FINAL TRANSCRIPT

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and thank you for standing by. Welcome to the Loblaw Companies Limited second-quarter results conference call. (OPERATOR INSTRUCTIONS). I would like to remind everyone that this conference call is being recorded on Friday, July 25, 2008 at 11:00 AM Eastern time and will now turn the conference over to Inge van den Berg, Vice President of Public Affairs and Investor Relations. Please go ahead.

Inge van den Berg - *Loblaw Companies - VP, Public Affairs & IR*

Good morning and welcome to the Loblaw Companies Limited second-quarter conference call. This call is also being webcast simultaneously on our website, www.loblaw.ca.

I am joined here this morning by Galen G. Weston, Executive Chairman; Allan Leighton, President and Deputy Chairman; Frank Rocchetti, Chief Merchandising Officer; Dalton Philips, Chief Operating Officer; Bob Vaux, Chief Financial Officer, and Sarah Burcher, Senior Vice President of Financial Operations.

Before we begin today's call, I want to remind you that the discussion will include forward-looking statements such as the Company's beliefs and expectations regarding certain aspects of its financial performance in 2008 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 second-quarter report. Any forward-looking statements speak only as of the day they are made. The Company disclaims any intention or obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise other than as required by law.

Certain non-GAAP financial measures may be discussed or referred to today. Please refer to our second-quarter report and other materials filed with the Canadian Securities Regulators from time to time for a reconciliation of each of these measures to the most directly comparable GAAP financial measures.

Our second-quarter report, as well as the archive of this conference call, will be available on our website.

I would now like to introduce Bob Vaux.

Bob Vaux - *Loblaw Companies - CFO*

Good morning and thank you for joining us today. Sales for the second quarter increased 1.5% over last year, and same-store sales increased 0.7%. Sales and same-store sales were influenced by Easter, which we will discuss shortly.

Q2 net earnings increased 17.6% over last year because of the year-over-year change in restructuring costs. Q2 earnings were also favorably impacted by a $14 million pre-tax gain on sale of investments. If not for these factors, Q2 net earnings would have been down year-over-year.

Total sales for the second quarter increased 1.5% to $7 billion, despite aggregate internal retail food price deflation. Sales and same-store sales growth were negatively impacted by approximately 0.7% due to the shift in Easter sales into the first quarter of this year as compared to the second quarter of 2007.

Sales growth in food was positive, and drugstore sales were particularly strong, while general merchandise sales were down compared to the second quarter of '07. Gas bar sales were strong in the second quarter as a result of fuel price inflation and volume growth. Operating income was $263 million for the second quarter of '08 compared to $218 million during the same period of '07. Operating margin was 3.7% compared to 3.1% in the second quarter of '07. The increase in operating income and margin was primarily due to lower structuring costs. Including the impact of restructuring and the gain on the sale of investments, operating and EBITDA margins declined in the second quarter of '08 as a result of our continued investment in lower retail prices. We initiated significant pricing investments in the third quarter of '07, and as a result, margins in the second quarter of '08 were negatively impacted when compared to the second quarter of '07.

Loblaw realized second-quarter basic net earnings per common share of $0.51 compared to $0.43 for the same period of '07, primarily as a result of the lower restructuring costs in the second quarter of '08 versus the second quarter of last year.

Free cash flow for the second quarter of '08 was $141 million compared to $346 million in '07. The change was primarily due to a decrease in cash flows from working capital of $216 million, driven by changes in cash flows related to inventories, accounts receivable and restructuring and other charges. These are partially offset by an improvement in net earnings and a decrease in capital expenditures of $44 million compared to last year.

For the balance of the year, the Company will direct its efforts towards building profitable sales momentum, while continuing to improve value for customers. The focus on cost and operating efficiencies will continue as margins are expected to remain under pressure.

I would now like to turn it over to Galen Weston.

Galen Weston - *Loblaw Companies - Executive Chairman*

Thank you, Bob. Performance in the second quarter was as expected. We increased sales and sales volume, customer and item counts, but as stated last quarter we are not yet operating as an effective selling organization.

Efforts to improve this are underway, and initial results are promising, but further time and effort is required. We made progress in our cost reduction efforts in the quarter. Advances continued in lower cost of sale and SG&A, shrink and availability.

