

FINAL TRANSCRIPT

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L.TO - Q1 2010 Loblaw Companies Earnings Conference Call

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PRESENTATION

Operator

Good morning. My name is Sarah, and I will be the conference operator today. At this time I would like to welcome everyone to the Loblaw Companies Ltd. first-quarter results conference call. (Operator Instructions).

Thank you. I would now like to turn the call over to our host, Kim Lee, Senior Director of Investor Relations. You may begin.

Kim Lee - *Loblaw Companies Limited - Senior Director, IR*

Thank you, Sarah. Good morning and welcome to the Loblaw Companies Ltd. first-quarter conference call. This call is being webcast simultaneously on our website at www.loblaw.ca.

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I'm joined here this morning by Galen G. Weston, Executive Chairman; Allan Leighton, President and Deputy Chairman; Bob Vaux, Chief Financial Officer; and Sarah Davis, Executive Vice President of Finance.

Before we begin today's call, I want to remind you that the discussions will include forward-looking statements, including the Company's beliefs and expectations regarding certain aspects of its financial performance in 2010 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 first-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 are referred to today. Please refer to our first-quarter report and other materials filed with the Canadian Securities regulators from time to time for a description of these measures and a reconciliation of each of them to the most directly comparable GAAP financial measure. Our first-quarter report, as well as the 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 Limited - Executive Chairman*

Good morning. Thank you for joining us. We have remained on track with our renewal program and continue to be focused on driving sustainable performance. You will hear a little bit more about that from Allan later in the call.

Our major investment in technology and supply chain will now start to ramp up, and as previously announced, we expect these investments to negatively impact 2010 operating income.

I will turn the call over to Robert Vaux to review our financial performance.

Bob Vaux - *Loblaw Companies Limited - CFO*

Thank you and good morning. Sales in the first quarter of 2010 increased by 3.1% to CAD6.9 billion. Same-store sales increased by 0.3%. The acquisition of T&T, which was completed in the third quarter of last year, positively impacted sales by 2%, and both sales and same-store sales in the quarter were about at 0.5% higher as a result of the lapping labor disruptions in certain Maxi stores in Quebec, which occurred during the first quarter last year.

Excluding these items, sales increased 0.6%, and same-store sales declined 0.2%. In the first quarter of 2010, sales growth in food was flat, and sales growth in drugstore was modest. Sales growth in apparel was strong, while sales of other general merchandise declined significantly, and gas card sales increased significantly as a result of higher retail gas prices and strong volume growth.

National food price inflation is measured by the Consumer Price Index for food purchased from stores was 0.7% in the first quarter of 2010. In Q1 we saw greater internal retail food price deflation than in Q4 of last year. In Q1 '09 we experienced internal retail food price inflation.

Gross profit in the quarter was CAD1.7 billion or 24.8% of sales versus CAD1.6 billion or 24% of sales in the first quarter of last year. The improvement was primarily due to buying synergies, disciplined vendor management, a stronger Canadian dollar, improved inventory management and controlled label profitability. Operating income was CAD260 million in the first quarter compared to CAD226 million in Q1 of '09. Operating margin was 3.8% in the quarter compared to 3.4% last year.

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The improvements in operating income and operating margin were primarily due to the increases in gross profit and gross margin and a lower charge related to stock-based compensation. These were partially offset by an increase in depreciation and incremental costs related to the Company's investment in information technology and supply chain. The Company incurred an incremental cost of CAD28 million in the first quarter related to the previously announced investment in IT and supply chain.

Loblaw realized first-quarter basic net earnings per common share of CAD0.50 compared to CAD0.40 in the first quarter of '09. Net debt at the end of the first quarter was CAD3 billion compared to CAD2.8 billion at year-end and CAD3.6 billion at the end of Q1 '09. The increase in net debt in the first quarter was due to the seasonal increase in operating working capital. Capital expenditures in Q1 were CAD148 million, and we estimate that capital expenditures for 2010 will be about CAD1 billion.

