FINAL TRANSCRIPT

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PRESENTATION

Operator

Good morning. My name is Jessica, and I'll be your conference operator today. At this time, I'd like to welcome everyone to the Loblaw Companies Ltd third quarter results conference call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. (Operator Instructions). Thank you. Kim Lee, you may begin your conference.

Kim Lee - *Loblaw Companies Ltd - Senior Director - IR*

Thank you, Jessica. Good morning, and welcome to the Loblaw Companies Ltd third quarter 2011 conference call. This call is also being webcast simultaneously on our website at Loblaw.ca. I'm joined here this morning by Galen D. Weston, Executive Chairman, Vicente Trius, President, and Sarah Davis, Chief Financial Officer. Before we begin today's call, I want to remind you that the discussion will include forward-looking statements, such as the Company's beliefs and expectations regarding certain aspects of its financial performance in 2011 and future years.

These statements are based on certain assumptions, and reflect management's current expectations and they are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations. These risks and uncertainties are discussed in the Company's materials, filed with the Canadian securities regulators from time to time, including the Company's annual report and third quarter report. Any forward-looking statements speak only as of the date they are made. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise, other than as required by law. Certain non-GAAP financial measures may be discussed or referred to today. Please refer to our third quarter report and other materials filed with the Canadian Securities regulators from time to time for a reconciliation of each of these measures to the most directly-comparable GAAP financial measures.

An archive of this conference call will be available on our website. I will now turn the call over to Galen Weston.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Good morning. Thank you for joining us. In the third quarter, Loblaw performed fairly well. As the organization settled into a new rhythm, execution continued to improve. This drove a satisfactory improvement in the top line, at the same time the team effectively leveraged expenses.

Even as underlying operating trends improved, our infrastructure program remains a primary focus. We are making steady progress, however, still expect it to negatively impact operating income going forward. And finally, our new president, Vicente Trius, has been with us for nearly four months. The transition has been smooth and he is now firmly established in his role and we look forward to his ongoing leadership. I'll now turn the call over to Sarah to walk us through the results.

Sarah Davis - *Loblaw Companies Ltd - CFO*

Thank you, Galen, and good morning. In the retail segment, sales increased by 2% to CAD9.6 billion in the third quarter of 2011. Same-store sales increased by 1.3%. The Q3 sales increase was mainly driven by moderate sales growth in food, as well as strong growth in gas bars and moderate growth in apparel sales. In dress store and other general merchandise, we saw year over year decreases. During the quarter, our average quarterly internal food price index experienced moderate inflation, which was lower than average CPI in the quarter of 4.9%. Internal food price was flat in Q3 of 2011.

The retail segment gross profit percentage was 21.7%, a decrease of 30 basis points over the third quarter of last year. This 30 basis point decrease was primarily driven by a greater penetration of lower margin gas bar sales and increased fuel costs. Gross profit dollars have increased by CAD11 million over the third quarter of last year. Operating income in the retail segment increased 10.9% to CAD397 million in the third quarter compared to CAD358 million in Q3 of 2010. Operating margin was 4.2% in the quarter, a 40 basis point improvement over last year, primarily due to reductions in SG&A.

Revenue in the financial services segment increased by 3.8% to CAD164 million, compared to CAD158 million in Q3 of 2010. The increase was primarily driven by increased credit card transaction values in the quarter, resulting in higher interchange fee income. Operating income in the financial services segment was CAD24 million in the third quarter of 2011, down from CAD31 million in the same quarter last year. The decrease was mainly due to significant marketing investments and customer acquisition costs, partially offset by the increase in revenue. On a consolidated basis, operating income was CAD421 million in the third quarter compared with CAD389 million in Q3 of 2010. Operating margin was 4.3%, compared with 4.1% in Q3 of last year.

Consolidated operating income in 2011 included CAD19 million in incremental costs related to supply chain and IT, a CAD15 million charge related to share-based compensation, net of equity forwards, a CAD12 million charge related to collective agreements ratified in Q3 of 2010, and a CAD14 million gain related to the sale of a portion of a property in North Vancouver, British Columbia. In Q3 of 2010, the Company reported a CAD17 million charge related to the ratification of Ontario labor agreements, and CAD9 million for share-based compensation net of equity forwards.