Margins were satisfactory. However, investments in our foundational infrastructure, offer improvements, and value for customers will continue, and therefore, margins will remain under pressure.

Last quarter we announced five areas of immediate focus to enhance our offering and better serve our customers. We have taken several steps forward.

I would now like to introduce Allan Leighton who will update you on our progress.

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

Thank you, Galen. As expected, this is a weak quarter in sales, but a more consistent quarter in terms of margin and costs. Therefore, building what we call smart sales momentum in the business has been our focus for the past few months.

Smart sales are sales that are driven through departments that are key in customer choice and in addition to delivering the banner relevant value in half the product mix for the Company.

As we stated on the last call, this would be and is a six to nine month exercise. It is focused around our simple five-point plan, which is where we expect momentum to come from, and so let me update you as to our progress.

One, the renovation of 20 conventional stores in Ontario, plus the associated investment in customer service, the fresh areas of the store and grocery availability. This is well on track. The majority of the stores have started their renovation work and will be complete for the latter part of this year. Almost 1000 new hires have joined these stores in front-line service roles. New uniforms have been introduced, and new standards adopted in the fresh areas.

We have also introduced a new food-centered graphics and advertising program based around eating well and saving more. We also adjusted some pricing as we said we would aligned to the improvement of the offer.

We are pleased with the early signs. All areas have improved, and we can see sales and mix benefits and importantly improvements in customer perception. We would expect to roll out the learning and success from this program to the majority of our conventional stores across the country.

Two, the 25 Superstore renovations in the West, plus the 20 No Frills conversions from Extra Foods and the 20 new infill No Frills. This, too, is on track. The majority of the Superstore renovations will be complete by the end of the second quarter of '09. Eight will be completed by this year-end, and built into all of these renovations is a very comprehensive training program for colleagues, refocusing on standards, process and service.

No Frills conversions from Extra Foods are also on track. 12 will be completed by this year-end. And we have confirmed locations for the first 10 new No Frills infill stores, and the first store will open in March 2009.

The West No Frills activity when combined with our other capital plans for No Frills will result in more than 40 No Frills openings in Canada in 2009.

Three, introducing local market merchants to bring back the localness to our banners and markets. This is nearly complete, and the program to support our national program is being developed. We expect to see most of the impact from this hitting down in early '09.

Four, we're focusing on our supply chain and our IT program on the foundational issues. This, too, is on track. The Ajax facility is open, and Erin Mills will now close earlier than planned in September of this year.

It is important to remember Ajax was opened with simple automation. It is pick by voice, it is pallet shrink wrappers, and it is forklift trucks. Nothing else. Harmony is now being reset in a similar fashion.

Construction has commenced on the expansion of our Calgary, which is a Freeport DC. The expansion of Pitt Meadows and the construction of our near 0.5 million square foot Vancouver Surrey facility will start next month.

On the IT front, our near-term focus will be on simple warehouse and transport systems to support the physical and operational changes in our DCs. We will start with support of systems renewals with our master datafile, which is where the real data complexity is in any retail business. But also where there are known solutions that are being implemented successfully elsewhere and, therefore, less risk.

A result of this foundational focus is that we will spend less than originally planned over the next three years on our system and supply chain infrastructure.

Fifthly and finally, the final element of the plan was around reenergizing the President's Choice brands on the 25th anniversary of Insiders in 2008 and throughout the whole of 2009, which celebrates 25 years of President's Choice.

We have now included a significant no name element to this program. As we believe, Canada's best value brand is and will become even more appropriate for our customers. This will impact more than 500 no name products.

On PC itself new packaging is being developed for the brand for 2009, and in addition, over 1000 product improvements will be made to align with the packaging change and over 500 new products will be introduced.

We are also in pretty good shape for the celebration of Insiders for this year-end.

In summary, we remain confident that we can build the smart sales momentum that the business requires around a simple five-point plan and within the six to nine month catchup period we outlined during our last call.

Operator, I would like now to open the call to questions.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS). Perry Caicco, CIBC World Markets.