This is my last quarterly conference call as CFO of Loblaw Companies Ltd. It has been a pleasure speaking with you, and I wish you all the best. I'm pleased to be passing the reins to Sarah Davis who will become CFO of Loblaw Companies Ltd. at our shareholders meeting tomorrow. I'm highly confident that Sarah will add significant value as the new CFO.

I would now like to turn it over to Allan Leighton who will provide some context on the remainder of the year.

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Thank you and good morning, everyone. From a market perspective, the quarter was a continuation of the last. Wobbly from week to week, market volume under pressure, but with deflation deflating at a faster rate. The key consumer trends from our perspective -- inflation, unemployment and household debt -- remain unhelpful and were unhelpful in this quarter.

These are the trends that we believe will prevail into the second half of this year, and we continue our balancing act of focusing on volume and volume share whilst executing our supply chain and IT infrastructure programs.

From an IT infrastructure renewal perspective, we remain on track. We spent below the CAD46 million quarterly average for the year but expect to spend at that level and recover the Q1 shortfall over the next couple of quarters.

We have also started the rollout of STAS, which is our store time and attendance system. It is in 36 stores largely in Ontario, and the results have been encouraging. We expect to be in over 120 stores by the end of Q2 and in 90% of all of our stores by year-end.

On supply chain 2010, it was a significant quarter. TMS and WMS continue to roll out with three more DCs on WMS bringing the total to six, and TMS is in six more depots bringing that total to 22. We are on plan to have all our depots on TMS by the year-end and 60% of depots on WMS by year-end.

On the physical infrastructure of supply chain, we opened a new frozen DC in Moncton. We did a small refresh of our Edmonton DC, and we opened four produce consolidation in Arizona. We expect to have six consolidation centers in the US by the year-end as we are constantly striving to improve the freshness of produce for our customers.

We also announced the closure of our Sudbury Depot.

This is all part of our plan to build significant flexibility into our supply chain infrastructure. That allows us to supply our stores at the lowest cost per case from the most efficient and flexible depots.

Subsequent to the quarter-end, we announced the closure of Quebec City DC and Boucherville meat facility. This will result in a charge of in the range of CAD30 million to CAD40 million, which we will take in Q2.



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In Quebec, as you know, we have been piloting a number of pilots in retail. Loblaw to Maxi and Maxi and co-conversions. So Maxi and co-renovations with less general merchandise and Maxi refreshes rurally throughout Provigo's franchising that banner and in the urban Provigo's converting them to a smaller version of Great Foods. And we have been renovating our Great Food stores in Loblaw.

And on the back of the results of these pilots, we intend to significantly ramp up our renovation and refresh programs in Quebec, and around 120 additional stores will be touched in some way during the remainder of this year.

The other major news in the quarter was the announcement of the Ontario drugs regulation. The P&L impacts on our business is substantial but not material, and we intend to mitigate as much as we can by aggressively driving share in our drugstore business. We have close to 500 pharmacies across our portfolio, and we intend to extend opening hours and services in the vast majority of them. We are also piloting a smaller footprint pharmacy, which may give us the opportunity to increase our pharmacy estate in smaller stores both in a retrofit and on a go forward basis.

We also have 84 medical centers in our stores, which are a real convenience for our customers. We see the opportunity to increase the service to more than 200 stores over the next few years. We've also commenced a program that will see state-of-the-art technology in more than half of our pharmacies by the year-end.

In summary, the balancing act continues. The period of maximum disruption draws even closer, and as always, we remain cautious in our outlook. With that, operator, I would like to hand over to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Perry Caicco, CIBC World Markets.

Perry Caicco - CIBC World Markets - Analyst

With same-store sales in positive territory and deflation lower than ever, I guess even with other pieces of noise in the business, the implication is the tonnage, I guess, on a same-store or a total basis may no longer be deteriorating. So I just kind of wonder how you feel about your tonnage growth right now compared to where the market is and how do you see the next few months playing out?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

I think on sales rather than talk about absolute tonnage is we have been pretty consistent with where we were a quarter ago. Our items are up. Our transactions are up. Our customer account is pretty consistent, and our transactions in terms of value are just down a tad.

