# 2010 Annual Report

George Weston Limited

**2010 Annual Report**

Financial Highlights **1** Report to Shareholders **2** Management's Discussion and Analysis **4** Financial Results **67**
Three Year Summary **124** Glossary **126** Corporate Directory **128** Shareholder and Corporate Information **129**

This Annual Report contains forward-looking information. See Forward-Looking Statements on page 5 of this Annual Report for a discussion of material factors that could cause actual results to differ materially from the conclusions, forecasts and projections herein and of the material factors and assumptions that were applied in presenting the conclusions, forecasts and projections presented herein. This Annual Report must be read in conjunction with George Weston Limited's filings with securities regulators made from time to time, all of which can be found at www.sedar.com.

# Financial Highlights

## CONSOLIDATED INFORMATION[(1)]

For the years ended December 31[(2)]
($ millions except where otherwise indicated)

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| **Operating Results** | | | |
| Sales | **$ 32,008** | $ 31,820 | $ 32,088 |
| EBITDA[(3)] | **2,192** | 1,654 | 1,808 |
| Operating income | **1,483** | 1,009 | 1,198 |
| Gain on disposal of business[(4)] | | | 335 |
| Interest expense and other financing charges | **388** | 363 | 360 |
| Net earnings from continuing operations | **452** | 127 | 647 |
| Net earnings[(5)] | **452** | 1,035 | 834 |
| **Cash Flow** | | | |
| Cash flows from operating activities of continuing operations | **$ 1,741** | $ 1,987 | $ 956 |
| Capital investment | **1,304** | 1,107 | 807 |
| **Per Common Share** ($) | | | |
| Basic net earnings from continuing operations | **$ 3.16** | $ 0.64 | $ 4.65 |
| Basic net earnings | **3.16** | 7.68 | 6.10 |
| **Financial Measures and Ratios** | | | |
| EBITDA margin[(3)] | **6.8%** | 5.2% | 5.6% |
| Operating margin | **4.6%** | 3.2% | 3.7% |
| Return on average net assets[(3)] | **13.3%** | 9.3% | 11.2% |
| Return on average common shareholders' equity | **7.1%** | 1.5% | 13.4% |
| Net debt[(3)] | **$ 501** | $ 299 | $ 3,251 |
| Net debt[(3)] to EBITDA[(3)] | **0.23x** | 0.18x | 1.80x |
| Net debt[(3)] to equity | **0.08** | 0.04 | 0.53 |
| **Reportable Operating Segments** | | | |
| Weston Foods | | | |
| Sales | **$ 1,624** | $ 1,686 | $ 2,197 |
| Operating income | **278** | 123 | 154 |
| Operating margin | **17.1%** | 7.3% | 7.0% |
| Return on average net assets[(3)] | **38.1%** | 19.2% | 22.6% |
| Loblaw | | | |
| Sales | **$ 30,997** | $ 30,735 | $ 30,802 |
| Operating income | **1,261** | 1,197 | 1,044 |
| Operating margin | **4.1%** | 3.9% | 3.4% |
| Return on average net assets[(3)] | **12.1%** | 11.8% | 10.4% |

(1) For financial definitions and ratios refer to the Glossary beginning on page 126.
(2) 2008 was a 53-week year.
(3) See non-GAAP financial measures beginning on page 61.
(4) Gain on disposal of business relates to the disposal of Weston Foods' dairy and bottling operations in 2008.
(5) 2009 net earnings include a gain on disposal of $939 million ($901 million, net of tax) recorded in discontinued operations.

## Report to Shareholders[1]

2010 was a successful year for George Weston Limited, with both operating segments, Weston Foods and Loblaw Companies Limited contributing positively to the Company's overall performance. Weston Foods delivered strong financial operating results and completed two successful bakery acquisitions during the year. Loblaw made real progress on its renewal program and delivered solid results despite a highly competitive and difficult economic environment for food retailers. Also during 2010, the Company was pleased to announce a $1 billion special common share dividend which was paid to shareholders in January 2011. Our balance sheet is strong, providing the Company with financial flexibility to meet its ongoing operational and capital requirements and to pursue growth opportunities to continue to drive shareholder value.

Basic net earnings per common share from continuing operations were $3.16 compared to $0.64 in 2009, an increase of $2.52. Of this increase, $0.53 was attributable to improvements in the operating performance of the Company's two operating segments, Weston Foods and Loblaw. The balance of the improvement was primarily attributable to the positive impact of the year-over-year reduction in foreign currency translation losses.

Sales increased 0.6% to $32.0 billion from $31.8 billion in 2009. Operating income increased 47.0% to $1,483 million from $1,009 million in 2009. Consolidated operating margin for 2010 was 4.6% compared to 3.2% in 2009.

The Weston Foods operating segment achieved strong financial results from its continuing operations despite soft sales in a challenging market. Weston Foods reported sales for 2010 decreased 3.7% compared to 2009. Excluding the impact of foreign currency translation and the acquisition of Keystone in the United States and ACE Bakery in Canada, sales decreased 2.1% primarily due to lower pricing in certain product categories. Growth in the *Gadoua* and *D'Italiano* brands and product innovation, with the introduction of new products such as *Wonder+ Invisibles, Country Harvest* Ancient Grains*, Country Harvest* Raisin Cinnamon with Whole Wheat, *Jake's Bake House*, *Wonder+ SimplyFree* and *D'Italiano* Focaccia, contributed positively to branded sales growth in 2010.

Weston Foods operating income in 2010 increased 126.0% to $278 million from $123 million in 2009, influenced by the non-cash goodwill impairment charge in 2009 and a number of other notable items. After taking into account these items, operating income in 2010 remained strong compared to 2009. The benefits realized from productivity improvements and other cost reduction initiatives, lower input costs, lower legal and restructuring charges and the results of the bakery acquisitions, which were partially offset by the impact of lower pricing in certain product categories, contributed to strong earnings growth for the Weston Foods segment. Operating margin for 2010 was 17.1% compared to 7.3% in 2009.

(1) To be read in conjunction with the Forward-Looking Statements section on page 5 of this Annual Report.

Weston Foods continues to evaluate strategic and cost reduction initiatives related to its manufacturing assets and distribution networks with the objective of ensuring a low cost operating structure. Initiatives are in place to help drive best practices, which are expected to result in the continued improvement of processes as well as lower costs.

As disclosed in the Loblaw Companies Limited Annual Report, Loblaw sales for 2010 were $31.0 billion compared to $30.7 billion for 2009, representing an increase of 0.9%. Sales were positively impacted by 1.4% by the acquisition of T&T Supermarket. Same-store sales declined 0.6%. Loblaw continued to make steady progress in its renewal program despite a difficult economic environment. Deflationary pressures combined with heightened promotional and competitive activity resulted in soft sales in 2010. Throughout the year, Loblaw delivered food offering enhancements, renovated stores, product innovation, infrastructure improvements and increased customer value.

Loblaw operating income in 2010 was $1,261 million compared to $1,197 million in 2009, resulting in an increase in operating margin to 4.1% in 2010 from 3.9% in 2009. The increase in operating income was primarily due to an improvement in gross profit, which is attributable to improved control label profitability, continued buying synergies and more disciplined vendor management, a stronger Canadian dollar and improved shrink. Increased transportation costs, incremental costs related to its investment in information technology and supply chain and a number of other notable items partially offset these improvements.

George Weston Limited has strategically well positioned companies with leading market positions in food retail and baking in Canada, U.S. frozen baking and biscuit manufacturing businesses and a significant amount of cash.

In 2011, Weston Foods expects continued progress in operating performance driven by sales growth in existing businesses, the full year impact of the 2010 bakery acquisitions and ongoing efforts to reduce costs through improved efficiencies and productivity. This outlook is tempered by the impact of rapidly rising commodity costs and escalating energy costs. While Weston Foods is planning to increase prices to absorb these cost increases, operating margins could be constrained in 2011 as the timing of price increases may lag cost increases.

Loblaw is entering its fifth and final year of renewal, and expects to continue its focus on executing the renewal plan in a market environment that remains unpredictable and competitively intense. Loblaw plans to increase its investments in information technology and supply chain which will negatively impact operating income in 2011.

On behalf of the Board of Directors and shareholders, I thank our loyal customers for their support and our more than 142,000 employees for their dedication and continued commitment to the Company.

**[*signed*]**
**W. Galen Weston**
Chairman and President

# Management's Discussion and Analysis


| | | |
|---|---|---|
| 1. | Forward-Looking Statements | 5 |
| 2. | Overview | 6 |
| 3. | Vision | 6 |
| 4. | Operating and Financial Strategies | 7 |
| 5. | Key Performance Indicators | 8 |
| 6. | Overall Financial Performance | 9 |
| | 6.1 Business Developments | 9 |
| | 6.2 Consolidated Results of Operations | 9 |
| | 6.3 Consolidated Financial Condition | 16 |
| 7. | Results of Reportable Operating Segments | 20 |
| | 7.1 Weston Foods Operating Results from Continuing Operations | 20 |
| | 7.2 Loblaw Operating Results | 22 |
| 8. | Liquidity and Capital Resources | 23 |
| | 8.1 Major Cash Flow Components | 23 |
| | 8.2 Sources of Liquidity | 25 |
| | 8.3 Contractual Obligations | 28 |
| | 8.4 Off-Balance Sheet Arrangements | 28 |
| 9. | Quarterly Results of Operations | 30 |
| | 9.1 Quarterly Financial Information | 30 |
| | 9.2 Fourth Quarter Results | 31 |
| 10. | Disclosure Controls and Procedures | 36 |
| 11. | Internal Control Over Financial Reporting | 36 |
| 12. | Enterprise Risks and Risk Management | 37 |
| | 12.1 Operating Risks and Risk Management | 38 |
| | 12.2 Financial Risks and Risk Management | 47 |
| 13. | Related Party Transactions | 50 |
| 14. | Critical Accounting Estimates | 50 |
| 15. | Accounting Standards Implemented in 2009 | 53 |
| 16. | International Financial Reporting Standards | 54 |
| 17. | Outlook | 61 |
| 18. | Non-GAAP Financial Measures | 61 |
| 19. | Additional Information | 66 |

# Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") for George Weston Limited ("GWL") and its subsidiaries (collectively, the "Company") should be read in conjunction with the consolidated financial statements and the accompanying notes on pages 67 to 123 of this Annual Report. The consolidated financial statements and the accompanying notes have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are reported in Canadian dollars. These consolidated financial statements include the accounts of the Company and variable interest entities ("VIEs") that the Company is required to consolidate in accordance with Accounting Guideline ("AcG") 15, "Consolidation of Variable Interest Entities". A Glossary of terms and ratios used throughout this Annual Report can be found beginning on page 126. The information in this MD&A is current to March 2, 2011, unless otherwise noted.

## 1. FORWARD-LOOKING STATEMENTS

This Annual Report, including this MD&A, contains forward-looking statements about the Company's objectives, plans, goals, aspirations, strategies, financial condition, results of operations, cash flows, performance, prospects and opportunities. Words such as "anticipate", "expect", "believe", "foresee", "could", "estimate", "goal", "intend", "plan", "seek", "strive", "will", "may" and "should" and similar expressions, as they relate to the Company and its management, are intended to identify forward-looking statements. These forward-looking statements are not historical facts but reflect the Company's current expectations concerning future results and events.

These forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations, including, but not limited to:

- the possibility that the Company's plans and objectives will not be achieved;
- changes in economic conditions including the rate of inflation or deflation and changes in interest and foreign currency exchange rates;
- changes in consumer spending and preferences;
- heightened competition, whether from new competitors or current competitors;
- the availability and increased costs relating to raw materials, ingredients and utilities, including electricity and fuel;
- changes in the Company's or its competitors' pricing strategies;
- failure of the Company's franchised stores to perform as expected;
- failure to realize sales growth, anticipated cost savings or operating efficiencies from the Company's major initiatives, including investments in the Company's information technology systems, supply chain investments and other cost reduction initiatives, or unanticipated results from these initiatives;
- the inability of the Company to successfully implement its infrastructure and information technology components of its plan;
- the inability of the Company's information technology infrastructure to support the requirements of the Company's business;
- the inability of the Company to manage inventory to minimize the impact of obsolete or excess inventory and to control shrink;
- failure to execute successfully and in a timely manner the Company's major initiatives, including the implementation of strategies and introduction of innovative and reformulated products or new and renovated stores;
- unanticipated results associated with the Company's strategic initiatives, including the impact of acquisitions or dispositions of businesses on the Company's future revenues and earnings;
- the inability of the Company's supply chain to service the needs of the Company's stores;
- failure to achieve desired results in labour negotiations, including the terms of future collective bargaining agreements which could lead to work stoppages;
- changes to and failure to comply with the legislative/regulatory environment in which the Company operates, including failure to comply with environmental laws and regulations;

- the adoption of new accounting standards and changes in the Company's use of accounting estimates;
- fluctuations in the Company's earnings due to changes in the value of stock-based compensation and equity derivative contracts relating to GWL and Loblaw Companies Limited ("Loblaw") common shares;
- changes in the Company's income, commodity and other tax liabilities including changes in tax laws or future assessments;
- reliance on the performance and retention of third-party service providers, including those associated with the Company's supply chain and apparel business;
- public health events;
- risks associated with product defects, food safety and product handling;
- the inability of the Company to collect on its credit card receivables;
- any requirement of the Company to make contributions to its funded defined benefit pension plans in excess of those currently contemplated;
- the inability of the Company to attract and retain key executives;
- supply and quality control issues with vendors; and
- failure by the Company to maintain appropriate documentation to support its compliance with accounting, tax or legal rules, regulations and policies.

These and other risks and uncertainties are discussed in the Company's materials filed with the Canadian securities regulatory authorities from time to time, including Section 12, "Enterprise Risks and Risk Management", of this MD&A. These forward-looking statements contained herein and in particular in the Report to Shareholders and MD&A reflect management's current assumptions regarding these risks and uncertainties and their respective impact on the Company.

Other risks and uncertainties not presently known to the Company or that the Company presently believes are not material could also cause actual results or events to differ materially from those expressed in its forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect the Company's expectations only as of the date of this Annual Report. The Company disclaims any intention or obligation to update or revise these forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

## 2. OVERVIEW

George Weston Limited is a Canadian public company, founded in 1882, engaged in food processing and distribution. The Company has two reportable operating segments: Loblaw and Weston Foods, and holds cash and short term investments. The Loblaw operating segment, which is operated by Loblaw Companies Limited and its subsidiaries, is Canada's largest food distributor and a leading provider of drugstore, general merchandise and financial products and services. The Weston Foods operating segment is a leading fresh and frozen baking company in Canada and is engaged in frozen baking and biscuit manufacturing in the United States.

## 3. VISION

The Company vision has been, and continues to be, centred on three main principles: growth, innovation and flexibility. The Company seeks long term, stable growth in its operating segments, while accepting prudent operating risks through continuous capital investment supported by a strong balance sheet with the goal of providing sustainable returns to its shareholders over the long term through a combination of common share price appreciation and dividends.

The Company believes that to be successful over the long term, it must deliver on what its customers and consumers want today and in the future. The Company encourages innovation in order to provide consumers with new products and convenient services at competitive prices that meet consumers' everyday household needs.

Looking ahead, the Company plans to achieve these goals by focusing on its long term operating and financial strategies as discussed below.

## 4. OPERATING AND FINANCIAL STRATEGIES

To be successful in achieving its vision, the Company employs various operating and financial strategies. The Company engages in strategic acquisitions and dispositions when it is in the best long term interests of its shareholders to do so.

Each of the Company's two reportable operating segments has its own risk profile and operating risk management strategies.

Weston Foods' mission is to be recognized by its customers as providing the best bakery solutions in North America.

This will be achieved by focusing on innovation, cost management and continuous process improvement while exceeding customer and consumer expectations through superior service and product quality.

Weston Foods' long term operating strategies include:

- maintaining customer alignment;
- focusing on brand development including introducing innovative new products to meet the nutritional and dietary concerns of consumers;
- optimizing plant and distribution networks including capital investment to strategically position facilities to support growth and enhance quality, productivity and efficiencies;
- realizing ongoing cost reduction initiatives with the objective of ensuring a low cost operating structure and economies of scale;
- completing strategic acquisitions and developing relationships to broaden market penetration and expand geographic presence; and
- building leadership capability.

Loblaw's mission is to be Canada's best food, health and home retailer by exceeding customer expectations through innovative products at great prices. Loblaw initiated renewal plans four years ago to achieve its mission by transforming into a centralized, marketing-led organization focused on customers, value, innovative and fresh products and stores, while leveraging its scale and asset base to drive profitable growth.

Loblaw is committed to providing Canadians with a wide range of products and services to meet the everyday household demands of Canadian consumers. Loblaw is known for the quality, innovation and value of its food offering. It offers Canada's strongest control (private) label program, including the unique *President's Choice*, *no name* and *Joe Fresh* brands. In addition, Loblaw makes available to consumers *President's Choice Financial* services and offers the *PC* points loyalty program.

While Loblaw achieved many of its goals in 2010, Loblaw expects to continue the pace and focus on execution of its renewal plan in a market environment that remains unpredictable and competitively intense. In 2011, Loblaw intends to continue to drive initiatives that strengthen its base business including investments in infrastructure, and keeping a vigilant watch on cost control and cash management as it turns its sights on new opportunities by:

- building out from its core food business to capitalize on opportunities in apparel, financial services, health and wellness and Canada's multicultural population;
- continuing to invest in and execute its information technology strategy through the rollout of subsequent supply chain and Enterprise Resource Planning ("ERP") functionality releases with a focus on rolling-out to its merchandising organization and ensuring converted data has integrity for its ERP implementation;

- improving in-store, distribution centre, and store support centre processes in an effort to make the business simpler and more efficient;
- continuing its store upgrade program that will roll out the food renewal and customer service enhancement programs;
- continuing to innovate its control label offering while enhancing profitability;
- continuing to improve its general merchandise range, assortment and profitability;
- focusing on in-store customer service and providing unmatched value; and
- optimizing its customer offering and shopping experience by re-aligning around a new organizational structure.

The Company's financial strategies include:
- maintaining a strong balance sheet;
- minimizing the risks and costs of operating and financing activities; and
- maintaining liquidity and access to capital markets.

The success of these and other plans and strategies discussed in this MD&A may be affected by risks and uncertainties, including those described in Section 12, "Enterprise Risks and Risk Management", of this MD&A.

GWL's Board of Directors ("Board") and senior management meet at least annually to review the Company's business strategy. The business strategy, which generally addresses a three to five year timeframe, targets specific issues in response to the Company's performance and changes in consumer needs and the competitive landscape.

The Company believes that if it successfully implements and executes the business strategy in support of its long term operating and financial strategies, it will be well positioned to fulfill its vision of providing sustainable value to its shareholders over the long term.

### 5. KEY PERFORMANCE INDICATORS

The Company continuously reviews and monitors its activities and key performance indicators, which it believes are important to measuring the success of the implementation of its operating and financial strategies. Some of the Company's key financial performance indicators are set out below:

| **Key Financial Performance Indicators** | **2010** | 2009 |
|---|---|---|
| Sales growth (decline) | **0.6%** | (0.8)%[2] |
| EBITDA[1] ($ millions) | **$ 2,192** | $ 1,654 |
| EBITDA margin[1] | **6.8%** | 5.2% |
| Net earnings from continuing operations ($ millions) | **$ 452** | $ 127 |
| Basic net earnings per common share from continuing operations ($) | **$ 3.16** | $ 0.64 |
| Net debt[1] ($ millions) | **$ 501** | $ 299 |
| Net debt[1] to EBITDA[1] | **0.23x** | 0.18x |
| Net debt[1] to equity | **0.08** | 0.04 |
| Interest coverage | **3.6x** | 2.6x |
| Return on average net assets[1] | **13.3%** | 9.3% |
| Return on average common shareholders' equity | **7.1%** | 1.5% |

(1) See non-GAAP financial measures beginning on page 61.
(2) Compared to a 53-week year in 2008.

In addition, other operating performance indicators include but are not limited to: same-store sales growth; operating and administrative cost management; new product development; customer service ratings; production waste; production efficiencies; and market share.

## 6. OVERALL FINANCIAL PERFORMANCE

### 6.1 BUSINESS DEVELOPMENTS

Significant business developments occurred in the Weston Foods operating segment during 2010 and 2009: the acquisition of ACE Bakery Ltd. ("ACE") and Keystone Bakery Holdings, LLC ("Keystone"), both in the second half of 2010, and the sale of the U.S. fresh bakery business on January 21, 2009.

**Acquisition of ACE Bakery Ltd.**

During the fourth quarter of 2010, the Company purchased ACE, a Canadian manufacturer and supplier of artisan and European-style rustic bread varieties, for $110 million. The results of ACE operations from the date of acquisition were included in the Company's operating results and are discussed in Section 7.1, "Weston Foods Operating Results from Continuing Operations" and Section 9.1, "Quarterly Financial Information", of this MD&A. The results of ACE were not significant to consolidated net earnings from continuing operations.

**Acquisition of Keystone Bakery Holdings, LLC**

During the third quarter of 2010, the Company purchased Keystone, a U.S. manufacturer and supplier of frozen cupcakes, doughnuts and cookies for approximately $188 million (U.S. $186 million). The results of Keystone operations from the date of acquisition were included in the Company's operating results and are discussed in Section 7.1, "Weston Foods Operating Results from Continuing Operations" and Section 9.1, "Quarterly Financial Information", of this MD&A. The results of Keystone were not significant to consolidated net earnings from continuing operations.

**Sale of U.S. Fresh Bakery Business**

On January 21, 2009, Dunedin Holdings S.à r.l. ("Dunedin"), a subsidiary of GWL, sold its U.S. fresh bakery business to Grupo Bimbo, S.A.B. de C.V. for gross and net proceeds of approximately U.S. $2.5 billion, including approximately U.S. $125 million for interest bearing assets. The sale resulted in a gain of $939 million ($901 million, net of tax). The results and the gain on the sale of the U.S. fresh bakery business have been reflected separately as discontinued operations in the comparative results.

### 6.2 CONSOLIDATED RESULTS OF OPERATIONS

| ($ millions except where otherwise indicated) | **2010** | 2009 | 2008[4] |
|---|---|---|---|
| Sales | **$ 32,008** | $ 31,820 | $ 32,088 |
| Operating income | **$ 1,483** | $ 1,009 | $ 1,198 |
| Gain on disposal of business[1] | | | $ 335 |
| Interest expense and other financing charges | **$ 388** | $ 363 | $ 360 |
| Net earnings from continuing operations | **$ 452** | $ 127 | $ 647 |
| Net earnings[2] | **$ 452** | $ 1,035 | $ 834 |
| Basic net earnings per common share from continuing operations ($) | **$ 3.16** | $ 0.64 | $ 4.65 |
| Diluted net earnings per common share from continuing operations ($) | **$ 3.14** | $ 0.63 | $ 4.65 |
| Basic net earnings per common share ($) | **$ 3.16** | $ 7.68 | $ 6.10 |
| Diluted net earnings per common share ($) | **$ 3.14** | $ 7.67 | $ 6.10 |
| EBITDA[3] | **$ 2,192** | $ 1,654 | $ 1,808 |
| EBITDA margin[3] | **6.8%** | 5.2% | 5.6% |

(1) Gain on disposal of business relates to the disposal of Weston Foods' dairy and bottling operations in 2008.
(2) 2009 net earnings include a gain on disposal of $939 million ($901 million, net of tax) recorded in discontinued operations.
(3) See non-GAAP financial measures beginning on page 61.
(4) 2008 was a 53-week year.

The Company's 2010 basic net earnings per common share from continuing operations were $3.16 compared to $0.64 in 2009, an increase of $2.52. Of this increase, $0.53 was attributable to improvements in the operating performance of the Company's two operating segments, Weston Foods and Loblaw. The balance of the improvement of $1.99 was primarily attributable to the following:

- the positive impact of $1.79 per common share related to the year-over-year reduction in foreign currency translation losses;
- the positive impact of $0.38 per common share related to the non-cash goodwill impairment recorded by Weston Foods in 2009; and
- the positive impact of $0.29 per common share related to the redemption of the GWL 12.7% Promissory Notes in 2009; partially offset by
- the negative impact of $0.44 per common share related to the accounting for Weston Holdings Limited's ("WHL"), a subsidiary of GWL, forward sale agreement for 9.6 million Loblaw common shares.

The Company's 2010 basic net earnings per common share were $3.16 compared to $7.68 in 2009. Included in 2009 net earnings per common share were net earnings per common share from discontinued operations of $7.04.

The Company's consolidated financial statements are expressed in Canadian dollars, however a portion of the Company's (excluding Loblaw's) net assets are denominated in U.S. dollars through both its net investment in self-sustaining foreign operations in the United States ("U.S. net investment"), and its net investment in integrated foreign subsidiaries held by Dunedin and certain of its affiliates. The U.S. dollar denominated net assets are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date.

As a result, the Company is exposed to foreign currency translation gains and losses. Prior to the sale of the U.S. fresh bakery business on January 21, 2009, all of the Company's (excluding Loblaw's) U.S. dollar denominated net assets were held in self-sustaining foreign operations and although changes in the value of the U.S. dollar impacted reported sales, operating income and net earnings related to these operations, foreign currency translation gains and losses due to the translation of their net assets were recorded in accumulated other comprehensive loss. After the sale of the U.S. fresh bakery business, Dunedin and certain of its affiliates became integrated foreign subsidiaries for accounting purposes. As a result, gains and losses arising from the translation of the U.S. dollar denominated net assets of these integrated foreign subsidiaries are included in operating income.

The Weston Foods operating segment achieved strong financial results despite soft sales in 2010. Weston Foods sales were negatively impacted by foreign currency translation and lower pricing in certain product categories, partially offset by the positive impact of the Keystone and ACE acquisitions. After excluding the impact of the commodity derivatives fair value adjustment, the impact of stock-based compensation net of equity derivatives, the non-cash goodwill impairment charge in Weston Foods' biscuits, cookies, cones and wafers business recorded in 2009 and also foreign currency translation, operating income in 2010 remained strong. Operating income was positively impacted by the benefits realized from productivity improvements and other cost reduction initiatives, lower input costs, lower legal and restructuring charges and the results of the bakery acquisitions, which were partially offset by the impact of lower pricing in certain product categories, continued escalation in labour and related benefit costs and promotional spending.

Over the past two years, the Weston Foods operating segment was impacted by the following key trends:

- a continuing consumer focus on healthier, more nutritious and value-added products as well as more portion controlled items that do not sacrifice great taste. This impacted Weston Foods sales mix and product innovation focus resulting in sales growth in whole grain products, nutritionally enhanced white breads, premium products such as artisan bakery offerings, reduced sodium, fat and no trans fat products, alternative and international products, including flatbreads;

- a continuing growth in the alternate format retail food channels. Weston Foods continues to grow with these alternate formats while retaining its strong position in conventional supermarkets;
- a trend toward more consumers eating at home as the North American economic environment deteriorated. For Weston Foods, this had a positive impact on volume growth with retail store customers but a negative impact with food service customers; and
- although cost pressures somewhat eased in 2009 and 2010 for certain key inputs, cost escalation continued in labour and related benefit costs as well as promotional spending.

Over the past two years, Weston Foods increased investment behind its brands, continued to introduce new products in response to changing consumer eating preferences, and invested capital to support growth and enhance quality and productivity. These investments, coupled with a continued focus on cost improvements, customer service and growth in higher margin product offerings, resulted in strong financial performance.

In 2010, Loblaw continued to make steady progress in its renewal program. Progress during the year was achieved despite a difficult economic environment. Deflationary pressures combined with heightened promotional and competitive activity resulted in soft sales throughout 2010. Throughout the year, Loblaw delivered enhanced fresh food offerings, renovated and revitalized stores, and introduced innovative and differentiated control label brands to provide an enhanced customer shopping experience. In addition, Loblaw continued to invest and build its core infrastructure, including both information technology and supply chain.

Some of Loblaw's key accomplishments in 2010 included:
- improved fresh food quality and assortment;
- touched over 200 stores as part of the store revitalization program of which 160 were considered renovations;
- continued *nofrills* expansion program with an additional nine *nofrills* stores in Western Canada and six more *nofrills* stores in Atlantic Canada;
- improved overall control brand profitability;
- completed the roll-out of a new transportation management system and continued to implement a new warehouse management system;
- enhanced supply chain efficiency that resulted in improved product availability;
- moved forward in implementing the ERP system by integrating the real estate and financial services divisions and the general ledger and related financial reporting across the business onto the new system with nearly 1,000 colleagues now using the system;
- initiated the next wave of ERP implementation with two successful pilots in merchandising involving approximately 20 categories;
- strengthened the balance sheet providing enhanced financial flexibility;
- successfully completed labour negotiations in Ontario and British Columbia providing new and critical scheduling flexibility; and
- recognized as one of Canada's Top 100 employers.

**Sales**

The Company's 2010 consolidated sales increased 0.6% to $32.0 billion from $31.8 billion in 2009.

Consolidated sales growth for 2010 was impacted by each reportable operating segment as follows:
- Negatively by 0.2% due to the sales decrease of 3.7% at Weston Foods. Foreign currency translation negatively impacted Weston Foods sales by approximately 4.4%, while the acquisition of ACE and Keystone positively impacted sales by 2.8%. Of the remaining decline of 2.1%, approximately 2.0% was attributable to lower pricing across key product categories. Volume increased 2.3% in 2010 compared to 2009, of which 2.4% was attributable to the acquisitions.

- Positively by 0.8% due to the sales increase of 0.9% at Loblaw. Same-store sales declined 0.6%. T&T Supermarket Inc. ("T&T") sales positively impacted sales by 1.4%. Loblaw's average annual internal retail food price index was deflated. This compared to average annual internal retail food price inflation in 2009. Net retail square footage increased 0.1 million square feet or 0.2% in 2010 to 50.7 million square feet. Corporate store sales per average square foot increased to $601 from $597 in 2009.

The Company's 2009 consolidated sales (52 weeks) decreased 0.8% to $31.8 billion from $32.1 billion in 2008 (53 weeks).

Consolidated sales growth for 2009 was impacted by each reportable operating segment as follows:

- Negatively by 1.6% due to the sales decrease of 23.3% at Weston Foods. The sale of the dairy and bottling operations and the additional week of operating results in 2008 negatively impacted reported sales growth by approximately 24.8% and 1.3%, respectively, while foreign currency translation positively impacted sales by approximately 2.4%. The combined effect of price increases implemented in 2008 across key product categories and changes in sales mix was a positive impact of 1.3% for 2009. Volume declined 41.8% for the year, of which 39.5% was due to the sale of the dairy and bottling operations and approximately 1.4% was due to the additional week of operating results in 2008.
- Negatively by 0.2% due to the sales decrease of 0.2% at Loblaw. Same-store sales declined 1.1%, including a decline in sales and same-store sales of approximately 1.8% due to the extra selling week in 2008. Net retail square footage increased 0.8 million square feet or 1.6% in 2009 to 50.6 million square feet. Corporate store sales per average square foot decreased to $597 in 2009 from $624 in 2008.

**Operating Income**

The Company's 2010 consolidated operating income was $1,483 million compared to $1,009 million in 2009, an increase of 47.0%. The consolidated operating margin in 2010 was 4.6% compared to 3.2% in 2009. The Company's 2010 consolidated operating income growth was impacted positively by 15.4% due to an increase of 126.0% in operating income at Weston Foods, and positively by 6.3% due to an increase of 5.3% in operating income at Loblaw. In addition, the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates positively impacted operating income growth by 25.3%.

The year-over-year change in the following items influenced the Company's operating income in 2010 compared to 2009:

- a charge of $56 million (2009 – $311 million), of which $56 million (2009 – $225 million) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and nil (2009 – $86 million) related to the reversal of cumulative foreign currency translation losses;
- nil (2009 – a charge of $73 million) related to the non-cash goodwill impairment in Weston Foods' biscuits, cookies, cones and wafers business;
- a charge of $26 million (2009 – nil) related to an asset impairment due to the closure of a Loblaw distribution centre in Quebec;
- income of $39 million (2009 – $24 million) related to the commodity derivatives fair value adjustment at Weston Foods; and
- a charge of $20 million (2009 – $12 million) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw.

