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L.TO - Loblaw Companies Ltd Conference Call to Discuss Definitive Agreement to Acquire Shoppers Drug Mart Corporation

EVENT DATE/TIME: JULY 15, 2013 / 12:00PM GMT



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PRESENTATION

Operator

Good morning. My name is Melissa, and I will be your conference operator today. At this time, I would like to welcome everyone to the Loblaw Company Limited and Shoppers Drug Mart transaction 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. And I will now turn the call over to your host, Ms. Janet Craig. You may begin your conference.

Janet Craig - Loblaw Companies Ltd - SVP, IR

Thanks, Melissa, and thank you everyone for joining us this morning. I am here today with Loblaw Executive Chairman, Galen Weston; Shoppers Drug Mart Chair, Holger Kluge -- Holger Kluge, sorry, Holger; Loblaw President, Vicente Trius; Shoppers Drug Mart President and Chief Executive Officer, Domenic Pilla, and Loblaw Chief Financial Officer, Sarah Davis.

Before we begin, I would like to remind you that this discussion will contain forward-looking statements about the proposed transaction. These forward-looking statements reflect current estimates, pro forma information, beliefs and assumptions which are based on Loblaw's and Shoppers Drug Mart's perception of factors management believes are appropriate in the circumstances. We can give no assurance that such estimates, pro



forma information, beliefs and assumptions will prove to be correct. Investors are cautioned that there are a number of risks and uncertainties that could also cause actual results or events to differ materially from those expressed in these forward-looking statements. For additional information regarding the forward-looking statements, please refer to full text of the press release issued by Loblaw and Shoppers Drug Mart earlier today, and to the slide contained in today's presentation materials.

In addition, I wish to point out that throughout the presentation this morning, management may reference to non-GAAP -- may make reference to non-GAAP measures such as EBITDA and free cash flow. Management of Loblaw and Shoppers Drug Mart believe that these non-GAAP measures provide useful information to both management and investors in discussing the proposed transaction. These measures do not have a standard meaning prescribed by GAAP, and therefore they may not be comparable to similarly-titled measures presented by other publicly-traded companies. Now let me turn the call over to Galen.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Thank you, Janet, and thank you all for joining us today. As we start our presentation, I would like to introduce the Chair of the Board of Shoppers Drug Mart, Holger Kluge. Making transformational transactions like this one happen takes vision, patience and stamina. Holger has demonstrated just such leadership. Today's announcement would not have taken place without him. Holger, can I ask you to make a few remarks?

Holger Kluge - *Shoppers Drug Mart - Chairman*

Thank you, Galen. I appreciate your kind words. This is a wonderful combination that paves the way for a terrific future for our two companies, as well as for investors, associate owners, and store teams and our customers. Transactions are about numbers for sure, but their success really depends on people and culture. Both Loblaw and Shoppers Drug Mart share a passion for our customers. And together, we will be able to serve them better than we ever could do alone. I am excited about this transaction, and look forward to the very bright future ahead of us. With that, let me turn it back to Galen.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

When Loblaw first opened its doors in 1919, we changed how Canadians shops for groceries. And when we launched our President's Choice and No Name house brands, we changed how Canadians view private label. President's Choice Financial changed how Canadians bank, and Joe Fresh changed affordable apparel for Canadians. I have long believed that the next chapter for growth at Loblaw should be based in a vision that combined health, wellness and nutrition. Loblaw combining with Shoppers Drug Mart is the ultimate expression of that vision. Not only does this transaction make compelling financial sense, it establishes a truly innovative platform for the future.

With today's transformational partnership between Loblaw and Shoppers Drug Mart, we are changing the retail landscape in Canada, combining two iconic companies and creating an innovative new retailer. We will put both company's trusted brands and services within closer reach of even more Canadians, and do so in a way that creates immediate value for the shareholders of both companies. Together, Shoppers Drug Mart and Loblaw will touch millions of Canadians every day, with 1 billion customer transactions per year, over 2,300 stores, nearly 1,800 pharmacies, and 65 million square feet of selling space. Had we been one Company in 2012, we would have generated CAD42 billion in annual revenue, CAD3 billion in EBITDA, and CAD1 billion in annual free cash flow.

But as big as this deal is, it is about an even bigger idea. This transaction enables us to harness the complementary strength of Canada's number one food retailer and Canada's number one pharmacy retailer, to serve customers better close to where they live and work. And with an even greater combination of value, assortment and service than either Company could provide alone. The profile and preferences of the Canadian consumer continue to change, as they have so many times in the more than nine decades since we opened our first grocery store, and in the five decades since Shoppers Drug Mart opened its first pharmacy. And we are confident that we will remain Canadians' first choice for health, wellness and nutrition.



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This transaction will enable us to offer Loblaw's portfolio of market-leading brands and convenience food and grocery products through Shoppers Drug Mart's store network. Likewise, we will begin to offer Shoppers Drug Mart's respected wellness brands and pharmacy services in Loblaw stores. We will benefit from, among other things the combination of Loblaw's PC Financial Services and Shoppers Drug Mart's incomparable Optimum Loyalty Program. And that is just the beginning. There are opportunities for savings and synergies in additional areas such as supply chain that will further strengthen the financial advantages of this combination.