So I'm relatively pleased with where we are tracking. The market, though, as I said earlier, is still a bit wobbly. In fact, that has not changed very much from where we were a quarter ago. As you know, my view is that this is going to be like this probably way into the second half of the year. If you look at inflation last year, it was clearly periods seven and eight that it really started to come down, and that is what we are planning on.



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Perry Caicco - CIBC World Markets - Analyst

Okay. And then if I could, kind of a two-part question. I'm just wondering what portion or percentage of senior management time and attention is taken up with the infrastructure project. Then, the second part of that is I'm wondering do you feel that this does in any way taking away from or somehow impacted day-to-day merchandising in operations?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, I mean the answer to the second question is probably. Because, as I have said from the outset, the senior management, this is not an IT project. It is a business project. And the top team are responsible for the systems implementation and the process changes in their areas. So I would believe there probably has been an impact, and as you know, my concern is for the rest of the year that that impact becomes greater because clearly it becomes -- it will take more of people's time.

We are still at the early stages of the work, and over the next five or six months, that really builds up. So it is always been one of the biggest issues for us.

Plus, the fact, as you know, it is not just the senior management issue. It does mean the whole business is going to be doing two other things as well as trading the Company. One is changing the processes, which is so important to do ahead of SAP, and then secondly, for a protracted period of time, coexisting with two different sets of systems. So that part of my caution has always been these things are all consuming. At the moment it is probably consuming 15% to 20% of people's time, and as it goes through the year, it is going to consume more than 50% of people's time.

Operator

Patricia Baker, Scotia Capital.

Patricia Baker - Scotia Capital - Analyst

I have two questions, and both of them may end up seeming a little bit maybe overly pedantic or nitpicky. But I just want to focus very carefully on what you said in your remarks.

First of all, you indicated that you will, in fact, spend the full CAD185 million on IT and supply chain in 2010 and that you expect to re-allocate the additional CAD18 million over the course of the next couple of quarters. Now I hate to be picky, but a couple to me means two. So we should just look for that to be in Q2 and Q3?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

That sounds a very good piece of analysis.

Patricia Baker - Scotia Capital - Analyst

Very simple. Okay. Now with respect to that shift in IT spend and I think it was a surprise to many people that we saw the run-rate at CAD28 million in the first quarter, and you indicated to us mid-February that you would be spending CAD185 million. Can you help me understand why you would not have indicated to us at that time that the actual ramp-up would not really start until we got into the second quarter?



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Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, two things, Patricia. Not wishing to be nitpicky, I think what we tried to give you some guidance that it would be equally spread over four quarters, and that is a piece of guidance. It is not going to be as exact as that for a number of reasons.

First of all, Q3 just happens to have four periods in it as opposed to every other quarter has only got three. The second thing is a lot of this, it sort of does change, not week-to-week, but you can spend so much in one week and then not as much the following week. So there's two or three weeks of volatility always in these numbers depending on how things are going. And lots of things flick around towards the end of periods and quarters.

So I'm not -- I'm slightly surprised we did not quite spend -- we did not quite spend the 45 in this particular quarter. But actually I can understand why because we have the same sort of volatility towards the end of last year.

So my sense is it is not an exactitude. It is a piece of guidance. It will move around a bit. But looking from what we can see over the next two quarters, it looks as if we will spend at about that right rate and also recover what was not spent in Q1. And part of that is because there are set dates where these pieces of work needs to be done, and the important thing is to arrive at the work done at the set date. It does not absolutely work exactly on the run-up to that.

So I think what we have given you now is pretty good guidance, but you cannot hold me to it entirely because it will move around a piece.

Patricia Baker - Scotia Capital - Analyst

That is always the case, though, isn't it? And I guess to be fair, what you're trying to say is you are more confident today in what you are guiding us to then you would have been on 17th of February?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Yes, but again, I would --

Patricia Baker - Scotia Capital - Analyst

But we should not be taking it to the bank. Okay.

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

No, I don't think so. But what you can do is the year number is a pretty bankable number.

Patricia Baker - Scotia Capital - Analyst

Okay. Well, we will just stop building quarterly models. That would help everybody.

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Then we would have to report quarterly.