SG&A expenses in the quarter as a percent of revenue were 18.6%, down from 19.2% in Q3 of 2010. In addition to the items impacting consolidated operating income mentioned above, the decrease in expenses was primarily due to continued labor and other operating cost efficiencies, and improvements in our investments in franchisees, partially offset by foreign currency exchange losses. Interest expense decreased CAD7 million to CAD95 million, compared to Q3 2010, primarily due to a decrease in interest expense in long-term debt. Our effective tax rate for the quarter decreased to 27.6% from 31.4% in Q3 of 2010, due primarily to further reductions in the federal and Ontario statutory income tax rate.

Loblaw realized third quarter basic net earnings per common share of CAD0.84, compared with CAD0.71 in the third quarter of 2010. Net debt at the end of the third quarter was CAD4.4 billion, down CAD152 million from the end of Q4 of 2010, primarily driven by EBITDA. Capital expenditures in Q3 were CAD324 million, and CAD640 million year to date. Our estimate for capital expenditures in 2011 continues to be approximately CAD1 billion. We are adjusting our guidance for the incremental supply chain and IT costs. Through the first quarter, we expect incremental spending of approximately CAD20 million, for a full-year incremental spend of roughly CAD90 million, down from our previous estimate of CAD100 million.

In the fourth quarter, we also expect costs associated with the transition of certain Ontario conventional stores under collective agreements ratified last year to range from CAD20 million to CAD30 million, for a full-year estimate of CAD32 million to CAD42 million. In addition, we expect the IFRS fixed asset impairment standard to potentially introduce more volatility in our earnings compared to Canadian GAAP. In Q4 2010, under IFRS accounting standards, we recorded an impairment recovery of CAD7 million. In Q4, we will be finalizing our store-level budget, and this may prompt asset impairment evaluations, which will determine whether any impairment or recovery will be required in 2011. I would now like to turn it over to Vicente, who will provide some context for the quarter.

Vicente Trius - *Loblaw Companies Ltd - President*

Thank you, Sarah. Good morning, everyone, and thank you for joining us this morning. This marks my first quarterly call as President of Loblaw Companies. I want to start by thanking the entire Loblaw team for delivering a good quarter. Considering moderate inflation and the competitive environment, we're pleased with the quarter.

The implementation of our two-division structure allow to us be more flexible and more agile, whilst enabling us to better meet market needs. The teams are now gaining traction, with new programs in place, but are showing good results in helping to drive the top line. I've now been here for three months. I have had the opportunity to meet with colleagues, customers, and suppliers. I have had an in-depth look at our business, and have thoroughly reviewed our strategy and plans. Our strategy is the right one. Its foundation is strong, and we have a solid base to build from.

Now, for the quarter, we achieved a number of accomplishments. Delivering on the right store experience, our real estate initiatives completed 28 renovations and opened three new stores in Q3. We opened two new No Frills in British Columbia, and one new RCSS in Edmonton. Upcoming is the much-anticipated opening of our store in Maple Leaf Gardens. The opening is within the next two to three weeks. We are very excited about this new store, a grand space for food where you will find innovative and stimulating food experiences, our core competency. I invite you all to go and take a look after it opens. I'm sure you will find it a worthwhile visit and shopping experience.

We continue to make progress defining our non-food offer, and now have 30 stores updated with the Everydayliving concept. Overall, we are pleased with the profitability and productivity contribution of the [right-hand side]. For Joe, we recently opened two more stand-alone stores in Canada, and four new locations in the US. It is still premature to say, but initial customer reaction has been encouraging for our new Joe stores. On the product front, our controlled brands continue to grow with improved penetration and profitability. We are passionate about our brands and we continue to innovate.

In October, we launched the President's Choice Black Label products, our exceptional new collection of fine foods. They taste like nothing else you've eaten before. Currently Black Label products are available in 140 stores and customer reaction has been very positive. Our colleagues, who are our best ambassadors, are really excited about the quality and innovation behind these new products. At PC financial, we have been focused on marketing to and attracting new customers. While it's still early days, this year we expect to process 50% more PC MasterCard applications than ever before. It's clear that Canadians get a lot of value from our PC MasterCard offer and value proposition of earning free food fast.

Driving efficiencies, our infrastructure implementation made steady progress. We now have approximately 70% of our volume in our warehouse management systems and remain on track for 90% in 2012. 130 users are now in our planning, forecasting, replenishment systems and all purchases of grocery, general merchandise, frozen meat, processed meat, deli, and HMR in bakery are on the system. Today, all merchandising category listings have been converted onto SAP. In other words, the master data for SKU we sell is now on the system and retail pricing is now sourced from SAP. This was a big job that involved touching and cleansing hundreds of thousands of data articles, without significant impact on our customers.