Included in the effect of foreign currency translation of $225 million reported in 2009 was a $48 million charge related to the conversion of U.S. $2.4 billion of cash and short term investments to approximately $3.0 billion Canadian dollars following the sale of the U.S. fresh bakery business. This loss was a result of the appreciation of the Canadian dollar relative to the U.S. dollar between the closing date of the sale and the dates on which the proceeds were converted to Canadian dollars.

Excluding the impact of the specific items noted above, operating income for 2010 remained strong compared to 2009.

The Company's 2010 consolidated EBITDA margin(1) increased to 6.8% from 5.2% in 2009.

The Company's 2009 consolidated operating income was $1,009 million compared to $1,198 million in 2008, a decrease of 15.8%. The consolidated operating margin in 2009 was 3.2% compared to 3.7% in 2008. The Company's 2009 consolidated operating income was impacted negatively by 2.6% due to a decrease of 20.1% in operating income at Weston Foods, and positively by 12.8% due to an increase of 14.7% in operating income at Loblaw. In addition, the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates negatively impacted operating income by 26.0%.

The year-over-year change in the following items influenced the Company's operating income in 2009 compared to 2008:

- a charge of $311 million (2008 – nil), of which $225 million (2008 – nil) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and $86 million (2008 – nil) related to the reversal of cumulative foreign currency translation losses;
- a charge of $73 million (2008 – nil) related to the non-cash goodwill impairment in Weston Foods' biscuits, cookies, cones and wafers business;
- income of $24 million (2008 – a charge of $46 million) related to the commodity derivatives fair value adjustment at Weston Foods;
- a charge of $12 million (2008 – income of $2 million) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw;
- nil (2008 – income of $47 million) related to the income of Weston Foods' dairy and bottling operations;
- nil (2008 – income of $22 million) related to the gain on the sale of Loblaw's food service business; and
- nil (2008 – income of $7 million) related to the redemption of the remaining outstanding GWL 3% Exchangeable Debentures and the sale of the Domtar (Canada) Paper Inc. shares.

Excluding the impact of the specific items noted above, operating income for 2009 was strong compared to 2008.

The Company's 2009 consolidated EBITDA margin(1) decreased to 5.2% from 5.6% in 2008.

**Gain on Disposal of Business**

In 2008, the Company recorded a pre-tax gain of $335 million ($281 million, net of tax) on the disposal of Weston Foods' dairy and bottling operations. The effect on basic net earnings per common share for 2008 was income of $2.18.

**Interest Expense and Other Financing Charges**

Interest expense and other financing charges consist primarily of interest on short and long term debt, interest and other financing charges on financial derivative instruments and dividends on capital securities, net of interest earned on short term investments and security deposits, and interest capitalized to fixed assets. In 2009, interest expense and other financing charges also included a loss on the redemption of debt.

In 2010, interest expense and other financing charges increased $25 million to $388 million from $363 million in 2009.

(1) See non-GAAP financial measures beginning on page 61.

The increase was mainly due to:

- an increase in the non-cash charge related to the fair value adjustment of WHL's forward sale agreement for 9.6 million Loblaw common shares of $75 million, when compared to 2009 (see notes 6 and 26 to the consolidated financial statements for additional information); partially offset by
- a loss of $49 million recorded in 2009 related to the redemption of the GWL 12.7% Promissory Notes.

Excluding the impact of the specific items noted above, interest expense and other financing charges in 2010 decreased $1 million when compared to 2009.

The 2010 weighted average fixed interest rate on long term debt (excluding capital lease obligations) was 6.3% (2009 – 6.5%) and the weighted average term to maturity was 14 years (2009 – 14 years).

In 2009, interest expense and other financing charges increased by $3 million to $363 million from $360 million in 2008.

The increase was mainly due to:

- a loss of $49 million recorded in 2009 related to the redemption of the GWL 12.7% Promissory Notes; offset by
- a $25 million decrease in interest on long term debt to $371 million compared to $396 million in 2008; and
- a decrease in the non-cash charge related to the fair value adjustment of WHL's forward sale agreement for 9.6 million Loblaw common shares of $24 million, when compared to 2008.

The 2009 weighted average fixed interest rate on long term debt (excluding capital lease obligations) was 6.5% (2008 – 6.6%) and the weighted average term to maturity was 14 years (2008 – 15 years).

**Income Taxes**

The Company's 2010 effective income tax rate decreased to 33.8% from 40.1% in 2009. The decrease in the effective income tax rate when compared to 2009 was mainly due to a decrease in non-deductible foreign currency translation losses, partially offset by an increase in income tax expense relating to certain prior year income tax matters and a charge of $15 million related to changes in the federal tax legislation that resulted in the elimination of the Company's ability to deduct costs associated with cash-settled stock options.

During 2010, GWL received a reassessment from the Canada Revenue Agency ("CRA") challenging GWL's characterization of a gain reported in a previous tax return filing. Should the CRA be successful in its assertion, the maximum exposure to the Company's net earnings would be approximately $62 million. GWL intends to vigorously defend its filing position. No amount has been recorded in the Company's financial statements.

The Company's effective income tax rate increased in 2009 to 40.1% from 25.9% in 2008. The increase in the effective income tax rate when compared to 2008 was mainly the result of non-deductible foreign currency translation losses recorded in 2009. The increase was partially offset by the cumulative reduction in income tax expense as a result of a reduction in Ontario statutory income tax rates enacted in the fourth quarter of 2009 and a decrease in income tax accruals relating to certain prior year income tax matters.

**Net Earnings from Continuing Operations**

Net earnings from continuing operations for 2010 were $452 million compared to $127 million in 2009. Basic net earnings per common share from continuing operations for 2010 were $3.16 compared to $0.64 in 2009.

Basic net earnings per common share from continuing operations were affected for 2010 compared to 2009 by the following factors:

- a $0.43 per common share charge (2009 – $2.22), of which $0.43 (2009 – $1.56) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and nil (2009 – a $0.66 per common share charge) related to the reversal of cumulative foreign currency translation losses;

- a $0.36 per common share non-cash charge (2009 – $0.08 per common share non-cash income) related to the accounting for WHL's forward sale agreement for 9.6 million Loblaw common shares;
- nil (2009 – a $0.38 per common share charge) related to the non-cash goodwill impairment in Weston Foods' biscuits, cookies, cones and wafers business;
- nil (2009 – a $0.29 per common share charge) related to the redemption of the GWL 12.7% Promissory Notes;
- a $0.09 per common share charge (2009 – nil) related to an asset impairment due to the closure of a Loblaw distribution centre in Quebec;
- $0.21 per common share income (2009 – $0.12) related to the commodity derivatives fair value adjustment at Weston Foods;
- a $0.08 per common share charge (2009 – nil) related to changes in the federal tax legislation that resulted in the elimination of the Company's ability to deduct costs associated with cash-settled stock options; and
- a $0.04 per common share charge (2009 – $0.09) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw.

Net earnings from continuing operations for 2009 were $127 million compared to $647 million in 2008. Basic net earnings per common share from continuing operations for 2009 were $0.64 compared to $4.65 in 2008.

Basic net earnings per common share from continuing operations were affected for 2009 compared to 2008 by the following factors:

- a $2.22 per common share charge (2008 – nil), of which $1.56 (2008 – nil) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and $0.66 (2008 – nil) related to the reversal of cumulative foreign currency translation losses;
- a $0.38 per common share charge (2008 – nil) related to the non-cash goodwill impairment in Weston Foods' biscuits, cookies, cones and wafers business;
- $0.12 per common share income (2008 – a $0.24 per common share charge) related to the commodity derivatives fair value adjustment at Weston Foods;
- a $0.29 per common share charge (2008 – nil) related to the redemption of the GWL 12.7% Promissory Notes;
- $0.08 per common share non-cash income (2008 – a $0.06 per common share non-cash charge) related to the accounting for WHL's forward sale agreement for 9.6 million Loblaw common shares;
- a $0.09 per common share charge (2008 – $0.06) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw;
- nil (2008 – a $0.03 per common share charge) related to the income tax effect of the fair value adjustment of the Domtar (Canada) Paper Inc. shares, net of the remeasurement of the GWL 3% Exchangeable Debentures;
- nil (2008 – $0.04 per common share income) related to the redemption of the remaining outstanding GWL 3% Exchangeable Debentures and the sale of the Domtar (Canada) Paper Inc. shares;
- nil (2008 – $0.07 per common share income) related to the gain on the sale of Loblaw's food service business;
- nil (2008 – $0.25 per common share income) related to the income of Weston Foods' dairy and bottling operations; and
- nil (2008 – $2.18 per common share income) related to the gain on disposal of Weston Foods' dairy and bottling operations.

**Discontinued Operations**

Net earnings from discontinued operations were nil in 2010 compared to $908 million in 2009 and $187 million in 2008. Included in 2009 net earnings from discontinued operations was a gain on disposal of $939 million ($901 million, net of tax) related to the sale of the U.S. fresh bakery business. For additional information, see note 4 to the consolidated financial statements.

**Net Earnings**

Net earnings for 2010 were $452 million compared to $1,035 million in 2009. Basic net earnings per common share for 2010 decreased to $3.16 compared to $7.68 in 2009, including basic net earnings per common share from discontinued operations of nil compared to $7.04 in 2009.

Net earnings for 2009 increased $201 million to $1,035 million compared to $834 million in 2008. Basic net earnings per common share for 2009 increased $1.58 to $7.68 compared to $6.10 in 2008, including basic net earnings per common share from discontinued operations of $7.04 compared to $1.45 in 2008.

There were no new accounting standards implemented in 2010. Accounting standards implemented in 2009 are discussed in Section 15, "Accounting Standards Implemented in 2009", of this MD&A and in note 2 to the consolidated financial statements.

Changes in minority interest did not have a significant impact on the growth of the Company's net earnings over the past two years. GWL's ownership of Loblaw was 62.9% as at the end of 2010, 62.5% as at the end of 2009 and 61.9% as at the end of 2008. The increase in GWL's ownership was primarily due to the Company's participation in the Loblaw Dividend Reinvestment Plan ("DRIP"). The increase in 2009 was also due to Loblaw's repurchase of 1.7 million of its common shares during the fourth quarter of 2009.

Subsequent to the end of 2010, the Loblaw Board of Directors approved that the DRIP be discontinued following the dividend payment on April 1, 2011 when approximately $300 million in Loblaw common share equity will have been raised through the program as planned.

## 6.3 CONSOLIDATED FINANCIAL CONDITION

| ($ millions except where otherwise indicated) | | **2010** | 2009 | 2008 |
|---|---|---|---|---|
| Total assets | | **$ 20,854** | $ 20,143 | $ 19,563 |
| Total long term debt (excluding amount due within one year) | | **$ 5,129** | $ 5,377 | $ 5,308 |
| Dividends declared per share ($) | – Common share(1) | **$ 9.19** | $ 1.44 | $ 1.44 |
| | – Preferred share: | | | |
| | Series I | **$ 1.45** | $ 1.45 | $ 1.45 |
| | Series II | | $ 0.32 | $ 1.29 |
| | Series III | **$ 1.30** | $ 1.30 | $ 1.30 |
| | Series IV | **$ 1.30** | $ 1.30 | $ 1.30 |
| | Series V | **$ 1.19** | $ 1.19 | $ 1.19 |

(1) 2010 includes the special one-time common share dividend of $7.75 per common share which was declared in the fourth quarter of 2010 and subsequently paid on January 25, 2011.

The Company's total assets in 2010 were greater than in 2009 and 2008. The 2010 increase was primarily due to the acquisition of Keystone and ACE by Weston Foods and an increase in fixed assets primarily as a result of Loblaw's capital investment program, including the incremental investment in information technology and supply chain. This increase was partially offset by the appreciation of the Canadian dollar relative to the U.S. dollar, which caused a decrease in the translated amounts of U.S. dollar denominated net assets. The increase in 2009 was primarily due to an increase in cash and short term investment balances net of the decrease in current assets of operations held for sale which were sold in 2009, an increase in goodwill and intangible assets as a result of the acquisition of T&T by Loblaw and an increase in fixed assets primarily as a result of Loblaw's capital investment program, including the incremental investment in information technology and supply chain and the acquisition of a distribution centre in 2009. This increase was partially offset by the appreciation of the Canadian dollar relative to the U.S. dollar, which caused a decrease in the translated amounts of U.S. dollar denominated net assets.

The Company holds significant cash and short term investments denominated in Canadian and United States dollars. Cash flows from operating activities, proceeds from the sale of the U.S. fresh bakery business in 2009 and the proceeds from the sale of the dairy and bottling operations in the fourth quarter of 2008 have covered a large portion of the funding requirements for the Company over the past two years.

Over the past two years, the Company's funding requirements resulted primarily from:

- capital investment programs;
- repayment of long term debt;
- acquisition of Keystone by Weston Foods;
- acquisition of ACE by Weston Foods;
- acquisition of T&T by Loblaw;
- dividends paid on common and preferred shares;
- redemption of the GWL preferred shares, Series II;
- redemption of the GWL 12.7% Promissory Notes; and
- settlement of Loblaw equity forward contracts.

During the fourth quarter of 2010, the Company declared a special one-time common share dividend of $7.75 per common share which was subsequently paid on January 25, 2011.

**Financial Ratios**

The Company's 2010 return on average net assets(1) of 13.3% was higher than the 2009 return of 9.3%. The 2010 return on average common shareholders' equity of 7.1% was higher than the 2009 return of 1.5%. The increase in both measures in 2010 was largely the result of higher reported operating income, while the increase in the return on average common shareholders' equity was also impacted by the accrual of the $1.0 billion special one-time common share dividend declared in the fourth quarter of 2010 and subsequently paid on January 25, 2011.

The Company's 2009 return on average net assets(1) of 9.3% was lower than the 2008 return of 11.2%, and the Company's 2009 return on average common shareholders' equity of 1.5% was lower than the 2008 return of 13.4%. The decrease in both measures in 2009 was largely the result of lower reported operating income, while the decrease in the return on average common shareholders' equity in 2009 was also impacted by the gain on sale of Weston Foods' dairy and bottling operations in 2008.

The Company's net debt(1) to EBITDA(1) ratio was 0.23 times at the end of 2010 compared to 0.18 times at the end of 2009. The increase in this ratio was driven primarily by an increase in net debt(1) as described below, which was partially offset by an increase in EBITDA(1). The increase in EBITDA(1) was primarily due to the reduction in foreign currency translation losses on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and increases in operating income at both Weston Foods and Loblaw. The Company's 2010 net debt(1) to equity(1) ratio was 0.08:1 compared to 0.04:1 in 2009. The increase in this ratio was also due primarily to the increase in net debt(1), as well as a decrease in shareholders' equity from 2009 to 2010. The decrease in shareholders' equity resulted from the accrual of the $1.0 billion special one-time common share dividend declared in the fourth quarter of 2010 and subsequently paid on January 25, 2011.

The Company's net debt(1) to EBITDA(1) ratio was 0.18 times at the end of 2009 compared to 1.8 times at the end of 2008. The decrease in this ratio was driven primarily by a reduction in net debt(1), which was partially offset by a decrease in EBITDA(1). The reduction in net debt(1) was primarily due to the proceeds from the sale of the U.S.

(1) See non-GAAP financial measures beginning on page 61.

fresh bakery business of $3,107 million and improvements in non-cash working capital at Loblaw, partially offset by the redemption of GWL preferred shares, Series II, for $265 million and the acquisition of T&T by Loblaw. The decrease in EBITDA[(1)] was primarily due to lower operating income. The Company's 2009 net debt[(1)] to equity[(1)] ratio was 0.04:1 compared to 0.53:1 in 2008. The decrease in this ratio was also due primarily to the decrease in net debt[(1)], as described above, as well as an increase in shareholders' equity from 2008 to 2009. The increase in shareholders' equity resulted primarily from the gain on disposal of the U.S. fresh bakery business.

The 2010 interest coverage ratio increased to 3.6 times compared to 2.6 times in 2009 primarily due to the increase in operating income. Interest expense and other financing charges included a non-cash charge of $62 million (2009 – non-cash income of $13 million) recorded in 2010 related to the fair value adjustment of WHL's forward sale agreement for 9.6 million Loblaw common shares, which negatively impacted the change in the interest coverage ratio by approximately 0.8 times.

The 2009 interest coverage ratio decreased to 2.6 times compared to 3.2 times in 2008 primarily due to the decrease in operating income. Interest expense and other financing charges included non-cash income of $13 million (2008 – a non-cash charge of $11 million) recorded in 2009 related to the fair value adjustment of WHL's forward sale agreement for 9.6 million Loblaw common shares, which positively impacted the change in the interest coverage ratio by approximately 0.2 times.

**Net Debt[(1)]**

Net debt[(1)] was $501 million as at December 31, 2010 compared to $299 million as at December 31, 2009. The increase was primarily due to fixed asset purchases at Loblaw, dividend payments and the acquisition of Keystone and ACE by Weston Foods, partially offset by positive cash flows from operating activities.

The Company's net debt[(1)] was $299 million as at December 31, 2009 compared to $3,251 million as at December 31, 2008. Of the $2,952 million reduction in net debt[(1)], the proceeds from the sale of the U.S. fresh bakery business accounted for $3,107 million. The reduction was also largely attributable to improvements in non-cash working capital at Loblaw, partially offset by the redemption of the GWL preferred shares, Series II, for $265 million and the acquisition of T&T by Loblaw.

**Outstanding Share Capital and Capital Securities**

GWL's outstanding share capital is comprised of common shares and preferred shares. The following table details the authorized and outstanding common shares and preferred shares:

| | Authorized | Outstanding |
|---|---|---|
| Common shares | Unlimited | 129,073,662 |
| Preferred shares – Series I | 10,000,000 | 9,400,000 |
| – Series II | 10,600,000 | |
| – Series III | 10,000,000 | 8,000,000 |
| – Series IV | 8,000,000 | 8,000,000 |
| – Series V | 8,000,000 | 8,000,000 |

GWL may, at its option, redeem for cash, in whole or in part, the preferred shares Series I, Series III, Series IV and Series V outstanding on or after the redemption dates specified by the terms of each series of preferred shares. GWL may at any time after issuance give the holders of these preferred shares the right, at the option of the holder, to convert the holder's preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

Further information on GWL's outstanding share capital is provided in note 22 to the consolidated financial statements.

On April 1, 2009, the Company redeemed for cash the 10.6 million outstanding Series II preferred shares for $25.00 per share, or $265 million in aggregate, plus accrued and unpaid dividends to but excluding April 1, 2009

(1) See non-GAAP financial measures beginning on page 61.

in accordance with the terms of the shares. At year end 2008, these preferred shares were presented as capital securities and were included in current liabilities.

Twelve million non-voting Loblaw second preferred shares, Series A, are authorized and 9.0 million were outstanding at year end 2010. These preferred shares are presented as capital securities and are included in long term liabilities on the consolidated balance sheet. Dividends on capital securities are presented in interest expense and other financing charges on the consolidated statements of earnings.

Further information on the Company's capital securities is provided in note 21 to the consolidated financial statements.

At year end, a total of 1,533,443 GWL stock options were outstanding, representing 1.2% of GWL's issued and outstanding common shares. At year end, a total of 9,320,865 Loblaw stock options were outstanding, representing 3.3% of Loblaw's issued and outstanding common shares. The number of stock options outstanding was within the Companies' guidelines of 5% of the total number of outstanding shares. Each stock option is exercisable into one common share of GWL or Loblaw at the price specified in the terms of the option agreement, or option holders may elect to receive in cash the share appreciation value equal to the excess of the market price at the date of exercise over the specified option price. Subsequent to the end of 2010, the right to receive a cash payment in lieu of exercising an option for shares was removed.

Further information on GWL's and Loblaw's stock-based compensation is provided in note 24 to the consolidated financial statements.

**Dividends**

The declaration and payment of dividends and the amounts thereof are at the discretion of the Board, which takes into account the Company's financial results, capital requirements, available cash flow and other factors the Board considers relevant from time to time. Over the long term, GWL's objective is for its common dividend payment ratio to be in the range of 20% to 25% of the prior year's basic net earnings per common share from continuing operations, adjusted as appropriate for items which are not regarded to be reflective of ongoing operations, giving consideration to the year end cash position, future cash flow requirements and investment opportunities. Currently, there is no restriction that would prevent GWL from paying common dividends at historical levels. Dividends on the preferred shares rank in priority ahead of the common shares.

During the fourth quarter of 2010, as a result of the Company's solid operating performance, significant cash balances and ample liquidity to grow the business, GWL declared a special one-time common share dividend of $7.75 per common share in excess of its normal dividends.

Subsequent to the end of 2010, common share dividends of $0.36 per share and preferred share dividends of $0.32 per share for the Series III and Series IV preferred shares and dividends of $0.30 per share for the Series V preferred shares, payable on April 1, 2011, were declared by the Board. In addition, dividends of $0.36 per share for the Series I preferred shares, payable on March 15, 2011 were also declared.

At the time such dividends are declared, GWL identifies on its website (www.weston.ca) the designation of eligible and ineligible dividends in accordance with the administrative position of the CRA.

**Equity Derivative Contracts**

As at year end 2010, Glenhuron Bank Limited ("Glenhuron"), a wholly owned subsidiary of Loblaw, had cumulative equity forwards to buy 1.5 million (2009 – 1.5 million) Loblaw common shares at an average forward contract price of $56.26 (2009 – $66.25), including $0.04 (2009 – $10.03) per common share of interest expense. As at year end 2010, the cumulative interest and unrealized market loss of $24 million (2009 – $48 million) was included in accounts payable and accrued liabilities relating to these equity forwards. As at year end 2010, GWL had equity swaps to buy 1.7 million (2009 – 1.7 million) GWL common shares at an average forward price of $103.17 (2009 – $103.17). As at year end 2010, the unrealized market loss of $32 million (2009 – $61 million) was recorded in accounts payable and accrued liabilities relating to these equity swaps. Subsequent to the end of 2010, GWL elected to adjust the forward price of these equity swaps by $7.75 to an average forward price of $95.42 as a result of the special one-time common share dividend of $7.75 per common share declared in the fourth quarter of 2010.

During 2009, Glenhuron paid $55 million to terminate equity forwards representing 3.3 million Loblaw common shares, which led to the extinguishment of a corresponding portion of the associated liability.

## 7. RESULTS OF REPORTABLE OPERATING SEGMENTS

The following discussion provides details of the 2010 results of operations of each of the Company's reportable operating segments.

### 7.1 WESTON FOODS OPERATING RESULTS FROM CONTINUING OPERATIONS

| ($ millions except where otherwise indicated) | 2010 | 2009 | Change |
|---|---|---|---|
| Sales | **$ 1,624** | $ 1,686 | (3.7)% |
| Operating income | **$ 278** | $ 123 | 126.0% |
| Operating margin | **17.1%** | 7.3% | |
| EBITDA[1] | **$ 332** | $ 179 | 85.5% |
| EBITDA margin[1] | **20.4%** | 10.6% | |
| Return on average net assets[1] | **38.1%** | 19.2% | |

(1) See non-GAAP financial measures beginning on page 61.

As previously discussed, the Company purchased Keystone, a U.S. manufacturer and supplier of frozen cupcakes, doughnuts and cookies during the third quarter of 2010 and ACE, a Canadian manufacturer and supplier of artisan and European-style rustic bread varieties during the fourth quarter of 2010. The results of Keystone and ACE from their respective dates of acquisition were included in Weston Foods 2010 results.

Sales and operating income in 2010 were impacted by the following trends:

- changing consumer eating preferences toward healthier, more nutritious and value-added offerings continued in 2010. Weston Foods responded to these trends with innovative and expanded products across its product portfolio resulting in new sales growth. These trends are expected to continue into 2011 and Weston Foods is well positioned to participate in this growth with its strong portfolio of on-trend offerings under its *Wonder*, *D'Italiano*, *Country Harvest* and *Gadoua* brands;
- the continuing shift in consumer food shopping patterns toward alternate format retail channels rather than traditional, conventional supermarket formats resulted in sales growth with these alternate format retailers. Weston Foods continues to focus on ensuring its products are well aligned to serve all its customers' needs;
- the continued focus on productivity and cost reduction contributed to the growth in operating income;
- lower pricing in 2010 mainly due to a new go-to-market strategy for wafers and cones;
- lower input costs were realized in 2010 compared to 2009, partially offset by continued cost escalation in labour and related benefit costs as well as increased promotional support; and
- the acquisition of Keystone and ACE which contributed positively to overall frozen bakery sales growth.

A detailed discussion on how these trends and other factors impacted sales and operating income in 2010 is set out below.

**Sales**

Weston Foods sales for 2010 of $1,624 million decreased 3.7% compared to 2009. Foreign currency translation negatively impacted sales by approximately 4.4%, while the acquisitions positively impacted sales by 2.8%. Of the remaining decline of 2.1%, approximately 2.0% was attributable to lower pricing in certain product categories. Volume increased 2.3% in 2010 compared to 2009, of which 2.4% was attributable to the acquisitions.

The following sales analysis excludes the impact of foreign currency translation.

Fresh bakery sales, principally bread, rolls, bagels, tortillas and fresh-baked sweet goods, decreased approximately 1.0% in 2010 compared to 2009 and represented approximately 39% of total Weston Foods sales, up from approximately 38% in 2009. The sales decline was primarily due to lower sales volumes, partially offset by higher pricing including increased promotional spending. Volumes decreased in 2010 due to lower sales of private label products and the continued softness in the food service market, partially offset by growth in the *Gadoua* and *D'Italiano* brands. The introduction of new products, such as *Wonder+ Invisibles, Country Harvest* Ancient Grains*, Country Harvest* Raisin Cinnamon with Whole Wheat*, Jake's Bake House, Wonder+ SimplyFree* and *D'Italiano* Focaccia, contributed positively to branded sales growth in 2010.

Frozen bakery sales, principally bread, rolls and sweet goods, increased approximately 6.8% in 2010 compared to 2009 and represented approximately 42% of total Weston Foods sales, up from approximately 40% in 2009. The sales growth was primarily driven by the acquisitions. Excluding the effect of these acquisitions, frozen bakery sales decreased approximately 0.3% in 2010 compared to 2009 due to lower pricing and lower sales volumes as a result of decreases in certain product categories including the continued softness in the food service market and the loss of certain distributed products.

Biscuit sales, principally wafers, ice-cream cones, cookies and crackers, decreased approximately 7.7% in 2010 compared to 2009 and represented approximately 19% of total Weston Foods sales, down from approximately 22% in 2009. The sales decline in this category was mainly due to lower pricing in certain product categories. Overall volumes increased compared to 2009 mainly due to growth in cookie and wafer sales, partially offset by lower cone and cup sales.

**Operating Income**

Weston Foods operating income for 2010 increased by $155 million, or 126.0%, to $278 million compared to $123 million in 2009. Operating margin for 2010 was 17.1% compared to 7.3% in 2009.

The year-over-year change in the following items influenced 2010 operating income compared to 2009:

- nil (2009 – a charge of $73 million) related to the non-cash goodwill impairment in Weston Foods' biscuits, cookies, cones and wafers business;
- income of $39 million (2009 – $24 million) related to the commodity derivatives fair value adjustment; and
- income of $17 million (2009 – $10 million) related to the effect of stock-based compensation net of equity derivatives.

In addition, operating income for 2010 was negatively impacted by foreign currency translation due to a stronger Canadian dollar relative to the U.S. dollar.

Weston Foods is exposed to commodity price fluctuations primarily as a result of purchases of certain raw materials, fuels and utilities. In accordance with the Company's risk management strategy, Weston Foods enters into commodity derivatives to reduce the impact of price fluctuations in forecasted raw material purchases over a specified period of time. These commodity derivatives are not acquired for trading or speculative purposes. Certain of these derivatives are not designated for financial reporting purposes as cash flow hedges of anticipated future raw material purchases, and accordingly hedge accounting does not apply. As a result, changes in the fair value of these derivatives, which include realized and unrealized gains and losses related to future purchases of raw materials, are recorded in operating income. Weston Foods recorded income of $39 million (2009 – $24 million) related to the fair value adjustment of exchange traded commodity derivatives that were not designated within a hedging relationship. Despite the impact of accounting for these commodity derivatives on the Company's reported results, the derivatives have the economic impact of largely mitigating the associated risks arising from price fluctuations in the underlying commodities during the period that the commodity derivatives are held.

Weston Foods continuously evaluates strategic and cost reduction initiatives related to its manufacturing assets, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. Restructuring activities related to these initiatives are ongoing. In 2010 a charge of $6 million (2009 – $9 million) was recorded in operating income related to restructuring activities, including accelerated depreciation of nil (2009 – $2 million).

Excluding these specific items described above, operating income in 2010 remained strong compared to 2009. Operating income was positively impacted by the benefits realized from productivity improvements and other cost reduction initiatives, lower input costs, lower legal and restructuring charges and the results of the bakery acquisitions, which were partially offset by the impact of lower pricing in certain product categories, the continued escalation in labour and related benefit costs and promotional spending.

Gross margin, including the impact of the commodity derivatives fair value adjustment, increased in 2010 compared to 2009.

EBITDA[(1)] increased by $153 million, or 85.5%, to $332 million in 2010 compared to $179 million in 2009. EBITDA margin[(1)] for 2010 increased to 20.4% from 10.6% in 2009, mainly due to the non-cash goodwill impairment charge recorded in the first quarter of 2009 and the increase in operating income as described above.

**Outlook[(2)]**

In 2011, Weston Foods expects continued progress in operating performance driven by sales growth in existing businesses, the full year impact of the 2010 bakery acquisitions and ongoing efforts to reduce costs through improved efficiencies and productivity. This outlook is tempered by the impact of rapidly rising commodity costs and escalating energy costs. While Weston Foods is planning to increase prices to absorb these cost increases, operating margins could be constrained in 2011 as the timing of price increases may lag cost increases.

### 7.2 LOBLAW OPERATING RESULTS

| ($ millions except where otherwise indicated) | **2010** | 2009 | Change |
|---|---|---|---|
| Sales | **$ 30,997** | $ 30,735 | 0.9% |
| Operating income | **$ 1,261** | $ 1,197 | 5.3% |
| Operating margin | **4.1%** | 3.9% | |
| EBITDA[(1)] | **$ 1,916** | $ 1,786 | 7.3% |
| EBITDA margin[(1)] | **6.2%** | 5.8% | |
| Return on average net assets[(1)] | **12.1%** | 11.8% | |

(1) See non-GAAP financial measures beginning on page 61.

While Loblaw delivered solid earnings growth, deflationary pressures and competitive intensity resulted in declines in sales and same-store sales, particularly in the fourth quarter of 2010.

**Sales**

Sales for 2010 increased 0.9% to $31.0 billion compared to $30.7 billion in 2009. The following factors explain the major components in the change in sales when compared to 2009:

- same-store sales declined 0.6%;
- T&T sales positively impacted sales by 1.4%;
- sales growth in food and drugstore were flat;
- sales growth in apparel was strong while sales of other general merchandise declined significantly due to lower discretionary consumer spending and reductions in assortment and square footage;
- gas bar sales increased significantly as a result of higher retail gas prices and strong volume growth;

(1) See non-GAAP financial measures beginning on page 61.
(2) This outlook should be read in conjunction with the Forward-Looking Statements section of this MD&A on page 5.

- Loblaw's average annual internal retail food price index was deflated. This compared to average annual internal retail food price inflation in 2009. Average annual national food price inflation was 1.0% (2009 – 5.5%) as measured by "The Consumer Price Index for Food Purchased from Stores" ("CPI"). CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores; and
- 11 (2009 – 41) corporate and franchised stores were opened and 13 (2009 – 33) corporate and franchised stores were closed, resulting in a net increase of 0.1 million square feet, or 0.2%.

