolidated balance sheets as they are redeemable for cash at the option of the holder, subject to certain restrictions. This liability is recorded at fair value at each reporting date based on the market price of Trust Units at the end of each period. An increase (decrease) in the market price of Trust Units results in a charge (income) to net interest expense and other financing charges.

**Fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares** The fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares is non-cash and is included in net interest expense and other financing charges. The adjustment is determined by changes in the value of the underlying Loblaw common shares. An increase (decrease) in the market price of Loblaw common shares results in a charge (income) to net interest expense and other financing charges.

## Management's Discussion and Analysis

**Adjusted Income Taxes and Adjusted Income Tax Rate** The Company believes the adjusted income tax rate applicable to adjusted earnings before taxes is useful in assessing the underlying operating performance of its business.

The following table reconciles the effective income tax rate applicable to adjusted earnings before taxes to the GAAP effective income tax rate applicable to earnings before taxes as reported for the periods ended as indicated.

(\$ millions except where otherwise indicated)	12 Weeks Ended		24 Weeks Ended	
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>
Adjusted operating income <sup>(i)</sup>	\$ 792	\$ 774	\$ 1,435	\$ 1,438
Adjusted net interest expense and other financing charges <sup>(i)</sup>	182	134	323	263
Adjusted earnings before taxes	\$ 610	\$ 640	\$ 1,112	\$ 1,175
Income taxes	\$ 126	\$ 140	\$ 232	\$ 241
Add: Tax impact of items excluded from adjusted earnings before taxes <sup>(ii)</sup>	38	33	67	78
Adjusted income taxes	\$ 164	\$ 173	\$ 299	\$ 319
Effective income tax rate applicable to earnings before taxes	61.8%	27.7%	33.7%	28.4%
Adjusted income tax rate applicable to adjusted earnings before taxes	26.9%	27.0%	26.9%	27.1%

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

(ii) See the adjusted EBITDA table and the adjusted net interest expense and other financing charges table above for a complete list of items excluded from adjusted earnings before taxes.

**Adjusted Net Earnings Available to Common Shareholders and Adjusted Diluted Net Earnings Per Common Share** 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.

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 reported for the periods ended as indicated.

(\$ millions except where otherwise indicated)	12 Weeks Ended		24 Weeks Ended	
	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>	Jun. 16, 2018	Jun. 17, 2017 <sup>(3)</sup>
Net earnings attributable to shareholders of the Company	\$ 38	\$ 170	\$ 228	\$ 288
Less: Prescribed dividends on preferred shares in share capital	(10)	(10)	(20)	(20)
Net earnings available to common shareholders of the Company	\$ 28	\$ 160	\$ 208	\$ 268
Less: Reduction in net earnings due to dilutive instruments at Loblaw	(1)	(2)	(2)	(2)
Net earnings available to common shareholders for diluted earnings per share	\$ 27	\$ 158	\$ 206	\$ 266
Net earnings attributable to shareholders of the Company	\$ 38	\$ 170	\$ 228	\$ 288
Adjusting items (refer to the following table)	182	56	180	132
Adjusted net earnings attributable to shareholders of the Company	\$ 220	\$ 226	\$ 408	\$ 420
Less: Prescribed dividends on preferred shares in share capital	(10)	(10)	(20)	(20)
Adjusted net earnings available to common shareholders of the Company	\$ 210	\$ 216	\$ 388	\$ 400
Less: Reduction in net earnings due to dilutive instruments at Loblaw	(1)	(2)	(2)	(2)
Adjusted net earnings available to common shareholders for diluted earnings per share	\$ 209	\$ 214	\$ 386	\$ 398
Weighted average common shares outstanding (millions) <sup>(i)</sup>	128.2	128.3	128.2	128.3

(i) Includes impact of dilutive instruments for purposes of calculating adjusted diluted net earnings per common share.

## 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 GAAP net earnings available to common shareholders of the Company and diluted net earnings per common share as reported for the periods ended as indicated.