The next step is to get IPFR ready for SAP and facing in the foundation for [promos] into SAP. This is already in the works, and we will continue into early 2012. From an SAP standpoint, next year is about integrating merchandising and supply chain, getting them ready to service our first store go-wide late in 2012. To allow us to transition stores smoothly, and to mitigate any impact to our customers, our overall stores will be staggered through 2013 and into 2014. Our Right Infrastructure program is a fundamental piece of our long-term strategy. The right systems, combined with the right processes will allow us to drive costs out of the business and drive efficiencies, while improving the experience in our stores for our customers. As I told you earlier, our strategy is the right one, and we are committed to consistently deliver on our plans.

Having said that, there are opportunities for us to continue our focus on the customer. Consistently striving to improve the experience in our value proposition across all our performance. Now, three months and a little bit into my tenure, we have started to build on our solid strategic base. As I complete my in-depth understanding of the business, we are sharpening our plans to consistently provide our customers with an overall improved experience across all of our banners. I am excited and energized to lead one of Canada's great retail companies into the next phase of its development. I look forward to sharing with you more detail of our move-forward plans early in the new year. With that, let's open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Your first question comes from the line of Michael van Aelst with TD Securities. Your line is open.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

I would like to start off with your IT rollout. I didn't quite catch all of that. I think you said you were going to be rolling it out into the stores mostly in 2013 and into 2014. Did you not say last quarter that you were going to be starting in 2012 and finishing up in 2013?

Vicente Trius - *Loblaw Companies Ltd - President*

Well, first, we are very pleased with the implementation process of our infrastructure in IT and technology. Yes, you're right. We will roll out the first store in Q4 of 2012, but the process of implementing all of the stores will take us all the way through 2014, which is a little over 1,200 stores.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

So why does it seem like it's being delayed by maybe up to a year?

Vicente Trius - *Loblaw Companies Ltd - President*

I believe that we are on track with the implementation and it's always been my understanding that it would run all the way into 2014. If you think, when you integrate the first store in 2012 and you have 1,200 stores, it's actually a pretty good process and plan to have them all by early 2014, 100% integrated. So far, there has been really no misses on the schedule, some adjustments from time to time, but overall, right on target.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

Then if you look at the IT spend, I know you probably don't want to give guidance for next year, but does the reduction in spend in 2011 point to higher spend in 2012, than what might have otherwise been the case, or is it savings?

Sarah Davis - *Loblaw Companies Ltd - CFO*

It's a little bit of both. Part of it would be a reduction. We did, as we had mentioned earlier, we did change the phasing of the plan a little bit this year in order to reduce the risk, which has reduced in some savings. Primarily in depreciation, though, that's where we're seeing the savings this year. So it's just a bit of a delay in spend upfront and having a reduction in depreciation. So that will spread out to other years. The depreciation will hit in other years, but doesn't mean the cash spending in 2012 will be any higher.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

And can you give us an indication as to when we expect spending to peak? Is it 2012 or 2013?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Cash spending will peak in 2012, and then the cash spend will reduce, but we'll have the tail of depreciation that will stay with us for three to five years as we depreciate those assets.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

When do you expect the depreciation part to peak?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Depreciation, it will -- well, it will be in 2012 as well. The cash and the depreciation peak and then it will reduce from there.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

Great, thank you.

Operator

Your next question comes from the line of Irene Nattel with RBC Capital Markets. Your line is open.

Irene Nattel - *RBC Capital Markets - Analyst*

Thanks, and good morning, everyone. This is the first quarter, in I believe about 13 or 14 that you have actually had gross margin contraction. And Metro on their call just said that inflation was somewhere in the range of about 2.5% and your same-store sales were 1.2%ish, 1.3% rather. So can you talk a little bit about what's going on, on the food side in terms of tonnage, in terms of inflation, in terms of promotion, and how much you're having to reinvest in order to keep the sales volume?

Vicente Trius - *Loblaw Companies Ltd - President*

First, the gross margin, the decrease of the 30 basis points in gross margin is mainly due to an increase in fuel sales, which is basically at lower margin, low fuel sales and higher transportation costs. Having said that, as a Company, if you compare to Q2, we are improving in our value proposition. The trending tonnage is improving, as well as in customer count, and our internal inflation rate is actually lower than CPI.