In 2010, Loblaw launched over 1,200 new control label products and redesigned the packaging of approximately 300 products. Sales of control label products for 2010 were $8.2 billion compared to $8.3 billion in 2009.

**Operating Income**

Operating income of $1,261 million for 2010 increased $64 million, or 5.3%, compared to $1,197 million in 2009 resulting in an increase in operating margin to 4.1% in 2010 from 3.9% in 2009.

2010 gross profit increased by $408 million to $7,604 million compared to $7,196 million in 2009. Gross profit as a percentage of sales was 24.5% in 2010 compared to 23.4% in 2009. The increase in gross profit was attributable to improved control label profitability, continued buying synergies and more disciplined vendor management, a stronger Canadian dollar, improved shrink and the shift of pharmaceutical vendor rebates from selling and administrative expenses to gross profit. Increased transportation costs partially offset these improvements.

The increase in operating income was primarily due to the improvement in gross profit, as described above, and the impact of the acquisition of T&T, partially offset by incremental costs of $142 million related to Loblaw's investment in information technology and supply chain, including incremental depreciation and amortization of $59 million, a charge of $37 million (2009 – $22 million) related to the effect of stock-based compensation net of equity forwards, a $26 million asset impairment due to the closure of a distribution centre in Quebec, a charge of $17 million in connection with the ratification of new collective agreements with certain Ontario union locals and a charge of $28 million (2009 – $27 million) for fixed asset impairments related to asset carrying values in excess of fair values for specific store locations. Operating income in 2009 included a gain of $8 million from the sale of financial investments by President's Choice Bank ("PC Bank"), a wholly owned subsidiary of Loblaw.

EBITDA(1) increased $130 million, or 7.3%, to $1,916 million in 2010 compared to $1,786 million in 2009. EBITDA margin(1) increased to 6.2% compared to 5.8% in 2009. The increases in EBITDA(1) and EBITDA margin(1) were primarily due to the increases in operating income and operating margin as described above.

**Outlook(2)**

Loblaw is entering its fifth and final year of renewal and expects to continue its focus on executing the renewal plan in a market environment that remains unpredictable and competitively intense. Loblaw plans to increase its investments in information technology and supply chain which will negatively impact operating income in 2011.

## 8. LIQUIDITY AND CAPITAL RESOURCES

### 8.1 MAJOR CASH FLOW COMPONENTS

| ($ millions) | **2010** | 2009 | Change |
|---|---|---|---|
| Cash flows from operating activities of continuing operations | **$ 1,741** | $ 1,987 | $ (246) |
| Cash flows used in investing activities of continuing operations | **$ (1,561)** | $ (3,152) | $ 1,591 |
| Cash flows used in financing activities of continuing operations | **$ (170)** | $ (867) | $ 697 |
| Cash flows from discontinued operations | | $ 3,017 | $ (3,017) |

(1) See non-GAAP financial measures beginning on page 61.
(2) This outlook should be read in conjunction with the Forward-Looking Statements section of this MD&A on page 5.

### Cash Flows from Operating Activities of Continuing Operations

Cash flows from operating activities of continuing operations in 2010 were $1,741 million compared to $1,987 million in 2009. The decrease when compared to 2009 was primarily due to a decrease in cash flows from non-cash working capital, partially offset by an increase in net earnings from continuing operations before non-cash items.

### Cash Flows used in Investing Activities of Continuing Operations

Cash flows used in investing activities of continuing operations in 2010 were $1,561 million compared to $3,152 million in 2009. The decrease when compared to 2009 was primarily due to the decrease in outflows relating to short term investments, partially offset by the increase in fixed asset purchases and the increase in outflows relating to security deposits as a result of PC Bank's accumulation of cash of $167 million in 2010. Also impacting cash flows used in investing activities of continuing operations was $309 million net cash consideration in connection with business acquisitions in 2010 by Weston Foods and $204 million net cash consideration in connection with the acquisition of T&T by Loblaw in 2009.

The Company's capital investment in 2010 was $1.3 billion (2009 – $1.1 billion). Weston Foods capital investment was $24 million (2009 – $40 million). Loblaw's capital investment was $1.3 billion (2009 – $1.1 billion). Approximately 10% (2009 – 9%) of Loblaw's investments were for new store developments, expansions and land, approximately 44% (2009 – 38%) were for store conversions and renovations, and approximately 46% (2009 – 53%) were for infrastructure investments. The capital investment benefited the regions to varying degrees and strengthened the existing store base.

In 2009, Loblaw's capital investment of $1.1 billion included the purchase of a distribution centre for $140 million plus closing costs. Loblaw assumed long term debt secured by a mortgage of $96 million in connection with the purchase, resulting in net fixed asset purchases of $971 million in 2009.

Loblaw expects to invest approximately $1.0 billion in capital expenditures in 2011. Approximately 50% of these funds are expected to be expended upgrading the information technology and supply chain infrastructure. The remainder will be spent on retail operations as Loblaw plans to renovate certain banners and also to add approximately 1.1 million square feet of retail space.

Loblaw's 2010 corporate and franchised store capital investment program, which included the impact of store openings and closures, resulted in an increase in net retail square footage of 0.2% compared to 2009. During 2010, 11 (2009 – 41) corporate and franchised stores were opened, 13 (2009 – 33) corporate and franchised stores were closed, resulting in a net increase of 0.1 million square feet (2009 – 0.5 million square feet). In 2010, 160 (2009 – 211) corporate and franchised stores underwent renovations.

At year end 2010, the Company had committed approximately $96 million (2009 – $76 million) for the construction, expansion and renovation of buildings and the purchase of real property.

### Cash Flows used in Financing Activities of Continuing Operations

Cash flows used in financing activities of continuing operations in 2010 were $170 million compared to $867 million in 2009.

During 2010, GWL and Loblaw completed the following financing activities:

- Loblaw issued $350 million of unsecured 5.22% Medium Term Notes ("MTN") Series 2-B;
- Loblaw repaid $300 million of 7.10% MTN; and
- GWL issued $36 million of Series B Debentures.

During the third quarter of 2010, PC Bank began accepting deposits under a new Guaranteed Investment Certificate ("GIC") program. The GICs, which are sold through the broker channel, are issued with fixed terms ranging from 12 to 60 months and are non-redeemable prior to maturity. Individual balances up to $100,000 are insured by Canada Deposit Insurance Corporation (CDIC). As at the end of 2010, $18 million of GICs was recorded as long term debt on the consolidated balance sheet, of which $5 million was due within one year.

Subsequent to the end of 2010, Loblaw repaid $350 million of 6.5% MTN.

During 2009, GWL and Loblaw completed the following financing activities:

- Loblaw issued $350 million of unsecured 4.85% MTN Series 2-A;
- Loblaw repaid $125 million of 5.75% MTN;
- Loblaw assumed a mortgage of $96 million;
- GWL redeemed $265 million of preferred shares, Series II;
- GWL repaid $250 million of 5.90% MTN;
- GWL redeemed the 12.7% Promissory Notes; and
- GWL issued $37 million of Series B Debentures.

See notes 17, 18, 21 and 22 to the consolidated financial statements for the terms and details of the debt, capital securities and share capital transactions.

**Employee Future Benefit Contributions**

During 2011, the Company expects to contribute approximately $120 million to its funded defined benefit pension plans. The actual amount paid may vary from the estimate based on actuarial valuations being completed, market performance and regulatory requirements. The Company also expects to make contributions in 2011 to defined contribution plans and multi-employer pension plans as well as benefit payments to the beneficiaries of the supplemental unfunded defined benefit pension plans and other benefit plans.

### 8.2 SOURCES OF LIQUIDITY

The Company holds significant cash and short term investments denominated in Canadian and United States dollars. These funds are invested in highly liquid marketable short term investments consisting primarily of government treasury bills, corporate commercial paper, banker’s acceptances and bank term deposits.

The Company obtains its short term financing through a combination of cash generated from operating activities, cash and cash equivalents, short term investments, bank indebtedness and amounts available to be drawn against Loblaw’s credit facility.

Loblaw expects that cash and cash equivalents, short term investments, future operating cash flows and the amounts available to be drawn against its committed credit facility will enable Loblaw to finance its capital investment program and fund its ongoing business requirements, including working capital, pension plan funding and financial obligations over the next 12 months. Loblaw has traditionally obtained its long term financing primarily through a Medium Term Notes program. Loblaw may refinance maturing long term debt with MTN if market conditions are appropriate or it may consider other alternatives. In addition, given reasonable access to capital markets, Loblaw does not foresee any impediments in obtaining financing to satisfy its long term obligations.

During the third quarter of 2010, Loblaw’s Short Form Base Shelf Prospectus dated June 5, 2008 which allowed for the issuance of up to $1.0 billion of unsecured debentures and/or preferred shares, expired. During the fourth quarter of 2010, Loblaw filed a Short Form Base Shelf Prospectus which allows for the issuance of up to $1.0 billion of unsecured debentures and/or preferred shares over a 25-month period.

During 2008, Loblaw entered into an $800 million, 5-year committed credit facility with a syndicate of third-party lenders. The facility contains certain financial covenants with which Loblaw was in compliance throughout the year. In addition to cash and short term investments, this facility is the primary source of Loblaw’s short term funding requirements and permits borrowings having up to a 180-day term that accrue interest based on short term floating interest rates. As at the end of both 2010 and 2009, Loblaw had not drawn on the 5-year committed credit facility.

PC Bank participates in various securitization programs that provide the primary source of funds for the operation of its credit card business. Under these securitization programs, a portion of the total interest in the credit card receivables is sold to independent trusts pursuant to co-ownership agreements. PC Bank purchases receivables from and sells receivables to the trusts from time to time depending on PC Bank's financing requirements. In 2010, PC Bank securitized $600 million (2009 – nil) credit card receivables and repurchased $690 million (2009 – $50 million) of co-ownership interests in the securitized receivables from independent trusts. On December 15, 2010, *Eagle Credit Card Trust* ("Eagle"), an independent trust through which Loblaw securitizes its accounts receivable, issued two series of senior and subordinated notes maturing December 17, 2013 and December 17, 2015 for notional amounts of $250 million and $350 million, respectively. A portion of the securitized receivables was also renewed for two years during 2010.

The independent trusts' recourse to PC Bank's assets is limited to PC Bank's excess collateral of $114 million (2009 – $121 million) as at the end of 2010 as well as standby letters of credit issued by Loblaw as at the end of 2010 of $48 million (2009 – $116 million) based on a portion of the securitized amount.

On March 17, 2011, the five-year $500 million senior and subordinated notes issued by Eagle will mature. In conjunction with this upcoming maturity, Loblaw accumulated $167 million of cash on December 1, 2010. Subsequent to the end of 2010, Loblaw accumulated $167 million in January 2011 and a further $166 million in February 2011. In addition, subsequent to the end of 2010, Loblaw increased its securitization of accounts receivable by approximately $230 million under one of the independent trusts and expects to securitize further amounts coincident with the maturity of the Eagle Notes.

During 2010, Dominion Bond Rating Service ("DBRS") and Standard & Poor's ("S&P") reaffirmed Loblaw's credit ratings and trend and outlook, respectively. These ratings organizations base their forward-looking credit ratings on both quantitative and qualitative considerations. The following table sets out the current credit ratings of Loblaw:

| | Dominion Bond Rating Service | | Standard & Poor's | |
|---|---|---|---|---|
| Credit Ratings (Canadian Standards) | Credit Rating | Trend | Credit Rating | Outlook |
| Commercial paper | R-2 (middle) | Stable | A-2 | Stable |
| Medium term notes | BBB | Stable | BBB | Stable |
| Preferred shares | Pfd-3 | Stable | P-3 (high) | Stable |
| Other notes and debentures | BBB | Stable | BBB | Stable |

The Company (excluding Loblaw) expects that cash and cash equivalents, short term investments and future operating cash flows will enable it to finance its capital investment program and fund its ongoing business requirements, including working capital and pension plan funding over the next 12 months. The Company (excluding Loblaw) may refinance maturing long term debt with MTN if market conditions are appropriate or it may consider other alternatives. In addition, the Company (excluding Loblaw) does not foresee any impediments in obtaining financing to satisfy its long term obligations.

During 2010, DBRS and S&P reaffirmed GWL's credit ratings and trend and outlook, respectively. These ratings organizations base their forward-looking credit ratings on both quantitative and qualitative considerations. The following table sets out the current credit ratings of GWL:

| | Dominion Bond Rating Service | | Standard & Poor's | |
|---|---|---|---|---|
| Credit Ratings (Canadian Standards) | Credit Rating | Trend | Credit Rating | Outlook |
| Commercial paper | R-2 (high) | Stable | A-2 | Stable |
| Medium term notes | BBB | Stable | BBB | Stable |
| Preferred shares | Pfd-3 | Stable | P-3 (high) | Stable |
| Other notes and debentures | BBB | Stable | BBB | Stable |

In 2010, GWL and Loblaw renewed their Normal Course Issuer Bid ("NCIB") programs to purchase on the Toronto Stock Exchange ("TSX") or enter into equity derivatives to purchase up to 5% of its common shares outstanding. In accordance with the requirements of the TSX, any purchases must be at the then market prices of such shares. GWL did not purchase any shares under its NCIB during 2010 or 2009. Loblaw did not purchase any shares under its NCIB during 2010. During 2009, Loblaw purchased for cancellation 1,698,400 of its common shares at a price of $33.14. In 2011, GWL and Loblaw each intend to renew their NCIB programs.

The Company establishes standby and documentary letters of credit used in connection with certain obligations related to the financing program for Loblaw's independent franchisees, the securitization of PC Bank's credit card receivables, real estate transactions, benefit programs, purchase orders and performance guarantees. At year end, the aggregate gross potential liability related to the Company's letters of credit was approximately $559 million (2009 – $588 million).

**Independent Funding Trust**

Certain independent franchisees of Loblaw obtain financing through a structure involving independent funding trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. These trusts are administered by a major Canadian chartered bank.

The gross principal amount of loans issued to Loblaw's independent franchisees by the independent funding trusts as at the end of 2010 was $405 million (2009 – $390 million), including $202 million (2009 – $163 million) of loans payable by VIEs consolidated by the Company. Loblaw has agreed to provide credit enhancement of $66 million (2009 – $66 million) in the form of a standby letter of credit for the benefit of the independent funding trust representing not less than 15% of the principal amount of the loans outstanding. This standby letter of credit has never been drawn upon. This credit enhancement allows the independent funding trust to provide financing to Loblaw's independent franchisees. As well, each independent franchisee provides security to the independent funding trust for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and Loblaw has not, within a specified time period, assumed the loan, or the default is not otherwise remedied, the independent funding trust would assign the loan to Loblaw and draw upon this standby letter of credit.

During the second quarter of 2010, the $475 million, 364-day revolving committed credit facility that is the source of funding to the independent trusts was renewed. The financing structure has been reviewed and the Company has determined there were no additional VIEs to consolidate as a result of this financing.

## 8.3 CONTRACTUAL OBLIGATIONS

The following illustrates certain of the Company's significant contractual obligations and discusses other obligations as at December 31, 2010:

### Summary of Contractual Obligations

| | Payments due by year | | | | | | |
|---|---|---|---|---|---|---|---|
| ($ millions) | 2011 | 2012 | 2013 | 2014 | 2015 | Thereafter | Total |
| Long term debt(1) | $ 733 | $ 77 | $ 419 | $ 682 | $ 182 | $ 3,769 | $ 5,862 |
| Operating leases(2) | 229 | 209 | 186 | 163 | 134 | 645 | 1,566 |
| Contracts for purchase of real property and capital investment projects(3) | 93 | | | 3 | | | 96 |
| Purchase obligations(4) | 122 | 41 | 26 | 10 | 10 | | 209 |
| Total contractual obligations | $ 1,177 | $ 327 | $ 631 | $ 858 | $ 326 | $ 4,414 | $ 7,733 |

(1) Long term debt includes capital lease obligations.
(2) Represents the minimum or base rents payable. Amounts are not offset by any expected sub-lease income.
(3) These obligations include agreements for the purchase of real property and capital commitments for construction, expansion and renovation of buildings. These agreements may contain conditions that may or may not be satisfied. If the conditions are not satisfied, it is possible the Company will no longer have the obligation to proceed with the underlying transactions.
(4) These include contractual obligations of a material amount to purchase goods or services where the contract prescribes fixed or minimum volumes to be purchased or payments to be made within a fixed period of time for a set or variable price. These are only estimates of anticipated financial commitments under these arrangements and the amount of actual payments will vary. The purchase obligations do not include purchase orders issued or agreements made in the ordinary course of business which are solely for goods that are meant for resale, nor do they include any contracts which may be terminated on relatively short notice or with insignificant cost or liability to the Company. Also excluded are purchase obligations related to commodities or commodity-like goods for which a market for resale exists.

As at year end 2010, the Company had other long term liabilities which included accrued benefit plan liabilities, future income tax liabilities, stock-based compensation liabilities and accrued insurance liabilities. These long term liabilities have not been included in the table above for the following reasons:

- future payments of accrued benefit plan liabilities, principally post-retirement benefits, depend on when and if retirees submit claims;
- future payments of income taxes depend on the levels of taxable earnings and income tax rates;
- future payments of the share appreciation value on employee stock options depend on whether employees exercise their stock options, the market price of GWL or Loblaw common shares on the exercise date and the manner in which employees exercise those stock options;
- future payments of restricted share units depend on the market prices of GWL and Loblaw common shares; and
- future payments of insurance related obligations can extend over several years and depend on the timing of anticipated settlements and results of litigation.

## 8.4 OFF-BALANCE SHEET ARRANGEMENTS

In the normal course of business, the Company enters into off-balance sheet arrangements including:

### Letters of Credit

Standby and documentary letters of credit are used in connection with certain obligations mainly related to real estate transactions, benefit programs, purchase orders and performance guarantees. The aggregate gross potential liability related to Loblaw's letters of credit is approximately $325 million (2009 – $277 million) at year end 2010.

**Guarantees**

The Company has entered into various guarantee agreements including standby letters of credit in relation to the securitization of PC Bank's credit card receivables, third-party financing made available to Loblaw's independent franchisees, and obligations to indemnify third parties in connection with leases, business dispositions and other transactions in the normal course of the Company's business. Additionally, Loblaw has a guarantee on behalf of PC Bank in the amount of U.S. $180 million. For a detailed description of the Company's guarantees, see note 29 to the consolidated financial statements.

**Securitization of Credit Card Receivables**

PC Bank participates in bank supported and term securitization programs. Under these programs, PC Bank sells a portion of the total interest in its credit card receivables to independent trusts in exchange for cash. The trusts fund these purchases by issuing debt securities in the form of asset-backed commercial paper or asset-backed term notes to third-party investors. The securitizations are accounted for as asset sales only when PC Bank transfers control of the transferred assets and receives consideration other than beneficial interests in the transferred assets. All transactions between the trusts and PC Bank have been accounted for as sales as contemplated by Canadian GAAP, specifically AcG 12, "Transfers of Receivables". The trusts are either not controlled by PC Bank or are qualifying special purpose entities and therefore the financial results of the trusts are not included in the Company's consolidated financial statements.

PC Bank sells interests in its credit card receivables to the trusts on a fully serviced basis. PC Bank does not receive a servicing fee from the trusts for its servicing responsibilities and accordingly a servicing obligation is recorded. When a sale occurs, PC Bank retains rights to future cash flows after obligations to the investors in the trusts have been met, which is considered to be a retained interest. The independent trusts' recourse to PC Bank's assets is limited to PC Bank's excess collateral as well as standby letters of credit provided by major Canadian chartered banks for 9% (2009 – 9%) on a portion of the securitized amount. These standby letters of credit could be drawn upon in the event of a major decline in the income flow from, or in the value of, the securitized credit card receivables. The subordinated notes issued by Eagle provide credit support to those notes which are more senior. The retained interest is recorded at fair value.

As at year end 2010, the total amount of securitized credit card receivables outstanding which PC Bank continues to service was $1.6 billion (2009 – $1.7 billion) and the associated retained interest was $21 million (2009 – $13 million). During 2010, PC Bank earned income of $245 million (2009 – $235 million) related primarily to PC Bank's rights to excess cash flows earned on the securitized credit card receivables. In the absence of securitization, Loblaw would be required to use its cash and short term investments or raise alternative financing by issuing debt or equity instruments. Further disclosure regarding this arrangement is provided in notes 1 and 10 to the consolidated financial statements.

**Independent Funding Trust**

Certain independent franchisees of Loblaw obtain financing through a structure involving independent trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. Further disclosure regarding this arrangement is provided in Section 8.2, "Independent Funding Trust", of this MD&A and in note 29 to the consolidated financial statements.

## 9. QUARTERLY RESULTS OF OPERATIONS

The 52-week reporting cycle is divided into four quarters of 12 weeks each except for the third quarter, which is 16 weeks in duration. The following is a summary of selected consolidated financial information derived from the Company's unaudited interim consolidated financial statements for each of the eight most recently completed quarters. This information was prepared in accordance with Canadian GAAP.

### 9.1 QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

| ($ millions except where otherwise indicated) | | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Total (audited) |
|---|---|---|---|---|---|---|
| Sales | **2010** | **$ 7,177** | **$ 7,530** | **$ 9,884** | **$ 7,417** | **$ 32,008** |
| | 2009 | $ 7,022 | $ 7,484 | $ 9,777 | $ 7,537 | $ 31,820 |
| Net earnings (loss) from continuing operations | **2010** | **$ 42** | **$ 125** | **$ 184** | **$ 101** | **$ 452** |
| | 2009 | $ (27) | $ 4 | $ 71 | $ 79 | $ 127 |
| Net earnings | **2010** | **$ 42** | **$ 125** | **$ 184** | **$ 101** | **$ 452** |
| | 2009 | $ 863 | $ 4 | $ 86 | $ 82 | $ 1,035 |
| Net earnings (loss) per common share from continuing operations ($) | | | | | | |
| Basic | **2010** | **$ 0.25** | **$ 0.89** | **$ 1.32** | **$ 0.70** | **$ 3.16** |
| | 2009 | $ (0.28) | $ (0.05) | $ 0.44 | $ 0.53 | $ 0.64 |
| Diluted | **2010** | **$ 0.25** | **$ 0.89** | **$ 1.31** | **$ 0.70** | **$ 3.14** |
| | 2009 | $ (0.28) | $ (0.05) | $ 0.44 | $ 0.52 | $ 0.63 |
| Net earnings (loss) per common share ($) | | | | | | |
| Basic | **2010** | **$ 0.25** | **$ 0.89** | **$ 1.32** | **$ 0.70** | **$ 3.16** |
| | 2009 | $ 6.61 | $ (0.05) | $ 0.56 | $ 0.56 | $ 7.68 |
| Diluted | **2010** | **$ 0.25** | **$ 0.89** | **$ 1.31** | **$ 0.70** | **$ 3.14** |
| | 2009 | $ 6.61 | $ (0.05) | $ 0.56 | $ 0.55 | $ 7.67 |

**Results by Quarter**

Consolidated quarterly sales for the last eight quarters were impacted by the following significant items: the acquisition of ACE by Weston Foods in the fourth quarter of 2010, the acquisition of Keystone by Weston Foods in the third quarter of 2010, the acquisition of T&T by Loblaw in the third quarter of 2009, foreign currency exchange rates, seasonality and the timing of holidays.

Loblaw's average quarterly internal retail food price deflation/inflation for 2010 and 2009 remained lower than the average quarterly national retail food price inflation as measured by CPI. CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores.

Weston Foods 2010 quarterly sales were negatively impacted by foreign currency translation and lower pricing including increased promotional spending compared to the same periods in 2009. Third and fourth quarter sales and volumes were positively impacted by the acquisition of Keystone and ACE.

Consolidated quarterly net earnings for the last eight quarters were impacted by the following significant items:

- the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates, beginning in the first quarter of 2009;
- the commodity derivatives fair value adjustment at Weston Foods;
- accounting for WHL's forward sale agreement of 9.6 million Loblaw common shares;
- fluctuations in stock-based compensation net of equity derivatives of both GWL and Loblaw;
- the effect of changes in the federal tax legislation that resulted in the elimination of the Company's ability to deduct costs associated with cash-settled stock options recorded in the fourth quarter of 2010;

- the asset impairment charge due to the closure of a Loblaw distribution centre in Quebec recorded in the second and third quarters of 2010;
- the loss on the redemption of the GWL 12.7% Promissory Notes in the second and third quarters of 2009;
- the non-cash goodwill impairment charge in Weston Foods' biscuits, cookies, cones and wafers business in the first quarter of 2009;
- the reversal of the cumulative foreign currency translation loss associated with Dunedin and certain of its affiliates in the first quarter of 2009;
- the reversal of the cumulative foreign currency translation loss associated with the reduction in the Company's U.S. net investment in self-sustaining foreign operations in the fourth quarter of 2009;
- the incremental costs related to Loblaw's investment in information technology and supply chain;
- restructuring and other charges incurred by Weston Foods and Loblaw;
- the gain on sale of Weston Foods' U.S. fresh bakery business in the first quarter of 2009; and
- seasonality and the timing of holidays.

At Loblaw, fluctuations in quarterly net earnings during 2010 reflect the underlying operations of Loblaw as well as the impact of specific charges including the impact of stock-based compensation net of equity forwards and costs related to the incremental investment in information technology and supply chain.

At Weston Foods, quarterly net earnings during 2010 were positively impacted by the benefits realized from cost reduction and productivity initiatives, lower input costs in the first three quarters, and lower legal and restructuring charges partially offset by lower pricing in certain product categories. The impact of seasonality is greatest in the third and fourth quarters and least in the first quarter.

## 9.2 FOURTH QUARTER RESULTS (UNAUDITED)

The following is a summary of selected unaudited consolidated financial information for the fourth quarter of 2010. This information was prepared in accordance with Canadian GAAP and is reported in Canadian dollars. The analysis of the data contained in the table focuses on the results of continuing operations and changes in the financial condition and cash flows in the fourth quarter.

**Selected Consolidated Information**

| (unaudited) | Quarters Ended | |
|---|---|---|
| ($ millions except where otherwise indicated) | **Dec. 31, 2010** | Dec. 31, 2009 |
| Sales | **$ 7,417** | $ 7,537 |
| Operating income | **$ 330** | $ 287 |
| Operating margin | **4.4%** | 3.8% |
| Interest expense and other financing charges | **$ 67** | $ 99 |
| Income taxes | **$ 101** | $ 39 |
| Net earnings from continuing operations | **$ 101** | $ 79 |
| Net earnings | **$ 101** | $ 82 |
| Basic net earnings per common share from continuing operations ($) | **$ 0.70** | $ 0.53 |
| Diluted net earnings per common share from continuing operations ($) | **$ 0.70** | $ 0.52 |
| Basic net earnings per common share ($) | **$ 0.70** | $ 0.56 |
| Diluted net earnings per common share ($) | **$ 0.70** | $ 0.55 |
| EBITDA(1) | **$ 497** | $ 442 |
| EBITDA margin(1) | **6.7%** | 5.9% |
| Cash flows from (used in) continuing operations: | | |
| Operating activities | **$ 641** | $ 638 |
| Investing activities | **$ (500)** | $ (717) |
| Financing activities | **$ 9** | $ (14) |

(1) See non-GAAP financial measures beginning on page 61.

The Company's fourth quarter 2010 basic net earnings per common share from continuing operations were $0.70 compared to $0.53 in the same period in 2009, an increase of $0.17. The year-over-year reduction in foreign currency translation losses positively impacted fourth quarter 2010 basic net earnings per common share from continuing operations by $0.27. Excluding these foreign currency translation losses and other specific items identified in the net earnings from continuing operations section below, the Company's basic net earnings per common share from continuing operations were $0.80 in the fourth quarter of 2010 compared to $0.89 in the same period in 2009. The strong improvement in operating performance from the Company's two operating segments, Weston Foods and Loblaw, was more than offset by an increase in income tax expense, primarily relating to certain prior year income tax matters, in the fourth quarter of 2010 compared to the same period in 2009.

***Sales***

Sales in the fourth quarter of 2010 were $7.4 billion compared to $7.5 billion for the same period in 2009, a decrease of 1.6%.

Consolidated sales for the fourth quarter of 2010 were impacted by each reportable operating segment when compared to the same period in 2009 as follows:

- Positively by 0.5% due to the sales increase of 9.7% and volume increase of 10.1% at Weston Foods. The acquisition of Keystone and ACE positively impacted sales growth and volume growth by approximately 11.0% and 9.1%, respectively, while foreign currency translation negatively impacted sales growth by approximately 1.9%. Excluding the acquisitions and foreign currency translation, sales increased 0.6% mainly due to an increase in volumes of 1.0% partially offset by the negative impact of lower pricing in certain product categories of 0.4%.
- Negatively by 2.0% due to the sales decrease of 2.1% at Loblaw. Same-store sales declined 1.6%. Loblaw's average quarterly internal retail food price index was flat. This compared to average quarterly internal retail food price deflation in the same period in 2009. Net retail square footage increased 0.1 million square feet or 0.3% in the fourth quarter of 2010 to 50.7 million square feet.

***Operating Income***

Operating income for the fourth quarter of 2010 was $330 million compared to $287 million in the same period in 2009, an increase of 15.0%. Consolidated operating margin of 4.4% for the fourth quarter of 2010 increased compared to 3.8% in the same period in 2009. The Company's fourth quarter 2010 consolidated operating income growth was positively impacted by 11.8% due to a reduction in foreign currency translation losses on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and by 4.2% due to an increase of 4.4% in operating income at Loblaw. Operating income growth was negatively impacted by 1.0% due to a decrease of 5.2% in operating income at Weston Foods.

The year-over-year change in the following items influenced the Company's operating income in the fourth quarter of 2010 compared to the same period in 2009:

- a charge of $12 million (2009 – $46 million), of which $12 million (2009 – a gain of $6 million) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and nil (2009 – a charge of $52 million) related to the reversal of cumulative foreign currency translation losses;
- a charge of $1 million (2009 – income of $11 million) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw; and
- income of $5 million (2009 – $12 million) related to the commodity derivatives fair value adjustment at Weston Foods.

Excluding the impact of the specific items noted above, operating income for the fourth quarter of 2010 remained strong compared to the same period in 2009.

The Company's consolidated EBITDA margin(1) for the fourth quarter of 2010 increased to 6.7% from 5.9% in the same period in 2009.

### *Interest Expense and Other Financing Charges*

Interest expense and other financing charges for the fourth quarter of 2010 were $67 million, compared to $99 million in the same period in 2009. This decrease was primarily due to a decrease in the non-cash charge related to the fair value adjustment of WHL's forward sale agreement for 9.6 million Loblaw common shares of $29 million when compared to the same period in 2009.

Excluding the impact of this specific item, interest expense and other financing charges in the fourth quarter of 2010 decreased $3 million when compared to the same period in 2009.

### *Income Taxes*

The fourth quarter 2010 effective income tax rate increased to 38.4% from 20.7% in the same period in 2009. The effective income tax rate for the fourth quarter of 2010 was affected by an increase in income tax expense relating to certain prior year income tax matters and a charge of $15 million related to changes in the federal tax legislation that resulted in the elimination of the Company's ability to deduct costs associated with cash-settled stock options.

### *Net Earnings from Continuing Operations*

Net earnings from continuing operations for the fourth quarter of 2010 were $101 million compared to $79 million in the same period in 2009. Basic net earnings per common share from continuing operations for the fourth quarter of 2010 were $0.70 compared to $0.53 in the same period in 2009.

Basic net earnings per common share from continuing operations were affected in the fourth quarter of 2010 compared to the same period in 2009 by the following factors:

- a $0.09 per common share charge (2009 – $0.36), of which $0.09 (2009 – $0.04 per common share income) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates and nil (2009 – a $0.40 per common share charge) related to the reversal of cumulative foreign currency translation losses;
- $0.04 per common share non-cash income (2009 – a $0.13 per common share non-cash charge) related to the accounting for WHL's forward sale agreement for 9.6 million Loblaw common shares;
- a $0.08 per common share charge (2009 – nil) related to changes in the federal tax legislation that resulted in the elimination of the Company's ability to deduct costs associated with cash-settled stock options;
- $0.02 per common share income (2009 – $0.07) related to the commodity derivatives fair value adjustment at Weston Foods; and
- $0.01 per common share income (2009 – $0.06) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw.