Loblaw and Shoppers Drug Mart bring complementary real estate positions. Loblaw has Canada's largest retail network, which already includes 500 pharmacies. And Shoppers Drug Mart has the most convenient retail network in Canada, including the best urban small format locations. Vicente will now elaborate on how they'll create value from this unique platform.

Vicente Trius - *Loblaw Companies Ltd - President*

Thank you, Galen, and thank you everyone for joining us this morning. We work passionately to put customers at the center of everything we do. Customers whose needs and preferences are changing quickly driven by a number of specific trends. More and more consumers are focused on health and wellness. They are demanding more convenient locations on which to shop. This creates a need for small format stores that offer value, with a range of high quality convenience foods and grocery products. Demographic trends are driving higher demand for pharmacy-related products and services. Consumers increasingly want to interact with each other, and with companies that are close to them through technology. And increasingly, consumers are pressed for time.

At Loblaw, we have worked hard to respond to our customers' needs. That work has begun to pay off, as we continue to succeed in creating an enhanced customer experience. But I know that a potential with Shoppers Drug Mart is much greater. This transaction catapults us into a position that would otherwise take decades to reach alone. We will grow faster with the help of the terrific platform that Shoppers Drug Mart and its associate owners provide. As proud as I am of the progress we have made, teaming with Shoppers Drug Mart immediately puts us much further down our strategic path in a single bold step.

I absolutely believe that the combination of convenience and value will create a significantly enhanced experience for our customers. Just imagine being able to go to Loblaw for a regular grocery shop, and having the option to buy a wide variety of the products you would expect to see at Shoppers Drug Mart, like the Life brand, in an enhanced in store pharmacy. Or being able to do a quick trip to your local Shoppers Drug Mart store, and while there being able to buy your favorite PC Blue Menu items, along with other great products and services that Shoppers Drug Mart offers.

We all know that prime locations are a key component of success, however this transaction is about more than physical locations. Shoppers Drug Mart brings the right set of brands, the right mix of formats, and the right expertise to enable us to serve our customers even better than we do today. We are very proud to welcome Shoppers Drug Mart trusted associate owners, store level teams, and central and regional office employees. They are known throughout Canada for their professional and friendly service, and their passion and commitment to the Shoppers Drug Mart brand. That will continue with Shoppers Drug Mart operating as a distinct division within our combined Company. Now let's hear Dominic's view of this compelling transaction, and the role that the special associate owner culture will play in our ability to deliver on this new proposition.

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

Thank you, Vicente, and thank you, Galen. I am delighted to be here today with you, and I am excited about the prospect of bringing together Shoppers Drug Mart and Loblaw. We too, pride ourselves on our customer focus, which is why I am so confident of the cultural fit between our two companies. We have both been thinking about the future opportunities for our businesses. And we both reached the same conclusion, in terms of how to change the game for Canadian retail. We both believe in the tremendous benefits that will come for the customer out of this partnership. That is why we are so excited to be partnering with Loblaw. Initiatives such as those as Vicente described, such as offering Loblaw's food products within our stores including their leading private labels are an enormous opportunity to provide additional value for our customers, while driving incremental front of store growth and margin enhancement for us.



Like Loblaw, Shoppers Drug Mart is also a pioneer in health and wellness. That really is our common purpose and our commitment. It is how we have built Shoppers Drug Mart into Canada's leading pharmacy brand, with customer loyalty and brand equity that reflects our position in our customers' hearts and minds. We understand that that leading position is earned and not given, and we work hard to maintain that reputation and trust every day. It is what prompted us to develop our front of store beauty offerings, which today are a true competitive advantage. It has led to our introduction of in-store value-added health services, so our customers can take care of an increasing number of their health requirements in a Shoppers Drug Mart store. It is rooted in the continued strength of our leading pharmacy networks.

This transaction is also attractive for our shareholders who will receive significant value, as well as the ability to benefit from the future upside through a combined investment -- in a continued investment in the combined Company. We have a shared vision on how this will unfold. We are aligned in our opinion of where the customer trends are taking us. And both companies want to ensure we are in front of those trends, offering customers the right suite of products and services. We are excited about the opportunity to partner with Loblaw, the sharing of ideas and expertise, as well as the ability to leverage each others unique strength is an avenue for mutual growth. We strongly feel that now is the time, and that this is the deal. I will now turn it over to Sarah to take us through some of the details of the transaction.

Sarah Davis - *Loblaw Companies Ltd - CFO*

Thank you, Domenic, and good morning, everyone. This is a strong deal from a financial perspective. Let me start with a few facts. The transaction equity value is CAD12.4 billion. Shoppers Drug Mart shareholders will receive CAD33.18 in cash, and 0.5965 Loblaw shares for each Shoppers Drug Mart share on a fully prorated basis. Total consideration will be 54% in cash, and 46% in Loblaw Common Stock. The offer price per share represents a premium of 29.4% over the 20 day VWAP of Shoppers Drug Mart Common Stock and an EBITDA multiple of 11.4 times. Shoppers Drug Mart shareholders will own approximately 29% of the combined Company. As announced in a separate press release this morning, George Weston Limited has agreed to subscribe for CAD500 million of additional Loblaw common shares to finance a portion of the cash consideration. In 2014, we expect the transaction to drive double-digit EPS accretion adjusted for the amortization of intangibles.