Irene Nattel - *RBC Capital Markets - Analyst*

Yes, so would it be lower than Metro's 2.5%?

Vicente Trius - *Loblaw Companies Ltd - President*

Our inflation rate is lower than CPI and I can tell you that we are very pleased with the performance in the trends that we have had this far in our (inaudible) and with our customers.

Irene Nattel - *RBC Capital Markets - Analyst*

Okay. And can you talk a little bit about tonnage?

Vicente Trius - *Loblaw Companies Ltd - President*

Our tonnage, as I said, our trends on our tonnage are improving, as well as our customer counts.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

They are slightly down, though, improving from trend perspective.

Irene Nattel - *RBC Capital Markets - Analyst*

Okay. So both customer counts and tonnage are slightly down, Galen?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Tonnage is down, but the customer count trend and the tonnage trends are both improving.

Irene Nattel - *RBC Capital Markets - Analyst*

Okay. That's great. Thank you.

Operator

Your next question comes from the line of Peter Sklar with BMO Capital Markets. Your line is open.

Peter Sklar - *BMO Capital Markets - Analyst*

Sarah, could you just -- all these unusuals you have, the share buyback comp, sorry, the share comp, the Ontario restructuring and the gain on the Vancouver property, you disclosed what the impact is on operating income, but what line do they go through on the P&L?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Okay. So if I go through the different pieces, the stock-based comp goes through SG&A and the labor deal also, and the -- what was the other one, oh, the gain. That does as well, they're all in SG&A. It wouldn't impact our gross profit. It would all be in SG&A.

Peter Sklar - *BMO Capital Markets - Analyst*

Okay, and lastly, you talked -- in your comments today, you've talked about the improved performance on your control label. If we talk to you about a year ago, I think you were well short of where you wanted to be. So part of the -- I think a substantial amount of the improvement is kind of catching up to where you should be. Are you where you want to be? I know there's always constant improvements, but are you essentially back to where you want to be on the control label, or is there still more catch-up to do there?

Vicente Trius - *Loblaw Companies Ltd - President*

I'll answer this one. We're pleased with improved penetration of portfolio and improved profitability, and we are pleased with the trends and we see an opportunity going forward as we improve our assortments, innovation, differentiation. For example, the Black Label introduction that we have done since October is showing very good signs, with the customer really liking the products, and we see actually additional opportunity going forward.

Peter Sklar - *BMO Capital Markets - Analyst*

Right, and just one last question, do you believe that as a whole, you're able to pass through all your cost of grocery pressure, in terms of cost of grocery inflation?

Vicente Trius - *Loblaw Companies Ltd - President*

If you look at our value proposition, has contained historical positioning versus our competitors or slightly improving. This is a process that you have forces on the cost of goods sold as much as forces on the value proposition, but overall, we're pleased with our performance and our rate, as you can see in margin as well.

Peter Sklar - *BMO Capital Markets - Analyst*

Okay, thank you.

Operator

Your next question comes from the line of David Hartley with Credit Suisse. Your line is open.

David Hartley - *BMO Capital Markets - Analyst*

Hi, thank you very much. I was wondering if, to the extent you can, you can talk a little bit about the competitive environment in Western Canada. Has that improved? Or what do you see over there?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Well, we generally don't talk about the individual regional performance. Overall, I think it's fair to say that, as you heard from Vicente, that the overall sales performance across the country has been satisfactory and, we expect that to continue as we move forward. The West, any particular difference over there that we would be prepared to comment on, no.

David Hartley - *BMO Capital Markets - Analyst*

Okay, thank you. And just thinking about financial services now, seeing increase in credit card balances is a good thing, but at the same time, do you worry about that when you see some of the increases and what it may mean for consumer spending?

Sarah Davis - *Loblaw Companies Ltd - CFO*

I think we're pretty happy with the performance of our credit card portfolio. What we have noticed is we actually have our customers actually paying down quicker, which has impacted the amount of interest income we earn, but because they are purchasing more purchases, we've increased our interchange income. So we are -- and because of the payments that they are making, quicker payments, so a better portfolio, less risky, we have been able to reduce the credit losses, so that has gone down as well. We actually feel that we've got a pretty stable portfolio with a good group of customers that actually pay down their portfolio almost every month.