### *Discontinued Operations*

Net earnings from discontinued operations for the fourth quarter of 2010 were nil compared to $3 million in the same period in 2009.

### *Net Earnings*

Net earnings for the fourth quarter of 2010 were $101 million compared to $82 million in the same period in 2009. Basic net earnings per common share for the fourth quarter of 2010 were $0.70 compared to $0.56 in 2009, including net earnings from discontinued operations per common share of nil compared to $0.03 in the same period in 2009.

(1) See non-GAAP financial measures beginning on page 61.

***Reportable Operating Segments***

The Company's consolidated sales and operating income were impacted by each of its reportable operating segments as follows:

**WESTON FOODS**

| (unaudited) | Quarters Ended | |
|---|---|---|
| ($ millions) | **Dec. 31, 2010** | Dec. 31, 2009 |
| Sales | **$ 386** | $ 352 |
| Operating income | **$ 55** | $ 58 |
| EBITDA(1) | **$ 69** | $ 70 |

(1) See non-GAAP financial measures beginning on page 61.

For the fourth quarter of 2010, Weston Foods sales of $386 million increased 9.7% and volumes increased 10.1% when compared to the same period in 2009. The acquisition of Keystone and ACE positively impacted sales growth and volume growth by approximately 11.0% and 9.1%, respectively, while foreign currency translation negatively impacted sales growth by approximately 1.9%. Excluding the acquisitions and foreign currency translation, sales increased 0.6% mainly due to an increase in volumes of 1.0% partially offset by the negative impact of lower pricing in certain product categories of 0.4%.

In the fourth quarter, the following sales analysis excludes the impact of foreign currency translation:

- fresh bakery sales, including fresh-baked sweet goods, decreased approximately 0.8%, mainly driven by lower sales volumes, partially offset by higher pricing. Volume declines were due to lower sales of private label products, partially offset by growth in the *Country Harvest* and *D'Italiano* brands. The introduction of new products, such as *Country Harvest* Ancient Grains*, Country Harvest* Raisin Cinnamon with Whole Wheat*, Jake's Bake House, Wonder+ SimplyFree* and *D'Italiano* Focaccia contributed positively to branded sales growth;
- frozen bakery sales increased by approximately 26.8%, mainly due to the acquisition of Keystone and ACE. Excluding the effects of these acquisitions, frozen bakery sales increased by approximately 2.8% primarily due to higher sales volumes. Increase in volume was due to increases in certain product categories, partially offset by the continued softness in the food service market and the loss of certain distributed products; and
- biscuit sales, principally wafers, ice-cream cones, cookies and crackers, decreased approximately 2.6% mainly due to lower prices in certain product categories. Volume increased in the fourth quarter of 2010 compared to the same period in 2009 due to growth in cookie and wafer sales, partially offset by lower cone and cup sales.

Weston Foods operating income was $55 million in the fourth quarter of 2010 compared to $58 million in the same period in 2009. Operating margin was 14.2% for the fourth quarter of 2010 compared to 16.5% in 2009.

The year-over-year change in the following items influenced operating income for the fourth quarter of 2010 compared to the fourth quarter of 2009:

- income of $6 million (2009 – $16 million) related to the effect of stock-based compensation net of equity derivatives; and
- income of $5 million (2009 – $12 million) related to the commodity derivatives fair value adjustment.

In addition, operating income for the fourth quarter of 2010 was negatively impacted by foreign currency translation due to a stronger Canadian dollar relative to the U.S. dollar.

Weston Foods continuously evaluates strategic and cost reduction initiatives related to its manufacturing assets, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. Restructuring activities related to these initiatives are ongoing. In the fourth quarter of 2010, a charge of $4 million (2009 – nil) was recorded in operating income related to restructuring activities.

Excluding these specific items described above, operating income in the fourth quarter of 2010 was strong compared to the same period in 2009. Operating income was positively impacted by sales growth as a result of the bakery acquisitions and by the benefits realized from productivity improvements and other cost reduction initiatives, which were partially offset by higher restructuring charges and the impact of lower pricing in certain product categories.

Gross margin, excluding the impact of the commodity derivatives fair value adjustment, was slightly lower in the fourth quarter of 2010 compared to the same period in 2009.

EBITDA[(1)]decreased to $69 million in the fourth quarter of 2010 compared to $70 million in the same period in 2009. EBITDA margin[(1)] decreased in the fourth quarter of 2010 to 17.9% from 19.9% in the same period in 2009, mainly due to the decrease in operating income as described above.

**LOBLAW**

| (unaudited) | Quarters Ended | |
|---|---|---|
| ($ millions) | **Dec. 31, 2010** | Dec. 31, 2009 |
| Sales | **$ 7,161** | $ 7,311 |
| Operating income | **$ 287** | $ 275 |
| EBITDA[(1)] | **$ 440** | $ 418 |

(1) See non-GAAP financial measures beginning on page 61.

Sales in the fourth quarter decreased 2.1% to $7.2 billion compared to $7.3 billion in the same period in 2009. The following factors explain the major components that influenced sales in the fourth quarter of 2010 compared to the same period in 2009:

- same-store sales declined 1.6%;
- sales in food declined marginally;
- sales in drugstore declined moderately, impacted by deflation due to regulatory changes in Ontario and the impact of generic versions of certain prescription drugs;
- sales growth in apparel was moderate while sales of other general merchandise declined significantly due to lower discretionary consumer spending and reductions in assortment and square footage;
- gas bar sales growth was strong as a result of higher retail gas prices and moderate volume growth;
- Loblaw's average quarterly internal retail food price index was flat. This compared to average quarterly internal retail food price deflation in the same period in 2009. Average quarterly national food price inflation was 1.5% as measured by CPI. CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores; and
- during the fourth quarter of 2010, six corporate and franchised stores were opened and one corporate store was closed, resulting in a net increase of 0.1 million square feet or 0.3%.

Operating income increased by $12 million to $287 million in the fourth quarter of 2010 compared to $275 million in the same period in 2009. Operating margin was 4.0% for the fourth quarter of 2010 compared to 3.8% in the same period in 2009.

Gross profit increased by $46 million to $1,774 million in the fourth quarter of 2010 compared to $1,728 million in the same period in 2009. Gross profit as a percentage of sales was 24.8% in the fourth quarter of 2010 compared to 23.6% in the same period in 2009. This increase was primarily attributable to improved control label profitability, continued buying synergies and disciplined vendor management, the shift of pharmaceutical vendor rebates from selling and administrative expenses to gross profit, improved shrink and a stronger Canadian dollar. Increased transportation costs partially offset these improvements.

(1) See non-GAAP financial measures beginning on page 61.

Contributing to the increase in operating income was improved gross profit, as described above, partially offset by incremental costs of $27 million related to Loblaw's investment in information technology and supply chain, including incremental depreciation and amortization of $14 million, a charge of $7 million (2009 – $5 million) related to stock-based compensation net of equity forwards and a charge of $28 million (2009 – $27 million) for fixed asset impairments related to asset carrying values in excess of fair values for specific store locations.

EBITDA(1) increased $22 million, or 5.3%, to $440 million in the fourth quarter of 2010 compared to $418 million in the same period in 2009. EBITDA margin(1) increased in the fourth quarter of 2010 to 6.1% compared to 5.7% in the same period in 2009. The increases in EBITDA(1) and EBITDA margin(1) were primarily due to the increases in operating income and operating margin, as described above.

**Liquidity and Capital Resources**

***Cash flows from operating activities of continuing operations***

The Company's fourth quarter 2010 cash flows from operating activities of continuing operations were $641 million compared to $638 million in the same period in 2009. The increase when compared to the same period in 2009 was primarily due to the increase in net earnings from continuing operations before non-cash items and the settlement of equity forwards in the fourth quarter of 2009, partially offset by the change in non-cash working capital.

***Cash flows used in investing activities of continuing operations***

The Company's fourth quarter 2010 cash flows used in investing activities of continuing operations were $500 million compared to $717 million in the same period in 2009. The decrease when compared to the same period in 2009 was primarily due to the decrease in outflows relating to short term investments and credit card receivables, after securitization. Also impacting fourth quarter 2010 cash flows used in investing activities of continuing operations was $121 million net cash consideration in connection with business acquisitions by Weston Foods. During the fourth quarter of 2009, a distribution centre that was sold in 2007 was acquired by Loblaw for approximately $140 million including the assumption of a mortgage for $96 million. Capital expenditures for the fourth quarter of 2010 were approximately $463 million (2009 – $467 million).

***Cash flows from (used in) financing activities of continuing operations***

The Company's fourth quarter 2010 cash flows from financing activities of continuing operations were $9 million compared to cash flows used in financing activities of continuing operations of $14 million in the same period in 2009. The change when compared to the same period in 2009 was primarily due to Loblaw's purchase of common shares in the fourth quarter of 2009.

## 10. DISCLOSURE CONTROLS AND PROCEDURES

Management is responsible for establishing and maintaining a system of disclosure controls and procedures to provide reasonable assurance that all material information relating to the Company and its subsidiaries is gathered and reported to senior management on a timely basis so that appropriate decisions can be made regarding public disclosure.

As required by National Instrument 52-109 (Certification of Disclosure in Issuers' Annual and Interim Filings), the Chairman and President and the Chief Financial Officer have caused to be evaluated under their supervision the effectiveness of such disclosure controls and procedures. Based on that evaluation, they have concluded that the design and operation of the system of disclosure controls and procedures were effective as at December 31, 2010.

## 11. INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is also responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

(1) See non-GAAP financial measures beginning on page 61.

As required by National Instrument 52-109 (Certification of Disclosure in Issuers' Annual and Interim Filings), the Chairman and President and the Chief Financial Officer have caused to be evaluated under their supervision the effectiveness of such internal controls over financial reporting using the framework established in "Internal Control – Integrated Framework (COSO Framework) published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)". Based on that evaluation, they have concluded that the design and operation of the Company's internal controls over financial reporting were effective as at December 31, 2010.

In designing and evaluating such controls, it should be recognized that due to inherent limitations, any controls, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and may not prevent or detect misstatements. Projections of any evaluations of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Additionally, management is required to use judgment in evaluating controls and procedures.

**Changes in Internal Control over Financial Reporting**
Management has also evaluated whether there were changes in the Company's internal controls over financial reporting that occurred during the period beginning on October 10, 2010 and ended on December 31, 2010 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Management has determined that no material changes occurred during this period.

During the first and third quarters of 2010, Loblaw successfully implemented the first and second phases of its ERP system. The implementation resulted in material changes in those periods to the internal controls over financial reporting for Loblaw's real estate and financial services divisions, corporate administration functions and the general ledger.

## 12. ENTERPRISE RISKS AND RISK MANAGEMENT

The Company is committed to establishing a framework that ensures risk management is an integral part of its activities. To ensure the continued growth and success of the Company, risks are identified and managed through GWL's and Loblaw's Enterprise Risk Management ("ERM") programs. The GWL and Loblaw Boards of Directors, respectively, have approved ERM policies and oversee the ERM programs through approval of risks and risk prioritization. The ERM programs assist all areas of the business in managing appropriate levels of risk tolerance by bringing a systematic approach, methodology and tools for evaluating, measuring and monitoring key risks. The results of the ERM programs and other business planning processes are used to identify emerging risks, prioritize risk management activities and develop risk-based internal audit plans.

Risk is not eliminated through the ERM programs. Risks are identified and managed within acceptable risk tolerances. The ERM programs are designed to:

- promote a cultural awareness of risk management and compliance within the Company;
- facilitate corporate governance by providing a consolidated view of risks across the Company and insight into the methodologies for identification, assessment, measurement and monitoring of the risks;
- assist in developing consistent risk management methodology and tools across the organization;
- ensure that resources are acquired economically, used efficiently and adequately protected; and
- allow the Company to focus on its key risks in the business planning process and optimize financial performance through responsible risk management.

Risk identification and assessments are important elements to the ERM framework. Annual ERM assessments are completed to assist in the update and identification of financial, operational or reputational risks and to effectively prioritize the risks. The annual ERM assessments are primarily carried out through interviews and risk assessments with senior management. Risks are assessed and evaluated based on vulnerability to the risk and the potential impact that the underlying risk would have on the ability to execute strategies and achieve objectives. Risks are assigned to appropriate risk owners and metrics are developed as appropriate for quarterly monitoring. Each quarter, management provides an update to the GWL or Loblaw Audit Committee of the status of the top risks based on significant changes from the prior quarter, anticipated impacts in future quarters and significant changes in key risk metrics. In addition, the long term (1-3 year) risk level is assessed in order to monitor potential long term impacts on the risk which may assist in risk mitigation planning activities.

The Internal Audit and Risk Management groups manage the ERM programs through the development of the risk framework and methodologies, completion of the annual ERM assessments, continuous monitoring of the key risks and quarterly reporting to the Audit Committees. The accountability for oversight of the management of each risk is allocated by the GWL or Loblaw Audit Committee to either the full Board or to a Committee of the Board. At least once a year, the relevant business owners update the applicable Committee or the full Board on their risk management activities over the course of the preceding year.

In the normal course of business, the Company is exposed to financial and market risks that have the potential to negatively affect its financial performance. The Company operates with policies and guidelines covering funding, investing, equity, commodity, foreign currency exchange and interest rate risk management. Policies and guidelines prohibit the use of any financial derivative instrument for speculative purposes.

The operating, financial and reputational risks and risk management strategies are discussed below. Any of these risks has the potential to negatively affect financial performance. The Company has risk management strategies including insurance programs, which are intended to mitigate the potential impact of these risks. Although these strategies are designed to minimize these risks, the strategies do not guarantee that the associated risks will be mitigated or not materialize or that events or circumstances will not occur which could negatively affect the Company's financial condition or performance.

## 12.1 OPERATING RISKS AND RISK MANAGEMENT

**Strategy Development and Execution**
The Company undertakes from time to time acquisitions and dispositions that meet its strategic objectives. As a result of recent dispositions, the Company holds significant cash and short term investments and is continuing to evaluate strategic opportunities for the use or deployment of these funds. The use or deployment of the funds and the execution of the Company's capital plans could pose a risk if they do not align with the Company's strategic objectives or if the Company experiences integration difficulties on the acquisition of any businesses. In addition, the Company may not be able to realize upon the synergies, business opportunities and growth prospects expected from any such investment opportunities or from the execution of the Company's strategies. Finally, any acquisition or divestiture activities may present unanticipated costs and managerial and operation risks, including the diversion of management's time and attention from day-to-day activities. If the Company's strategies are not effectively developed and executed, the financial performance of the Company could be adversely affected.

**ERP and Other Systems Implementations**
Information technology ("IT") systems have been assessed by Loblaw management as needing significant upgrading in certain areas in order to act as an enabler for the businesses. An IT strategic plan was developed to guide the new systems environment that Loblaw requires.

In 2010, Loblaw began to deploy its new ERP system. This project, along with other systems implementations planned for 2011 and beyond, is one of the largest technology infrastructure programs ever implemented by Loblaw and is fundamental to its long term growth strategies. The work will transform the systems used in virtually every area of Loblaw's business. Completing it will require continued focus and significant investment over the next two years. The failure to successfully migrate from legacy systems to the ERP could negatively affect Loblaw's reputation and operations, and the Company's revenues and financial performance. Failure or disruption in Loblaw's IT systems during the implementation of the ERP or other new systems may result in a lack of relevant and reliable information to enable management to effectively achieve its strategic plan or manage the day-to-day operations of the business, causing significant disruptions to business and potential financial losses to the

Company. In addition, the failure to implement appropriate processes to support the ERP system may result in inefficiencies and duplication in current processes.

Change management risk and other associated risks will arise from the various projects which will be undertaken to upgrade existing systems and introduce new systems. Failure by the Company to appropriately invest in IT or failure to implement IT infrastructure in a timely or effective manner may negatively impact the Company's financial performance.

**Information Integrity and Reliability**
To support the current and future requirements of the business the Company is reliant on IT systems. These systems are essential to provide management with the appropriate information for decision making, including its key performance indicators, and when necessary must be appropriately supported through systems upgrades to and maintenance of infrastructure.

Although Loblaw has the appropriate controls in place over the conversion of data, the process of converting data from legacy systems to the ERP and other new systems increases the risk of poor data integrity and reliability if the data are not accurate and complete upon conversion. In addition, for the next few years Loblaw will operate in new and old systems at the same time. Ensuring that the data is flowing accurately between all systems and ensuring the integrity of this data once it is converted will be critical to maintain the integrity and reliability of Loblaw's financial information. Ownership of data management is essential to ensure ongoing reliability and relevancy of the data. Any failure or disruption of these systems during Loblaw's data conversion process for the ERP could negatively affect the Company's reputation, its operations, revenues and financial performance. Lack of relevant, reliable and accessible information that enables management to effectively manage the business may preclude the Company from optimizing its overall performance.

**Change Management and Process Execution**
Significant initiatives in support of Loblaw's renewal plan are underway or planned. These initiatives include the execution of its IT strategic plan and its ongoing organizational changes. Success of these initiatives is dependent on management effectively realizing the intended benefits and effectively executing the related processes. To assist in the management of change throughout the organization, the Company has positioned teams to support its major change initiatives. Certain employees have been assigned and are dedicated to business change management activities with a focus on integration of the business process and systems changes through communication, training and other change events in support of major change initiatives within the Company.

Ineffective change management or inexperienced employees leading change management could result in disruptions to the operations of the business or affect the ability of the Company to implement and achieve its long term strategic objectives. This could result from a lack of clear accountabilities, communication, training or lack of requisite knowledge, which may cause employees to act in a manner which is inconsistent with Company objectives. Failure to properly execute the various processes may increase the risk of customer dissatisfaction, which in turn could adversely affect the reputation, operations and financial performance of the Company. The failure to properly integrate several large, complex initiatives in a timely manner will adversely impact the operations of the Company. If employees are not able to develop and perform new roles, processes and disciplines, the Company may not always achieve the expected cost savings and other benefits of its initiatives.

**Economic Environment**
Economic factors that impact consumer spending patterns could deteriorate or remain unpredictable due to global economic volatility. These factors include continued high levels of unemployment, household debt, changes in interest rates, changes in inflation, changes in foreign currency exchange rates and access to consumer credit. Management regularly monitors economic conditions and estimates their impact on the Company's operations and incorporates these estimates in short term operating and longer term strategic decisions. Despite these

activities, one or more of these factors could negatively affect the Company's sales and margins. Inflationary trends are unpredictable and changes in the rate of inflation or deflation will affect consumer prices, which in turn could have a negative impact on the results of the Company.

**Competitive Environment**
The Company operates in increasingly competitive North American food processing and retail markets. Consumer demands and preferences for food products change continually. These demands and preferences are impacted by changing demographic and economic trends such as changes in disposable income, ethnic diversity, health and environmental awareness and time availability. Customer satisfaction is central to the Company's business. Over the past several years, consumers have demanded more choice, value and convenience and healthier products. If the Company is ineffective in responding to or identifying new trends in consumer preferences and demands, its revenues and financial performance could be negatively impacted.

The Company reviews and monitors operating plans and results, including market share in its reportable operating segments. When necessary, the operating segments will modify their operating strategies, including but not limited to, relocating production facilities or stores, closing underperforming assets, relocating stores or reformatting them under a different banner, reviewing and adjusting pricing, product offerings, brand positioning and/or marketing programs to take into account competitive activity. A significant competitive advantage the Company has developed is its brands. Both operating segments focus on brand development and building upon their core brand equity. Weston Foods' premium and mainstream brands provide Weston Foods with strong core brands and product lines that enhance consumer loyalty, trusted as they are for quality, great taste and freshness. Loblaw's control label program represents a competitive advantage because it enhances customer loyalty by offering superior value and provides some protection against national brand pricing strategies.

As cost pressures remain in the food processing industry and the competitive sales environment, Weston Foods anticipates that industry restructurings are likely. Although the outcome and the impact, if any, on the Company's consolidated financial results from this anticipated restructuring are uncertain, Weston Foods will closely monitor developments in the food processing industry and food retail market and, if required, adjust its strategies and programs as necessary.

Loblaw's competitors include traditional supermarket operators, as well as mass merchandisers, warehouse clubs, drugstores, limited assortment stores, discount stores, convenience stores and specialty stores. Many of these competitors now offer a selection of food, drugstore and general merchandise. Others remain focused on supermarket-type merchandise.

The Company is also subject to competitive pressures from new entrants into the marketplace and from the expansion or renovation of existing competitors, particularly those expanding into the grocery market. Some of these competitors have extensive resources that allow them to compete vigorously in the market. Several of these competitors operate in a non-union environment. The Company's unionized workforce environment may reduce the ability of the Company to compete on labour costs or may adversely impact the Company's ability to react to the competition in a timely manner. Increased competition and pressures on growth and pricing could adversely affect the Company's ability to achieve its objectives. The Company's inability to effectively predict market activity or compete effectively with its current or future competitors could result in, among other things, reduced market share and lower pricing in response to its competitors' pricing activities.

**Food Safety and Public Health**
The Company is subject to risks associated with food safety and general merchandise product defects. These risks may arise as part of the manufacturing, procurement, storage, distribution, preparation and display of products and, with respect to the Company's control label or branded products and contract manufactured products, in relation to the production, packaging and design of products. A majority of the Company's sales are generated from food products and thus the Company could be vulnerable in the event of a significant outbreak

of food-borne illness or other public health concerns related to food products. The occurrence of such events or incidents could result in negative publicity, damage to the Company's brands and potentially lead to legal claims. In addition, failure to trace or locate any contaminated or defective products and ingredients may affect the Company's ability to be effective in a recall situation. Any of these events could negatively impact the Company's revenues and financial performance.

In addition, failure to maintain the cleanliness and health standards at Loblaw's store level, including pest control, may negatively impact Loblaw's revenues and reputation.

Incident management processes are in place to manage such events, should they occur. The programs identify risks, provide clear procedures for communication to employees and consumers and are aimed at ensuring that potentially harmful products are expeditiously removed from inventory and are not available for sale. The Company also has extensive food safety procedures and training programs which address safe food handling and preparation standards. The Company endeavours to employ current best practices for the manufacturing, procurement, storage, distribution and preparation and display of food products. Also, it actively supports customer awareness of safe food handling and healthy choices. The Company places special focus on applying safety and quality management systems to ensure Weston Foods' products and Loblaw's control label products meet all food safety and regulatory requirements. The ability of these programs and procedures to address such events is dependent on their successful execution. The existence of these procedures does not mean that the Company will in all circumstances be able to mitigate the underlying risks and any event related to these matters has the potential to adversely affect the Company's reputation and its financial performance.

**Distribution and Supply Chain**
The need to invest in and improve the Company's supply chain may adversely affect the Company's capacity to effectively and efficiently attract and retain current and potential customers. A significant restructuring of Loblaw's supply chain will continue for the next eighteen months. Although this initiative is expected to result in improved service levels and product availability for Loblaw's stores, the scale of the change and the implementation of new processes could cause disruption in the flow of goods to stores, which would negatively affect the Company's revenues and financial performance. In addition, the integration of new supply chain systems with Loblaw's ERP could cause disruptions to the network if not properly executed which would also negatively affect the Company's revenues and financial performance.

**Employee Retention and Succession Planning**
The degree to which the Company is not effective in establishing appropriate succession planning processes and retention strategies could lead to a lack of requisite knowledge, skills and experience on the part of management. This, in turn, could affect the Company's ability to execute its strategies, efficiently run its operations and meet its goals for financial performance. Effective succession planning for senior management and employee retention are essential to sustaining the growth and success of the Company. In addition, loss of talent to the competition can be a significant risk to the Company's business strategy. Effective retention strategies will be necessary due to the significant changes, potential increase in workload and marketability of those employees who have developed specialized skills during the implementation of Loblaw's ERP and other significant initiatives in the Company.

Loblaw has implemented new programs throughout 2010 to assist in employee retention, succession planning and development. These will continue into 2011. The initiatives are focused on improving employee engagement and succession plans as well as supporting Loblaw's goal to "Be a Great Place to Work". Should these initiatives not be successful, Loblaw may not be able to execute its strategies or efficiently run its operations which in turn could negatively affect the Company's financial performance.

**Merchandising**
Loblaw's merchandising process may create inventory that customers don't want or need, is not reflective of current trends in customer tastes, habits, or regional preferences, is priced at a level customers are not willing to

pay, is late in reaching the market or does not have optimal commercial product placement on store shelves. Innovation is critical in order to respond to customer demands and to stay competitive in the marketplace. In addition, the Company's operations as they relate to food, sales volumes and product mix are impacted to some degree by certain holiday periods in the year. In 2010, Loblaw's active trading initiative was rolled out which included a focus on the merchandising group strategy, structure, roles and process improvements, to assist in installing best practices and efficiencies throughout the merchandising organization. If Loblaw is not successful with these initiatives, or if merchandising efforts are not effective or responsive to customer demand, the Company's revenues and financial performance could be negatively impacted.

**Labour Relations**

A significant portion of the Company's workforce is unionized. Renegotiating collective agreements may result in work stoppages or slowdowns, delays to construction projects and increases in costs. Any of these could negatively affect the Company's financial performance. The Company successfully negotiated 69 collective agreements in 2010 and the Company continues to negotiate the 88 remaining collective agreements carried over from prior years. In 2011, 59 collective agreements affecting approximately 16,000 employees expire with the largest of the agreements covering approximately 11,000 employees in Ontario expiring in June 2011. Although the Company attempts to mitigate work stoppages and disputes through early negotiations, work stoppages or slowdowns and the resulting negative effects on the Company's revenues and financial performance are possible.

**Disaster Recovery and Business Continuity**

The Company's ability to continue critical operations and processes could be negatively impacted by a weather disaster, work stoppage, prolonged IT failure, terrorist activity, power failures, border closures, a pandemic or other national or international catastrophe. The Company has a business continuity program which is being continually matured. However, ineffective contingency planning could result in reputational and/or financial losses to the Company. There can be no assurance that the existence of the program will ensure that the Company responds appropriately in the event of business interruptions, crises or potential disasters and negative impacts on revenue and financial performance could occur.

**Inventory Management**

Inappropriate inventory management may lead to excess inventory or a shortage of inventory which may impact customer satisfaction and overall financial performance. Loblaw may experience excess inventory that cannot be sold profitably or which could increase levels of inventory shrink which in turn could negatively impact the Company's financial performance. Loblaw focuses on reducing inventory levels and early identification of inventory at risk. New information systems are being implemented that are expected to improve demand forecasting. In order to reduce the amount of excess inventory, Loblaw monitors the impact of customer trends. Despite these efforts, Loblaw may experience excess inventory that cannot be sold profitably, which may negatively impact the Company's financial performance.

**Commodity Prices**

Weston Foods costs are directly impacted by fluctuations in the prices of commodity-linked raw materials such as wheat flours, sugars, vegetable oils, cocoa powders and chocolate. Loblaw is also exposed to commodity prices as a result of the direct link between commodities and the cost of consumer products. In addition, both Weston Foods and Loblaw are exposed to increases in the prices of electricity, natural gas and fuel in operating, in the case of Weston Foods, its bakeries and distribution centres, and, in the case of Loblaw, its stores and distribution centres. Both Weston Foods and Loblaw use purchase commitments and financial and non-financial derivative instruments in the form of futures contracts, option contracts and forward contracts to manage their current and anticipated exposure to fluctuations in commodity prices. Despite these strategies, high commodity prices could negatively impact the Company's financial performance.

**Privacy and Information Security**

The Company is subject to various laws regarding the protection of personal information of its customers and employees and has adopted a Privacy Code setting out guidelines for the handling of personal information. Any failure of the Company to comply with these laws could result in damage to its reputation and negatively affect financial performance. The Company's information systems contain personal information of customers and employees. Any failures or vulnerabilities in these security systems or non-compliance with information security standards, including those in relation to personal information belonging to the Company's customers and employees, could result in harm to the reputation of the Company and negatively affect financial performance.

Information security risks will also arise in the implementation of Loblaw's IT strategic plan. The strategic plan includes the upgrading of information security systems to adhere to information security standards by instituting more stringent security system protocols and corporate information security policies. A failure in Loblaw's information systems or non-compliance with information security standards, including those in relation to personal information belonging to Loblaw's customers and employees, could result in harm to the reputation or competitive position of Loblaw and could negatively affect the Company's financial performance.

**Tax and Regulatory**

Changes to any of the laws, rules, regulations or policies related to the Company's business including income, commodity and other taxes, and the production, processing, preparation, distribution, packaging and labelling of its products could have an adverse impact on the Company's financial and operational performance. New accounting pronouncements introduced by appropriate authoritative bodies may also impact the Company's financial results including the Company's transition to International Financial Reporting Standards. In the course of complying with such changes, the Company may incur significant costs. Changing regulations or enhanced enforcement of existing regulations could restrict its operations or profitability and thereby threaten the Company's competitive position and its capacity to efficiently conduct business. Failure by the Company to comply with applicable laws, rules, regulations and policies may subject it to civil or regulatory actions or proceedings, including fines, assessments, injunctions, recalls or seizures, which in turn could have an adverse effect on the Company's financial results. PC Bank operates in a highly regulated environment. Failure by PC Bank to comply with, understand, acknowledge and effectively respond to the regulators could result in monetary penalties, regulatory intervention and reputational damage. Taxing authorities may also disagree with the positions and conclusions taken by the Company in its filings with such authorities. An unfavourable resolution to any such dispute could have an adverse effect on the Company's financial results.

In 2010, the provincial governments of Quebec, Ontario, Alberta, Nova Scotia and British Columbia introduced amendments to the regulation of generic prescription drug prices paid by provincial governments pursuant to their respective public drug benefit plans. Under these amendments, manufacturer costs of generic drugs paid by the provincial drug plans are being reduced, and in Ontario, the current system of drug manufacturers paying professional allowances to pharmacies will be eliminated. The amendments also reduce the manufacturer costs of generic drugs purchased out-of-pocket or through private employer drug plans. Loblaw continues to identify opportunities to mitigate the impact of these amendments, including the introduction of programs to add new services and enhance existing services to attract customers. The amendments could have a material impact on the financial results of the Company if Loblaw is not able to effectively mitigate their negative impact.

**Vendor Management and Third-Party Service Providers**

Certain aspects of the Company's business rely on third-party providers of goods and services. Although contractual arrangements are put in place with these suppliers, the Company has no direct influence over how the companies are managed. Negative events affecting the suppliers could in turn negatively impact the Company's reputation, operations and its financial performance. Inefficient, ineffective or incomplete vendor management strategies, policies and/or procedures may impact the Company's ability to optimize financial performance, meet customer needs and control costs and quality.

Vendor production capacity or IT capabilities may limit the Company's ability to service its customers or implement new processes to increase efficiencies and consistencies across vendors. Sourcing from developing markets results in enhanced risk which requires mitigation through additional safety, quality and management reviews.

Certain of Weston Foods' products and Loblaw's control label products are manufactured under contract by third-party suppliers. Product development and sourcing of Loblaw's control brand apparel products is conducted by a third party. In order to preserve brand equity, these suppliers are held to high standards of quality. Ineffective selection, contract terms, management and reliance on third-party service providers may impact the Company's ability to source Weston Foods' third-party manufactured products and Loblaw control brand products, to have products available for customers, to market to customers and to operate efficiently and effectively on a day to day basis.

The Company also uses third-party logistic services including the operation of dedicated warehouse and distribution facilities and third-party common carriers. The Company maintains a strategy of multiple sources for logistics providers so that in the event of a disruption of service from one supplier another supplier can be used. However, disruption in these services is possible, which could interrupt the flow of goods thereby negatively affecting sales.