Perry Caicco - *CIBC World Markets - Analyst*

I want to start by diving a bit into same-store sales. You mentioned that you grew in customer and item counts, suggesting that I guess dollars per basket may have declined. And if that is the case, I'm just kind of wondering what consumer behaviors you are experiencing? Was the penetration of promotional goods and private-label items up in the quarter? Was there a shift from conventional to hard discount?

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

Not really. I mean, to be honest, there has not been much movement around. Generally what we're seeing on a banner by banner basis is roughly the same. There may be a little bit more movement towards no name recently, but generally it has been very much as it is.

Perry Caicco - *CIBC World Markets - Analyst*

And further to that then, on the overall slight price deflation, I'm assuming that is a year-over-year measurement. I'm wondering what happened on a sequential basis? Were prices up over Q1, and if so, what were the dynamics behind that?

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

If you look at it, we have still got deflation in the business in Q2, and the Q2 deflation was marginally less than it was in Q1.

Perry Caicco - *CIBC World Markets - Analyst*

Okay. And quickly is gas in your same-store sales number, and what would that number -- what would the number be excluding gas?

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

Well, we would not give you the number excluding gas. It is in the numbers. Gas is about 2% of sales. That is the way to think about it.

Perry Caicco - *CIBC World Markets - Analyst*

Okay. And just one last question if I could. I think we are all concerned about the softness in the economy, and I'm wondering about just how regionalized your sales results are. Is your overall number truly sort of a national number, or are there significant differences by region?

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

Again, Perry, we would not really want to go into the regional performances, regional differences. Very much the same pattern as has always been. As you know, each one of the markets has its own particular characteristics. There has not really been that much change quarter on quarter in the performance in the individual markets.

Operator

Winston Lee, Credit Suisse.

Winston Lee - *Credit Suisse - Analyst*

Regarding the financial gain of $14 million, I just wanted to know just color-wise what that was, and what was the after-tax impact on that?

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

Okay. Bob will pick that up.

Bob Vaux - *Loblaw Companies - CFO*

The $14 million gain, a couple of years ago MasterCard issued shares in MasterCard to all issuers, including ourselves, and notice that we sold half those shares in the second quarter for a $14 million gain. It is tax-affected at about a 32% tax rate.

Winston Lee - *Credit Suisse - Analyst*

Great. And on the -- just another financial question -- Bob, you have got $7 million of setup on the balance sheet for projects to simplify and $2 million I think for your store operations restructuring, and you did not take any charges on that this quarter. Is that still a good liability, or do you think that will reverse?

Bob Vaux - *Loblaw Companies - CFO*

No, I think to the best of our knowledge, it is still a good liability.

Winston Lee - *Credit Suisse - Analyst*

Okay. And I just wanted to ask on the shrink issue, I know that shrink improved you said year-over-year, and I think last quarter you said it improved as well. But I wondered sequentially are you seeing improvements there, and how did that happen if it did?

Bob Vaux - *Loblaw Companies - CFO*

I mean we are seeing improvements in shrink. We are very pleased with our shrink performance. It was better in Q2 than it was in Q1.

Winston Lee - *Credit Suisse - Analyst*

Okay. And my last question on general merchandise. Can you talk a little bit about the business there?

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

Yes, I mean the weakness is where it has been. And I think as always, if you think about it, it is core general merchandise. Our drugstore business was very good. We're very pleased with that.

Joe, as you know, actually performed reasonably well. It took some marketshare, but has suffered in the same way as every other clothing business in the country, if not in the world. But we're pretty pleased with where that has come through.

It is in the core GM business where we've still have got some issues. Clearly a lot of that business is seasonal, so the weather does not help that, too. We have still got some assortment issues, and we're working on it. I think we believe that there is still some real upside in that business if we can get our act in order.

Operator

Irene Nattel, RBC Capital Markets.

Irene Nattel - *RBC Capital Markets - Analyst*

A couple of questions if I may. First of all, you mentioned a couple of times that margins are going to remain under pressure. Should we then assume that for the balance of 2008 we should be anticipating year-over-year declines?

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

That is a leading question (multiple speakers) and, therefore, would be guidance in some way, shape or form. I think, suffice it to say, that there are two or three elements in margin. Clearly there is the sort of gross margin, the buying margin, clearly there is the sort of mix, and then clearly there's all the operating costs.