In terms of financing sources, we have laid out on this slide the details of the transaction. As we outlined in the press release we issued this morning, under the agreement between Loblaw and Shoppers Drug Mart we have CAD5.1 billion in committed financing consisting of a CAD3.5 billion five-year term loan, and a CAD1.6 billion bridge loan, which we intend to repay through the issuance of notes and with Shoppers Drug Mart cash. We will have a strong balance sheet post transaction with a CAD1 billion of cash, and an CAD800 million undrawn revolver that we intend to increase to CAD1 billion. This deal was structured with the intent to maintain our BBB mid credit ratings. Our leverage will move as a result of this transaction to 3.1 times adjusted debt to EBITDA. However, we will use the strong free cash flow to delever back to 2.5 times within 24 months of the transaction close.

Our dividend policy remains unchanged, and we anticipate closing the transaction within six to seven months. We have identified approximately CAD300 million of run rate synergies that we expect to achieve over a three-year period, phased in approximately equally. Opportunities to achieve these synergies include, expense reductions in areas such as marketing, supply chain, IT, and shared infrastructure, reductions in cost of goods sold through efficiencies in purchasing, and increased private label penetration, realizing opportunities in our loyalty programs and expansion of financial services. With that, let me turn the call back to Galen for some concluding remarks.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Thanks, Sarah. Well, you have heard today why we are all so excited about this transaction. And it is one that I have been working on for some considerable time. As I said earlier, I have long believed that becoming a Canadian health and wellness and nutrition champion represented a powerful next chapter for the Company. But to be frank, if we were really going to be serious about it, we had to go out and add the very best pharmacy retailer in Canada. And that is just what we have done. We are confident that the two great companies will come together to serve our customers better and create shareholder value. We are building on a strong foundation.

Loblaw and Shoppers Drug Mart have created unique industry leading enterprises, brands and reputations that have taken decades to build. And by working together, we will expand our customer proposition. And in a way, in a stronger position to anticipate and respond to future changes



in the way that Canadians live and shop. Together, we will have the scale, diversification, financial strength and flexibility to compete and succeed in an increasingly competitive and rapidly changing marketplace. Shareholders of both Shoppers Drug Mart and Loblaw will benefit, both immediately and in the long-term, as will all of our stakeholders including the communities in which we operate as we work to help Canadians live life well. We are now delighted to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Your first question comes from Irene Nattel from RBC Capital Markets. Your line is open.

Irene Nattel - RBC Capital Markets - Analyst

Thanks, and good morning, everyone. A couple of questions if I might. In the press release you note that you will continue to operate the two Shoppers as a standalone division. Yet it is clear that you are anticipating a fair amount of cross-pollination and integration between the two. Can you walk us through how that is going to work, please?

Vicente Trius - Loblaw Companies Ltd - President

Yes, good morning, Irene. First of all, let me just say -- before I address your question, I think this is a great opportunity for us. And when I look at strategically placed, through the short, to the mid and to the long-term, it brings us stronger into the small formats. You know, Irene, that I always believe that there is room for all of our formats. But I do believe that for the long-term, small formats that can create convenience and value are critical. You know through the press that we have opened a small store in Calgary, which is about low prices and full shop. And we are thinking very, very seriously on an experience of convenience and value.

As you look at Shoppers Drug Mart and ask, we are leveraging the talent, the best practices, the knowledge and capabilities of both companies. So this, to answer your question translates into. For example, food proposition into Shoppers Drug Mart, the drug and pharmacy, patient services, the model of the pharmacy and the health and beauty into Loblaw. Imagine the control brand, imagine seeing our President's Choice Blue Menu in their stores, visa versa Life into our stores. Imagine the potential that we could have even in other areas like PC Financials. So we see it all in all, a very, very good combination.

Irene Nattel - RBC Capital Markets - Analyst

That's great. Thank you. And can you give us some an idea of what the combined Rx market share will be for Loblaw Shoppers?

Domenic Pilla - Shoppers Drug Mart - President and CEO

We are talking about 125 million prescriptions. I don't know what the market share number equivalent of that is. Around 25%, Irene.

Irene Nattel - RBC Capital Markets - Analyst

That's great. Thanks, Domenic.



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Janet Craig - Loblaw Companies Ltd - SVP, IR

Thanks, Irene. And before we get the next caller, I forgot to mention at the beginning of the call, that one question and a follow-up would be greatly appreciated.

Operator

Your next question is from the line of Patricia Baker from Scotiabank. Your line is open.

Patricia Baker - Scotiabank - Analyst

Good morning, and thank you very much. And it is not usually my style to break the rules, but I am going to break the rules today, Janet. I apologize in advance. First of all, was there an auction process associated with the sale of Shoppers?

Holger Kluge - Shoppers Drug Mart - Chairman

We have always kept our shareholders in mind, and we have looked at various opportunities over the last two years, which is natural. And in the end, when we got the approach that we did, and you see in front of you, it was by far superior to anything else that we have seen to our discussions over the last two years.

Patricia Baker - Scotiabank - Analyst

Okay. And just related to that, I guess this would be a question for Sarah or Galen. Did Loblaw or Weston, at either of those levels own any Shoppers shares before prior to the transaction being announced?

Sarah Davis - Loblaw Companies Ltd - CFO

No.