	12 Weeks Ended			
	Jun. 16, 2018		Jun. 17, 2017 <sup>(3)</sup>	
	Net Earnings Available to Common Shareholders of the Company (\$ millions)	Diluted Net Earnings Per Common Share	Net Earnings Available to Common Shareholders of the Company (\$ millions)	Diluted Net Earnings Per Common Share
(\$ except where otherwise indicated)				
As reported	\$ 28	\$ 0.21	\$ 160	\$ 1.23
Add impact of the following <sup>(i)</sup> :				
Amortization of intangible assets acquired with Shoppers Drug Mart	\$ 42	\$ 0.33	\$ 42	\$ 0.33
CREIT acquisition and other related costs	51	0.39	—	—
Fair value adjustment on investment properties	4	0.03	—	—
Loblaws Card Program	(4)	(0.03)	—	—
Pension annuities and buy-outs	1	0.01	—	—
Restructuring and other related costs	—	—	3	0.02
Fair value adjustment of derivatives	(3)	(0.02)	3	0.03
Wind-down of PC Financial banking services	(2)	(0.02)	—	—
Inventory loss, net of recoveries	(1)	(0.01)	(2)	(0.02)
Asset impairments, net of recoveries	—	—	3	0.02
Fair value adjustment of the Trust Unit liability	85	0.67	(1)	(0.01)
Fair value adjustment of the forward sale agreement for 9.6 million Loblaws common shares	17	0.14	2	0.02
Foreign currency translation	(8)	(0.07)	6	0.05
Adjusting items	\$ 182	\$ 1.42	\$ 56	\$ 0.44
Adjusted	\$ 210	\$ 1.63	\$ 216	\$ 1.67

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

	24 Weeks Ended			
	Jun. 16, 2018		Jun. 17, 2017 <sup>(3)</sup>	
	Net Earnings Available to Common Shareholders of the Company (\$ millions)	Diluted Net Earnings Per Common Share	Net Earnings Available to Common Shareholders of the Company (\$ millions)	Diluted Net Earnings Per Common Share
(\$ except where otherwise indicated)				
As reported	\$ 208	\$ 1.61	\$ 268	\$ 2.08
Add impact of the following <sup>(i)</sup> :				
Amortization of intangible assets acquired with Shoppers Drug Mart	\$ 86	\$ 0.67	\$ 84	\$ 0.65
CREIT acquisition and other related costs	55	0.43	—	—
Impact of healthcare reform on inventory balances	7	0.05	—	—
Fair value adjustment on investment properties	4	0.03	—	—
Loblaw Card Program	3	0.02	—	—
Pension annuities and buy-outs	1	0.01	2	0.02
Restructuring and other related costs	11	0.09	10	0.08
Fair value adjustment of derivatives	(11)	(0.08)	9	0.07
Wind-down of PC Financial banking services	(7)	(0.05)	—	—
Inventory loss, net of recoveries	(1)	(0.01)	(2)	(0.02)
Asset impairments, net of recoveries	—	—	3	0.02
Fair value adjustment of the Trust Unit liability	66	0.51	4	0.03
Fair value adjustment of the forward sale agreement for 9.6 million Loblaw common shares	(14)	(0.11)	14	0.11
Foreign currency translation	(20)	(0.16)	8	0.06
Adjusting items	\$ 180	\$ 1.40	\$ 132	\$ 1.02
Adjusted	\$ 388	\$ 3.01	\$ 400	\$ 3.10

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

**Free Cash Flow** The Company believes free cash flow is useful in assessing the Company's cash available for additional financing and investing activities.

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

(\$ millions)	12 Weeks Ended		24 Weeks Ended	
	Jun. 16, 2018	Jun. 17, 2017	Jun. 16, 2018	Jun. 17, 2017
Cash flows from operating activities	\$ 601	\$ 916	\$ 1,059	\$ 1,300
Less: Interest paid	104	86	283	257
Fixed asset purchases	210	207	368	340
Intangible asset additions	74	80	160	134
Free cash flow	\$ 213	\$ 543	\$ 248	\$ 569

## **Management's Discussion and Analysis**

### **ADDITIONAL INFORMATION**

Additional information about the Company has been filed electronically with the Canadian securities regulatory authorities through the System for Electronic Document Analysis and Retrieval (SEDAR) and is available online at [www.sedar.com](http://www.sedar.com).

This Quarterly Report includes selected information on Loblaw, a public company with shares trading on the TSX. For information regarding Loblaw, readers should also refer to the materials filed by Loblaw with SEDAR from time to time. These filings are also available on Loblaw's website at [www.loblaw.ca](http://www.loblaw.ca).

Toronto, Canada

July 30, 2018

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**Footnote Legend**

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- (1) See “Non-GAAP Financial Measures” section of the Company’s 2018 Second Quarter Management’s Discussion and Analysis beginning on page 37.
  - (2) To be read in conjunction with “Forward-Looking Statements” beginning on page 2.
  - (3) Certain figures have been restated as a result of IFRS 15, “Revenue from Contracts with Customers” and a change in accounting policy. See Note 2 in the Company’s 2018 second quarter unaudited interim period condensed consolidated financial statements.
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