David Hartley - *BMO Capital Markets - Analyst*

Okay, that's helpful. And when you look at the financial services business and the amount of money and time that you're spending in terms of marketing, customer acquisition, how do you see that spend as we look out? Do you see it kind of bottoming out and potentially seeing a rise in the contribution to the profit line for that business?

Sarah Davis - *Loblaw Companies Ltd - CFO*

2011, so this year is our biggest year of investments and we should see it starting to improve in 2012, but not by a huge amount, just big investments this year starting to pay off next year.

David Hartley - *BMO Capital Markets - Analyst*

Okay, and finally, could you talk a little bit about Joe? I know it's early days, but is there any thoughts or color you can provide us on some of the new stores down the US and in some of the new stand-alones here in Canada?

Vicente Trius - *Loblaw Companies Ltd - President*

Yes, just opened in the US a total of five stores, two pop-ups and three new stores, including in two different malls and one in Manhattan. And we are pleased actually with the reaction from our customers, and initial performance of the stores. The same thing would apply to Canada. We have this far 12 stand-alone stores and we are also very pleased with the reaction. We just opened, I think the last one was in Portland and here in Toronto, it was a very good opening. We are encouraged with the performance of Joe Fresh in both our stand-alone and in our existing business.

David Hartley - *BMO Capital Markets - Analyst*

And does that encouragement, is it enough at this moment in time to potentially warrant a greater, or a faster rollout of the concept into 2012? I'll leave it there.

Vicente Trius - *Loblaw Companies Ltd - President*

Well, I mean, we do have -- we haven't changed our plans for 2012, and to speak to the US I would say, it's still early stages, we just opened the store, so we need to run the store straight and have a proper sample before we would be talking about any different plans.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Just to add to that, it's Galen, if you think about why we went into New York as opposed to another part of the US, it is because we believe that's the best place to build the brand and we won't be expanding the network until we're comfortable that we've established the brand in that marketplace, and so far, all signs are good. But it doesn't mean any change to the rollout strategy.

David Hartley - *BMO Capital Markets - Analyst*

Thanks.

Operator

Your next question comes from the line of Patricia Baker with Scotia Capital. Your line is open.

Patricia Baker - *Scotia Capital - Analyst*

Thank you very much, and good morning, everyone. I have three questions. One of them is actually on Joe or apparel. Simple question. Can you tell us exactly, referenced in the release, the increase in square footage devoted to apparel? Can you share with us how much additional square footage is devoted to apparel this year versus last year?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

We'll get back to you on that, but it really is specific, the majority of the incremental square footage growth has come from the new stores, the stand-alone stores. There's been a little bit of expansion in the departments as we renovate the superstores, but the primary contributor is the new sites.

Patricia Baker - *Scotia Capital - Analyst*

That's a good enough answer, Galen. That kind of answers what I wanted to know. Secondly, and Vicente, you referenced twice, you made the statement that you think the strategy going forward is the right strategy, and this is probably me who is at fault here, but I would love to hear you articulate what the Loblaw strategy is going forward, because in the tos and fros of the last 12 to 18 months, I've kind of lost sight of what the strategy is, so if you could help me.

Vicente Trius - *Loblaw Companies Ltd - President*

Well, like I said, the current strategy I believe is the right one, especially when you look at all of the transformation that we are doing in infrastructure and IT, as well as building of the core. Having said that, there are opportunities going forward where we can, I believe, improve the business, and we would be more than happy to share that high confidence in the new year during Q1, we'll invite you all here in Brampton.

Patricia Baker - *Scotia Capital - Analyst*

Okay, perfect. And then secondly, my third question is, relates to something that Galen said in his remarks, and either one of you, Vicente or Galen could answer this, but you referenced the fact that you're seeing a new rhythm in the business and improved execution. And in the past, there's been a lot of commentary around the inconsistency of the execution. Can you share with us some of the execution metrics or what you're really talking about there in the new rhythm and the improvement in the execution. Where is that showing up?

Vicente Trius - *Loblaw Companies Ltd - President*

Well, I see, I see execution improving from a regional standpoint, as I visit stores, and I visit unannounced, as well as announced. You see that across all of the patterns, whether it's conventional or discount. I also see consistencies in different metrics. If you look at availability of product for the customer, it is actually very good, north of 98%, and we have consistently been there.