Patricia Baker - Scotiabank - Analyst

Okay. And here is my really important question. When you look at the integration, can you talk about the strategy from an integration perspective, how it is going to be handled because you will be doing the integration -- you'll still be in the tail end of SAP at the Loblaw level. So if you talk a little bit about how you're setting up the integration and how it's going to proceed?

Vicente Trius - Loblaw Companies Ltd - President

Yes, good morning, Patricia.

Patricia Baker - Scotiabank - Analyst

Thank you.

Vicente Trius - Loblaw Companies Ltd - President

First off, we see Shoppers Drug Mart as an independent separate division.



Patricia Baker - Scotiabank - Analyst

Okay.

Vicente Trius - Loblaw Companies Ltd - President

We see ourselves as obviously having a separate integration team, that will work on delivering the synergies. We are communicating about CAD300 million of synergies in COGS and expense over the first three years, which we believe they are realistic and achievable. And as far as SAP, I mean, we are actually on target. We have rolled out 60 [seats], we are in the process of rolling out our stores. We are in the process of building a strong foundation, and behind SAP and the IT infrastructure, and we see us delivering according to our commitments. So we see no, no issues.

Patricia Baker - Scotiabank - Analyst

Okay, thank you. I will get back in the queue.

Janet Craig - Loblaw Companies Ltd - SVP, IR

Thanks, Patricia.

Operator

Your next question is from the line of Chris Li from Bank of America. Your line is open.

Chris Li - BofA Merrill Lynch - Analyst

Hi, good morning. First question, is just for the associate owners of Shoppers, do you expect any changes to their current compensation arrangement, and what are your plans in terms of retention?

Domenic Pilla - Shoppers Drug Mart - President and CEO

Chris, it's Domenic Pilla. So we are not planning to -- as part of this combination to close any stores, and we are not planning to change the associate model, and we will continue to operate under that model. We like that model. You have heard me say that before. We think it is a strategic and competitive advantage. And we really value the contribution that they make, and the creativity entrepreneurship that they bring, and the stewardship that they bring to the store level. So we are not anticipating making any changes there.

Galen Weston - Loblaw Companies Ltd - Executive Chairman

And maybe I can also add that we operate a very powerful franchise business that is similar in many respects to the associate model that Shoppers Drug Mart operates. And we believe wholeheartedly in its effectiveness, and so we think we understand it well.

Chris Li - BofA Merrill Lynch - Analyst

Okay. And just a quick follow-up question. With respect to the 25% market share, based on this do you expect any material store -- required store divestitures from an anti-trust perspective?



Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

No. These are two big businesses, but they are complementary businesses, not substantially overlapping businesses. So we think it will be fine.

Chris Li - *BofA Merrill Lynch - Analyst*

Okay, thank you.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Thanks, Chris.

Operator

Your next question is from the line of Perry Caicco from CIBC World Markets. Your line is open.

Perry Caicco - *CIBC World Markets - Analyst*

Yes, thank you. How compatible, once SAP is kind of completed, how compatible are the IT infrastructures and logistics of the two companies?

Vicente Trius - *Loblaw Companies Ltd - President*

Well the two companies have invested on building a solid infrastructure behind the technology. And I think that we can leverage the capabilities [on their end] with the capabilities [on our end], and this is something of obviously the next process as we move deeper into both businesses.

Perry Caicco - *CIBC World Markets - Analyst*

And what are the -- I guess it's CAD45 million to synergies specific to loyalty in Financial Services. What are those exactly?

Vicente Trius - *Loblaw Companies Ltd - President*

Well, this is about, obviously if you look at their loyalty card, they have about 10 million customers. We launched PC Plus, and we said all along that we told you we felt 10 to 12 [million], so maybe now it's about 15 [million]. And it's about reaching every Canadian family in this country. And when see -- when we look at PC Financial, imagine the capability to reach all those customers in our MasterCard, insurance business, I think this is very, very good.

Perry Caicco - *CIBC World Markets - Analyst*

Sorry. But are the CAD45 million in synergies, are those cost-related synergies or sales-related synergies?

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

They are both, Perry.

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

And really, Perry it is about adding significant customer insights and significant customer reach to the direction that we have already had which is creating tailored relevant offers to those individuals. And by the combination of our insights and access to customer information and their preferences, we can really leverage that across a much larger base. So it is a -- we actually have a very aligned direction. We just have now more scale and more insights, and therefore I, we think we can accelerate the direction each of our companies was already in.

Perry Caicco - *CIBC World Markets - Analyst*

Okay. And my last question is I guess for Galen. Weston is, as part of the deal, is dropping its Loblaw ownership below 50%, when I guess another CAD800 million or so would have kept you above 50%. Just wondering what we should read into that? Like what does that mean to not have full economic control of Loblaw?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Well, we don't believe it means much. Our decision to finance it that way was a combined decision between Weston and Loblaw. We believe that we will still consolidate the full financial results of Loblaw into Weston's. And it is de facto control based on voting patterns. So yes, it drops below our historically immovable object of 51%. But when an opportunity like this comes along, then you are prepared to bend the rules ever so slightly. But is it an expression of a lack of long-term enthusiasm for this transaction? I suspect based on the tone of this call, you will see that it certainly isn't. And CAD500 million is a lot of money by any stretch of the imagination, going by Weston to support the deal.