I think you can assume that we're still continuing to work on operating costs, and we have shown some good progress in that area. The mix has quite a big impact on margins, and that is pretty difficult to predict at the moment because there are some -- as you can see, there are some shifts around the economy, and we will have to see how that pans out. But we are still very fixated on our value position. We made quite a significant adjustment during the course of the last 12 months that really re-established that price position. We will still continue to enhance our price position where we need to be. But I would read into what I said about the margins in the period were more consistent than they have been in the past.

Irene Nattel - *RBC Capital Markets - Analyst*

Okay, thank you. And just taking a little bit of a step back, you have now had I guess three, four months to work on these five initiatives. Could you give us just a little bit of color as to where you think your biggest wins have been? Where you may have had some favorable surprises and the reverse, where you think it is now a little bit tougher or going to take a little bit longer than what you had hoped?

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

I mean as I said, my comment is that they are on track and they are. It is early days on some of them. As we say, I think in the Back-to-Best stores, the Ontario stores, we're pretty pleased with how that is panning out. The others are -- there is a lot of physical change taking place in the business. There's a lot of renovations taking place, and you clearly don't see through that the benefits of that until it is done.

And then a lot of the other work is in terms of the Frills conversions and the West Superstores. So a lot of this is actually in progress, and therefore, you will not really see until we get to the end of it.

I think I feel pleased that we are on track. You know, there are five simple things, but they have got some scale to them. And I think we have enhanced them a little bit over the last few months as we have been able to give them a bit more thought. So all I would reiterate is what I said is, I'm confident that we will get ourselves back on track in that six to nine-month period. And I'm confident that these programs will deliver.

Operator

Michael Van Aelst, TD Newcrest.

Michael Van Aelst - *TD Newcrest - Analyst*

First of all, you talk in the press release about your price investments and how they started in Q3 '07. It seems to be implied that you're looking forward to lapping them this year. I guess the question is, have your price investments continued to increase since you started in Q3 '07, and therefore, there will still be pressure from the run-rate when we get through Q3? Or are you just pretty much cycling through the level of investments that you made in Q3 last year?

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

Again, I think that is another leading question. As we said, we have got a -- we're pretty comfortable with our general overall price platform basically, as we say, having made this adjustment, which we made over the last 12, 15 months. But pricing is something that in a strange way happens every week. And so our ability to still be flexible is important, and we will still invest in price where we need to to maintain our value position. But I would read into the fact that we made a significant investment last year. That is largely not going to clearly be repeated. And that we are now much more in how most retailers would be is sort of managing our pricing on a view where we're really looking it to be sustainable what we do as opposed to a bit schizophrenic, which is where we may have been in the past.

Michael Van Aelst - *TD Newcrest - Analyst*

Okay. I know you don't like to talk too much about regional, but is it fair to say that Western Canada would be seeing the remainder of the price cuts or the bulk of the price cuts now given the activity over there is more recent?

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

No, as I say, as we invest in price, we look at it on a market by market, banner by banner position. And, as I say, we are comfortable with our underlying platform. But this is something that in retail you adjust all of the time.

Michael Van Aelst - *TD Newcrest - Analyst*

Okay. You did not mention your consulting fees that were expensed this year. Could you tell us what they were and whether they were up or down from last year?

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

Our consulting fees generally on general stuff will be down from last year, much along the lines that we've talked about in the past. We're desperately trying not to talk about consulting fees at all anymore because we think they are sort of pretty passe.

Michael Van Aelst - *TD Newcrest - Analyst*

So they are pretty meaningless now relative to where they were last year?

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

In the core business, yes.

Operator

Jim Durran, National Bank Financial.

Jim Durran - *National Bank Financial - Analyst*

I just want to go back to the comp store sales number. In the past several quarters, you have provided your volume growth number. Are you prepared to give us that this quarter?

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

No.

Jim Durran - *National Bank Financial - Analyst*

Okay, fair enough.

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

I could have flowered it up, but it is best to get to it.

Jim Durran - *National Bank Financial - Analyst*

No, that is fair. I guess all my -- I was somewhat surprised at how weak the comp store sales number was given that we have not reached the Q3 '07 lapping period. And so I assume that volume growth compared to the last several quarters must have slowed this quarter.