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Patricia Baker - Scotia Capital - Analyst

That would be nice, too. Okay. Secondly, and again it is a bit nitpicky, but on this pharmacy regulation and you have outlined, it sounds as if you're getting a lot more aggressive on the pharmacy side. You did indicate that in terms of what the impact would be on your business, substantial but not material. And I would like you to help me understand what is the delta between substantial and not material? They sound almost like synonyms to me if you leave out the not.

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

So I mean the important thing here is that clearly we have a pretty big drugstore business, and these regulations do have an impact on that. But it is a relatively small part of our overall business, and therefore, that is why it is not material. It is pretty substantial to the drugstore business.

Patricia Baker - Scotia Capital - Analyst

Okay. So that is what you mean; substantial to the drugstore business but not substantial to overall LCL?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

And then I think the second thing on this is that we have always felt that this is an area of opportunity for us. As you know, I have always said we underperformed, and you have two options. Our view is that this is probably now what is going to happen, and so we're very focused on how we use that. And, as I say, we see it as a big opportunity now for us to drive our drugstore business, and frankly, we are going to have to do that as part of the mitigation. So our mitigation is to drive share.

Patricia Baker - Scotia Capital - Analyst

Okay. If your mitigation is to drive share and you say how do you use this opportunity to take this opportunity, would you be actively pursuing file buys?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Yes, I mean we do anyway, and that is a part of what we do. But there are two ways you can grasp this. You can sit on your hands or you can get very front-footed about it. And in the end, it is still going to be a huge amount of consumers out there who are going to be looking for improving service, and that is what we intend to do. We have been on this for a period of time. I have always felt we've underplayed it, and you can assume from what I said today we intend to be very aggressive about it.

Patricia Baker - Scotia Capital - Analyst

And you are already front-footed and not sitting on your hands until it is over? You have already started to get aggressive?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Yes, we have been on this really for the last four or five months. In our view, when you know these types of things are coming out, you have a couple of plans. You have a plan where you think everything is going to be fine, and you have a plan for when you don't think it's going to be fine. And so we are in I feel in very good shape.

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So the 500 pharmacies we can really roll out the medical clinics. We call it the smaller version of the pharmacy. It is a very interesting piece of innovation.

Patricia Baker - Scotia Capital - Analyst

Where are you testing that, Allan?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

In one of our stores and we will let you know at another stage, and there is a huge opportunity to retrofit those. So for us our guys are very front-footed about this and we think pushing strongly from behind.

Operator

Irene Nattel, RBC Capital Markets.

Irene Nattel - RBC Capital Markets - Analyst

As you were walking through the contributors to the gross margin gains, you mentioned improvements in private labeled profitability. And I know this is clearly a big initiative for the next, let's call it, 12 to 18 months. Could you give us an idea of where you stand with that? Because it seems to me that we are still in the relatively early stages.

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Yes, we are. There are three -- I think you listed five contributors to the gross margin improvement. There are really three key ones -- continue vendor management, the Canadian dollar and controlling profitability. We are probably at about a third of the way through where we need to be on that. Clearly it is beginning to have an impact as it should be, and I would expect that to grow as the year continues.

Irene Nattel - RBC Capital Markets - Analyst

That's great. And can you talk a little bit about -- although you said that from week-to-week things are being a little bit wobbly. But are you seeing a stabilization at this point in time of consumer purchasing patterns overall? Are you seeing them starting to come back perhaps a little bit to some of the higher margin products ex private label?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Not really. It is a -- the one thing that has changed significantly, and you know we do a huge amount of consumer research -- and the one thing that has changed I think it may have changed forever, is the amount of shopping around there is. People are much more promiscuous than where they are. Probably on the type of work we do is that it is twice the level of promiscuity as you would have found a year ago. So that is at quite a big change I think and something that is still growing a bit. And, of course, the fact that all of the flyer programs have become so aggressive plays to that promiscuity, too. But the rest of it is being as much as it's being for a period of time, but that is the big change. But I would not describe it settling down by any measure yet. There are some very odd terms on a week by week basis.