Perry Caicco - *CIBC World Markets - Analyst*

Okay, thank you.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Thanks, Perry.

Operator

Your next question is from the line of Michael Van Aelst of TD Securities. Your line is open.

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

Yes, hi. Can you give us some color as to what kind of food offering, or how you expect the food offering to change within the Shoppers stores? Is the square footage expected to be roughly the same, and you are just optimizing the mix? Or do you expect to give it a much more bigger profile within their locations?

Vicente Trius - *Loblaw Companies Ltd - President*

We did a very in-depth study on what this food proposition would look like, to the point that we actually developed what we call a mock-up store. Inside a mock-up store, which is like a dark store, non-trading but we kept all of the core from Shoppers Drug Mart. And we looked at how we can actually leverage the space that they had in food. And we feel that we can put a very, very compelling offer based on fresh, ready meals, frozen, convenience food and healthy products. Where you can go into the stores, and imagine going into the stores and being able to do a very basic full grocery shop.



Domenic Pilla - *Shoppers Drug Mart - President and CEO*

And from our perspective, we had clearly identified that opportunity, as you have heard us say before, we absolutely like the combination of food and health and nutrition and health. And it drives certainly drives traffic and is something that has been very accretive to us. But as we have identified the opportunity of what the customer wants in our food offering, in terms of the elements that Vicente has described, we didn't have the capability, and certainly we didn't have the access to the sources of supply that Loblaw has. And so the combination of bringing their capability and access to product, against what we see as strong customer need and demand we see as a really winning combination.

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

Okay. And just a small one. In your press release, you talk about double-digit accretion in year one, adjusted for intangible or amortization. Can you give us any idea of the number -- the size of that intangible amortization?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Hi, Michael, it's Sarah. So the goodwill on the deal will be about CAD11 billion. And we haven't done the split between intangible and tangible yet, so that is work that's still to come. But as soon as we have the details, we will make sure that we highlight that to you. And generally, it will be the scripts that we will be amortizing, so it will be over the life of the scripts that it will come into our earnings.

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

That is typically like a reasonably short period though, is it not like five or six years?

Sarah Davis - *Loblaw Companies Ltd - CFO*

Yes, so it will be a big number.

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

Okay, thank you.

Operator

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

David Hartley - *Credit Suisse - Analyst*

Yes, thanks. Good morning, and congratulations. I am just wondering if you can give us a little bit of color on -- if you haven't answered this already, on market share in various categories other than the scripts, so food, beauty, apparel, those kind of things?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Well, let me start answering that question, because I am not sure that it makes sense for us to go into a ton of detail. Some walking around numbers. Loblaw has about 5% share in the pharmacy business. So in that sense, an addition to Shoppers Drug Mart doesn't profoundly change the market share numbers. We are a CAD30 billion food business, and Shoppers Drug Mart has somewhere in the range of CAD1 billion in food. So this is a



complementary transaction about leveraging existing strengths and retail assets, as opposed to the combination of fundamentally overlapping sales bases.

David Hartley - *Credit Suisse - Analyst*

Okay, thanks. And just following on Michael's question, should we expect investments on the capital side to increase? Are you looking to expand footprints in your -- in the Shoppers stores as we move forward, as you think about new categories or expanding the food offering, et cetera in those store?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

So it's Galen. So just before I turn it over to Domenic, one of the things that makes this so attractive from our perspective in terms of food, is that Shoppers already has a food space. And our work is demonstrated in our own minds that we think we can considerably increase the productivity without increased space. And so the capital cost of building that convenience food proposition is very, very low. And so the short -- the early contribution to earnings if the sales come should be very attractive. So no big change to the footprints of either model.

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

Yes. And I agree with that. And in fact, as we have pointed out, in fact as some of you pointed out, we do have areas of our stores that are not very productive, like photo and photo development for example, where we have additional capacity to bring in additional categories. And we have been working hard on that, and this is obviously an enhanced opportunity to do the trajectory -- to accelerate the trajectory we are already on.

David Hartley - *Credit Suisse - Analyst*

Okay, thanks. And then just last question, just on the deal itself, could you give us a sense of how long this deal was in the works? And the kind of process that took place here, i.e. Shoppers fielding offers or opportunities or offers from others? Could you talk a little bit about that?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

So again, I will start, and then Holger may want to comment. A long time, so say, 3.5 years, and lots of conversations and discussions. I think the takeaway from my perspective on today's announcement is the timing of the transaction right now is optimal. It is optimal from a leadership perspective. It is optimal from a culture perspective. It is optimal from a regulatory perspective, and it is optimal from a fundamental sales and earnings trend perspective for both of these businesses.

David Hartley - *Credit Suisse - Analyst*

And -- (Multiple Speakers).

Holger Kluge - *Shoppers Drug Mart - Chairman*

And as you would expect from a Shoppers perspective, over the last few years, yes, we have had off and on discussions with Galen, but a lot of other people as well. We have had approaches from many firms saying, well, could we do this combination? We also had reached out to a number of firms and said, can we do deals together? And in the end, it just happened to be the right time, when these two minds came together, and came together quickly at what we believe at the right price for our shareholders. And so we have looked at many different combinations over the last few years, both solicited and unsolicited. And in the end, this came together quickly, because it was at the right time and for our shareholders, the right solution.