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

I think two things really. As we say, deflation is less in Q2 than it was in Q1, and the volume growth in Q2 would have been less than it was in Q1.

I mean I would not be too surprised. What is clear, and we have always been consistent on it certainly for the last three or four months, is what is driving this is we're not an effective selling organization. The issue that was there that we made the changes for does not get turned overnight, and that is why we said that this is a six or nine month catchup period, and we have got to get sales growth that is sustainable in the business.

So deflation has an impact on that. I would read into this point I'm making about smart sales. We're looking at driving sales momentum that is sustainable over a period of time, not that comes and goes on a week by week or period by period basis. But don't read into it in any way, shape or form that we will be backing off our value position.

Jim Durran - *National Bank Financial - Analyst*

No, I assume you are talking about planned promotions where you are not investing an egregious amount of gross margin?

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

Yes. And secondly, but remember the bulk of sales does not come off the promotions. The bulk of sales in all these businesses is still driven in the vast majority of promotion. And that is why you have to have programs that are -- that cover all of the areas. This smart sales idea covers all the areas of the business. You know, I always think promotions are often like a drug. You got to do them, but don't rely on them to drive your sustainable sales momentum because they don't.

Jim Durran - *National Bank Financial - Analyst*

Okay. Free cash flow intention for the year, are you still committed to trying to be around the 250 mark, excluding the preferred share issue?

Bob Vaux - *Loblaw Companies - CFO*

Yes, we are.

Jim Durran - *National Bank Financial - Analyst*

Okay. Then going back to the margin question that Irene asked, I know you're not providing guidance. But at the Investor Day, there was pretty adamant commentary from the Company that you expected that your EBITDA margins would improve materially in the second half of the year as cost savings came in. So I'm going to go back and ask the question again.

In terms of EBITDA margin separate from gross margin, is your expectation now you will still be investing EBITDA margin in the second half of the year?

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

Again, if we start talking about EBITDA margins, we get into guidance territory. I'm sort of -- I would not want to add to anything I said to Irene's question in reality.

I think it is -- just we said two things you know. One is that we have still got a program that will still require some price investment. And the second thing we said is that we feel pretty good about what has happened on the cost front. And I would just sort of leave it at that.

Jim Durran - *National Bank Financial - Analyst*

Okay. So the last question here is just the Great Canadian Food Stores. I'm talking about the ones that are being renovated that don't qualify for the new labor agreement. I have the joy of shopping at one of those right now.

There has been a lot of money spent on new refrigeration units. There has been a lot of revamping of planograms in the dry grocery area, etc. So there has been a lot of money spent, and there has also about 1500 items dropped in price in that store. Can you give us some idea of what is happening to the sales line in those stores and how you expect to scramble back to a good margin and a good ROE on that investment?

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

Well, in reverse order there has been what I describe as good money spent on those renovations. So each one of these clearly has a return and a pretty good return actually. And so we spent good money when I think about it rather than lots of money.

Secondly, clearly you're right in terms of frozen and refrigerated capacity in these stores is very important. We have not spent money in that area for a period of time. It is a big growth area, and therefore, that is where we have clearly put some money in.

We have reduced prices as we said we would as we believe that we have enhanced the offer, but pricing, there has been a big service element to what has happened there. The availability in those stores is also improving.

So again, go back to what I said at the beginning. We feel good about what we have seen so far. But the real test of them will be when they completely come out of renovation, and everything is in sync and working together, not just the price, the service, the product, the availability, the ranging, all of the things that drive retail businesses and drive sales in the retail business in a sustained way.

Operator

Ryan Balgopal, Scotia Capital.

Ryan Balgopal - *Scotia Capital - Analyst*

I wanted to talk a bit about supply chain. I guess two fronts. In stock or on shelf levels of availability, so your always available program, how is that sort of performing?

And also from the distribution centers, what are your service levels at now? And I guess finally, if we think about Supply Chain 2010, are we still looking at 2009 as being the time period when you go to a flow system, and is that still on track?

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

Well, the availability program that Dalton and Tim run is having real impact. So we are very pleased with what is happening to our on-shelf availability in store.