The Company continues to implement practices and performance expectations with its supplier base, including asking suppliers to support sales plans and cost reduction initiatives and to align with major program changes. However, failure to effectively implement these programs will have a negative impact on the Company's ability to realize the expected benefits and could negatively impact revenues and financial performance.

*President's Choice Financial* banking services are provided by a major Canadian chartered bank. PC Bank uses third-party service providers to process credit card transactions, operate call centres and operationalize certain risk management strategies for the *President's Choice Financial* MasterCard®. To minimize operating risk, PC Bank and Loblaw actively manage and monitor their relationships with all third-party service providers. In addition, PC Bank has developed an outsourcing risk policy, approved by its Board of Directors, and has established a vendor governance team that provides its Board of Directors with regular reports on vendor governance and annual vendor risk assessments. Despite these activities, a significant disruption in the services provided by the bank would negatively impact revenues and the financial performance of the Company.

The Company relies on third parties for investment management, custody and other services for its cash equivalents, short term investments, security deposits and pension assets. Any disruption in the services provided by these suppliers could affect the return on these assets or liquidity of the Company.

**Workplace Health and Safety**
The failure of the Company to adhere to appropriate health and safety procedures and to ensure compliance with applicable laws and regulations could have an adverse effect on the organization's operations and financial performance.

The Company has established a national health and safety policy, a national health and safety management system and an injury reduction plan. Periodic updates are provided by health and safety employees to the executive team and quarterly updates are made to the Environmental, Health and Safety Committee of the Board. Loblaw has also developed a 3 year plan to establish a corporate wellness program. These initiatives cannot, however, prevent all workplace incidents. It remains possible that any such incident or series of incidents could have a negative impact on the Company's reputation, operations and financial performance.

**Environmental**
The Company maintains a large portfolio of real estate and infrastructure and is subject to environmental risks associated with the contamination of such properties and facilities, whether by previous owners or occupants, neighbouring properties or from its own operations.

The Company operates a number of underground storage tanks, the majority of which are used for the retailing of automotive fuel. Contamination resulting from leaks from these tanks is possible. The Company employs monitoring and testing regimens, in addition to risk assessments and audits, to minimize the potential for subsurface impacts from fuel losses. Loblaw also operates refrigerant equipment in its stores and distribution centres to preserve perishable products through the supply chain. These systems contain refrigerant gases which could be released if the related equipment fails. It is possible that a release of these gases could have adverse affects on the environment. To minimize the potential for refrigerant releases, the Company has implemented preventative maintenance programs and refrigeration system inspections and is considering the implementation of new refrigeration system technologies.

In recent years, provincial, municipal and other government bodies have introduced legislation that imposes liabilities on retailers, brand owners and importers for costs associated with recycling and disposal of consumer goods packaging and printed materials distributed to consumers. This is a growing trend and the Company expects to be subject to increased costs associated with these laws.

The Company has environmental programs and has established policies and procedures aimed at ensuring compliance with applicable environmental legislative requirements. To this end, the Company employs environmental risk assessments and audits using internal and external resources together with employee awareness programs throughout its operating locations. The Environmental, Health and Safety Committee of the Board receives regular reporting from management addressing current and potential future issues, risks, programs/initiatives, identifying new regulatory concerns and related communication efforts. The Company's Environmental Affairs department works closely with the operations to help ensure requirements are met.

Despite these mitigation activities, the Company could be subject to increased or unexpected costs associated with environmental incidents and the related remediation activities, including litigation and regulatory related costs, all of which could negatively impact the Company's reputation and financial performance.

Recent consumer trends include an increasing demand for products with less impact on the environment and that the Company's operations demonstrate environmentally responsible practices. As set out in its annual Corporate Social Responsibility report, Loblaw sets environmental goals and monitors its progress towards their achievement. Should the Company fail to meet consumer demand in this area or otherwise face adverse publicity with respect to the environmental impact of its business practices, its reputation may be negatively affected which may lead to decreased revenues and a negative impact on financial performance.

**Franchise and Independent Business Relationships**
A significant portion of the Company's revenues and earnings arise from franchisee type relationships. Franchisees and independent operators are independent businesses and, as such, their operations may be negatively affected by factors beyond the Company's control, which in turn may damage the Company's reputation and potentially affect revenues and financial performance. Revenues and earnings could also be negatively affected, and Loblaw's reputation could be harmed, if a significant number of retail franchisees were to experience operational failures, including health and safety exposures, financial difficulty, or were unwilling or unable to pay Loblaw for products, rent or other fees, or fail to enter into renewals of franchise agreements. Loblaw's franchise system is also subject to franchise legislation enacted by a number of provinces. Any new legislation or failure to comply with existing legislation may negatively affect operations and could add administrative costs and burdens, any of which could affect the Company's relationship with its franchisees and independent operators. These relationships could pose significant risks if they are disrupted which could result in legal action, reputational damage and/or adverse financial consequences. Supply chain or system changes by the Company could cause or be perceived to cause disruptions to franchise operations and could result in negative effects on franchisee revenues or earnings. Reputational damage or adverse consequences for the Company, including litigation and disruption to sales from franchised stores, could result.

### Contract Management and Records Retention

The Company's contract management and records management processes are being upgraded. A lack of effective processes for the tendering, drafting, review and approval of Company contracts and the appropriate level of management and legal involvement increases the risk of financial losses to the business. In addition, inefficient, ineffective or incomplete document management and retention policies, procedures and practices increase the risk of incomplete Company records and potential non-compliance with laws and regulations, which could negatively impact the Company's reputation and financial performance.

### Trademark and Brand Protection

Decrease in value of the Company's trademarks, banners or control brands, as a result of adverse events, changes to the branding strategies or otherwise, could weaken the demand for the Company's products or services or damage the Company's reputation. The Company endeavours to have the appropriate contractual protections in Loblaw's arrangements with control label vendors and suppliers of all marketing elements including printing, flyers and advertising agencies, and Weston Foods' arrangements with contract manufacturers, distributors and customers. The Company actively monitors and manages its trademark portfolio. Despite these activities, adverse events could impact the value of the Company's trademarks, banners or brands and may negatively affect revenues and financial performance.

### Employee Future Benefit Contributions

The Company manages the assets in its defined benefit pension plans by engaging professional investment managers who operate under prescribed investment policies and procedures in respect of permitted investments and asset allocations. The future contributions to the Company's pension plans are impacted by a number of variables, including the investment performance of the plan assets and the discount rate used to value the liabilities of the plans. The Company regularly monitors and assesses plan performance and the impact of changes in participant demographics, changes in capital markets and other economic factors that may impact funding requirements, employee future benefit costs and actuarial assumptions. If capital market returns are below assumed levels, or if the discount rate drops, the Company may be required to make contributions to its funded defined benefit pension plans in excess of those currently contemplated, which in turn may have a negative effect on the Company's financial performance and cash flows.

### Multi-Employer Pension Plans

In addition to the Company-sponsored pension plans, the Company participates in various multi-employer pension plans, providing pension benefits to union employees pursuant to provisions of collective bargaining agreements. Approximately 39% (2009 – 39%) of employees of the Company and of its independent franchisees participate in these plans. The administration of these plans and the investment of their assets are controlled by boards of independent trustees generally consisting of an equal number of union and employer representatives. In some circumstances, the Company may have a representative on the board of trustees of these multi-employer pension plans. The Company's responsibility to make contributions to these plans is limited by the amounts established pursuant to its collective agreements; however, poor performance of these plans could have an adverse impact on the Company's employees and former employees who are members of these plans. Pension cost for these plans is recognized as contributions are due.

Loblaw is the largest participating employer in the Canadian Commercial Workers Industry Pension Plan ("CCWIPP"), with approximately 54,000 (2009 – 55,000) employees as members. In 2010, Loblaw contributed $55 million (2009 – $54 million) to CCWIPP. At the end of 2010, the CCWIPP actuarial accrued benefit obligations exceeded the value of the assets held in trust. As a result of this underfunding, CCWIPP received approval from the pension regulator to reduce the accrued benefits and future service benefits of certain participants. Further benefit reductions would negatively affect the retirement benefits of Loblaw's employees, which in turn could negatively affect their morale and performance.

### Real Estate and Store Renovations

Loblaw maintains a significant portfolio of owned retail real estate and, whenever practical, pursues a strategy of purchasing sites for future store locations. This enhances Loblaw's operating flexibility by enabling Loblaw to introduce new departments and services that could be precluded under third-party operating leases. As part of its ongoing review of the performance of its stores, Loblaw from time to time undertakes store renovations. Efforts are made to minimize the duration of these projects in order to limit the disruption at store level. However, the Company's revenues and financial performance will be negatively impacted if such renovations and remodelling are carried out in a manner that is disruptive to Loblaw's ongoing store operations or results in a poor customer experience.

### Ethical Business Conduct

The Company has adopted a Code of Business Conduct which colleagues and directors of the Company are required to acknowledge on a regular basis. The Company has in place an Ethics and Business Conduct Committee which monitors compliance with the Code of Business Conduct and determines how the Company can best ensure it is conducting its business in an ethical manner. The Company encourages reporting of unethical conduct and has established a toll-free anonymous response line, which can be used by employees to report suspected accounting, internal control or auditing irregularities and unethical behaviour impacting the Company. Loblaw has also adopted a Vendor Code of Conduct which outlines its ethical expectations to its vendor community in a number of areas, including social responsibility. Any failure of the Company or its vendors to adhere to ethical business conduct policies could significantly affect the Company's reputation and brands and could, therefore, negatively impact the Company's financial performance.

### Holding Company Structure

GWL is a holding company. As such, it does not carry on business directly but does so through its subsidiaries. It has no major source of operating income or assets of its own, other than the interests it has in its subsidiaries, which are all separate legal entities. GWL is therefore financially dependent on dividends and other distributions it receives from its subsidiaries.

## 12.2 FINANCIAL RISKS AND RISK MANAGEMENT

### Foreign Currency Exchange Rate

The Company's consolidated financial statements are expressed in Canadian dollars, however a portion of the Company's (excluding Loblaw's) net assets are denominated in U.S. dollars through both its net investment in self-sustaining foreign operations in the United States, and its net investment in integrated foreign subsidiaries through Dunedin and certain of its affiliates. The U.S. dollar denominated net assets are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. As a result, the Company is exposed to foreign currency translation gains and losses. Those gains and losses arising from the translation of the U.S. dollar denominated assets of integrated foreign subsidiaries are included in operating income, while for the self-sustaining operations in the United States, foreign currency translation gains and losses are recorded in accumulated other comprehensive loss. In addition, revenues and expenses of these integrated and self-sustaining foreign operations are translated into Canadian dollars at the foreign currency exchange rates that approximate the rates in effect at the dates when such items are recognized. An appreciating Canadian dollar relative to the U.S. dollar will negatively impact year-over-year changes in reported sales, operating income and net earnings, while a depreciating Canadian dollar relative to the U.S. dollar will have the opposite impact.

Loblaw is exposed to foreign currency exchange rate variability, primarily on U.S. dollar denominated cash and cash equivalents, short term investments, security deposits held by Glenhuron, foreign denominated and foreign currency based purchases in accounts payable and accrued liabilities, and U.S. dollar private placement notes included in long term debt. Loblaw and Glenhuron have cross currency swaps and foreign exchange forward contracts that partially offset their respective exposure to fluctuations in foreign currency exchange rates. Cross currency swaps are transactions in which interest payments and principal amounts in one currency are exchanged against the receipt of interest payments and principal amounts in a second currency.

Despite these mitigation strategies the Company's financial performance could be negatively impacted by foreign currency variability.

**Credit**

The Company is exposed to credit risk resulting from the possibility that counterparties may default on their financial obligations. Exposure to credit risk relates to derivative instruments, cash and cash equivalents, short term investments, security deposits, pension assets held in the Company's defined benefit plans**,** PC Bank's credit card receivables and other receivables from Weston Foods' customers and Loblaw's independent franchisees, associated stores and independent accounts.

The Company may be exposed to losses if a counterparty to the Company's financial or non-financial derivative agreements fails to fulfill its obligations. Potential counterparty risk and losses are limited to the net amounts recoverable under such derivative agreements with any specific counterparty. These risks are further reduced by entering into derivative agreements with counterparties that have at minimum a long term "A" credit rating from a recognized credit rating agency and by placing risk adjusted limits on exposure to any single counterparty for financial derivative agreements. Internal policies, controls and reporting processes, which require ongoing assessment and corrective action, if necessary, are in place with respect to derivative transactions.

Credit risk associated with cash equivalents, short term investments and security deposits results from the possibility that a counterparty may default on the repayment of a security. Efforts to mitigate credit risk include policies and guidelines that require issuers of permissible investments to have at minimum a long term "A" credit rating from a recognized credit rating agency and that specify minimum and maximum exposures to specific industries, issuers and types of investment instruments. These investments are purchased and held directly in custody accounts and have limited exposure to third-party money market portfolios and funds.

Credit risk associated with investments in the Company's defined benefit pension plans is described in the Employee Future Benefits Contributions discussion in Section 12.1, "Operating Risks and Risk Management", of this MD&A.

Credit risk from PC Bank's credit card receivables, receivables from Weston Foods' customers and Loblaw's independent franchisees, associated stores and independent accounts results from the possibility that customers may default on their payment obligations. PC Bank manages the credit card receivable risk by employing stringent credit scoring techniques, actively monitoring the credit card portfolio, and reviewing techniques and technology that can improve the effectiveness of the collection process. In addition, these receivables are dispersed among a large, diversified group of credit card customers.

Receivables from Weston Foods' customers and suppliers and Loblaw's independent franchisees, associated stores and independent accounts are actively monitored and counterparties are assessed for credit risk on an ongoing basis.

Despite the mitigation strategies described above, it is possible that the Company's financial performance could be negatively impacted by the failure of a counterparty to fulfill its obligations, whether as a result of loss of value of receivables or increased costs associated with counterparty default.

**Interest Rate**

Interest rate risk arises from the issuance of short term debt and equity derivatives, net of cash and cash equivalents, short term investments and security deposits. The Company is exposed to changes in short term interest rates which are offset partly by Glenhuron's and Loblaw's interest rate swaps. Interest rate swaps are transactions in which interest flows are exchanged with a counterparty on a specified notional amount for a pre-determined period based on agreed-upon fixed and floating interest rates. Despite these interest rate swaps, changes in interest rates could negatively affect the Company's cash flows and financial performance.

**Common Share Market Price**

GWL and Loblaw issue stock-based compensation to certain of their employees in the form of stock options and Restricted Share Units ("RSUs") based on their respective underlying common shares. Consequently, operating results are negatively impacted when the common share prices increase and positively impacted when the share prices decline. The equity derivatives provide a partial offset to fluctuations in stock-based compensation cost. The equity derivatives allow for settlement in cash, common shares or net settlement. These derivatives change in value as the market prices of the respective underlying common shares change and provide a partial offset to fluctuations in stock-based compensation costs, including RSU plan expense. The partial offset between stock-based compensation costs, including RSU plan expense, and the equity derivatives is more effective when the market price of the respective underlying common shares exceeds the exercise price of the employee stock options. When the market price of the respective underlying common shares is lower than the exercise price of the employee stock options, these equity derivatives provide a partial offset only to the RSU plan expense. The amount of net stock-based compensation cost recorded in operating income is mainly dependent upon the number of unexercised stock options and RSUs, their vesting schedules relative to the number of respective underlying common shares on the equity derivatives, and the level of fluctuations in the market price of the respective underlying common shares.

Changes in the Loblaw common share price impact the Company's interest and other financing charges. In 2001, Weston Holdings Limited ("WHL") entered into an equity forward sale agreement based on 9.6 million Loblaw common shares at an original forward price of $48.50 per Loblaw common share which, under the terms of the agreement, had increased to a forward price of $84.09 (2009 – $80.28) per Loblaw common share as at December 31, 2010. The forward matures in 2031 and will be settled in cash as follows: WHL will receive the forward price and will pay the market value of the underlying Loblaw common shares at maturity. The obligation of WHL under this forward is secured by the underlying Loblaw common shares. WHL recognizes a non-cash charge or income, which is included in consolidated interest expense and other financing charges, representing the fair value adjustment of WHL's forward sale agreement for 9.6 million shares. The fair value adjustment in the forward contract is a non-cash item resulting from fluctuations in the market price of the underlying Loblaw shares that WHL owns. WHL does not record any change in the market price associated with the Loblaw shares it owns. At maturity, if the forward price is greater than the market price, WHL will receive a cash amount equal to the difference. If the forward price is less than the market price, WHL will pay a cash amount equal to the difference. Any cash paid under the forward contract could be offset by the sale of Loblaw shares.

**Liquidity and Capital Availability**

Liquidity risk is the risk that the Company cannot meet a demand for cash or fund its obligations as they come due. Liquidity risk also includes the risk of not being able to liquidate assets in a timely manner at a reasonable price. Insufficient access to capital would impair the Company's capacity to grow, execute its business model and generate financial returns.

The Company mitigates liquidity and capital availability risks by maintaining appropriate levels of cash and cash equivalents and short term investments, committed lines of credit as required, actively monitoring market conditions and by diversifying its sources of funding and maturity profile of its debt and capital obligations.

Should Loblaw's or PC Bank's financial performance and condition deteriorate or downgrades in Loblaw's current credit ratings occur, Loblaw's or PC Bank's ability to obtain funding from external sources may be restricted. In addition, credit and capital markets are subject to inherent risks that may negatively affect Loblaw's access and ability to fund its financial and other liabilities.

Should GWL's financial performance and condition deteriorate or downgrades in GWL's current credit ratings occur, GWL's ability to obtain funding from external sources may be restricted. In addition, credit and capital markets are subject to inherent risks that may negatively affect GWL's access and ability to fund its financial and other liabilities.

### Derivative Instruments

Over-the-counter derivative instruments offset certain risks. Policies and guidelines prohibit the use of any derivative instrument for trading or speculative purposes. See notes 1 and 26 to the consolidated financial statements for additional information about the Company's financial derivative instruments. The fair value of derivative instruments is subject to changing market conditions which could negatively impact the Company's cash flows and financial performance.

## 13. RELATED PARTY TRANSACTIONS

The Company's majority shareholder, Wittington Investments, Limited ("Wittington"), and its affiliates are related parties. The Company, in the normal course of business, has routine transactions with these related parties, including the rental of office space at market prices from Wittington. In 2010, rental payments amounted to approximately $3 million (2009 – $3 million). It is the Company's policy to conduct all transactions and settle balances with related parties on market terms and conditions.

From time to time, the Company, Wittington and its affiliates may enter into agreements to make elections that are permitted or required under applicable income tax legislation with respect to affiliated corporations. These elections and accompanying agreements did not have a material impact on the Company in 2010.

## 14. CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts and disclosures made in the consolidated financial statements and accompanying notes. Management continually evaluates the estimates and assumptions it uses. These estimates and assumptions are based on management's historical experience, best knowledge of current events and conditions and activities that the Company may undertake in the future. Actual results could differ from these estimates.

The estimates and assumptions described in this section depend upon subjective or complex judgments about matters that may be uncertain and changes in these estimates and assumptions could materially impact the consolidated financial statements.

### Inventories

The Company's inventories are stated at the lower of cost and estimated net realizable value. For its retail store inventories, Loblaw is required to make estimations or judgments in the determination of (i) discount factors used to convert inventory to cost after a physical count at retail has been completed and (ii) estimated inventory losses, or shrinkage, occurring between the last physical inventory count and the balance sheet date.

Inventories counted at retail are converted to cost by applying a discount factor to retail selling prices. This discount factor is determined at the category level, is calculated in relation to historical gross margins and is reviewed on a regular basis for reasonableness. Inventory shrinkage, which is calculated as a percentage of sales, is evaluated throughout the year and provides for estimated inventory shortages from the last physical count to the balance sheet date. To the extent that actual losses experienced vary from those estimated, both inventories and operating income will be impacted. Changes or differences in these estimates may result in changes to inventories on the consolidated balance sheet and a charge or credit to operating income in the consolidated statement of earnings.

Additional information on inventories is provided in note 12 to the consolidated financial statements.

### Fixed Assets

Fixed assets are reviewed for impairment annually and when events or circumstances indicate that their carrying value exceeds the sum of the undiscounted future cash flows expected from their use and eventual disposition. An impairment loss is measured as the amount by which the fixed assets carrying value exceeds the fair value. As discussed in note 13 to the consolidated financial statements, Loblaw recorded a fixed asset impairment charge of $28 million (2009 – $27 million) and other related charges of $18 million (2009 – $19 million) in 2010.

In addition, Loblaw recorded in operating income an asset impairment charge of $26 million (2009 – nil) related to the closure of a distribution centre in Quebec. Weston Foods recorded a fixed asset impairment charge of $1 million (2009 – $1 million) and accelerated depreciation of nil (2009 – $2 million).

The factor that most significantly influences the impairment assessments is the determination of future cash flows. Loblaw uses its internal plans in estimating future cash flows. These plans reflect Loblaw's current best estimate of future cash flows but may change due to uncertain competitive and economic market conditions or changes in business strategies. Changes or differences in these estimates may result in changes to fixed assets on the consolidated balance sheet and a charge to operating income on the consolidated statement of earnings.

**Employee Future Benefits**

The cost and accrued benefit plan obligations of the Company's defined benefit pension plans and other benefit plans are accrued based on actuarial valuations which are dependent on assumptions determined by management. These assumptions include the discount rate, the expected long term rate of return on plan assets, the expected growth rate of health care costs, the rate of compensation increase, retirement rates, termination rates and mortality rates. These assumptions are reviewed annually by management and the Company's actuaries.

The discount rate, the expected long term rate of return on plan assets and the expected growth rate in health care costs are the three most significant assumptions.

The discount rates are based on market interest rates, as at the Company's measurement date of September 30 on a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the accrued benefit plan obligations. The discount rates used to determine the 2010 net cost for defined benefit pension and other benefit plans were 5.7% and 5.5%, respectively, on a weighted average basis, compared to 6.0% and 5.9%, respectively, in 2009.

The expected long term rate of return on plan assets is based on current market conditions, the asset mix, the active management of defined benefit pension plan assets and historical returns. The 2010 expected long term rate of return on plan assets was 6.75% in Canada and 6.50% in the United States.

The expected growth rate in health care costs for 2010 was based on external data and the Company's historical trends for health care costs. In 2011, the growth rate of health care costs in Canada is estimated at 8.0% and is assumed to gradually decrease to 5.0% by 2015, remaining at that level thereafter. The growth rate of health care costs in the United States is estimated at 8.5% and is assumed to gradually decrease to 5.0% by 2019, remaining at that level thereafter.

Since the three key assumptions discussed above are forward-looking and long term in nature, they are subject to uncertainty and actual results may differ materially. In accordance with Canadian GAAP, differences between actual results and the assumptions, as well as the impact of changes in the assumptions, are accumulated as unamortized net actuarial gains or losses and amortized over future periods, affecting the recognized cost of defined benefit pension plans and other benefit plans and the accrued benefit plan obligation in future periods. Although the Company believes that its assumptions are appropriate, differences in actual results or changes in the Company's assumptions may materially affect its defined benefit pension plans and other benefit plans accrued benefit plan obligations and future costs.

Additional information regarding the Company's pension and other benefit plans, including a sensitivity analysis for changes in key assumptions, is provided in note 16 to the consolidated financial statements and in the Employee Future Benefit Contributions discussion in Section 12.1, "Operating Risks and Risk Management", of this MD&A.

### Goodwill and Intangible Assets

Goodwill is assessed for impairment at the reporting unit level at least annually. Any potential goodwill impairment is identified by comparing the fair value of a reporting unit to its carrying value. If the carrying value of the reporting unit exceeds its fair value, a more detailed goodwill impairment assessment must be undertaken. A goodwill impairment charge is recognized in operating income to the extent that, at the reporting unit level, the carrying value of goodwill exceeds the implied fair value.

The Company determines the fair value of its reporting units using a discounted cash flow model corroborated by other valuation techniques such as market multiples. The process of determining these fair values requires management to make estimates and assumptions of a long term nature regarding projected future sales, earnings and capital investment, discount rates and terminal growth rates. Projected future sales, earnings and capital investment are consistent with strategic plans presented to GWL's and Loblaw's Boards. Discount rates are based on an industry weighted average cost of capital. These estimates and assumptions may change in the future due to uncertain competitive and economic market conditions and changes in business strategies.

During the fourth quarter of 2010, the Company performed its annual goodwill impairment test and determined that the fair value of each of the reporting units exceeded its respective carrying value and therefore no goodwill impairment was identified.

During 2009, subsequent to the disposition of its U.S. fresh bakery business on January 21, 2009, Weston Foods reorganized its remaining operations. The reorganization changed the composition of Weston Foods' reporting units for the purpose of goodwill impairment testing. As a result of this change, the goodwill related to the biscuits, cookies, cones and wafers business was determined to be impaired and a write-down of $73 million was recorded in the first quarter of 2009.

Intangible assets with an indefinite useful life are not subject to amortization and are tested at least annually for impairment. Any potential intangible asset impairment is identified by comparing the fair value of the indefinite life intangible asset to its carrying value. If the carrying value of the intangible asset exceeds its fair value, impairment is identified as the difference between the fair value and the carrying value and will result in the recognition of a non-cash impairment charge in operating income.

The Company determines the fair value of its trademarks and brand names by using the "Relief from Royalty" method, a discounted cash flow model. Weston Foods determines the fair values of its customer relationships by using an income approach, specifically the "Excess Earnings" method, a discounted cash flow model. The process of determining the fair values requires management to make assumptions of a long term nature regarding projected future sales, terminal growth rates, royalty rates and discount rates. Projected future sales are consistent with strategic plans presented to GWL's and Loblaw's Boards and discount rates are based on an industry after-tax cost of equity. Intangible assets with a finite life are amortized over their estimated useful lives, ranging from 10 to 30 years. These estimates and assumptions may change in the future due to uncertain competitive and economic market conditions or changes in business strategies.

During the fourth quarter of 2010, the Company performed the annual impairment test of its indefinite life intangible assets and determined that there was no impairment of the carrying value of indefinite life intangible assets.

### Income and Other Taxes

Future income tax assets and liabilities are recognized for the future income tax consequences attributable to temporary differences between the financial statement carrying values of assets and liabilities and their respective income tax bases. Future income tax assets or liabilities are measured using enacted or substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The calculation of current and future income taxes requires management to make estimates and assumptions and to exercise judgment regarding the financial statement carrying values of assets and liabilities which are subject to accounting estimates inherent in those balances, the interpretation of income tax legislation across various jurisdictions, expectations about future operating results, the timing of reversal of temporary differences and possible audits of income tax filings by the tax authorities. Management believes it has adequately provided for income taxes based on currently available information.

At each balance sheet date, future income tax assets are reviewed to determine whether a valuation allowance is required. Such an allowance is not required when it is deemed more likely than not that projected future taxable income will be sufficient to realize the future income tax benefits.

Changes or differences in the underlying estimates or assumptions may result in changes to the current or future income tax balances on the consolidated balance sheet, a charge or credit to income tax expense in the consolidated statement of earnings and may result in cash payments or receipts.

All income, capital and commodity tax filings are subject to audits and reassessments. Management believes that adequate provisions have been made for all income and other tax obligations. However, changes in interpretations or judgments may result in a change in the Company's income, capital or commodity tax provisions in the future. The amount of such a change cannot be reasonably estimated.

## 15. ACCOUNTING STANDARDS IMPLEMENTED IN 2009

### Goodwill and Intangible Assets

In November 2007, the Canadian Institute of Chartered Accountants ("CICA") issued amendments to Section 1000, "Financial Statement Concepts" and AcG 11, "Enterprises in the Development Stage", issued a new Section 3064, "Goodwill and Intangible Assets" ("Section 3064") to replace Section 3062, "Goodwill and Other Intangible Assets", withdrew Section 3450, "Research and Development Costs" and amended EIC Abstract 27, "Revenues and Expenditures During the Pre-operating Period" to not apply to entities that have adopted Section 3064. These amendments, in conjunction with Section 3064, provide guidance for the recognition of intangible assets, including internally developed assets from research and development activities, ensuring consistent treatment of all intangible assets, whether separately acquired or internally developed. The Company implemented these requirements as of January 1, 2009, retroactively with restatement.

### Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

On January 20, 2009, the Emerging Issues Committee ("EIC") issued Abstract 173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities". The committee reached a consensus that a company's credit risk and the credit risk of its counterparties should be considered when determining the fair value of its financial assets and financial liabilities, including derivative instruments. The transitional provisions required the abstract to be applied retrospectively without restatement of prior periods. Financial assets and financial liabilities, including derivative instruments, were remeasured as at January 1, 2009 to take into account the appropriate Company's credit risk and counterparty credit risk. As a result, a decrease in other assets of $12 million, a decrease in other liabilities of $4 million, a decrease in minority interest of $3 million, an increase net of income taxes and minority interest in accumulated other comprehensive loss of $1 million and a decrease in retained earnings net of income taxes and minority interest of $4 million were recorded on the consolidated balance sheet.

### Financial Instruments – Disclosures

In June 2009, the CICA amended Section 3862, "Financial Instruments – Disclosures" to include additional disclosure relating to the measurement of fair value for financial instruments and liquidity risk. The amendment establishes a three level hierarchy that reflects the significance of the inputs used in fair value measurements on financial instruments. The amendment was implemented by the Company in 2009 (see note 27 to the consolidated financial statements). The implementation of these amendments did not have an impact on the Company's results of operations or financial condition.

## 16. INTERNATIONAL FINANCIAL REPORTING STANDARDS

The Canadian Accounting Standards Board requires that all public companies adopt International Financial Reporting Standards ("IFRS") for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. As a result, the Company's audited annual consolidated financial statements for the year ending December 31, 2011 will be the first audited annual consolidated financial statements that will be prepared in accordance with the requirements of IFRS. Starting in the first quarter of 2011 the unaudited interim period consolidated financial statements will be prepared in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting", including 2010 comparative figures and required reconciliations prepared in accordance with IFRS 1, "First-Time Adoption of International Financial Reporting Standards" ("IFRS 1").

### Project Structure and Status

The Company has an IFRS team led by the Chief Financial Officer to ensure the timely and appropriate implementation of IFRS. The IFRS team consists of dedicated resources as well as consultants and other employees on an as needed basis. This team reports regularly to a steering committee comprised of senior management, as well as to the Audit Committee.

The Company's IFRS conversion project plan consists of three main phases:

**Phase One: Diagnostic Impact Assessment** This phase consisted of a high-level impact assessment that identified the key areas of accounting differences between Canadian GAAP and IFRS that were likely to impact the Company. The diagnostic impact assessment was completed in 2008 and resulted in the ranking of accounting differences as high, medium, or low priority.

**Phase Two: Detailed Assessment** This phase involved a comprehensive assessment of the differences between IFRS and the Company's current accounting policies and included reviews with the various finance groups and business process owners to further understand the impact of these differences. The detailed assessment was completed in April 2009 at which time the changes required to existing accounting policies, business process and information systems were identified.

**Phase Three: Implementation** This phase includes two components: implementation development and implementation transition and resulted in the compilation of IFRS transitional adjustments, as required, as well as IFRS financial statements for 2010 with required reconciliations to Canadian GAAP. To achieve this result the changes identified in the detailed assessment phase were implemented as discussed below.

***Policy Selection*** The analysis of policy alternatives under IFRS, including certain exemptions and elections available on transition in accordance with IFRS 1, was completed in 2010. Management has preliminarily concluded on all of its policy alternatives, and obtained preliminary audit committee approval of these choices. These preliminary conclusions and approvals will be finalized prior to the end of the first quarter of 2011.

***Business Processes*** Changes to business processes, including the budgeting and planning process, arising as a result of IFRS were also identified in the detailed assessment phase. Certain immaterial changes were taken into account in the budgeting and planning cycle that occurred throughout 2010. All other required business process changes were also implemented by the end of 2010.