David Hartley - *Credit Suisse - Analyst*

Thank you.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Thanks, David.

Operator

Your next question is from the line of Vishal Shreedhar from National Bank. Your line is open.

Vishal Shreedhar - *National Bank - Analyst*

Thank you very much. Just in terms of the pricing of the deal, did you make assumptions regarding the ultimate price of generic prescription drugs, say three to five years down the line, and how did you do that?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Well, certainly, we are very cognizant of that. And we have our own views. As you know, there is ongoing effect on price reimbursement right now through 2013 and 2014, and we are very close to that. What I will tell you though is that we are being very successful in shifting the debate in Canada, from one around price reimbursement to one around expanded scope of practice and the ability to leverage our assets to provide additional services to patients. So we can lower the cost of providing healthcare in Canada and improve patient outcomes. And it's resonating very much with Provincial health ministry. And this combination actually helps us deliver those services faster and have a greater impact on patient outcomes, and in fact lower the cost for government. So I believe this combination will reduce the pressure to look at the reimbursement as the only vehicle to improve overall healthcare costs. Because we can deliver additional services that actually have a bigger impact on costs for government. And we see us as a great ally to provincial governments and have bigger scale and capabilities to do that.

Vishal Shreedhar - *National Bank - Analyst*

Okay, understood. So in terms of pricing the deal, should we think that when Loblaw has priced it, they used run rate assumptions or would they use lower generic drug price assumptions and lower, call it, commercial terms or professional [ounces]?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Look, I think we have been conservative and I think we were delighted to see through the due diligence process that our approach to assessing the regulatory environment was very consistent with the way that Shoppers Drug Mart did. And so, our vision or view of the future in terms of rebates and the price of generics is very consistent.

Vishal Shreedhar - *National Bank - Analyst*

Okay. And in terms of Shoppers being an independently-managed Company -- obviously Shoppers has been regarded by many as a very well-managed Company for a long period of time. So how should investors think about the management of Shoppers through Loblaw's standpoint? Is this independent management in place for a period of time, or is it for the foreseeable future?



Vicente Trius - *Loblaw Companies Ltd - President*

We are delighted to have the whole team of management of Shoppers Drug Mart. I mean, they are bringing an incredible strength and capabilities to the organization. We believe that they have to have the autonomy to build their business, and we believe that they can actually add a lot of value into our business. And we believe the combined business offers great opportunity for colleagues, associate owners, and employees of both companies. This actually offers growth to the overall organization.

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

And what I will tell you is I am personally committed to this combination, and very excited about it, as an opportunity for me. And as I have been working with the Loblaw team, I see tremendous cultural fit and am very excited about the opportunity it creates for our management team and the rest of our employees, both at central office, regional office and associate owners. And this is a great opportunity for us to collaborate and work with another great team. And so, we are very excited about the combination.

Vishal Shreedhar - *National Bank - Analyst*

Okay. So is it too early to comment on the period of time at which management will be, at which Shoppers will be managed independently, or is that still ongoing? Or should we just think that the structure that is in place now, is the structure that is being in place for the foreseeable future?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

So this is -- it's Galen. Loblaw's operates a series of businesses with independent autonomy, ranging from a financial services business to a T&T business to, to even the two existing major supermarket divisions, a conventional division and a discount division. So we believe that we already have a management construct or an organizational construct that this will bolt into very, very nicely. Are there going to be areas where services get centralized? Sure. But that is going to take some time. And we believe that the opportunity to get value in the short-term comes from some of the buying synergies and marketing synergies and that sort of thing, the straight costs.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Vishal, we are going to take the next caller now.

Vishal Shreedhar - *National Bank - Analyst*

Okay. Thanks for your color, and good luck and congratulations.

Operator

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

Peter Sklar - *BMO Capital Markets - Analyst*

Okay, thank you. Sarah, you ran -- in your commentary, you ran through the list of synergies. Do you mind running through the, that list, the synergy list again? And to the extent you haven't already, perhaps you and the other members of the management team could elaborate somewhat further? And as well the CAD300 million of synergies that you anticipate to achieve in year three, do you anticipate booking the full CAD300 million of synergies in year three, or is that -- do you hope to get to the, that kind of run rate by the end of year three?



Sarah Davis - Loblaw Companies Ltd - CFO

Okay. So the -- I will do the second part first. So the CAD300 million is the run rate we expect in year three, and we expect to get -- to ramp it up. So with about evenly -- so CAD100 million, CAD200 million, CAD300 million would be how we see it over the first three years. When we talk about where do we expect to see the synergies? From a -- we have about 40% we are saying through expenses, which would be as Galen mentioned, the combined marketing, supply chain, IT and some shared infrastructure. We have about 45% or CAD135 million coming from COGS, either from purchasing synergies or private label penetration. And the last piece that we talked about was on the loyalty and financial services, which is both cost and revenue synergies of about CAD45 million. So through the combination of growth in PC financial, as well as the Optimum and PC Plus integration.

Vicente Trius - Loblaw Companies Ltd - President

The one thing I want to reemphasize is that they are very realistic and achievable. And when you heard me talk about the food proposition into Shoppers Drug Mart, or when we talk about the capacity to leverage the expertise and pharmacy health and beauty side of our business, which at the end of the day would translate into more revenue and more customers and a much better customer proposition, none of that obviously, is factored in. So we see very good potential.