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Irene Nattel - RBC Capital Markets - Analyst

And can you talk a little bit about what is going on in terms of discount versus conventional?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Again, much the same. It is -- there is this move a bit more towards discount and to have discount and to superstore, I guess. But again, our commercial businesses have been holding up pretty well, too. So I think actually in a strange way people are still shopping -- the balance of shop between physically where you go, how discount and conventional is not changing very much. But what does change from a week to week basis is what you purchase in there, and that is a bit of what we are seeing in terms of shopping around.

Irene Nattel - RBC Capital Markets - Analyst

That is great. And just for housekeeping purposes, can we quantify what the impact was on same-store sales of the higher gas prices in the quarter?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Again, we do not give that. I will give you a bit of guidance. It would have been more than it would have been in the last quarter.

Operator

Jim Durran, National Bank Financial.

Jim Durran - National Bank Financial - Analyst

I just wanted to go by region. I know you don't provide details, but if you were to describe where you're at in terms of the stored network in Ontario in terms of how finished it is, in terms of refresh, etc., where would you say Western Canada is in comparison to that?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, they are both in a similar place. A lot of our work -- we have done a lot of work on the Loblaw banner in Ontario, which has been very good, so that Loblaw banner is in pretty good shape. No Frills is consistently we build new ones and spend money on renovations and refresh.

The big program in Ontario at the moment tends to be around Zehrs because that has been the one that has been the most neglected from a physical sense. But bit by bit we are beginning to cover most of the bases. And Vince is working hard in terms of what he wants to do in terms of Fortinos, where, again, we will put quite a bit of investment in towards the end of the year.

In the West clearly the Extra Foods have been converted to No Frills, and that still continues on. And the superstores have been a very big part of the program in the second half of last year and next. We will have done probably up to 60% of all of the superstores in the West probably towards the end of this year.

But we have got big programs. This is probably the biggest capital program we have ever had on our existing stores in process at the moment, and (inaudible) just added to that in the last two or three weeks by insisting on this work in Quebec because

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we feel pretty good about what we have seen from the pilots so far. So a big year, hopefully by the end of this year, two-thirds of the state will be in pretty good shape.

Jim Durran - *National Bank Financial - Analyst*

And do you see a material improvement in [retail] in superstore in Western Canada?

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

What do you mean, in terms of performance or in terms of what it looks like?

Jim Durran - *National Bank Financial - Analyst*

In terms of performance.

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

Yes. We are very pleased with what has happened in the West.

Jim Durran - *National Bank Financial - Analyst*

And are you able to give us any specificity on the IT side in terms of what is going to be done in the next six months?

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

No, I think the key thing is CR2, which is at the moment they are in the design phase, which is primarily the merchandising and some finance systems. For me they are sort of major risk, and this is around (inaudible) probably rather than finance.

The middle of June is a very important date because that is when that design work is complete. If that design work is complete, which it should be, because it is on schedule today, then we start to move really into implementation mode, and that is going to be when it gets really tested. And that is really end of June, July, August, into September. And those four months are going to feel like it is the dark side of the moon.

Jim Durran - *National Bank Financial - Analyst*

And the last question, just back to the drugstore issue, in terms of materiality, every quarter you do disclose the impact of your equities forwards, which this quarter was only a couple of cents. In your materiality test, does the drugstore number exceed that number?

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

I'm looking at Sarah actually.

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Sarah Davis - Loblaw Companies Limited - EVP, Finance

I think the reason that we put out the equity forwards is it's not an operating item. So that is why we have always done that for the last few years. On the drug reform because it is part of the day-to-day business, we have not put out a specific numbers, but it is fair to say it is going to be a bigger number than the equity forwards.

Operator

Peter Sklar, BMO Capital Markets.

Peter Sklar - BMO Capital Markets - Analyst

Just going back to the incremental spend on IT and supply chain in terms of your accounting forward, I presume some of it is expense and some of it is capital, which will be amortized or depreciated over time. So does the CAD185 million represent the cash, the total cash outflow effect in 2010, or does that represent the P&L effect in terms of the hit on your earnings?

Sarah Davis - Loblaw Companies Limited - EVP, Finance

Okay. So the CAD185 million is the incremental impact on the operating income. So it includes both the cash and the associated depreciation of the capital spend.