***Information Systems*** Changes to supporting information systems were identified in the detailed assessment phase. Required changes to supporting information systems were designed, developed and implemented by the end of 2010. The IFRS conversion project is integrated with Loblaw's ERP implementation. As ERP phases have been deployed, Loblaw has ensured that the requirements of IFRS adoption were incorporated. For ERP phases that have not yet been deployed, Loblaw is ensuring that the requirements of IFRS are identified and incorporated.

***Financial Statement Presentation*** In accordance with the Company's transition plan, the Company also completed its preliminary first quarter 2011 IFRS financial statement format and draft note disclosures. In addition, the Company has completed its preliminary unaudited opening transitional balance sheet as well as financial statements for each of the quarters of 2010 based on the preliminary elections and exemptions as discussed below. A summary of the significant impacts is provided below.

***Training*** Targeted training regarding anticipated changes resulting from IFRS implementation was provided to appropriate business units and finance colleagues throughout 2010 and will continue as appropriate into 2011. In addition, the Company provided quarterly and supplementary IFRS information sessions to the Board which included updates on certain preliminary transitional and 2010 quarterly IFRS adjustments including preliminary policy choices, implications of IFRS standards to the business, and their impacts on financial statement disclosures. As previously announced, the Company will provide an information session on March 3, 2011 to key external stakeholders regarding the impacts of IFRS.

***Contractual Arrangements and Covenants*** The implementation of IFRS is expected to have an impact on certain financial metrics that are used in calculating Loblaw's financial covenants under certain of its debt agreements. These debt agreements provide for the opportunity to renegotiate the covenants to reflect the impact of the transition to IFRS. Loblaw has reached an understanding with certain of its lenders to defer any adjustments that may be required to its borrowing agreements until such later date that the parties may agree following the adoption of IFRS. Loblaw will continue to demonstrate compliance with its borrowing agreements on a basis that is consistent with Canadian GAAP as it exists immediately prior to the conversion to IFRS, until such time that the parties agree to formalize the adjustments for IFRS.

***Internal Control Compliance*** Changes to the Company's internal controls over financial reporting and disclosure controls and procedures, which include enhancement of existing controls and the design and implementation of new controls, where needed, are in process and progressing to plan. At this time the Company expects no material change in internal controls over financial reporting or disclosure controls and procedures resulting from the adoption and implementation of IFRS.

**Preliminary Estimated Impact of Conversion**

The information below is provided to allow investors and others to obtain an understanding of the preliminary unaudited effects on the Company's consolidated financial statements and operating performance measures. The changes described below should not be regarded as a complete description of the changes resulting from the transition to IFRS. Readers are cautioned that it may not be appropriate to use such information for any other purpose and the information is subject to change.

The International Accounting Standards Board has significant ongoing projects that could change the current standards under IFRS and their impact on the Company's consolidated financial statements. Therefore, the Company's analysis of changes and accounting policy decisions have been made based on the accounting standards that are currently in effect. To date, the Company has made preliminary decisions relating to certain IFRS policies as discussed below. The following information is contingent on the standards that will be effective as at December 31, 2011, the date of the Company's first audited annual consolidated financial statements prepared in accordance with IFRS.

The table below summarizes the estimated impact of conversion to IFRS on the Company's key financial highlights from the unaudited (except where otherwise noted) consolidated statements of earnings for each of the interim periods and year ended December 31, 2010, based on the preliminary elections and exemptions noted below:

| | First Quarter | | Second Quarter | | Third Quarter | | Fourth Quarter | | 2010 | |
|---|---|---|---|---|---|---|---|---|---|---|
| ($ millions, except where otherwise indicated) | Canadian GAAP | IFRS | Canadian GAAP | IFRS | Canadian GAAP | IFRS | Canadian GAAP | IFRS | Canadian GAAP (audited) | IFRS |
| Revenue | $ 7,177 | $ 7,165 | $ 7,530 | $ 7,480 | $ 9,884 | $ 9,827 | $ 7,417 | $ 7,366 | $ 32,008 | $ 31,838 |
| Operating income | $ 274 | $ 304 | $ 389 | $ 397 | $ 490 | $ 493 | $ 330 | $ 322 | $ 1,483 | $ 1,516 |
| Net earnings attributable to shareholders of the Company | $ 42 | $ 41 | $ 125 | $ 123 | $ 184 | $ 176 | $ 101 | $ 86 | $ 452 | $ 426 |
| Basic net earnings per common share ($) | $ 0.25 | $ 0.24 | $ 0.89 | $ 0.88 | $ 1.32 | $ 1.25 | $ 0.70 | $ 0.59 | $ 3.16 | $ 2.96 |
| Diluted net earnings per common share ($) | $ 0.25 | $ 0.17 | $ 0.89 | $ 0.84 | $ 1.31 | $ 1.18 | $ 0.70 | $ 0.52 | $ 3.14 | $ 2.74 |
| EBITDA | $ 438 | $ 458 | $ 550 | $ 549 | $ 707 | $ 704 | $ 497 | $ 488 | $ 2,192 | $ 2,199 |
| EBITDA margin | 6.1% | 6.4% | 7.3% | 7.3% | 7.2% | 7.2% | 6.7% | 6.6% | 6.8% | 6.9% |

The table below reconciles EBITDA to the unaudited IFRS net earnings attributable to shareholders of the Company for each of the interim periods and year ended December 31, 2010, based on the preliminary elections and exemptions noted below:

| ($ millions) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | 2010 |
|---|---|---|---|---|---|
| Net earnings attributable to shareholders of the Company | $ 41 | $ 123 | $ 176 | $ 86 | $ 426 |
| Add impact of the following: | | | | | |
| Non-controlling interest | 51 | 66 | 72 | 48 | 237 |
| Income taxes | 68 | 92 | 118 | 99 | 377 |
| Net interest expense and other financing charges | 144 | 116 | 127 | 89 | 476 |
| Operating income | $ 304 | $ 397 | $ 493 | $ 322 | $ 1,516 |
| Depreciation and amortization | 154 | 152 | 211 | 166 | 683 |
| EBITDA | $ 458 | $ 549 | $ 704 | $ 488 | $ 2,199 |

In addition, the table below summarizes the estimated impact of conversion to IFRS on the Company's unaudited opening transitional balance sheet as at January 1, 2010 and as at December 31, 2010, based on the preliminary elections and exemptions noted below:

| | Jan. 1, 2010 | | | Dec. 31, 2010 | | |
|---|---|---|---|---|---|---|
| ($ millions) | Canadian GAAP (audited) | IFRS (unaudited) | % Change | Canadian GAAP (audited) | IFRS (unaudited) | % Change |
| Total assets | $ 20,143 | $ 21,158 | 5.0% | $ 20,854 | $ 21,661 | 3.9% |
| Total liabilities | $ 13,201 | $ 13,171 | (0.2)% | $ 14,722 | $ 14,416 | (2.1)% |
| Total equity(1) | $ 6,942 | $ 7,987 | 15.1% | $ 6,132 | $ 7,245 | 18.2% |

(1) Includes non-controlling interest of $2,379 million as at January 1, 2010 and $2,596 million as at December 31, 2010, which was presented in total liabilities under Canadian GAAP.

## First-Time Adoption of IFRS

The adoption of IFRS will require the application of IFRS 1, which provides guidance for an entity's initial adoption of IFRS. IFRS 1 generally requires retrospective application of all IFRS standards, with the exception of certain mandatory exceptions and limited optional exemptions provided in the standard. The following are the significant optional exemptions that the Company expects to apply in preparing the opening transitional balance sheet in accordance with IFRS 1.

***Employee Benefits*** The Company expects to apply the election to recognize, for all defined benefit plans, all cumulative unamortized actuarial gains and losses, which are currently deferred under Canadian GAAP, through opening retained earnings. The Company will apply this exemption to all defined benefit plans consistently and the expected impact has been quantified by the Company's external actuaries. The expected impact of IAS 19, "Employee Benefits" ("IAS 19"), including this IFRS 1 exemption is disclosed in the Changes in Accounting Policies – Employee Benefits section below.

***Borrowing Costs*** The Company expects to apply IAS 23, "Borrowing Costs", prospectively and expects to eliminate all previously capitalized interest costs as at the date of transition through opening retained earnings. Upon implementation of IFRS, the Company expects to record a decrease in total assets and liabilities of approximately $220 million and $21 million, respectively, with a corresponding impact to opening retained earnings of $125 million and minority interest of $74 million. Minority interest is referred to as "non-controlling interest" under IFRS and is presented within total equity.

***Foreign Currency*** The Company expects to apply the election whereby cumulative translation gains or losses in accumulated other comprehensive loss are deemed to be zero at the date of transition to IFRS. Upon implementation of IFRS, the Company expects to reclassify the cumulative translation loss of $103 million recorded in accumulated other comprehensive loss at December 31, 2009 to opening retained earnings. Cumulative translation gains and losses will be recognized prospectively from the date of transition.

***Business Combinations*** The Company expects to apply IFRS 3, "Business Combinations" prospectively only to those business combinations that occur after the date of transition.

## Changes in Accounting Policies

***Consolidation*** IAS 27, "Consolidated and Separate Financial Statements" and Standing Interpretations Committee Interpretation 12, "Consolidation – Special Purpose Entities" ("IAS 27") assess consolidation based on the control model and IFRS does not include the concept of a variable interest entity. Accordingly, Loblaw will no longer be required to consolidate certain independent franchisees and other entities subject to warehouse and distribution service agreements that were previously consolidated under Canadian GAAP pursuant to the requirements of Accounting Guideline 15, "Consolidation of Variable Interest Entities" ("AcG 15"). The independent funding trust through which franchisees obtain financing and Eagle, the independent credit card trust that finances certain PC Bank credit card receivables, will be subject to consolidation under IFRS based on the indicators of control as assessed in accordance with Standing Interpretations Committee Interpretation 12. As a result of the above, Loblaw will be required to remeasure the initial consideration received from the independent franchisee, in the form of a loan receivable, to exclude the benefit of the credit enhancement provided to the independent funding trust by Loblaw. Upon implementation of IFRS, the Company expects to record an increase in total assets and liabilities of approximately $719 million and $739 million, respectively, with a corresponding impact to opening retained earnings of $7 million and non-controlling interest of $27 million, primarily resulting from the items described above. In addition, upon implementation the Company expects to record additional total assets and liabilities of $39 million and $117 million, respectively, with a corresponding impact to opening retained earnings of $49 million and non-controlling interest of $29 million related to immaterial adjustments of prior period balances. The Company has determined that these amounts were not material to its consolidated financial statements for any prior interim or annual periods.

***Revenue*** Under Canadian GAAP each franchise arrangement was evaluated under AcG 15. Revenues for independent franchisees that were not consolidated under AcG 15 were accounted for under AcG 2 "Franchise Fee Revenue". As a result of Loblaw no longer consolidating certain independent franchisees, Loblaw was required to evaluate the sale of each franchise arrangement under IAS 18, "Revenue" ("IAS 18") at its inception. Based on the guidance in IAS 18, Loblaw concluded that each franchise arrangement contains separately identifiable components. As a result of this multi-element arrangement, Loblaw will be required to determine the fair value of all consideration exchanged including certain loans and receivables. The impact of applying these requirements will result in the fair value of certain consideration being less than the amounts recorded at inception. Furthermore, Loblaw allocated the consideration to each component in the multi-element arrangement, on a relative fair value basis to both the delivered and undelivered components. The total impact of these items is included within the overall financial instruments impacts described below.

***Financial Instruments*** As a result of no longer consolidating the franchise arrangements under IAS 27, Loblaw will recognize and evaluate additional financial assets and financial liabilities in accordance with IAS 39, "Financial Instruments: Recognition and Measurement" ("IAS 39") which requires application retrospectively to the inception of each arrangement. Loblaw's evaluation has identified one or more events that provide objective evidence that the cash flows associated with certain of these financial assets are such that the fair value has been determined to be impaired. Upon implementation of IFRS, the Company expects to record a decrease in certain financial assets and a corresponding decrease to total equity.

IAS 39 contains different criteria than Canadian GAAP for the derecognition of financial assets and requires an evaluation of the extent to which an entity retains the risks and rewards of ownership as well as control over the transferred assets. Under Canadian GAAP these financial assets qualify for sale treatment. The Company has determined that under IFRS, securitized credit card receivables will not qualify for derecognition. Upon implementation of IFRS, the Company expects to record an increase in credit card receivables of approximately $1,179 million, excluding Eagle of $500 million which is discussed above, before the provision for loan losses with a corresponding increase to liabilities.

Cross currency and interest rate swaps were effective cash flow hedging relationships under Canadian GAAP. Certain tranches of the swaps that were part of the hedging relationship have expired in 2010 and will continue to expire up to mid-2011. Loblaw has decided not to apply hedge accounting under IFRS which will result in derecognition at the date of transition to IFRS. Upon implementation of IFRS, the Company expects to reclassify approximately $10 million of deferred gains net of allocation of non-controlling interest, from accumulated other comprehensive income to retained earnings within total equity.

As a result of IAS 39 and IAS 18, the Company expects to record an increase in total assets and liabilities of approximately $958 million and $1,290 million, respectively, with a corresponding impact to opening retained earnings of $198 million, accumulated other comprehensive loss of $10 million and non-controlling interest of $124 million, primarily resulting from the items described in IAS 18 and IAS 39 above.

***Employee Benefits*** IAS 19 provides a policy choice regarding recognition of actuarial gains and losses for defined benefit pension plans and other defined benefit plans, permitting deferred recognition using the corridor method or immediate recognition in either other comprehensive income within equity or through earnings. Under Canadian GAAP the Company applies the corridor method. Upon implementation of IFRS, the Company intends to recognize actuarial gains and losses immediately in other comprehensive income within equity for defined benefit pension plans and other defined benefit plans and immediately in net earnings for other long term employee benefits. Upon implementation of IFRS, the Company expects to record a decrease in total assets and an increase in total liabilities of approximately $266 million and $81 million, respectively, with a corresponding impact to opening retained earnings of $247 million and non-controlling interest of $100 million, primarily resulting from the items described above and the IFRS 1 exemption described in the First-Time Adoption of IFRS section above. In addition, upon implementation the Company expects to record additional total assets and liabilities of $14 million and $56 million, respectively, with a corresponding impact to opening retained earnings of $28 million and non-controlling interest of $14 million, related to immaterial adjustments of prior period balances. The Company has determined that these amounts were not material to its consolidated financial statements for any prior interim or annual periods.

***Share-based Payments*** IFRS 2, "Share-Based Payments", requires that cash-settled stock-based compensation be measured based on the fair value of the awards. Canadian GAAP requires that such compensation be measured based on the intrinsic value of the awards. This difference is expected to impact the accounting measurement of the Company's stock options, restricted share units and deferred share units. Upon implementation of IFRS, the Company expects to record an increase in total assets and liabilities of approximately $5 million and $15 million, respectively, with a corresponding impact to opening retained earnings of $8 million and non-controlling interest of $2 million, primarily resulting from the items described above.

***Property, Plant and Equipment*** IAS 16, "Property, Plant and Equipment", provides specific guidance such that when an individual component of an item within property, plant and equipment is replaced and capitalized, the carrying value of the replaced component of the original asset must be derecognized even if the replacement part was not separately accounted for. In addition IFRS is more prescriptive with respect to eligible costs such as site-dismantling and restoration costs. Upon implementation of IFRS, the Company expects to record a decrease in total assets and liabilities of approximately $74 million and $3 million, respectively, with a corresponding impact to opening retained earnings of $49 million and non-controlling interest of $22 million, primarily resulting from the items described above.

***Impairment of Assets*** IAS 36, "Impairment of Assets", requires that assets be tested for impairment at the level of cash generating units ("CGU"), which are defined as the smallest group of assets that generate largely independent cash inflows. The Company has completed its analysis and has concluded that the CGU for Weston Foods will be at a lower level than under Canadian GAAP but will continue to be the major production categories and geographic regions where cash inflows are largely depending on each other. For Loblaw, the CGU will predominantly be an individual retail location compared to Canadian GAAP where store net cash flows are grouped together by primary market areas, where they are largely dependent on each other. The Company has completed its preliminary assessment of the events triggering potential impairments and the events triggering the reversal of previously recorded impairments. Upon implementation of IFRS, the Company expects to record a decrease in total assets and liabilities of approximately $216 million and $29 million, respectively, with a corresponding impact to opening retained earnings of $117 million and non-controlling interest of $70 million, primarily resulting from the items described above.

***Leases*** IAS 17, "Leases" ("IAS 17") requires the allocation of minimum lease payments between the land and building elements of a lease to be in proportion to the relative fair values of the leasehold interests in the land and building, whereas under Canadian GAAP it is based on the fair value of the land and building in aggregate. In addition, IFRS permits the immediate recognition of gains and losses on sale leaseback transactions which result in an operating lease, provided that the transaction is established at fair value. Under Canadian GAAP, gains and losses are generally deferred and amortized in proportion to the lease payments over the lease term. IAS 17 also provides additional indicators of a capital lease that were not provided under Canadian GAAP. Capital leases are referred to as finance leases under IFRS. Upon implementation of IFRS, the Company expects to record an increase in total assets and liabilities of approximately $62 million and $70 million, respectively, with a corresponding impact to opening retained earnings of $2 million and non-controlling interest of $6 million, primarily resulting from the items described above. In addition, upon implementation the Company expects to record additional total assets and liabilities of $50 million and $61 million, respectively, with a corresponding impact to opening retained earnings of $7 million and non-controlling interest of $4 million, related to immaterial unrecorded capital leases from prior periods. The Company has determined that these immaterial unrecorded amounts were not material to its consolidated financial statements for any prior interim or annual periods.

***Customer Loyalty Programs*** International Financial Reporting Interpretations Committee 13, "Customer Loyalty Programs", requires the fair value of loyalty programs to be recognized as a separate component of the related sales transaction, such that a portion of the revenue from the initial sales transaction in which the awards were granted is deferred until the points are redeemed. Loblaw has made a policy choice to defer the relevant portion of the sales transaction based on the relative fair value of the awards granted. Under Canadian GAAP, Loblaw recognizes the net cost of the program in operating expenses measured at the cost to service the liability. Upon implementation of IFRS, the Company expects to record an increase in total assets and liabilities of approximately $5 million and $19 million, respectively, with a corresponding impact to opening retained earnings of $9 million and non-controlling interest of $5 million, primarily resulting from the items described above.

***Provisions*** IAS 37, "Provision, Contingent Liabilities and Contingent Assets" requires an entity to recognize a provision when a contract is determined to be onerous. A contract is onerous when the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. Canadian GAAP only requires the recognition of such a liability in certain prescribed situations. This difference could result in the recognition of a liability under IFRS that was not previously recognized under Canadian GAAP. Other measurement differences under IFRS could result in the earlier recognition of provisions or the recognition of a different amount than under Canadian GAAP. Upon implementation of IFRS, the Company expects to record an increase in total assets and liabilities of approximately $3 million and $19 million, respectively, with a corresponding impact to opening retained earnings of $9 million and non-controlling interest of $7 million, primarily resulting from the items described above.

**Changes in Financial Statement Presentation and Cash Flows**
In addition to the changes in recognition and measurement described above, the conversion to IFRS will result in a number of changes to financial statement presentation. On the consolidated balance sheets, the significant required reclassifications from Canadian GAAP to IFRS include: presenting all future income taxes as long term, rather than presenting current and long term future income taxes separately; presenting investment properties separately from fixed assets; presenting current and long term provisions separately from accounts payable and accrued liabilities and other liabilities, respectively; and presenting non-controlling interest as a component of equity instead of as a liability.

On the statement of earnings, non-controlling interests will be presented as an allocation of net earnings rather than as a deduction in the calculation of net earnings. In addition, the Company has made a policy choice under IAS 19 to disaggregate pension and post retirement benefit costs on the statement of net earnings, and present the interest and expected return on asset components within interest and other financing charges. This change related to pension costs will have the effect of increasing operating income and EBITDA[(1)] and increasing interest and other financing charges reported under Canadian GAAP in 2010.

The impact of IFRS on total consolidated cash flows is due only to the change in entities that Loblaw will recognize on-balance sheet under IFRS as compared to Canadian GAAP, as discussed above related to IAS 39 and IAS 27. In addition, within the consolidated statements of cash flows, there will be differences in the presentation of cash flows between operating, investing and financing.

(1) See non-GAAP financial measures beginning on page 61.

## 17. OUTLOOK[1]

The consolidated results of George Weston Limited will continue to reflect the performance of both the Weston Foods and Loblaw operating businesses. In addition, the Company's results will be subject to earnings volatility caused by the impact of changes in U.S. foreign currency exchange rates on a portion of the Company's U.S. dollar denominated cash and short term investments. Earnings volatility may also result from other non-operating factors including commodity prices and their impact on the Company's commodity derivatives, the Loblaw common share price and its impact on the forward sale agreement for 9.6 Loblaw common shares and short term interest rates.

In 2011, Weston Foods expects continued progress in operating performance driven by sales growth in existing businesses, the full year impact of the 2010 bakery acquisitions and ongoing efforts to reduce costs through improved efficiencies and productivity. This outlook is tempered by the impact of rapidly rising commodity costs and escalating energy costs. While Weston Foods is planning to increase prices to absorb these cost increases, operating margins could be constrained in 2011 as the timing of price increases may lag cost increases.

Loblaw is entering its fifth and final year of renewal and expects to continue its focus on executing the renewal plan in a market environment that remains unpredictable and competitively intense. Loblaw plans to increase its investments in information technology and supply chain which will negatively impact operating income in 2011.

George Weston Limited continues to assess opportunities for the deployment of its significant holdings of cash and short term investments.

## 18. NON-GAAP FINANCIAL MEASURES

The Company uses the following non-GAAP financial measures: EBITDA and EBITDA margin, net debt, net debt to EBITDA, net debt to equity and return on average net assets. The Company believes these non-GAAP financial measures provide useful information to both management and investors in measuring the financial performance and financial condition of the Company for the reasons outlined below. These measures do not have a standardized meaning prescribed by Canadian GAAP and therefore they may not be comparable to similarly titled measures presented by other publicly traded companies, and they should not be construed as an alternative to other financial measures determined in accordance with Canadian GAAP.

(1) This outlook should be read in conjunction with the Forward-Looking Statements section of this MD&A on page 5.

**EBITDA and EBITDA margin**

The following tables reconcile earnings from continuing operations before minority interest, income taxes, interest expense and other financing charges, gain on disposal of business and depreciation and amortization ("EBITDA") to Canadian GAAP net earnings from continuing operations reported in the consolidated statements of earnings for the quarters and years ended as indicated. For each of its reportable operating segments, segment EBITDA is reconciled to segment operating income.

EBITDA margin is calculated as EBITDA divided by sales.

EBITDA is useful to management in assessing the performance of the Company's ongoing operations and its ability to generate cash flows to fund its cash requirements, including the Company's capital investment program.

| | Quarter Ended Dec. 31, 2010 | | | | Year Ended Dec. 31, 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| ($ millions) | Weston Foods | Loblaw | Other[2] | Consolidated | Weston Foods | Loblaw | Other[2] | Consolidated |
| Net earnings from continuing operations | | | | $ 101 | | | | $ 452 |
| Add impact of the following: | | | | | | | | |
| Minority interest | | | | 61 | | | | 273 |
| Income taxes | | | | 101 | | | | 370 |
| Interest expense and other financing charges | | | | 67 | | | | 388 |
| Operating income (loss) | $ 55 | $ 287 | $ (12) | $ 330 | $ 278 | $ 1,261 | $ (56) | $ 1,483 |
| Depreciation and amortization[1] | 14 | 153 | | 167 | 54 | 655 | | 709 |
| EBITDA | $ 69 | $ 440 | $ (12) | $ 497 | $ 332 | $ 1,916 | $ (56) | $ 2,192 |

(1) Includes depreciation of $11 million and $43 million for the quarter and the year, respectively, presented in cost of inventories sold.

(2) Operating income for the quarter and the year includes a loss of $12 million and $56 million, respectively, related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates, which are integrated foreign subsidiaries for accounting purposes.

| ($ millions) | Quarter Ended Dec. 31, 2009 Weston Foods | Loblaw | Other(2) | Consolidated | Year Ended Dec. 31, 2009 Weston Foods | Loblaw | Other(2) | Consolidated |
|---|---|---|---|---|---|---|---|---|
| Net earnings from continuing operations | | | | $ 79 | | | | $ 127 |
| Add impact of the following: | | | | | | | | |
| Minority interest | | | | 70 | | | | 260 |
| Income taxes | | | | 39 | | | | 259 |
| Interest expense and other financing charges | | | | 99 | | | | 363 |
| Operating income (loss) | $ 58 | $ 275 | $ (46) | $ 287 | $ 123 | $ 1,197 | $ (311) | $ 1,009 |
| Depreciation and amortization(1) | 12 | 143 | | 155 | 56 | 589 | | 645 |
| EBITDA | $ 70 | $ 418 | $ (46) | $ 442 | $ 179 | $ 1,786 | $ (311) | $ 1,654 |

(1) Includes depreciation of $10 million and $44 million for the quarter and the year, respectively, presented in cost of inventories sold.

(2) Operating income for the quarter and the year includes a gain of $6 million and a loss of $225 million, respectively, related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates, which are integrated foreign subsidiaries for accounting purposes. Operating income for the quarter and the year also includes a loss of $52 million and $86 million, respectively, related to the reversal of cumulative foreign currency translation losses.

| ($ millions) | Year Ended Dec. 31, 2008 Weston Foods | Loblaw | Consolidated |
|---|---|---|---|
| Net earnings from continuing operations | | | $ 647 |
| Add impact of the following: | | | |
| Minority interest | | | 222 |
| Income taxes | | | 304 |
| Interest expense and other financing charges | | | 360 |
| Gain on disposal of business | | | (335) |
| Operating income | $ 154 | $ 1,044 | $ 1,198 |
| Depreciation and amortization(1) | 60 | 550 | 610 |
| EBITDA | $ 214 | $ 1,594 | $ 1,808 |

(1) Includes depreciation of $44 million presented in cost of inventories sold.

### Net Debt

The following table reconciles net debt used in the net debt to EBITDA and net debt to equity ratios to Canadian GAAP measures reported as at the years ended as indicated.

The Company calculates net debt as the sum of bank indebtedness, short term debt, long term debt, certain other liabilities and the fair value of the related financial derivatives less cash and cash equivalents, short term investments, security deposits and the fair value of the related financial derivatives.

The Company believes this measure is useful in assessing the amount of financial leverage employed.

| ($ millions) | **Dec. 31, 2010** | Dec. 31, 2009 | Dec. 31, 2008 |
|---|---|---|---|
| Bank indebtedness | **$ 4** | $ 2 | $ 93 |
| Short term debt | **336** | 300 | 453 |
| Long term debt due within one year | **733** | 343 | 415 |
| Long term debt | **5,129** | 5,377 | 5,308 |
| Certain other liabilities | **35** | 36 | |
| Fair value of financial derivatives related to the above | **(352)** | (327) | (261) |
| | **5,885** | 5,731 | 6,008 |
| Less: Cash and cash equivalents | **1,528** | 1,535 | 621 |
| Short term investments | **3,234** | 3,371 | 1,519 |
| Security deposits | **435** | 348 | 560 |
| Fair value of financial derivatives related to the above | **187** | 178 | 57 |
| | **5,384** | 5,432 | 2,757 |
| Net debt | **$ 501** | $ 299 | $ 3,251 |

Capital securities are excluded from the calculation of net debt. For the purpose of calculating net debt, fair values of financial derivatives are not credit value adjusted in accordance with EIC Abstract 173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities" ("EIC 173"). As at the end of 2010, the credit value adjustment was $4 million (2009 – $4 million).

**Net Assets**

The following table reconciles net assets used in the return on average net assets ratio to Canadian GAAP measures reported on the consolidated balance sheet as at the years ended as indicated.

Net assets is calculated as total assets less cash and cash equivalents, short term investments, security deposits, the fair value of Weston Holdings Limited's ("WHL"), a subsidiary of GWL, forward sale agreement for 9.6 million Loblaw common shares, assets of operations held for sale and accounts payable and accrued liabilities. Return on average net assets is calculated as operating income for the year divided by average net assets.

The Company believes the return on average net assets ratio is useful in assessing the return on productive assets.

| ($ millions) | Dec. 31, 2010 Weston Foods | Loblaw | Other[(1)] | Consolidated |
|---|---|---|---|---|
| Canadian GAAP total assets | **$ 1,868** | **$ 16,091** | **$ 2,895** | **$ 20,854** |
| Less: Cash and cash equivalents | **157** | **932** | **439** | **1,528** |
| Short term investments | **43** | **735** | **2,456** | **3,234** |
| Security deposits | **81** | **354** | | **435** |
| Fair value of WHL's forward sale agreement for 9.6 million Loblaw shares | **421** | | | **421** |
| Accounts payable and accrued liabilities[(2)] | **301** | **3,416** | | **3,717** |
| Net assets | **$ 865** | **$ 10,654** | **$** | **$ 11,519** |

(1) Other includes cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates.

(2) Excludes the accrual of $1.0 billion related to the special one-time common share dividend declared in the fourth quarter of 2010 and subsequently paid on January 25, 2011.

| ($ millions) | Dec. 31, 2009 Weston Foods | Loblaw | Other[(1)] | Consolidated |
|---|---|---|---|---|
| Canadian GAAP total assets | $ 1,674 | $ 15,151 | $ 3,318 | $ 20,143 |
| Less: Cash and cash equivalents | 165 | 776 | 594 | 1,535 |
| Short term investments | 33 | 614 | 2,724 | 3,371 |
| Security deposits | 98 | 250 | | 348 |
| Fair value of WHL's forward sale agreement for 9.6 million Loblaw shares | 446 | | | 446 |
| Accounts payable and accrued liabilities | 337 | 3,279 | | 3,616 |
| Net assets | $ 595 | $ 10,232 | $ | $ 10,827 |

(1) Other includes cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates.

| ($ millions) | Weston Foods | Loblaw | Discontinued Operations | Consolidated |
|---|---|---|---|---|
| | | | | Dec. 31, 2008 |
| Canadian GAAP total assets | $ 2,892 | $ 14,083 | $ 2,588 | $ 19,563 |
| Less: Cash and cash equivalents | 378 | 243 | | 621 |
| Short term investments | 1,009 | 510 | | 1,519 |
| Security deposits | 123 | 437 | | 560 |
| Current assets of operations held for sale | | | 2,588 | 2,588 |
| Fair value of WHL's forward sale agreement for 9.6 million Loblaw shares | 397 | | | 397 |
| Accounts payable and accrued liabilities | 298 | 2,823 | | 3,121 |
| Net assets | $ 687 | $ 10,070 | $ | $ 10,757 |

**Equity**

The following table reconciles equity used in the net debt to equity ratio to Canadian GAAP measures reported in the audited consolidated financial statements as at the years ended as indicated.

Equity is calculated as the sum of GWL capital securities and shareholders' equity as follows:

| ($ millions) | **Dec. 31, 2010** | Dec. 31, 2009 | Dec. 31, 2008 |
|---|---|---|---|
| Capital securities | | | $ 264 |
| Shareholders' equity | **$ 6,132** | $ 6,942 | 5,910 |
| Equity | **$ 6,132** | $ 6,942 | $ 6,174 |

## 19. ADDITIONAL INFORMATION

The following table provides additional financial information as at the years ended as indicated.

| ($ millions) | **Dec. 31, 2010** | Dec. 31, 2009 | Dec. 31, 2008 |
|---|---|---|---|
| Market price per common share ($) | **$ 84.20** | $ 66.92 | $ 59.90 |
| Actual common shares outstanding (in millions) | **129.1** | 129.1 | 129.1 |
| Weighted average common shares outstanding (in millions) | **129.1** | 129.1 | 129.1 |

Additional information about the Company, including its Annual Information Form and other disclosure documents, has been filed electronically with the Canadian securities regulatory authorities in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR) and is available online at www.sedar.com.