Peter Sklar - BMO Capital Markets - Analyst

Okay, Sarah, I am not quite clear. The CAD300 million, do you anticipate achieving CAD300 million in the full year three, or do you anticipate achieving that run rate during year three?

Sarah Davis - Loblaw Companies Ltd - CFO

The full year of -- in year three.

Peter Sklar - BMO Capital Markets - Analyst

Okay.

Sarah Davis - Loblaw Companies Ltd - CFO

CAD300 million in year three.

Peter Sklar - BMO Capital Markets - Analyst

Okay. And lastly, can you give us some idea, or a rough idea of the terms you expect to achieve on the term loan and the unsecured financing?

Sarah Davis - Loblaw Companies Ltd - CFO

We are not ready to give the details quite yet on that.

Peter Sklar - BMO Capital Markets - Analyst

Great. Okay, thank you.

Sarah Davis - Loblaw Companies Ltd - CFO

Thanks, Peter.

Operator

Your next question is from the line of Kenric Tyghe from Raymond James. Your line is now open.

Kenric Tyghe - Raymond James - Analyst

Thank you, good morning. I just to go back on the loyalty aspect here, looking at the game changer on that as well, with a combination of Loblaw shoppers and [RBC], I mean you have a potentially very compelling coalition within that. And I would like to understand your thinking with respect to how to further lever that? And then perhaps finally, we focused on the data analytics and back end integration. I am also curious with respect to the currency in the front end, and if there is an end game here, where there is a blend of currency and the like? And how that could perhaps could work as well, because that would certainly just further enhance how compelling the loyalty offering could be?

Galen Weston - Loblaw Companies Ltd - Executive Chairman

So I will begin just, Kenric, to comment on the idea of the coalition between the three organizations. I think it is premature to comment on this, as far as it might pertain to a third party. So you will have to wait for news on that. And as far as how do you combine the two loyalty programs? We don't at this stage anticipate a merging of the two currencies. We've got some real technological innovation that Loblaw has just brought to market around one-to-one marketing. And you combine that with the incredible analytical capabilities of what you see in the Optimum team and Shoppers Drug Mart. The details, we haven't worked out yet, but the potential is enormous.

Domenic Pilla - Shoppers Drug Mart - President and CEO

Yes, and the direction of travel or the trajectory is the same, which is around becoming relevant, customized to individual customers based on their needs and their purchase history. And so both programs want to go in the same direction, and we can use our complementary strengths to strengthen in fact both programs.

Vicente Trius - Loblaw Companies Ltd - President

It's interesting when we look at the two companies, that we have very similar strategies in many fronts. And when you look at the whole play of the omni channel and technology and how this ties in with the loyalty, both companies have been working on that. So I think for the future, we can actually leverage it even better.

Kenric Tyghe - Raymond James - Analyst

And just a follow-up there if I could. Domenic, on the Optimum program, is the move next year to sort lever what Shoppers -- what Loblaw has done with their Smart loyalty into the smartphone-enabled loyalty? I mean is that one of the earlier potential wins here, as we look to better monetize the loyalty offerings of both companies?

Domenic Pilla - Shoppers Drug Mart - President and CEO

It is a great example of a terrific complement between our two programs.



Kenric Tyghe - *Raymond James - Analyst*

Great. Thanks very much. I will leave it there.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Thanks, Kenric.

Operator

Your next question is from the line of Keith Howlett from Desjardins Capital. Your line is open.

Keith Howlett - *Desjardins Securities - Analyst*

Yes, I was wondering on the drug procurement side, Shoppers purchases and distributes directly. I think Loblaw uses a third-party. How long does it take to transition from third-party to Shoppers platform?

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

Well, we are early days in terms of understanding what that benefit is, and there is benefit both ways. And even in our system, we use third-parties for some of our needs, so something we are going to work through. But from a capability standpoint, if we make that decision it is a fairly easy transition. But early days, in terms of identifying that as an opportunity and putting it into our integration plan.

Keith Howlett - *Desjardins Securities - Analyst*

And then just a question on the advantages of Loblaw's brings to the pharmaceutical services, but you mentioned that, which are those advantages -- at the medical clinic in the store or?

Vicente Trius - *Loblaw Companies Ltd - President*

The advantages I was referring a lot more on Shoppers Drug Mart bringing into Loblaws. Having said that, we do have medical clinic and optical centers that we could leverage. But we see the strength of the model that Shoppers Drug Mart has as a strength that actually we can leverage into our business.

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

And certainly there is areas that we see a great opportunity around professional services, around the operation of the pharmacy, our proprietary pharmacy system and so on, so we think those are opportunities for us to leverage against Loblaws pharmacies. But the opposite is true as well. Certainly around medical clinics, optical, around adherence working with Rx Canada on adherence, there is areas that Loblaws has actually been quite innovative, and we are very excited about being able to bring some of those innovations into our pharmacy. And really it is complementary across all of the dimensions, and again, a real reason why we are excited.

Keith Howlett - *Desjardins Securities - Analyst*

And is it envisioned that the in-store pharmacies will be managed by Shoppers Drug Mart under the Shoppers brand?