The service levels from the DCs have improved quite a lot in the last few weeks. There has been a lot of -- as some of these changes that we put into place are really beginning to kick in.

Ryan Balgopal - *Scotia Capital - Analyst*

So where would you be on a service level percentage?

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

We would not give that number anymore.

Ryan Balgopal - *Scotia Capital - Analyst*

Okay.

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

But take it from the tone of my voice, that I feel we are in a better place than we were, but there is still a bit to go.

On Supply Chain 2010, again a lot of work is actually taking place. I mean we have put this date in the sand 2010. There is a huge amount of work taking place in the supply chain now. I mean the work that's taking -- Ajax is a big move forward. The sort of renovations that are taking place in these DCs is a very important piece of all of that. They are for me the foundational pieces of 2010. Because unless you get physical infrastructure right, which we're now beginning to do and unless you make that a pretty simple operation which we're now beginning to do, then you can add whatever you want on top of it. It does not work.

And so I think we are on track on 2010. I think the supply chain has made a lot of progress in the last couple of months. I think these physical changes and operational changes are having an impact and will continue to have an impact.

As to flow, that is part of 2010. Really the big piece of flow does not kick in until much later on in the program. And so at this moment in time and certainly over the next 12 or 15 months, that is not going to be an important element of what we do.

Ryan Balgopal - *Scotia Capital - Analyst*

Okay, thanks. I just wanted to ask about also on your Superstores, you have got some third-party providers on meat and seafood in some of your newer stores. I'm wondering how do you actually control that operation, and what is that they really bring to the table? Because at the end of the day, you are still a supermarket.

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

Yes, are you thinking about Scarborough particularly?

Ryan Balgopal - *Scotia Capital - Analyst*

Yes.

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

Yes. Two things. First of all, we have done that in No Frills for years. And so we've got a pretty good experience of how to do it and how to control it and of the operators.

For what it is worth, both of them have been pretty successful in Scarborough, and there are two things in it for us. One is I think it allows us to tailor in those really ethnic catchments products that we probably cannot do ourselves in the same degree. But secondly, it is a huge learning exercise for us. We believe there's a big ethnic opportunity. Clearly we should be leading that in terms of its scale and substance, and that is why Scarborough is a really important piece of learning for us.

Operator

Keith Howlett, Desjardins Securities.

Keith Howlett - *Desjardins Securities - Analyst*

Yes, I had a question on the inventory levels. They seem to be up quite a bit year-over-year, a bit over 8%, so I guess there's two questions. Why is it up that much? And the second part is, how do you feel about your seasonal and clothing inventory as we go through the clearance part of Q3?

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

Two things really. First of all, we are not at all worried about the inventory. It is up a bit. A bit of that is seasonal, and a bit of that has to do with the weather. We tend to look at it on days on hand basis, which (inaudible) look at it, and we're pretty happy with it.

If behind the question is there a question, are there some big markdowns coming off the back of this or write-downs? The answer is absolutely not. The seasonal -- including the seasonal piece actually has cleared up quite a lot recently in the last couple of weeks.

At Joe we carried slightly more inventory, which was largely to do with the slowdown in sales, but that too has worked its way through.

So there is a tad more inventory. We do not think it is an issue, but the days on hand are the way we look at it, and there is no real -- I would not know that you should be worrying about any great write-downs coming down the track.

A lot of it is food as well. And so a slight slowdown in the food sales, you get a bit more inventory, but you can recorrect it pretty quickly. But we don't have any issue on our GM inventory.

Keith Howlett - *Desjardins Securities - Analyst*

Then just on the customer actions, are you seeing any customer movement to no name from branded or even from President's Choice I suppose? Are you seeing any consumer anxiety in your basket, so to speak?

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

No, I think we see -- I mean the whole value piece has clearly become more important, and that is why I'm glad in a way that we have got ourselves in a position where we have shifted our value position in the market. Because I think that will see us in very good stead. There is not that much movement.

Probably if you look in the last four or five weeks, you can see some marginal movement towards no name, but nothing too significant. I think remember that in Canada at the moment, you have got probably the lowest food price inflation in the world. And, therefore, the Canadian consumer at this moment in time is getting a pretty good deal in terms of value on pricing.