If you look at customer satisfaction metrics that we measure on a monthly basis, for the most part, they are spot-on, or they are actually improving, whether it is on value, whether it is on fresh, whether it is on quality, or the overall experience of the stores. This is a business about being consistent because our stores are open between whatever, 8.00 and 10.00, or 7.00 to 11.00, seven days a week. It is about having the processes that allow you to be consistent, and it is building on that, that we need to do that. We see some positive trends.

Patricia Baker - *Scotia Capital - Analyst*

Okay. That's very useful. Thank you so much.

Operator

Your next question comes from the line of Keith Howlett with Desjardins Securities. Your line is now open.

Keith Howlett - *Desjardins Securities - Analyst*

Yes, I had a question on the labor deals, the payments to transition to the new labor deals. Will that continue? Will there be -- have you finished with that now, or will there be additional payments across 2012?

Sarah Davis - *Loblaw Companies Ltd - CFO*

We're not finished with them. It will continue through 2012 and 2013, there's approximately CAD100 million still left to be spent and it will be monthly as we go through the next 2, 2.5 years and as we transfer them to the new deal, but we'll let you know about the costs and how they're coming into the quarters.

Keith Howlett - *Desjardins Securities - Analyst*

Is it all Ontario?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Yes.

Keith Howlett - *Desjardins Securities - Analyst*

Okay. And just on the loyalty program, I was just wondering if you would update us on where, what your thinking is there, whether it's tied into this marketing spend that's taking place in the credit card division?

Vicente Trius - *Loblaw Companies Ltd - President*

We're still in the process -- I am still in the process of analyzing the whole opportunity behind the loyalty program, so I'm in the analysis process, and maybe in the New Year, when we invite you in, we can talk a little bit more about it.

Keith Howlett - *Desjardins Securities - Analyst*

And just on the process of taking some of the T&T expertise, and getting the benefit of that across the rest of the network, how far along do you think you are in that process?

Vicente Trius - *Loblaw Companies Ltd - President*

Well, I think we're leveraging -- this is again is consistency, and it's a journey. It's a long process. I believe we're leveraging T&T expertise more and more into our business, specifically obviously on the sourcing side and product, as well as some of the best practices in ethnic products; Fresh, sushi, sashimi, and all those categories. It is something that we're leveraging. It is something that obviously we still have a ways to go, but it's improving. We're pleased to have them onboard with us.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Maybe I can give you a couple of specific examples to support Vicente's comments. We looked, for example, at the top 50 fastest-moving Asian items in T&T with the help of the T&T team, and we've taken those, and where appropriate, made sure they were lifted in our assortment. They have exclusivity arrangements with brands coming from Asia that flow through their wholesale business that we now have access to in our stores. When you come down and see Maple Leaf Gardens, you'll see what we call an east meets west effort where the T&T brand will show up in one of our departments for the first time. So I think this is the early signs of it, but by and large, it's quite an exciting journey we're on.

Keith Howlett - *Desjardins Securities - Analyst*

Great, and I just had a question on the pharmacy business. What your approach is to the script buying process and whether you're -- you have information as to what is going on with the Target takeover of Zellers stores.

Vicente Trius - *Loblaw Companies Ltd - President*

The script buying process is an ongoing process, and obviously depends on the economics behind each one of them. As far as Target or any competitor, there's always opportunities out there that we should look at when we go through a transformation process and the opportunities there -- obviously, we'll take a look at it, and we'll leverage that. As far as the pharmacy and the script business, we're pleased with our performance and we have an overall strategy behind health and wellness and actually our script count from Q3 was up 4.1%, so we are pleased with our performance.

Keith Howlett - *Desjardins Securities - Analyst*

Great. Thanks very much.

Operator

Your next question comes from the line of Chris Li with Bank of America-Merrill Lynch. Your line is open.

Christopher Li - *BofA Merrill Lynch - Analyst*

Hi. Sorry if you've answered this already, but can you maybe break out for us a little bit of the gross margin decrease from the quarter, how much of that was related to the increase in the gas sales?

Vicente Trius - *Loblaw Companies Ltd - President*

Like I said before, the increase of fuel sales and higher transportation costs achieved was about 30 basis points versus last year.

Christopher Li - *BofA Merrill Lynch - Analyst*

Okay, and you mentioned tonnage was down slightly, but improved sequentially. Where was the improvement coming from? Was it fairly broad-based, or was it coming more from one banner over the other, or from one particular region?

Vicente Trius - *Loblaw Companies Ltd - President*

We see really improvements for the most part across both businesses, conventional and discount, and we see the strengths more so in the food side of the business and groceries and fresh.