This Annual Report includes selected information on Loblaw Companies Limited, a 62.9%-owned public reporting subsidiary company with shares trading on the Toronto Stock Exchange. For information regarding Loblaw, readers should also refer to the materials filed by Loblaw with the Canadian securities regulatory authorities from time to time. These filings are also available on Loblaw's corporate website at www.loblaw.ca.

Toronto, Canada

March 2, 2011

# Financial Results


| | | |
|---|---|---|
| Management's Statement of Responsibility for Financial Reporting | | 68 |
| Independent Auditors' Report | | 69 |
| Consolidated Financial Statements | | 70 |
| Consolidated Statements of Earnings | | 70 |
| Consolidated Statements of Changes in Shareholders' Equity | | 71 |
| Consolidated Statements of Comprehensive Income | | 71 |
| Consolidated Balance Sheets | | 72 |
| Consolidated Cash Flow Statements | | 73 |
| Notes to the Consolidated Financial Statements | | 74 |
| Note 1. | Summary of Significant Accounting Policies | 74 |
| Note 2. | Implementation of New Accounting Standards | 81 |
| Note 3. | Business Acquisitions | 82 |
| Note 4. | Discontinued Operations | 84 |
| Note 5. | Distribution Network Costs | 84 |
| Note 6. | Interest Expense and Other Financing Charges | 85 |
| Note 7. | Income Taxes | 85 |
| Note 8. | Basic and Diluted Net Earnings per Common Share from Continuing Operations | 86 |
| Note 9. | Cash and Cash Equivalents, Short Term Investments and Security Deposits | 87 |
| Note 10. | Accounts Receivable | 88 |
| Note 11. | Allowances for Receivables | 89 |
| Note 12. | Inventories | 90 |
| Note 13. | Fixed Assets | 90 |
| Note 14. | Goodwill and Intangible Assets | 91 |
| Note 15. | Other Assets | 92 |
| Note 16. | Employee Future Benefits | 92 |
| Note 17. | Short Term Debt | 96 |
| Note 18. | Long Term Debt | 97 |
| Note 19. | Other Liabilities | 98 |
| Note 20. | Leases | 99 |
| Note 21. | Capital Securities | 99 |
| Note 22. | Share Capital | 100 |
| Note 23. | Capital Management | 102 |
| Note 24. | Stock-Based Compensation | 104 |
| Note 25. | Accumulated Other Comprehensive Loss | 108 |
| Note 26. | Financial Derivative Instruments | 109 |
| Note 27. | Fair Values of Financial Instruments | 111 |
| Note 28. | Financial Risk Management | 114 |
| Note 29. | Contingencies, Commitments and Guarantees | 118 |
| Note 30. | Variable Interest Entities | 120 |
| Note 31. | Related Party Transactions | 121 |
| Note 32. | Segment Information | 122 |

## Management's Statement of Responsibility for Financial Reporting

The management of George Weston Limited is responsible for the preparation and fair presentation of the accompanying consolidated financial statements, Management's Discussion and Analysis and all other information in the Annual Report. This responsibility includes the selection and consistent application of appropriate accounting principles and methods in addition to making the judgments and estimates necessary to prepare the consolidated financial statements in accordance with Canadian generally accepted accounting principles ("GAAP"). It also includes ensuring that the financial information presented elsewhere in the Annual Report is consistent with that in the consolidated financial statements.

Management is also responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. Internal auditors, who are employees of the Company, review and evaluate internal controls on management's behalf. KPMG LLP, whose report follows, were appointed as independent auditors by a vote of the Company's shareholders to audit the consolidated financial statements.

The Board of Directors, acting through an Audit Committee comprised solely of directors who are independent, is responsible for determining that management fulfills its responsibilities in the preparation of the consolidated financial statements and the financial control of operations. The Audit Committee recommends the independent auditors for appointment by the shareholders. The Audit Committee meets regularly with senior and financial management, internal auditors and the independent auditors to discuss internal controls, auditing activities and financial reporting matters. The independent auditors and internal auditors have unrestricted access to the Audit Committee. These consolidated financial statements and Management's Discussion and Analysis have been approved by the Board of Directors for inclusion in the Annual Report based on the review and recommendation of the Audit Committee.

| | |
|---|---|
| **[*signed*]** | **[*signed*]** |
| **W. Galen Weston** | **Paviter S. Binning** |
| Chairman and President | Chief Financial Officer |

Toronto, Canada
March 2, 2011

# Independent Auditors' Report

**To the Shareholders of George Weston Limited:**

We have audited the accompanying consolidated financial statements of George Weston Limited, which comprise the consolidated balance sheets as at December 31, 2010 and 2009, the consolidated statements of earnings, changes in shareholders' equity and comprehensive income, the consolidated cash flow statements for the years then ended and a summary of significant accounting policies and other explanatory information.

**Management's Responsibility for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

**Auditors' Responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform an audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinions.

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of George Weston Limited as at December 31, 2010 and December 31, 2009 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Toronto, Canada
March 2, 2011

Chartered Accountants, Licensed Public Accountants

## Consolidated Statements of Earnings

| For the years ended December 31<br>($ millions except where otherwise indicated) | 2010 | 2009 |
|---|---|---|
| **Sales** | **$ 32,008** | $ 31,820 |
| **Operating Expenses** | | |
| Cost of inventories sold (note 12) | **23,775** | 24,015 |
| Selling, administrative and other expenses | **6,084** | 6,122 |
| Depreciation and amortization (note 12) | **666** | 601 |
| Goodwill impairment (note 14) | | 73 |
| | **30,525** | 30,811 |
| **Operating Income** | **1,483** | 1,009 |
| Interest Expense and Other Financing Charges (note 6) | **388** | 363 |
| **Earnings from Continuing Operations Before the Following:** | **1,095** | 646 |
| Income Taxes (note 7) | **370** | 259 |
| | **725** | 387 |
| Minority Interest | **273** | 260 |
| **Net Earnings from Continuing Operations** | **452** | 127 |
| **Discontinued Operations** (note 4) | | 908 |
| **Net Earnings** | **$ 452** | $ 1,035 |
| **Net Earnings per Common Share – Basic** ($) | | |
| Continuing Operations (note 8) | **$ 3.16** | $ 0.64 |
| Discontinued Operations | | $ 7.04 |
| Net Earnings | **$ 3.16** | $ 7.68 |
| **Net Earnings per Common Share – Diluted** ($) | | |
| Continuing Operations (note 8) | **$ 3.14** | $ 0.63 |
| Discontinued Operations | | $ 7.04 |
| Net Earnings | **$ 3.14** | $ 7.67 |

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Changes in Shareholders' Equity

For the years ended December 31

| ($ millions except where otherwise indicated) | 2010 | 2009 |
|---|---|---|
| **Share Capital** | | |
| Preferred Shares | **$ 817** | $ 817 |
| Common Shares | **133** | 133 |
| **Total Share Capital, Beginning and End of Year** (note 22) | **$ 950** | $ 950 |
| | | |
| **Retained Earnings, Beginning of Year** | **$ 6,084** | $ 5,282 |
| Cumulative impact of implementing new accounting standards (note 2) | | (4) |
| Net earnings | **452** | 1,035 |
| Dividends declared | | |
| Per common share ($) – $9.19 (2009 – $1.44) | **(1,186)** | (186) |
| Per preferred share ($) – Series I – $1.45 (2009 – $1.45) | **(13)** | (13) |
| – Series III – $1.30 (2009 – $1.30) | **(10)** | (10) |
| – Series IV – $1.30 (2009 – $1.30) | **(10)** | (10) |
| – Series V – $1.19 (2009 – $1.19) | **(10)** | (10) |
| **Retained Earnings, End of Year** | **$ 5,307** | $ 6,084 |
| | | |
| **Accumulated Other Comprehensive Loss, Beginning of Year** | **$ (92)** | $ (322) |
| Cumulative impact of implementing new accounting standards (note 2) | | (1) |
| Other comprehensive (loss) income (note 25) | **(33)** | 231 |
| **Accumulated Other Comprehensive Loss, End of Year** (note 25) | **$ (125)** | $ (92) |
| | | |
| **Total Shareholders' Equity** | **$ 6,132** | $ 6,942 |

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Comprehensive Income

For the years ended December 31

| ($ millions) | 2010 | 2009 |
|---|---|---|
| Net earnings | **$ 452** | $ 1,035 |
| Other comprehensive (loss) income, net of income taxes and minority interest | | |
| Foreign currency translation adjustment (note 25) | **(28)** | 35 |
| Reclassification of cumulative foreign currency translation loss to net earnings | | 196 |
| | **(28)** | 231 |
| Net unrealized loss on available-for-sale financial assets | **(8)** | (14) |
| Reclassification of loss on available-for-sale financial assets to net earnings | **8** | 1 |
| | | (13) |
| Net gain on derivatives designated as cash flow hedges | **1** | 4 |
| Reclassification of (gain) loss on derivatives designated as cash flow hedges to net earnings | **(6)** | 9 |
| | **(5)** | 13 |
| Other comprehensive (loss) income (note 25) | **(33)** | 231 |
| **Total Comprehensive Income** | **$ 419** | $ 1,266 |

See accompanying notes to the consolidated financial statements.

## Consolidated Balance Sheets

As at December 31

| ($ millions) | 2010 | 2009 |
|---|---|---|
| **ASSETS** | | |
| **Current Assets** | | |
| Cash and cash equivalents (note 9) | **$ 1,528** | $ 1,535 |
| Short term investments (note 9) | **3,234** | 3,371 |
| Accounts receivable (notes 10 & 11) | **820** | 851 |
| Inventories (note 12) | **2,208** | 2,210 |
| Future income taxes (note 7) | **61** | 87 |
| Prepaid expenses and other assets | **90** | 98 |
| **Total Current Assets** | **7,941** | 8,152 |
| Fixed Assets (note 13) | **9,584** | 9,020 |
| Goodwill and Intangible Assets (note 14) | **1,571** | 1,296 |
| Future Income Taxes (note 7) | **33** | 61 |
| Security Deposits (note 9) | **435** | 348 |
| Other Assets (note 15) | **1,290** | 1,266 |
| **Total Assets** | **$ 20,854** | $ 20,143 |
| **LIABILITIES** | | |
| **Current Liabilities** | | |
| Bank indebtedness | **$ 4** | $ 2 |
| Accounts payable and accrued liabilities | **4,717** | 3,616 |
| Income taxes | **20** | 78 |
| Short term debt (notes 17 & 18) | **336** | 300 |
| Long term debt due within one year (note 18) | **733** | 343 |
| **Total Current Liabilities** | **5,810** | 4,339 |
| Long Term Debt (note 18) | **5,129** | 5,377 |
| Future Income Taxes (note 7) | **311** | 269 |
| Other Liabilities (note 19) | **655** | 617 |
| Capital Securities (note 21) | **221** | 220 |
| Minority Interest | **2,596** | 2,379 |
| **Total Liabilities** | **14,722** | 13,201 |
| **SHAREHOLDERS' EQUITY** | | |
| Share Capital (note 22) | **950** | 950 |
| Retained Earnings | **5,307** | 6,084 |
| Accumulated Other Comprehensive Loss (note 25) | **(125)** | (92) |
| **Total Shareholders' Equity** | **6,132** | 6,942 |
| **Total Liabilities and Shareholders' Equity** | **$ 20,854** | $ 20,143 |

Contingencies, commitments and guarantees (note 29). Leases (note 20).
See accompanying notes to the consolidated financial statements.

Approved on behalf of the Board

[*signed*]
**W. Galen Weston**
Director

[*signed*]
**A. Charles Baillie**
Director

# Consolidated Cash Flow Statements

| For the years ended December 31<br>($ millions) | 2010 | 2009 |
|---|---|---|
| **Operating Activities** | | |
| Net earnings from continuing operations before minority interest | **$ 725** | $ 387 |
| Depreciation and amortization | **709** | 645 |
| Goodwill impairment (note 14) | | 73 |
| Foreign currency translation losses (note 32) | **56** | 311 |
| Loss on redemption of debt (notes 6 & 18) | | 49 |
| Settlement of equity forward contracts (note 26) | | (55) |
| Future income taxes | **94** | (79) |
| Fair value adjustment of Weston Holdings Limited's forward sale agreement (note 6) | **62** | (13) |
| Change in non-cash working capital | **26** | 675 |
| Fixed asset and other related impairments | **73** | 47 |
| Other | **(4)** | (53) |
| **Cash Flows from Operating Activities of Continuing Operations** | **1,741** | 1,987 |
| **Investing Activities** | | |
| Fixed asset purchases | **(1,304)** | (1,011) |
| Short term investments | **50** | (2,052) |
| Proceeds from fixed asset sales | **90** | 27 |
| Purchase of subsidiary interests (note 3) | | (35) |
| Business acquisitions – net of cash acquired (note 3) | **(309)** | (204) |
| Credit card receivables, after securitization (note 10) | **7** | 8 |
| Franchise investments and other receivables | **(11)** | 6 |
| Security deposits | **(104)** | 159 |
| Other | **20** | (50) |
| **Cash Flows used in Investing Activities of Continuing Operations** | **(1,561)** | (3,152) |
| **Financing Activities** | | |
| Bank indebtedness | **(1)** | (95) |
| Short term debt (notes 17 & 18) | **36** | (153) |
| Long term debt (note 18) – Issued | **450** | 402 |
| – Retired | **(368)** | (490) |
| Capital securities (note 21) – Retired | | (265) |
| Cancellation of subsidiary share capital (note 3) | | (21) |
| Dividends – To common shareholders | **(186)** | (139) |
| – To preferred shareholders | **(44)** | (36) |
| – To minority shareholders | **(57)** | (70) |
| **Cash Flows used in Financing Activities of Continuing Operations** | **(170)** | (867) |
| Effect of Foreign Currency Translation on Cash and Cash Equivalents (note 9) | **(17)** | (71) |
| Cash Flows used in Continuing Operations | **(7)** | (2,103) |
| Cash Flows from Discontinued Operations (note 4) | | 3,017 |
| Change in Cash and Cash Equivalents | **(7)** | 914 |
| Cash and Cash Equivalents, Beginning of Year | **1,535** | 621 |
| **Cash and Cash Equivalents, End of Year** (note 9) | **$ 1,528** | $ 1,535 |

See accompanying notes to the consolidated financial statements.

# Notes to the Consolidated Financial Statements

December 31, 2010
($ millions except where otherwise indicated)

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements were prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are reported in Canadian dollars.

### Basis of Consolidation

The consolidated financial statements include the accounts of George Weston Limited ("GWL") and its subsidiaries (collectively, the "Company") with provision for minority interest. The Company's interest in the voting share capital of its subsidiaries is 100% except for Loblaw Companies Limited ("Loblaw"), which is 62.9% (2009 – 62.5%). In addition, the Company consolidates variable interest entities ("VIEs") pursuant to the Canadian Institute of Chartered Accountants ("CICA") Accounting Guideline 15, "Consolidation of Variable Interest Entities" ("AcG 15"), that are subject to control by Loblaw on a basis other than through ownership of a majority of voting interest. AcG 15 defines a variable interest entity as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. AcG 15 requires the primary beneficiary to consolidate VIEs and considers an entity to be the primary beneficiary of a VIE if it holds variable interests that expose it to a majority of the VIEs' expected losses or that entitle it to receive a majority of the VIEs' expected residual returns or both. The Company has two reportable operating segments: Weston Foods and Loblaw.

### Fiscal Year

The Company's year end is December 31. Activities are reported on a fiscal year ending on the Saturday closest to December 31.

As a result, the Company's fiscal year is usually 52 weeks in duration but includes a 53rd week every five to six years. Each of the years ended December 31, 2010 and December 31, 2009 contained 52 weeks.

### Revenue Recognition

Weston Foods recognizes sales upon delivery of its products to customers and acceptance of its products by customers net of provisions for returns, discounts and allowances. Loblaw sales include revenues, net of estimated returns, from customers through corporate stores operated by Loblaw and independent franchisee stores that are consolidated by Loblaw pursuant to AcG 15. In addition, sales include sales to and service fees from associated stores and independent account customers and franchised stores excluding VIE stores net of sales incentives offered by Loblaw. Loblaw recognizes revenue at its corporate and VIE stores at the time the sale is made to its customers and at the time of delivery of inventory to its associated and franchised stores.

### Net Earnings per Common Share

Basic net earnings per common share is calculated by dividing the net earnings available to common shareholders by the weighted average number of common shares outstanding during the year. Diluted net earnings per common share is calculated using the treasury stock method and the if converted method. The treasury stock method assumes that all outstanding stock options with an exercise price below the average market price during the year are exercised and the assumed proceeds are used to purchase the Company's common shares at the average market price during the year. Under the if converted method, diluted net earnings per common share also takes into consideration the dilutive effect of the conversion options on the Loblaw capital securities and a component of Loblaw's other liabilities, which are assumed to be converted using the market share price at the end of the year.

**Cash and Cash Equivalents and Bank Indebtedness**
Cash equivalents consist of highly liquid marketable investments with a maturity of 90 days or less from the date of acquisition (see note 9). Cash equivalents are either designated as held-for-trading financial assets or classified as available-for-sale financial assets and the carrying value approximates the fair value of these instruments. Bank indebtedness is classified as other financial liabilities and the carrying value approximates the fair value of this instrument.

**Short Term Investments**
Short term investments are either designated as held-for-trading financial assets or classified as available-for-sale financial assets and the carrying value approximates the fair value of these instruments. See note 9 for the types of investments held.

**Security Deposits**
Security deposits are either designated as held-for-trading financial assets or classified as available-for-sale financial assets and the carrying value approximates the fair value of these instruments. See note 9 for the types of investments held.

**Credit Card Receivables**
The Company, through President's Choice Bank ("PC Bank"), a wholly owned subsidiary of Loblaw, has credit card receivables that are stated net of an allowance for credit losses. Any credit card receivable with a payment that is contractually 180 days in arrears, or where the likelihood of collection is considered remote, is written off. Interest income on credit card receivables is recorded on an accrual basis and is recognized in operating income.

PC Bank maintains an allowance for probable credit losses on aggregate exposures for which losses cannot be determined on an item-by-item basis. The allowance is based upon a statistical analysis of past and current performance, the level of allowance already in place and management's judgment. The allowance for credit losses is deducted from the credit card receivables balance. The net credit loss experience for the year is recognized in operating income.

PC Bank securitizes credit card receivables through the sale of a portion of the total interest in certain receivables to independent trusts. These trusts are either not controlled by PC Bank or are qualifying special purpose entities. The credit card receivables are removed from the consolidated balance sheet when PC Bank has surrendered control and are considered sold for accounting purposes pursuant to AcG 12, "Transfers of Receivables". When PC Bank sells credit card receivables in a securitization transaction, it retains servicing responsibilities, certain administrative responsibilities and the rights to future cash flows after obligations to investors have been met. Although PC Bank remains responsible for servicing all credit card receivables, it does not receive additional compensation for servicing those credit card receivables and accordingly a servicing liability is recorded. The servicing liability is recorded at fair value upon initial recognition. In the absence of quoted market rates for servicing securitized assets, fees payable to a replacement servicer, in the event that a replacement servicer was to be appointed, formed the basis of determination of fair value of the servicing liability. Gains or losses on the securitization of the receivables depends, in part, on the previous carrying amount of receivables involved in the transfer, allocated between the assets sold and retained interest, based on their relative fair values at the date of transfer. The fair value of the retained interest is determined as the best estimate of the net present value of expected future cash flows using management's best estimates of key assumptions such as net yield, monthly payment rates, weighted average life, expected annual credit losses and discount rates. Any gain or loss on a sale is recognized in operating income at the time of the securitization. Retained interest is primarily designated as a held-for-trading financial asset and is recorded at fair value on the consolidated balance sheet.

**Vendor Allowances**

The Company receives allowances from certain of its vendors whose products it purchases. These allowances are received for a variety of buying and/or merchandising activities, including vendor programs such as volume purchase allowances, purchase discounts, listing fees and exclusivity allowances. Consideration received from a vendor is a reduction in the cost of the vendor's products or services and is recognized as a reduction in the cost of inventories sold and the related inventory when recognized in the consolidated statement of earnings and the consolidated balance sheet. Certain exceptions apply if the consideration is a payment for assets or services delivered to the vendor or for reimbursement of selling costs incurred to promote the vendor's products, provided that these costs are separate, incremental and identifiable.

**Inventories**

The Company values inventories at the lower of cost and net realizable value. Cost includes the costs of purchases, net of vendor allowances, plus other costs that are directly incurred to bring inventories to their present location and condition. Loblaw's seasonal general merchandise, Loblaw's inventories at the distribution centres and Weston Foods inventories are measured at weighted average cost. Loblaw uses the retail method to measure the cost of certain retail store inventories. Loblaw estimates net realizable value as the amount that inventories are expected to be sold taking into consideration fluctuations in retail prices due to seasonality less estimated costs necessary to make the sale. Inventories are written down to net realizable value when the cost of inventories is estimated to be unrecoverable due to obsolescence, damage or declining selling prices. When circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in selling prices, the amount of the write-down previously recorded is reversed. Storage costs, indirect administrative overhead and certain selling costs related to inventories are expensed in the period that these costs are incurred.

**Fixed Assets**

Fixed assets are recorded at cost including capitalized interest. Depreciation commences when the assets are put into use and is recognized on a straight-line basis to depreciate the cost of these assets over their estimated useful lives. Estimated useful lives range from 10 to 40 years for buildings, up to 10 years for building improvements and from 3 to 16 years for equipment and fixtures. Leasehold improvements are depreciated over the lesser of the lease term and their estimated useful lives and may include renewal options when an improvement is made after inception of the lease, to a maximum of 25 years, which approximates economic life. Equipment and buildings under capital leases are depreciated over the term of the lease.

Fixed assets are reviewed for impairment annually and when events or changes in circumstances indicate that the carrying value exceeds the sum of the undiscounted future cash flows expected from their use and eventual disposal. These events or changes in circumstances include a commitment to retire or transfer manufacturing assets for Weston Foods and to close a Loblaw store or distribution centre or to relocate or convert a Loblaw store. For purposes of annually reviewing assets for impairment, asset groups are reviewed at the lowest level for which identifiable cash flows are largely independent of cash flows of other assets and liabilities. Therefore, Weston Foods manufacturing asset net cash flows are grouped together by major production categories, where cash flows are largely dependent on each other. Loblaw's store net cash flows are grouped together by primary market areas, where cash flows are largely dependent on each other. Primary markets are regional areas where a number of store formats operate within close proximity to one another. If an indicator of impairment exists, such as sustained negative operating cash flows of the respective asset group, then an estimate of undiscounted future cash flows of each such major production category for Weston Foods, or each such store for Loblaw, within this group is prepared and compared to its carrying value. For purposes of annually reviewing Loblaw's distribution centre assets for impairment, distribution centre net cash flows are grouped with the respective net cash flows of the stores they service. An impairment in the Loblaw store network serviced by the distribution centre may indicate an impairment in the distribution centre assets as well. If any of Weston Foods or Loblaw's assets are determined to be impaired, the impairment loss is measured as the excess of the carrying value over fair value.

**Goodwill and Intangible Assets**

Goodwill represents the excess of the purchase price of a business acquired over the fair value of the underlying net assets acquired at the date of acquisition. Other intangible assets are recorded at fair value at the date of acquisition. Goodwill is assessed for impairment at the reporting unit level at least annually. Any potential goodwill impairment is identified by comparing the fair value of a reporting unit to its carrying value. If the carrying value of the reporting unit exceeds its fair value, a more detailed goodwill impairment assessment must be undertaken. A goodwill impairment charge is recognized in operating income to the extent that, at the reporting unit level, the carrying value of goodwill exceeds the implied fair value.

The Company determines the fair values of its reporting units using a discounted cash flow model corroborated by other valuation techniques such as market multiples. The process of determining these fair values requires management to make estimates and assumptions of a long term nature regarding projected future sales, earnings and capital investment, discount rates and terminal growth rates. Projected future sales, earnings and capital investment are consistent with strategic plans presented to GWL's and Loblaw's Boards of Directors. Discount rates are based on an industry weighted average cost of capital. These estimates and assumptions may change in the future due to uncertain competitive and economic market conditions or changes in business strategies.

Intangible assets with an indefinite life are not subject to amortization and are tested at least annually for impairment. Any potential intangible asset impairment is identified by comparing the fair value of the indefinite life intangible asset to its carrying value. If the carrying value of the intangible asset exceeds its fair value, impairment is identified as the difference between the fair value and the carrying value and will result in the recognition of a non-cash impairment charge in operating income.

The Company determines the fair values of its trademarks and brand names by using the "Relief from Royalty" method, a discounted cash flow model. Weston Foods determines the fair values of its customer relationships by using an income approach, specifically the "Excess Earnings" method, a discounted cash flow model. The process of determining the fair values requires management to make assumptions of a long term nature regarding projected future sales, terminal growth rates, royalty rates and discount rates. Projected future sales are consistent with strategic plans presented to GWL's and Loblaw's Boards of Directors and discount rates are based on an industry after-tax cost of equity. These estimates and assumptions may change in the future due to uncertain competitive and economic market conditions or changes in business strategies. Intangible assets with a finite life are amortized over their estimated useful lives, ranging from 10 to 30 years.

Additional disclosure regarding the results of the annual goodwill impairment test is provided in note 14.

**Foreign Currency Translation**

***Self-Sustaining Foreign Operations***

Assets and liabilities of self-sustaining foreign operations denominated in foreign currencies are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. The resulting translation gains or losses on translation are recognized as part of shareholders' equity in accumulated other comprehensive loss. When there is a reduction in the Company's net investment in self-sustaining foreign operations, the proportionate amount of accumulated other comprehensive loss is recognized in net earnings. Revenues and expenses denominated in foreign currencies are translated into Canadian dollars at the foreign currency exchange rates that approximate the rates in effect at the dates when such items are recognized.

***Other***

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. Translation gains or losses arising from the translation of these balances denominated in foreign currencies are recognized in operating income, except for items which are designated in a cash flow hedge and are deferred in accumulated other comprehensive loss and reclassified to net earnings when realized. Revenues and expenses denominated in foreign currencies are translated into Canadian dollars at the foreign currency exchange rates that approximate the rates in effect at the dates when such items are recognized.

**Financial Instruments**

Financial instruments are classified into a defined category, namely, held-for-trading financial assets or financial liabilities, held-to-maturity investments, loans and receivables, available-for-sale financial assets, or other financial liabilities. Financial instruments are included on the Company's balance sheet and measured at fair value, except for loans and receivables, held-to-maturity financial assets and other financial liabilities which are measured at cost or amortized cost. Financial assets and financial liabilities have been initially remeasured as at January 1, 2009 to take into account the appropriate credit risk and counterparty credit risk (see note 2). Gains and losses on held-for-trading financial assets and financial liabilities are recognized in net earnings in the period in which they arise. Unrealized gains and losses, including those related to changes in foreign currency exchange rates on available-for-sale financial assets, are recognized in accumulated other comprehensive loss until the financial asset is derecognized or determined to be impaired, at which time any unrealized gains or losses are recorded in net earnings. Transaction costs other than those related to financial instruments classified as held-for-trading, which are expensed as incurred, are amortized using the effective interest method.

The following classifications have been applied:

- Cash and cash equivalents, short term investments and security deposits are designated as held-for-trading with the exception of certain Loblaw U.S. dollar denominated cash equivalents, short term investments and security deposits designated in a cash flow hedging relationship, which are classified as available-for-sale financial assets.
- Accounts receivable and other receivables are classified as loans and receivables.
- Investments in equity instruments are classified as available-for-sale.
- Bank indebtedness, accounts payable and certain accrued liabilities, short term debt, long term debt, capital lease obligations, certain other liabilities and capital securities have been classified as other financial liabilities.
- Certain accrued liabilities are classified as held-for-trading.

The Company has not classified any financial assets as held-to-maturity.

**Derivative Instruments**

Derivative instruments in the form of cross currency swaps, interest rate swaps and equity swaps and forwards partially offset exposure to fluctuations in foreign currency exchange rates, interest rates and the market prices of GWL and Loblaw common shares. Financial and non-financial derivative instruments in the form of futures contracts, option contracts and forward contracts mitigate current and anticipated exposure to fluctuations in commodity prices and foreign currency exchange rates. Policies and guidelines prohibit the use of any derivative instruments for trading or speculative purposes.

All financial derivative instruments are recorded at fair value on the consolidated balance sheet. Derivative instruments have been initially remeasured as at January 1, 2009 to take into account the appropriate credit risk and counterparty credit risk (see note 2). Non-financial derivative instruments, such as certain contracts that are linked to commodity prices, are recorded at fair value on the consolidated balance sheet unless they are exempt from this treatment based upon expected purchase, sale or usage requirements. Embedded derivative instruments which are not closely related to the host contract are separated from their host contract and recorded on the consolidated balance sheet at fair value. Fair values are based on quoted market prices where available from active markets; otherwise fair values are estimated using valuation methodologies, primarily discounted cash flow analysis (see note 27).

Derivative instruments are recorded in current or non-current assets and liabilities based on their remaining terms to maturity. All changes in fair value of the derivative instruments are recorded in net earnings unless cash flow hedge accounting is applied.

The Company formally identifies, designates and documents the relationships between hedging instruments and hedged items including cross currency swaps and interest rate swaps as cash flow hedges against the exposure to fluctuations in the foreign currency exchange rate and variable interest rates, and certain commodity futures as cash flow hedges against the exposure to commodity price fluctuations (see note 26). The Company assesses whether these derivative instruments continue to be highly effective in offsetting changes in the cash flows of hedged items. If and when a derivative instrument is no longer expected to be highly effective, hedge accounting is discontinued. Hedge ineffectiveness, if any, is included in current period net earnings.

**Income Taxes**
The asset and liability method of accounting is used for income taxes. Under the asset and liability method, future income tax assets and liabilities are recognized for the future income tax consequences attributable to temporary differences between the financial statement carrying values of existing assets and liabilities and their respective income tax bases. Future income tax assets and liabilities are measured using enacted or substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in income tax rates is recognized in income tax expense when enacted or substantively enacted. Future income tax assets are evaluated and a valuation allowance, if required, is recorded against any future income tax asset if it is more likely than not that the asset will not be realized.

**Employee Future Benefits**
The Company sponsors a number of pension plans, including funded defined benefit pension plans, defined contribution pension plans and supplemental unfunded arrangements providing pension benefits in excess of statutory limits. The Company also offers other employee benefit plans comprised of post-retirement and post-employment benefit plans which are generally unfunded and non-contributory. Post-retirement benefit plans include health care, life insurance and dental benefits during retirement, while post-employment benefit plans include long term disability benefits and the continuation of health and dental benefits while on disability. The Company also contributes to various multi-employer pension plans which provide pension benefits.

***Defined Benefit Plans***
The cost and accrued benefit plan obligations of the Company's defined benefit pension plans and other benefit plans, including post-retirement and post-employment, are based on actuarial valuations. The actuarial valuations for the defined benefit plans are determined using the projected benefit method prorated on service and management's best estimate of the discount rate, the expected long term rate of return on plan assets, the expected growth rate of health care costs, the rate of compensation increase, retirement rates, termination rates and mortality rates. Actuarial valuations are performed using a September 30 measurement date for accounting purposes. Market values used to value benefit plan assets are as at the measurement date and then adjusted for employer contributions made between the measurement date and the fiscal year end. The discount rate used to value the accrued benefit plan obligation is based on market interest rates as at the measurement date, assuming a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the accrued benefit plan obligations.

Past service costs arising from plan amendments are amortized over the expected average remaining service period of the active employees. The unamortized net actuarial gain or loss that exceeds 10% of the greater of the accrued benefit plan obligation or the fair value of the benefit plan assets at the beginning of the year is amortized over the expected average remaining service period of the active employees for defined benefit pension and post-retirement benefit plans unless the plan covers mostly inactive members, in which case life expectancy is used. The amortization period for the defined benefit pension plans ranges from 7 to 23 years, with a weighted average of 11 years. The amortization period for the post-retirement benefit plans ranges from 8 to 21 years, with a weighted average of 14 years. The unamortized net actuarial gain or loss for post-employment benefits is amortized over a period not exceeding three years.