Peter Sklar - BMO Capital Markets - Analyst

Okay. And do you know what the actual cash outflow would be then associated with the entire program for the year?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, we would but I'm not sure we would say what it is actually. So there is something about that off-line, and if need be, we will come back to you.

Peter Sklar - BMO Capital Markets - Analyst

Okay. And then the other thing, in your comments on gross margin and the improvement in gross margin, one of the things you referred to was the impact of the strong Canadian dollar, and obviously you are referring to the impact of wholesale food deflation in Canada. So I'm just wondering, what are you saying there? Is that -- is the industry as a whole not -- is all of the savings not getting passed through into retail food inflation? Is some of that deflation being retained by the industry and is not just flowing through to retail? Is that what you are saying?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, it would be a mixture because remember they are all ingredients. So you may have a positive on the margin in terms of the price that you buy it, but you may decide to invest that somewhere else in the business. I think the real reason we flagged the Canadian dollar this time is because clearly it has had an impact, particularly on produce margins, but secondly, the dollar has been a bit more consistent. The reason we have never really flagged it before is it is a bit up and down. But with this more consistency, we will play a slightly stronger play in terms of our margin.

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However, the other way to think about it is we buy a lot of our produce clearly in the US, but we buy a lot of our GM from the Far East that we pay in dollars. We have seen a complete split. A year ago we would have looked very bad in terms of the purchasing. So there is also bit of year-on-year effect in general merchandise. So that is why I say of the total gross margin increase, the three big ones are Canadian dollar, which then either gets translated into lower prices somewhere else or you take it in produce, but also the GM impact; controlled label, which is clearly straight to the margin because that is the idea; and vendor management, which is business as usual.

Operator

Winston Lee, Credit Suisse.

Winston Lee - Credit Suisse - Analyst

I just wonder when you look at the gross margin performance in this quarter and over the last several quarters, does it surprise you that you have been able to do what you have been doing in moderating inflation environments are deflating?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

I think that to a degree, yes, but I think what you learned to do -- and I've had to do it a few times in my life -- is you have to manage businesses in a slightly different way when you have got a deflationary environment. And I think that everybody is trying to manage it in a certain way. We have had -- clearly the dollar helps. Clearly the control profitability was a piece of action that we decided upon 12 months ago, which is clearly making a difference. So whether this is sustainable, I don't know, but I think what happened is not by accident. It is because we have done some things basically.

Winston Lee - Credit Suisse - Analyst

Would you say that the wobbly volumes in the industry have garnered increased vendor support or vendor investment?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

I think clearly the vendors are in the same position, and therefore, they, too, are jostling for marketshare. And, therefore, they, too, have to be more aggressive and sharper and everything else. And that is very good. When you have got the vendor community, you're also in a similar position. That tends to give the opportunity to get CAD4.00. Whether there are more dollars in the market, I don't know. I think the most important thing is to take more than your fair share of that.

Winston Lee - Credit Suisse - Analyst

Any thoughts on your PC Points Program, if there is anything more that you can do there? It seems a lot of retailers are going back to their loyalty programs. Do you feel satisfied with that?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

No. I mean we are -- we did a very interesting piece of work a few weeks ago in the superstore. We did 20 times on PC Points in our Ontario superstore, and we are very pleased with that. So I think there is more that we can do with PC Points. And (inaudible) who runs all that and our whole loyalty approach by using the bank data is very heavily engaged at the moment in developing programs which we think will be significant.

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Winston Lee - *Credit Suisse - Analyst*

And in terms of IT and supply chain costs, how much -- and maybe you might have to go back and dig this up if you could provide it, it would be great -- but how much of the CAD73 million last year of incremental spend was in G&A versus in the SG&A and same with the question this quarter of the 28 --

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

We will dig it up and come back to you.

Winston Lee - *Credit Suisse - Analyst*

Okay. And then lastly, on the IT and supply chain going forward and as we think beyond this year, is 2010 the peak year for incremental IT spend?

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

No. I mean it is a -- 2011 will be big, too.

Winston Lee - *Credit Suisse - Analyst*

Sorry, I did not hear that last part.

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

Yes, 2011 will be a big year, too.