Christopher Li - *BofA Merrill Lynch - Analyst*

Okay, and just on the Ontario collective agreements, Sarah I just want to confirm what you said earlier. So you expect there's another roughly CAD100 million of payments in 2012?

Sarah Davis - *Loblaw Companies Ltd - CFO*

In 2012 and 2013, so 2.5 years, actually, we expect it will take to get through all of them, and it will be determined as we go through and decide how we want to convert over the stores.

Christopher Li - *BofA Merrill Lynch - Analyst*

Sure, okay.

Sarah Davis - *Loblaw Companies Ltd - CFO*

So it's not 100 million in 2012. It will be over 2.5 years.

Christopher Li - *BofA Merrill Lynch - Analyst*

Over 2.5 years. And in terms -- it will flow through SG&A expense depending on what happens this quarter?

Sarah Davis - *Loblaw Companies Ltd - CFO*

That's right.

Christopher Li - *BofA Merrill Lynch - Analyst*

Okay, and just in terms of the rationalization of the [non-apparel] general merchandise, how far are you in terms in that program and how much more is to be done?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Our expectation is that we will be largely complete by the end of 2012.

Christopher Li - *BofA Merrill Lynch - Analyst*

And are we starting to see some of the benefits in the financials, or is it the bulk of it will come?

Vicente Trius - *Loblaw Companies Ltd - President*

We're seeing -- if you look at general merchandise as a whole from a contribution perspective, it is better than food, and if we look at apparel, we do see some improvements in apparel.

Christopher Li - *BofA Merrill Lynch - Analyst*

Okay. Great. Thank you.

Operator

Your final question comes from the line of Michael van Aelst with TD Securities. Your line is open.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

Thank you. The new labor agreements that you are bringing on and resulting in these charges, are these also mostly responsible for your improved operating cost performance?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Well, there's a couple things that are happening. So we do have labor improvement. So our labor productivity has improved. That's related to store time and attendance, and new -- some technology we've put in that allows for better visibility to scheduling. And there is some flexibility that comes through, so there is a positive payback to the deals that we have, where we've gone through, but it wouldn't be entirely the reason for the operating expense reduction, it would be just a portion of it.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

What would be the other components, major components on the operating cost?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Well, just some corporate cost reductions, as well as the performance of our franchisees has also improved, and some of those costs will go through SG&A as well.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

Corporate cost reductions, are those related to getting the SAP up in certain parts and being able to rationalize departments, or is that still to come?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Most of that's still to come.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

I think maybe just for a little bit of emphasis around Sarah's comment, this store time and attendance system, which really, this is the first full year that it's been in operation, is performing extremely well for us. And when you think about productivity enhancements that come from systems investments, this gives us confidence as we move forward, that the returns are absolutely there and when we spend the money, I think we'll net directly.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

Okay, and final question would be on the, I guess on the sales side. To what degree do you think Loblaw had to ease up on the merchandising programs during the last two quarters, as you rolled out the new systems and you got it in front of the merchandisers?

Vicente Trius - *Loblaw Companies Ltd - President*

Could you repeat that? To what degree, and Loblaw would have to do what?

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

Ease up on some of your merchandising programs, like not push quite as hard as you're getting the systems in front of the merchandisers.

Vicente Trius - *Loblaw Companies Ltd - President*

We actually have not eased up, we have very strong merchandising plan quarter over quarter. And like I said before, we believe that our value proposition is improving if you compare Q3 versus Q2.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Just to speak to the first two quarters of the year, do you remember, we implemented the divisional structure change? And we've said a number of times on this call and in other cases, that created executional challenges as the organization got used to the new structure and in Q3 is evidence in our judgment at any rate that now that the organization has settled down, they are focused on delivering programs that are resonating better with the customers, and that's one of the reasons that you're seeing such a substantial change in the sales trends. So it wasn't to do with a planned reduction in the amount of competitive intensity, just weaker execution in the first two quarters. We're coming out of that nicely now.

Michael Van Aelst - *TD Newcrest/Waterhouse Securities - Analyst*

Thank you.

Operator

There are no further questions at this time. I'll turn the call back over to the presenters.

Kim Lee - *Loblaw Companies Ltd - Senior Director - IR*

That concludes our call. Thank you for joining us. Thanks, and have a great day.

Operator

This concludes today's conference call. You may now disconnect.