Keith Howlett - *Desjardins Securities - Analyst*

And then just in terms of your No Frills stores in Ontario, are you satisfied with the physical state or environment in those stores relative to I guess the new entrants in the market?

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

Yes. I mean it isn't like all there, and we have got some old stores and we have got some new stores. And you are forever trying to tie the old end of it. Some of them are pretty old and not had money spent on it for a period of time. But we do not think that the physical state of the No Frills estate in Ontario is an issue for us at all.

Keith Howlett - *Desjardins Securities - Analyst*

I have just got a couple of questions for Bob. One on -- are there any major amount of severance costs in the quarter?

Bob Vaux - *Loblaw Companies - CFO*

No.

Keith Howlett - *Desjardins Securities - Analyst*

Okay. And the second question was on the preferred share. It just goes to the capital structure just what your policy or thinking is on using the preferred shares?

Bob Vaux - *Loblaw Companies - CFO*

Well, the preferred shares become part of our capital structure. We have been looking for some time at just simply diversifying our sources of capital in the Company. The opportunity came along on the preferred shares. We felt it was appropriate, and therefore, we did it.

Keith Howlett - *Desjardins Securities - Analyst*

And is that sort of an area that you would see more room on the preferred front or you are happy where you are?

Bob Vaux - *Loblaw Companies - CFO*

Well, we will look at that over time. I mean the market has changed from time to time and different sources of capital become available at different costs. So we're not saying that we're going to increase the preferred shares and carry on the balance sheet. That will depend on market conditions going forward.

Keith Howlett - *Desjardins Securities - Analyst*

Just last one question on the food inflation. Are you seeing pressure down the pipe, and are you seeing many manufacturers -- I see a few in Canada shrunk their package size. Sort of what are you seeing across that front?

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

A continuation really. I mean there clearly is some pressure to take cost increases and put prices up. I don't think that has changed too much. We're not seeing too much of the shifting down in size or any of those other pieces.

Operator

David Hartley, BMO Capital Markets.

David Hartley - *BMO Capital Markets - Analyst*

Just some questions on some initiatives you have in terms of their timing. First, the deployment of 1000 new people in your stores. You made reference to that that the majority of them had been either hired or put in place. Could you give us the timing as to when that took place?

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

It has been happening over the last couple of months. It will continue on for the next three or four weeks, and you should see it really if you look at queue lengths and if you look at fill in those stores, you should see a noticeable difference.

David Hartley - *BMO Capital Markets - Analyst*

Okay. And in terms of -- was there any pricing investments made in conventional stores in the quarter?

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

No.

David Hartley - *BMO Capital Markets - Analyst*

None at all?

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

Only day to day tactical adjustments.

David Hartley - *BMO Capital Markets - Analyst*

Okay. And is it still the Company's position -- I just want to be clear on this -- that the Company plans to make price investments non-tactical in conventional stores in the coming future?

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

If you look in the stores today, I think a couple of people have mentioned it, is that part of the program that has been run is, on a customer by customer basis, as we get the mix right and we get the availability right, we have been adjusting prices, and we will continue to do that.

David Hartley - *BMO Capital Markets - Analyst*

So those are the investments you are making. So in effect you have made investments then?

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

We always make -- we have made some investments, and we will continue to make some investments.

David Hartley - *BMO Capital Markets - Analyst*

Okay, great. I'm just wondering in the quarter, I don't want to point anything out untoward here, but in terms of the return you are getting on these price investments whether they be over the last 12 months or just recently, how do you feel about that? Can you give us some color on -- do you expect those returns to improve over time?

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

The whole idea, and again we sort of -- I think the point I'm trying to make is that I think we and you to a degree have been all fixated on price. And if you look at what we're looking to do in that simple five-point plan, it is to do with all the other things that really make a difference.

And so, as I say, I think our idea is a very simple one. We're trying to drive sustainable sales, and therefore, that is where our focus is. And so value and price will be just part of the equation.

We've made a substantial adjustment. We will continue to make sure that our position is competitive. There are still some formats where we need to do some more alignment. But we're only interested in doing that as we improve the rest of the offer. Because, to be honest, you cannot see the return just purely on pricing.