Vicente Trius - *Loblaw Companies Ltd - President*

Look, I mean early stages to even talk about brands. And what we will do is really leverage the talent of the both companies.

Keith Howlett - *Desjardins Securities - Analyst*

Great. Thanks very much.

Operator

(Operator Instructions)

Your next question is from the line of Patricia Baker from Scotiabank. Your line is open.

Patricia Baker - *Scotiabank - Analyst*

Oh, sorry. It's all right, my follow-up questions were already asked. Thank you.

Operator

Your next question is from the line of Mike Van Aelst from TD Securities. Your line is open.

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

Sorry, been asked as well, thank you.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Thanks, Michael.

Operator

Your next question is from the line of Keith Howlett from Desjardins Capital. Your line is open.

Keith Howlett - *Desjardins Securities - Analyst*

Yes. I just wanted to ask on the real estate development plans going forward, are the -- is the real estate departments going to combine, or will they continue to sort of prepare separate capital plans?

Galen Weston - *Loblaw Companies Ltd - Executive Chairman*

Well, look, these are all good questions and fair questions. I think give us the appropriate amount of time to come back to you with a formal plan. But obviously, I mean if you were to take the choice properties, this is an incredible vehicle to work with, now that we have an entirely different real estate platform for growth. So we would expect like -- in so many of these areas to see really attractive synergies. I think that the point that we



are making here is this is not just about stripping out costs and banging the businesses together. This is about taking best practices from both organizations in a very compelling way, focusing on growth, and finding costs in intelligent parts of the P&L.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Great, thanks, Galen. And we have time for one more question.

Operator

Your next question is from the line of Jim Durran from Barclays. Your line is open.

Jim Durran - *Barclays Capital - Analyst*

Yes, just wanted to go back to private label. I am just trying to wrap my head around the Sanis opportunity at Loblaw. I assume you have incorporated that in your assumptions. But can you give us some idea as to how important Sanis private label would be, relative to the inverse side of the equation being Loblaw's private label into Shoppers?

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

Well, I don't have a relative figure to share. But certainly, we believe that Sanis has been a tremendous development for us, and has allowed us to lower our cost of goods and improve service levels, and provide better service to our patients. And we think we can certainly leverage that strength into the Loblaw pharmacies, and is one of the complementary activities that we plan to undertake.

Vicente Trius - *Loblaw Companies Ltd - President*

And from a standpoint --

Jim Durran - *Barclays Capital - Analyst*

And the third --

Vicente Trius - *Loblaw Companies Ltd - President*

Go ahead? (Multiple Speakers).

Jim Durran - *Barclays Capital - Analyst*

Sorry, go ahead.

Vicente Trius - *Loblaw Companies Ltd - President*

No, go ahead.



Jim Durran - *Barclays Capital - Analyst*

Go ahead, Vicente.

Vicente Trius - *Loblaw Companies Ltd - President*

No, you asked about -- (Laughter).

Jim Durran - *Barclays Capital - Analyst*

On the food side --

Vicente Trius - *Loblaw Companies Ltd - President*

Loblaw, and you were asking, as well from Loblaw into Shoppers Drug Mart, and I was trying to address that question. And we see that much more around obviously our control brand, President's Choice, President's Choice Blue Menu, No Name, that we can actually bring into their stores. And I think it will add a lot of value to those locations.

Jim Durran - *Barclays Capital - Analyst*

And from a DC integration standpoint, are the things that we should understand that are different about the Shoppers distribution center technology that would not allow a merging of those types of facilities, that they would have to remain standalone?

Vicente Trius - *Loblaw Companies Ltd - President*

I believe that you have two very good supply chain networks. Having said that, there are synergies that we can use obviously using their capabilities in some range of the products that they have. And using our capabilities on the food side of the business, there could be combinations where we use their transfer and consolidation facilities, and we use our sourcing capabilities. So there is many pieces that you can put together on the supply chain that I believe will bring synergies and say, efficiencies.

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

We both use Manhattan.

Vicente Trius - *Loblaw Companies Ltd - President*

Oh, okay.

Jim Durran - *Barclays Capital - Analyst*

Right. Sorry, Domenic. What is your capacity utilization of your distribution network right now?

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

We have plenty of capacity.



JULY 15, 2013 / 12:00PM, L.TO - Loblaw Companies Ltd Conference Call to Discuss Definitive Agreement to Acquire Shoppers Drug Mart Corporation

Jim Durran - *Barclays Capital - Analyst*

Okay, that's great. Because it certainly seems to me like the Sanis private label opportunity to Loblaw from a synergy standpoint, seems quite substantial on my rough cut of numbers. So I was just trying to get a sense of whether that had been fulsomely reflected or not?

Domenic Pilla - *Shoppers Drug Mart - President and CEO*

Yes, we haven't done that. We are not at that level of detail.

Jim Durran - *Barclays Capital - Analyst*

That's great. Thank you.

Operator

This concludes today's question and answer session. Ms. Janet Craig, I turn the call back over to you.

Janet Craig - *Loblaw Companies Ltd - SVP, IR*

Thanks, Melissa. I wanted to thank everyone for coming to our call on such short notice. I know there were some challenges getting on the call, because there were hundreds of people calling in. But we certainly appreciate the interest, and we are available for questions in the minutes and days to come. Thank you.

Operator

And this concludes today's conference call. You may now disconnect.

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