Winston Lee - *Credit Suisse - Analyst*

Oh, 2011 will be a big year, too. Okay. Thanks very much.

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

2010 and 2011 are the big years in investment.

Operator

Michael Van Aelst, TD Newcrest.

Michael Van Aelst - *TD Newcrest - Analyst*

I would like to touch on the general merchandise to start. You commented that it was down significantly, but clearly a lot of that has to do with SKU reduction. If you were to back out the SKU reduction and the planned reductions I guess then, how are the core categories that you want to stay in doing?

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Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, first of all, power has been stellar. So their power performance is very, very strong. And so we are very pleased with that, and Joe is very pleased with that.

Secondly, the core businesses that Joe has been working on really because you know there's two things you have to do. You have to get the SKUs out, and then you have to get the right SKUs in because of just the timelines of managing these businesses. These are the 12, 15 months worth of work. You just cannot switch it on, switch it off.

I think that we are -- and I know Joe is beginning to feel pretty pleased about his core offer. And when you start to take this space, the reduction off and the SKUs off then, that is beginning to look quite encouraging, particularly in the stores which we are renovating.

So I think that I feel the same way and I think Joe feels the same way that that core home business is beginning to get in good shape, and clearly we are planning on not just getting some sales growth but also getting some margin growth in that business.

Michael Van Aelst - TD Newcrest - Analyst

Over what period?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, Joe, at the moment is working on -- and I just got the right-hand side of the store -- and really he has been on home for about nine months, and that is starting to come to through. The other element he has just taken over. So this is for me is another 12 or 18 months worth of work. But it is not all going to come at the end. We are sort of building out our way through it.

Michael Van Aelst - TD Newcrest - Analyst

And flipping to T&T, it seems like you're getting some pretty good growth there. Because I think when you bought it, it was around 1.6% of sales, and now it looks like it is about 2% of sales. So that would imply some pretty good growth. Can you comment on that at all?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Again, we do not comment on individual banners, but to say we are very pleased with the T&T acquisition for two reasons. One is, not just as performance, but the amount that we are learning about ethnic business, which is a very important thing for us, and where we believe that the idea of buying T&T was not just to buy that business, but it was to really improve and increase our understanding and marketing capability in ethnic food. And we are certainly getting that benefit, too.

Michael Van Aelst - TD Newcrest - Analyst

How many T&Ts have you opened since you bought it?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

I think we have only opened one actually, and the idea is to doubleup over the next couple of years.

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Michael Van Aelst - TD Newcrest - Analyst

And then on the operating expense line, it looks like you had some good management of those costs. Are you going to highlight some of the areas where you might be having success in reducing costs or at least maintaining them?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, it is across the board. We run a very tight ship. By running a tight ship, it means that people have to be much more efficient. It drives productivity. That is what it does. And so most of the areas are in pretty good shape actually. We ended being like that for the last 12 or 15 months.

Michael Van Aelst - TD Newcrest - Analyst

Are there any main buckets that are going to roll off at any time, or is it just an ongoing effort?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

We are not banking on any buckets rolling over.

Michael Van Aelst - TD Newcrest - Analyst

I guess one last question, the D&A jumped about 15%, and I think last quarter it was suggested it would be up over at least more than the 7% that we saw in 2009. Is this the level that we should be looking for for the year?

Sarah Davis - Loblaw Companies Limited - EVP, Finance

Okay. So we are up CAD20 million Q1 this year versus last year, but I think the CAD20 million is a pretty good estimate for the remaining quarters other than Q3, which has a four period quarter, so you just have to factor that in.

Operator

Keith Howlett, Desjardins Securities.

Keith Howlett - Desjardins Securities - Analyst

I had a question on deflation. As you exited the quarter, was deflation higher than when you entered or about the same?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Higher.

Keith Howlett - Desjardins Securities - Analyst

And so are you expecting sort of peak deflation by the midsummer, or where do you see that?

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Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, I have always said look at it the way, I think we are into -- my idea has always been the same. It is going to be the second half of the year before we really start to see inflation. We may get a few pigments like everything else, but there may be a few false horizons. It may well be in the next six weeks as there are one or two weeks where you think there is a bit of inflation back. But I think that that will not be -- that will not sustain itself. So my sense is really second half of the year before we see any pickup.