David Hartley - *BMO Capital Markets - Analyst*

Yes, I understand and I agree. (multiple speakers)

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

The return is in the total store. And that is why pricing is 20, 25% of the equation. The other 75% is now the piece that we're going to work on, and that is where the sustainable momentum comes from.

David Hartley - *BMO Capital Markets - Analyst*

Okay. I know the question was brought up on consultant costs, not something you want to talk too much about. But when you say it is passe, I just want to be clear on this as well. There were some costs of $80 million or so on top of your what you would call normal consultant costs that had been in your P&L. Are these costs in some way, shape and form here to stay? If they are not consultant costs today or if they are consultant costs today, in the future are they simply going to flow through as being transformed into other costs that will stay within the system?

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

Well, the answer to the first thing is, is there are -- clearly we have got what gets called consultancy is in some of the supply chain and IT work, and for me that is non-core. That is basically using other heads basically rather than recruiting heads inside the business.

And the reason you do that is, at the end of the projects, at the end of the work, those heads disappear. So the idea is not to inject this amount of money to get the work done and then to keep that cost. It is the reverse. So those costs will disappear over time.

And, of course, the other side of it, the reason we're doing this, is to also improve our cost base. So two things should happen. One is the overall costs will come down because clearly when the work is done, the people go away.

Secondly, the only reason we're doing this work is either to drive sales, improve margin or take down costs.

David Hartley - *BMO Capital Markets - Analyst*

Okay. So you are leaving us with the impression I think then that there is $80 million worth of cost to come out of the system over the next three to five years. Would that be correct?

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

Absolutely.

David Hartley - *BMO Capital Markets - Analyst*

And finally, just to be clear as well on margins being under pressure for the remainder of the year, is this -- when you say that, do you speak net of cost containment initiatives or do you mean pre-?

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

We are talking total margin.

David Hartley - *BMO Capital Markets - Analyst*

Total margin. Okay. So all-in. Okay. That is it for me. Thank you.

Operator

Irene Nattel, RBC Capital Markets.

Irene Nattel - *RBC Capital Markets - Analyst*

Two questions if I may. Just expanding a little bit on the food price inflation issue, you know clearly manufacturers they took rounds of inflation in Q1, some in Q2. But again, they are talking about it on a go forward basis. The last time we chatted you indicated that keeping prices low was a priority for you and that you kind of to some -- for lack of a better way of putting it, you would expect to share the pain with the manufacturers. Is that still your stance?

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

Two things really. First of all, I want to go back to the point is, we still in Q2 have deflation in the business. So that means the prices were coming down faster than we were putting costs through.

And the second thing is that it is a personal thing. This inflation thing is something that you can never count on. And so one of the things we have in the business is we assume there is not going to be any. Because if you assume there is not going to be any, if you get any, it is in upside. If you don't get it or it does not come when you think you're going to get it, it does not become a downside. So we are sort of not so infatuated by inflation.

So do I think that in the second half of the year there may be a little bit of inflation compared to the first half? Probably.

And remember the big driver of deflation and, therefore, to a degree inflation when you look at it our way, is in the fresh areas. Produce is a big piece of this. And so that will cycle over in 12 months time.

But the way we look at it, it is something that we sort of handle on a day by day basis when we are talking to the manufacturers. But we don't now build in any assumption on inflation in our numbers because it is the one thing you cannot control.

Irene Nattel - *RBC Capital Markets - Analyst*

That is great. And the other question is I wanted to come back to the rejuvenation, if you will, of the no name brand, which I think is very interesting certainly given how important no name is to the overall value offering. Could you expand a little bit on some of the perhaps where you are looking to upgrade or expand the selection?

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

Two areas of direction rather than specifics. It will primarily be in grocery, and it will be a combination of product enhancement and value enhancement.

Inge van den Berg - *Loblaw Companies - VP, Public Affairs & IR*

Great, everyone. This is Inge speaking. Thank you very much for your interest in Loblaw, and we will look forward to speaking with you again on our third-quarter call.

Operator

Ladies and gentlemen, this concludes the conference call for today. Thank you for participating, and please disconnect your lines.