Keith Howlett - Desjardins Securities - Analyst

Just on the labor agreements, there's quite a few outstanding labor agreements. Is there any issue there, or is it just normal course?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Well, I mean I think it is normal course, but I think it is not in a normal market. We are really looking -- in the supply chain, we have talked about what we're trying to do, which is to create this flexibility that enables us to supply our stores at the lowest cost per case from the most flexible location.

We have got much the same is the issue in our retail business. We have got some big contracts that are up. In the good half of our conventional banners in Ontario, we have a 10% cost disadvantage to our competitors and 15% flexibility advantage. And that is not sustainable. And probably for the first time this year, nonunionized labor will be higher than unionized labor in our industry. So there is -- I think we are just trying to make sure that everybody understands that.

Now it is time for -- it is a very competitive time. There is a lot of competition coming in, taking business. A lot of that is nonunionized, and to a degree I do not mind being the highest payer in the industry. In a strange way, I quite like the idea of being the highest payer in the industry. I just don't like the idea of having that flexibility in our competitors.

Keith Howlett - Desjardins Securities - Analyst

I know another initiative had been to increase the ratio of full-time to part-time. So I guess that goes to you are really trying to seek productivity rather than wage reduction?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Absolutely. I think, first of all, you cannot survive without flexibility. Any retail business around the world that has been successful has flexibility, and that is the paramount thing. Now in lots of parts of our business we do, and it works incredibly well. In lots of our parts of our business, we don't. And we just have to place into that.

Keith Howlett - Desjardins Securities - Analyst

Just a few questions on the banners. In terms of T&T, are you already putting learnings from T&T into your other store banners, or is that still to come?

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Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

No, bit by bit, it is gradual, but in terms of ranges particularly, we've got some very interesting learning. We have taken a number of lines at the T&T sale and put it into our core business, and they have done incredibly well, particularly in the West. So no, there is a very good relationship between the ethnic team here and the T&T team who in many ways are very integrated.

Keith Howlett - Desjardins Securities - Analyst

And then the No Frills in Western Canada, I'm wondering if you can update us on how they are doing?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Yes, I mean the conversions are going ahead, and we are pretty pleased with what we see. We still are building new ones. We have got about 10 or 12 now either in the ground or coming out of the ground. And we feel there is a real role for No Frills to play in the West, in that infill capacity where the superstores are.

Keith Howlett - Desjardins Securities - Analyst

Are they pretty much priced the same as the Western superstore?

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

We do not talk about (inaudible) pricing.

Keith Howlett - Desjardins Securities - Analyst

I thought I would try anyway.

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

I nearly answered it.

Keith Howlett - Desjardins Securities - Analyst

Then just on the Maxi & Cie in the province of Quebec, I know you converted at least two Loblaw to Maxi & Cie. I wonder if you could update us on that project.

Allan Leighton - Loblaw Companies Limited - President & Deputy Chairman

Yes, we are pleased with the performance, and that is why we are going to roll it to another number, probably somewhere between six and eight.

Operator

Jim Durran, National Bank Financial.

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Jim Durran - *National Bank Financial - Analyst*

Actually my question has been answered. Thank you.

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

We like those questions, Jim.

Jim Durran - *National Bank Financial - Analyst*

No problem, Allan.

Operator

(Operator Instructions). Patricia Baker, Scotia Capital.

Patricia Baker - *Scotia Capital - Analyst*

Actually I'm just like Jim, and the question I was going to have as a follow-up has been asked and answered.

Allan Leighton - *Loblaw Companies Limited - President & Deputy Chairman*

Okay. Well, if that is the case, operator, and if there are no more questions, then I think it would be -- I wish you to bring the call to an end.

Operator

There are no more questions at this time. I will turn the call back over to Ms. Lee.

Kim Lee - *Loblaw Companies Limited - Senior Director, IR*

Thank you, everyone, for your interest in Loblaw Companies. We look forward to speaking to you on our Q2 conference call. Thanks, again.

Operator

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

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