The net accrued benefit plan asset or liability represents the cumulative difference between the cost and the funding contributions and is recorded in other assets and other liabilities.

***Defined Contribution and Multi-Employer Pension Plans***

The costs of pension benefits for defined contribution pension plans and multi-employer pension plans are expensed as contributions are due.

**Stock Option Plan and Share Appreciation Rights**

The Company recognizes a compensation cost in operating income and a liability related to employee stock option grants that allow for settlement in shares or in the share appreciation value in cash at the option of the employee and employee share appreciation right grants that will be settled in cash, using the intrinsic value method. Under the intrinsic value method, the stock-based compensation liability is the amount by which the market price of the common shares at the balance sheet date exceeds the exercise price of the stock options. A year-over-year change in the stock-based compensation liability is recognized in operating income on a prescribed vesting basis.

**Restricted Share Unit ("RSU") Plan**

The Company recognizes a compensation cost in operating income on a prescribed vesting basis for each RSU granted equal to the market value of a GWL or Loblaw common share at the date on which RSUs are awarded to each participant, prorated over the performance period, and adjusts for changes in the market value until the end of the performance period. The cumulative effect of the changes in market value is recognized in operating income in the period of the change.

**Director Deferred Share Unit ("DSU") Plan**

Members of GWL's and Loblaw's Boards of Directors who are not management may elect annually to receive all or a portion of their annual retainer(s) and fees in the form of DSUs. The DSU compensation liability is accounted for based on the number of units outstanding and the market value of the underlying GWL or Loblaw common share at the balance sheet date. The year-over-year change in the DSU compensation liability is recognized in operating income.

**Executive Deferred Share Unit ("EDSU") Plan**

Under this plan, executives may elect to defer up to 100% of the Short Term Incentive Plan ("STIP") bonus earned in any year into the EDSU plan, subject to an overall cap of three times the executive's base salary. All EDSUs held by an executive will be paid out in cash by December 15 of the year following the year in which the executive's employment ceases for any reason. An election to participate in the plan in any year must be made before the beginning of the year and is irrevocable. The number of EDSUs granted in respect of any year will be determined by dividing the STIP bonus that is subject to the EDSU plan election by the value of GWL or Loblaw common shares on the date the STIP bonus would otherwise be payable. For this purpose, and for purposes of determining the value of an EDSU upon conversion of the EDSUs into cash, the value of the EDSUs will be calculated by using the weighted average of the trading prices of GWL or Loblaw common shares on the Toronto Stock Exchange for the five trading days prior to the valuation date.

**Employee Share Ownership Plan ("ESOP")**

GWL and Loblaw maintain ESOPs which allow employees to acquire GWL and Loblaw common shares through payroll deductions of up to 5% of their gross regular earnings. GWL and Loblaw contribute an additional 25% of each employee's contribution to their respective plans, which is recognized in operating income as a compensation cost when the contribution is made.

**Use of Estimates and Assumptions**

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts and disclosures made in the consolidated financial statements and accompanying notes. These estimates and assumptions are based on management's historical experience, best knowledge of current events and conditions, and activities that may be undertaken in the future. Actual results could differ from these estimates.

Certain estimates, such as those related to valuation of inventories, impairment of fixed assets, employee future benefits, goodwill and intangible assets and income and other taxes, depend upon subjective or complex judgments about matters that may be uncertain, and changes in those estimates could materially impact the consolidated financial statements. Illiquid credit markets, volatile equity, foreign currency and energy markets and declines in consumer spending have combined to increase the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods.

**Comparative Information**
Certain prior year's information was reclassified to conform with the current year's presentation.

**Future Accounting Standards**
The Company will adopt International Financial Reporting Standards effective January 1, 2011.

## 2. IMPLEMENTATION OF NEW ACCOUNTING STANDARDS

**Accounting Standards Implemented in 2009**
***Goodwill and Intangible Assets***
In November 2007, the CICA issued amendments to Section 1000, "Financial Statement Concepts" and AcG 11, "Enterprises in the Development Stage", issued a new Section 3064, "Goodwill and Intangible Assets" ("Section 3064") to replace Section 3062, "Goodwill and Other Intangible Assets", withdrew Section 3450, "Research and Development Costs" and amended Emerging Issues Committee ("EIC") Abstract 27, "Revenues and Expenditures During the Pre-operating Period" to not apply to entities that have adopted Section 3064. These amendments, in conjunction with Section 3064, provide guidance for the recognition of intangible assets, including internally developed assets from research and development activities, ensuring consistent treatment of all intangible assets, whether separately acquired or internally developed. The Company implemented these requirements as of January 1, 2009, retroactively with restatement.

***Credit Risk and the Fair Value of Financial Assets and Financial Liabilities***
On January 20, 2009, the EIC issued Abstract 173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities". The committee reached a consensus that a company's credit risk and the credit risk of its counterparties should be considered when determining the fair value of its financial assets and financial liabilities, including derivative instruments. The transitional provisions required the abstract to be applied retrospectively without restatement of prior periods. Financial assets and financial liabilities, including derivative instruments, were remeasured as at January 1, 2009 to take into account the appropriate Company's credit risk and counterparty credit risk. As a result, a decrease in other assets of $12, a decrease in other liabilities of $4, a decrease in minority interest of $3, an increase net of income taxes and minority interest in accumulated other comprehensive loss of $1 and a decrease in retained earnings net of income taxes and minority interest of $4 were recorded on the consolidated balance sheet.

***Financial Instruments – Disclosures***
In June 2009, the CICA amended Section 3862, "Financial Instruments – Disclosures" to include additional disclosure relating to the measurement of fair value for financial instruments and liquidity risk. The amendment establishes a three level hierarchy that reflects the significance of the inputs used in fair value measurements on financial instruments. The amendment was implemented by the Company in 2009 (see note 27). The implementation of these amendments did not have an impact on the Company's results of operations or financial condition.

## 3. BUSINESS ACQUISITIONS

Weston Foods' acquisitions of ACE Bakery Ltd. ("ACE") and Keystone Bakery Holdings, LLC ("Keystone") were accounted for using the purchase method of accounting under Section 1581, "Business Combinations". Accordingly, the consolidated financial statements include the results of operations since the date of the acquisition and are reported in the Weston Foods segment.

### ACE Bakery

On November 1, 2010, Weston Foods (Canada) Inc., a subsidiary of GWL, acquired all of the outstanding shares of ACE, for total consideration of $110. Transaction costs incurred in connection with the acquisition were nominal.

The preliminary purchase equation includes estimates of fair value. The actual amount allocated to certain of the identifiable net assets could vary as the purchase equation is finalized.

The preliminary purchase price allocation as at December 31, 2010 is as follows:

| | | |
|---|---|---|
| Net assets acquired: | | |
| Accounts receivable | $ | 13 |
| Inventories | | 3 |
| Fixed assets | | 21 |
| Goodwill | | 63 |
| Intangible assets (note 14) | | 35 |
| Accounts payable and accrued liabilities | | (13) |
| Income taxes | | (2) |
| Future income taxes | | (10) |
| Cash consideration, net of cash acquired | $ | 110 |

The goodwill associated with the above transaction is not deductible for tax purposes.

### Keystone Bakery

On September 24, 2010, Maplehurst Bakeries, LLC, a subsidiary of GWL, acquired all of the outstanding shares of Keystone, for total consideration of approximately $188 (U.S. $186), including $1 of transaction costs.

The purchase price allocation as at December 31, 2010 is as follows:

| | | |
|---|---|---|
| Net assets acquired: | | |
| Accounts receivable | $ | 9 |
| Inventories | | 6 |
| Fixed assets | | 20 |
| Goodwill | | 95 |
| Intangible assets (note 14) | | 66 |
| Accounts payable and accrued liabilities | | (8) |
| Cash consideration, net of cash acquired | $ | 188 |

The goodwill associated with the above transaction is deductible for tax purposes.

### T&T Supermarket

Loblaw acquired all of the outstanding common shares of T&T Supermarket Inc. ("T&T") in the third quarter of 2009 for cash consideration of $200, $191 of which was paid on the date of acquisition. Loblaw also assumed a liability of $34 associated with the preferred shares issued by T&T to a vendor prior to the acquisition. The liability will increase with a favourable performance of the T&T business and the increase in the liability will be expensed as incurred. Acquisition costs of $4 were incurred in connection with the acquisition. The acquisition was accounted for using the purchase method of accounting and its results of operations from the date of the acquisition have been included by the Company.

The preferred shares are classified as other liabilities on the consolidated balance sheets. Redemption or purchase of the preferred shares may take place upon the occurrence of certain events, including the expiry of 5 years from the closing date of the acquisition. The preferred shareholder may increase this period up to a further 5 years if certain conditions are met. The preferred share liability may be satisfied in cash, Loblaw common shares, or a combination thereof, at the option of Loblaw.

During 2010, Loblaw finalized the purchase price allocation related to the acquisition which resulted in a reduction of goodwill of $2 (see note 14). The final purchase price allocation, based on Loblaw's assessment of fair value was as follows:

| | | |
|---|---|---|
| Net assets acquired: | | |
| Inventory | $ | 39 |
| Other current assets | | 9 |
| Fixed assets | | 73 |
| Goodwill | | 129 |
| Indefinite life intangible assets (trademarks and brand names) | | 51 |
| Definite life intangible assets | | 14 |
| Current liabilities | | (60) |
| Other liabilities | | (39) |
| Future income taxes | | (16) |
| Cash consideration | $ | 200 |

In connection with the acquisition of T&T, Loblaw also acquired certain net assets for $5.

The goodwill associated with these transactions is not deductible for tax purposes.

**Dividend Reinvestment Plan**

In 2009, Loblaw commenced a Dividend Reinvestment Plan ("DRIP"). Under the terms of the DRIP, eligible holders of common shares may elect to automatically reinvest their regular quarterly dividends in additional common shares of Loblaw without incurring any commissions, service charges or brokerage fees. The Company has elected to participate in the DRIP with respect to approximately 160 million Loblaw common shares owned by the Company. As a result of the common shares issued under the DRIP, the Company's proportional ownership of Loblaw increased and was accounted for as a step acquisition of Loblaw by the Company, resulting in an increase to goodwill of $12 and $9 during 2010 and 2009, respectively (see note 14).

Subsequent to year end 2010, the Loblaw Board of Directors approved that the DRIP be discontinued following the dividend payment on April 1, 2011 when approximately $300 in Loblaw common share equity will have been raised through the program as planned.

**Other**

During 2010, Weston Foods purchased a frozen bakery manufacturing facility in Ontario, Canada for cash consideration of $11. The acquisition was accounted for using the purchase method of accounting. Weston Foods acquired net assets of $4 and goodwill of $7.

In the normal course of business, Loblaw may acquire from time to time franchisee stores and convert them to corporate stores. In 2009, Loblaw acquired 3 franchisee stores for cash consideration of $6, resulting in goodwill acquired of $5.

During the fourth quarter of 2009, Loblaw purchased for cancellation 1.7 million of its common shares for $56. As a result, the Company's proportionate ownership of Loblaw increased and was accounted for as a step acquisition, resulting in an increase to goodwill of $11 (see note 14).

## 4. DISCONTINUED OPERATIONS

As part of the sale of the fresh bread and baked goods business in the United States ("U.S. fresh bakery business") in the first quarter of 2009 and typical of the normal process of selling a business, Dunedin Holdings S.à r.l. ("Dunedin"), a subsidiary of GWL, agreed to indemnify Grupo Bimbo in the event of inaccuracies in representations and warranties or if it fails to perform agreements and covenants provided for in the agreement of purchase and sale. The terms of the indemnification provisions vary in duration and may extend for an unlimited period of time. The indemnification provisions could result in future cash outflows and statement of earnings charges. The Company is unable to reasonably estimate its total maximum potential liability as certain indemnification provisions do not provide for a maximum potential amount and the amounts are dependent on the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time.

The results of discontinued operations presented in the comparative year consolidated statement of earnings were as follows:

| | | 2009[1] |
|---|---|---|
| Sales | $ | 145 |
| Operating income | | 9 |
| Gain on disposal[2] | | 939 |
| Interest income and other financing charges[3] | | (1) |
| Earnings before the following: | | 949 |
| Income taxes | | 41 |
| Earnings from discontinued operations | $ | 908 |

(1) Reflects results of the U.S. fresh bakery business up to the date of sale, January 21, 2009, and the gain on disposal.
(2) Net of the reclassification of the cumulative foreign currency translation loss of $110 associated with the U.S. fresh bakery business that was previously reflected in accumulated other comprehensive loss (see note 25).
(3) In calculating earnings from discontinued operations, no general interest expense has been allocated to these operations.

The cash flows from discontinued operations presented in the comparative year consolidated cash flow statement were as follows:

| | | 2009[1] |
|---|---|---|
| Cash flows used in operations | $ | (105) |
| Cash flows from investing | | 3,107 |
| Cash flows from financing | | 15 |
| Cash flows from discontinued operations | $ | 3,017 |

(1) Reflects the proceeds received on the sale and the cash flows of the U.S. fresh bakery business up to the date of sale, January 21, 2009.

## 5. DISTRIBUTION NETWORK COSTS

During 2010, Loblaw announced changes to its distribution network in Quebec. In connection with these changes a certain distribution centre was closed and an asset impairment charge in 2010 of $26 was recorded in operating income as the carrying value of the facility exceeded the fair value. In addition, employee termination charges and other costs of $16 were recorded in operating income. As at December 31, 2010, $7 was recorded on the consolidated balance sheet in accounts payable and accrued liabilities related to these charges.

## 6. INTEREST EXPENSE AND OTHER FINANCING CHARGES

The components of interest expense and other financing charges were as follows:

| | **2010** | 2009 |
|---|---|---|
| Interest on long term debt | **$ 373** | $ 371 |
| Loss on redemption of debt (note 18) | | 49 |
| Interest expense on financial derivative instruments (note 26) | **2** | 3 |
| Other financing charges(1) | **42** | (33) |
| Net short term interest income (note 9) | **(21)** | (20) |
| Interest income on security deposits | **(1)** | (4) |
| Dividends on capital securities | **14** | 18 |
| Capitalized to fixed assets | **(21)** | (21) |
| Interest expense and other financing charges | **$ 388** | $ 363 |

(1) Other financing charges for 2010 includes a non-cash charge of $62 (2009 – non-cash income of $13) related to the fair value adjustment of Weston Holdings Limited's ("WHL"), a subsidiary of GWL, forward sale agreement for 9.6 million Loblaw common shares (note 26). The fair value adjustment of the forward contract is a non-cash item resulting from fluctuations in the market price of the underlying Loblaw common shares that WHL owns. WHL does not record any change in the market price associated with the Loblaw common shares it owns. Any cash paid under the forward contract could be offset by the sale of Loblaw common shares. Also included in other financing charges is forward accretion income of $37 (2009 – $36) and the forward fee of $17 (2009 – $16) associated with WHL's forward sale agreement.

During 2010, net interest expense of $356 (2009 – $403) was recorded related to the financial assets and financial liabilities not classified as held-for-trading. In addition, $17 (2009 – $19) of income from cash and cash equivalents and short term investments held primarily by Dunedin and certain of its affiliates and Glenhuron Bank Limited ("Glenhuron"), a wholly owned subsidiary of Loblaw, was recognized in net short term interest income.

Interest on debt and dividends on capital securities paid in 2010 was $475 (2009 – $511), and interest received on cash and cash equivalents, short term investments and security deposits in 2010 was $67 (2009 – $93).

## 7. INCOME TAXES

The effective income tax rate in the consolidated statements of earnings is reported at a rate different than the weighted average basic Canadian federal and provincial statutory income tax rate for the following reasons:

| | **2010** | 2009 |
|---|---|---|
| Weighted average basic Canadian federal and provincial statutory income tax rate | **30.0%** | 30.4% |
| Net (decrease) increase resulting from: | | |
| Earnings in jurisdictions taxed at rates different from the Canadian statutory income tax rates | **(1.7)** | (1.6) |
| Unrecognized benefit of foreign currency translation losses and impact of the reversal of cumulative foreign currency translation losses | **0.8** | 4.4 |
| Non-taxable and non-deductible amounts (including capital gains/losses and cash-settled stock options) | **2.8** | 8.5 |
| Impact of statutory income tax rate changes on future income tax balances | | (0.2) |
| Impact of resolution of certain income tax matters from a previous year and other | **1.9** | (1.4) |
| Effective income tax rate applicable to earnings from continuing operations before income taxes and minority interest | **33.8%** | 40.1% |

Net cash income taxes paid in 2010 were $336 (2009 – $299).

The cumulative effects of changes in Canadian federal and certain provincial statutory income tax rates on future income tax assets and liabilities are included in the consolidated financial statements at the time of substantive enactment. Accordingly, in 2009 a net reduction of $1 to the future income tax expense was recognized as a result of the changes in the Canadian federal and certain provincial statutory income tax rates.

The income tax effects of temporary differences that gave rise to significant portions of the future income tax assets (liabilities) were as follows:

| | **2010** | 2009 |
|---|---|---|
| Accounts payable and accrued liabilities | **$ 55** | $ 72 |
| Other liabilities | **157** | 166 |
| Losses carried forward (expiring 2015 to 2029) | **117** | 121 |
| Fixed assets | **(317)** | (295) |
| Goodwill and intangible assets | **(2)** | 11 |
| Other assets | **(248)** | (217) |
| Other | **21** | 21 |
| Net future income tax liabilities | **$ (217)** | $ (121) |

| | **2010** | 2009 |
|---|---|---|
| Recorded on the consolidated balance sheets as follows: | | |
| **Future income tax assets** | | |
| Current | **$ 61** | $ 87 |
| Non-current | **33** | 61 |
| | **94** | 148 |
| **Future income tax liability** | | |
| Non-current | **(311)** | (269) |
| | **(311)** | (269) |
| Net future income tax liabilities | **$ (217)** | $ (121) |

## 8. BASIC AND DILUTED NET EARNINGS PER COMMON SHARE FROM CONTINUING OPERATIONS

| | **2010** | 2009 |
|---|---|---|
| Net earnings from continuing operations | **$ 452** | $ 127 |
| Prescribed dividends on preferred shares in share capital | **(44)** | (44) |
| Net earnings from continuing operations available to common shareholders for basic earnings per share | **$ 408** | $ 83 |
| Reduction in net earnings due to dilution at Loblaw | **(2)** | (2) |
| Net earnings from continuing operations available to common shareholders for diluted earnings per share | **$ 406** | $ 81 |
| Weighted average common shares outstanding (in millions) (note 22) | **129.1** | 129.1 |
| Dilutive effect of stock-based compensation(1) (in millions) | | |
| Diluted weighted average common shares outstanding (in millions) | **129.1** | 129.1 |
| Basic net earnings per common share from continuing operations ($) | **$ 3.16** | $ 0.64 |
| Diluted net earnings per common share from continuing operations ($) | **$ 3.14** | $ 0.63 |

(1) Stock options outstanding with an exercise price greater than the average market price of GWL's common shares are not included in the computation of diluted net earnings per common share from continuing operations. Accordingly, for 2010, 425,684 (2009 – 1,252,630) stock options, with a weighted average price of $100.64 (2009 – $85.92), were excluded from the computation of diluted net earnings per common share from continuing operations.

## 9. CASH AND CASH EQUIVALENTS, SHORT TERM INVESTMENTS AND SECURITY DEPOSITS

The components of cash and cash equivalents, short term investments and security deposits as at December 31, 2010 and December 31, 2009 were as follows:

| | | | | 2010 |
|---|---|---|---|---|
| | Cash and Cash Equivalents | Short Term Investments | Security Deposits | Total |
| Cash | **$ 200** | | | **$ 200** |
| Government treasury bills | **244** | **$ 1,642** | **$ 296** | **2,182** |
| Corporate commercial paper | **427** | **1,227** | | **1,654** |
| Banker's acceptances | **252** | | **92** | **344** |
| Bank term deposits | **287** | | | **287** |
| Other | **118** | **365** | **47** | **530** |
| Total | **$ 1,528** | **$ 3,234** | **$ 435** | **$ 5,197** |

| | | | | 2009 |
|---|---|---|---|---|
| | Cash and Cash Equivalents | Short Term Investments | Security Deposits | Total |
| Cash | $ 295 | | $ 51 | $ 346 |
| Government treasury bills | 265 | $ 2,305 | 277 | 2,847 |
| Corporate commercial paper | 405 | 833 | | 1,238 |
| Banker's acceptances | 348 | | | 348 |
| Bank term deposits | 70 | | | 70 |
| Other | 152 | 233 | 20 | 405 |
| Total | $ 1,535 | $ 3,371 | $ 348 | $ 5,254 |

As at December 31, 2010 and December 31, 2009, U.S. $2,151 and U.S. $2,220 (December 31, 2010 – $2,147; December 31, 2009 – $2,338), respectively, was included in cash and cash equivalents, short term investments and security deposits on the consolidated balance sheets.

The following is a summary of foreign currency translation losses as a result of translating U.S. dollar denominated cash and cash equivalents, short term investments and security deposits:

| | 2010 | 2009 |
|---|---|---|
| Loblaw(1) | **$ 52** | $ 146 |
| The Company (excluding Loblaw)(2) | **62** | 181 |
| Consolidated | **$ 114** | $ 327 |

(1) Includes losses of $8 (2009 – $27) related to cash and cash equivalents for 2010.

During 2010, the loss on cash and cash equivalents, short term investments and security deposits was offset in operating income and other comprehensive (loss) income by the foreign currency translation gain of $52 (2009 – $145) on Loblaw's cross currency swaps (see note 26).

(2) Includes losses of $9 (2009 – $44) related to cash and cash equivalents for 2010.

During 2010, foreign currency translation losses associated with the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates of $56 (2009 – $177) were recognized in operating income (see note 32). The remaining foreign currency translation losses as a result of translating U.S. dollar denominated net assets, including cash and cash equivalents, short term investments and security deposits held in self-sustaining foreign operations are recognized in other comprehensive (loss) income (see note 25).

## 10. ACCOUNTS RECEIVABLE

The components of accounts receivable as at December 31, 2010 and December 31, 2009 were as follows:

| | 2010 | 2009 |
|---|---|---|
| Credit card receivables | **$ 2,015** | $ 2,128 |
| Amount securitized | **(1,635)** | (1,725) |
| Net credit card receivables | **380** | 403 |
| Other receivables | **440** | 448 |
| Accounts receivable | **$ 820** | $ 851 |

**Credit Card Receivables**

PC Bank securitizes certain credit card receivables as described in note 1.

In 2010, $600 (2009 – nil) of credit card receivables were securitized which yielded a net loss of $3 (2009 – nil). During 2010, PC Bank repurchased $690 (2009 – $50) of the co-ownership interest in the securitized receivables from several independent trusts. A portion of the securitized receivables that is held by an independent trust facility was renewed for two years during 2010. During 2010, PC Bank received income of $245 (2009 – $235) related primarily to PC Bank's right to excess cash flows earned on the securitized credit card receivables. A decrease in servicing liability of nil (2009 – $3) was recognized during the year on securitization and as at year end 2010, the servicing liability was $8 (2009 – $8). The independent trusts' recourse to PC Bank's assets is limited to PC Bank's excess collateral of $114 (2009 – $121) as well as standby letters of credit for $48 (2009 – $116) based on a portion of the securitized amount (see note 28).

On March 17, 2011, the five year $500 of senior and subordinated notes issued by *Eagle Credit Card Trust* ("Eagle") will mature. In conjunction with this upcoming maturity, Loblaw accumulated $167 of cash on December 1, 2010. Subsequent to the end of 2010, Loblaw accumulated $167 in January 2011 and a further $166 in February 2011. In addition, subsequent to the end of 2010, Loblaw increased its securitization of accounts receivable by approximately $230 under one of the independent trusts and expects to securitize further amounts coincident with the maturity of the Eagle Notes.

Net credit loss experience of $16 (2009 – $21) includes $110 (2009 – $139) of credit losses on the total portfolio of credit card receivables net of credit losses of $94 (2009 – $118) relating to securitized credit card receivables.

The following table displays the sensitivity of the current fair value of the retained interest to an immediate 10% and 20% adverse change in the 2010 key assumptions. The sensitivity analysis provided in the table is hypothetical and should be used with caution. The sensitivities of each key assumption have been calculated independently of any changes in other key assumptions. Actual experience may result in changes in a number of key assumptions simultaneously. Changes in one factor may result in changes in another, which could amplify or reduce the impact of such assumptions.

| | | Change in assumptions | |
|---|---|---|---|
| | **2010** | **10%** | **20%** |
| Carrying value of retained interest | **$ 21** | | |
| Payment rate (monthly) | **49%** | **$ (2)** | **$ (3)** |
| Weighted average life (years) | **0.7** | | |
| Expected credit losses | **5.67%** | **$ (1)** | **$ (3)** |
| Annual discount rate applied to residual cash flows | **9.13%** | | |
| Net yield | **14.11%** | **$ (4)** | **$ (8)** |
| Cost of funds | **2.60%** | **$ (1)** | **$ (1)** |

The details on the cash flows from securitization are as follows:

| | 2010 | 2009 |
|---|---|---|
| Proceeds from new securitizations | **$ 600** | |
| Repurchase of co-ownership interests | **$ (690)** | $ (50) |
| Net cash flows received on retained interest | **$ 250** | $ 244 |

**Other Receivables**

Other receivables consist mainly of receivables from Loblaw's vendors, independent franchisees, associated stores and independent accounts and receivables from Weston Foods customers.

**Aging of Receivables**

The following is an aging of the Company's credit card and other receivables as at December 31, 2010 and December 31, 2009:

| | 2010 | | | | 2009 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Current** | **> 30 days** | **> 60 days** | **Total** | Current | > 30 days | > 60 days | Total |
| Credit card receivables | **$ 370** | **$ 3** | **$ 7** | **$ 380** | $ 390 | $ 4 | $ 9 | $ 403 |
| Other receivables | **361** | **27** | **52** | **440** | 342 | 55 | 51 | 448 |
| Total | **$ 731** | **$ 30** | **$ 59** | **$ 820** | $ 732 | $ 59 | $ 60 | $ 851 |

Credit card receivables that are past due but not impaired totaled $10 (2009 – $13) as at year end 2010 as they are either less than 90 days past due or are reasonably expected to remedy the past due status. Any credit card receivable balances that are 180 days in arrears or where the likelihood of collection is considered remote are written off. Credit risk on the credit card receivables is managed as described in note 28.

Other receivables that are past due but not impaired totaled $21 (2009 – $54) as at year end 2010.

## 11. ALLOWANCES FOR RECEIVABLES

The allowance for receivables recorded on the consolidated balance sheets is maintained at a level which is considered adequate to absorb credit related losses on credit card receivables and losses on other receivables. The receivables for PC Bank credit card, Loblaw associated stores and independent accounts and Weston Foods customers are presented net of allowances in accounts receivable on the consolidated balance sheets. A continuity of the Company's allowances for receivables is as follows:

| **Credit Card Receivables** | 2010 | 2009 |
|---|---|---|
| Allowances, beginning of year | **$ (16)** | $ (15) |
| Provision for losses | **(16)** | (21) |
| Recoveries | **(11)** | (9) |
| Write-offs | **27** | 29 |
| Allowances, end of year | **$ (16)** | $ (16) |

| **Other Receivables** | 2010 | 2009 |
|---|---|---|
| Allowances, beginning of year | **$ (27)** | $ (32) |
| Provision for losses | **(108)** | (102) |
| Write-offs | **112** | 107 |
| Allowances, end of year | **$ (23)** | $ (27) |

## 12. INVENTORIES

The components of inventories as at December 31, 2010 and December 31, 2009 were as follows:

| | 2010 | 2009 |
|---|---|---|
| Raw materials and supplies | **$ 39** | $ 36 |
| Finished goods | **2,169** | 2,174 |
| Inventories | **$ 2,208** | $ 2,210 |

Cost of inventories sold includes $43 (2009 – $44) of depreciation in 2010.

For inventories recorded as at year end 2010, Loblaw recorded $17 (2009 – $15) as an expense for the write-down of inventories below cost to net realizable value. There were no reversals of inventories written down previously that are no longer estimated to sell below cost.

## 13. FIXED ASSETS

The components of fixed assets as at December 31, 2010 and December 31, 2009 were as follows:

| | | | **2010** | | | 2009 |
|---|---|---|---|---|---|---|
| | **Cost** | **Accumulated Depreciation** | **Net Book Value** | Cost | Accumulated Depreciation | Net Book Value |
| Assets under construction | **$ 1,172** | | **$ 1,172** | $ 685 | | $ 685 |
| Land | **1,787** | | **1,787** | 1,862 | | 1,862 |
| Buildings | **6,183** | **$ 1,866** | **4,317** | 6,099 | $ 1,703 | 4,396 |
| Equipment and fixtures | **6,030** | **4,148** | **1,882** | 5,488 | 3,779 | 1,709 |
| Buildings and leasehold improvements | **631** | **335** | **296** | 583 | 278 | 305 |
| | **15,803** | **6,349** | **9,454** | 14,717 | 5,760 | 8,957 |
| Capital leases – buildings and equipment | **248** | **118** | **130** | 180 | 117 | 63 |
| Fixed assets | **$ 16,051** | **$ 6,467** | **$ 9,584** | $ 14,897 | $ 5,877 | $ 9,020 |

Included in land and buildings was $73 (2009 – $58) of properties held for sale. Loblaw recorded fixed asset impairment charges of $28 (2009 – $27), other related charges of $18 (2009 – $19) and an impairment charge of $26 (2009 – nil) related to the closure of a distribution centre in Quebec (see note 5). In addition, Weston Foods recorded a fixed asset impairment charge of $1 (2009 – $1) and accelerated depreciation of nil (2009 – $2).

During 2009, Loblaw completed the purchase of a distribution centre for consideration of $140 plus closing costs. Loblaw assumed a mortgage of $96 in connection with the purchase, of which $2 (2009 – $2) is included in long term debt due within one year (see note 18).

## 14. GOODWILL AND INTANGIBLE ASSETS

Changes in the carrying value of goodwill and intangible assets were as follows:

| | | | **2010** | | | 2009 |
|---|---|---|---|---|---|---|
| | **Weston Foods** | **Loblaw** | **Total** | Weston Foods | Loblaw | Total |
| Goodwill, beginning of year | **$ 92** | **$ 1,103** | **$ 1,195** | $ 169 | $ 947 | $ 1,116 |
| Goodwill acquired during the year[(1)] | **165** | **13** | **178** | | 156 | 156 |
| Adjusted purchase price allocation (note 3) | | **(2)** | **(2)** | | | |
| Goodwill impairment[(2)] | | | | (73) | | (73) |
| Impact of foreign currency translation | **(2)** | | **(2)** | (4) | | (4) |
| Goodwill, end of year | **255** | **1,114** | **1,369** | 92 | 1,103 | 1,195 |
| Trademarks and brand names | **20** | **51** | **71** | 13 | 51 | 64 |
| Other intangible assets[(3)] | **95** | **36** | **131** | 5 | 32 | 37 |
| Goodwill and intangible assets | **$ 370** | **$ 1,201** | **$ 1,571** | $ 110 | $ 1,186 | $ 1,296 |

(1) Goodwill acquired during 2010 includes $63, $95 and $7 in connection with Weston Foods' acquisitions of ACE, Keystone and the frozen bakery manufacturing facility, respectively, and $12 (2009 – $9) related to the Company's participation in the Loblaw DRIP. During 2009, Loblaw acquired T&T which resulted in goodwill of $131. During 2010, Loblaw finalized the purchase price allocation which resulted in a reduction of goodwill of $2. Goodwill acquired during 2009 also includes $11 related to Loblaw's repurchase of 1.7 million of its common shares and $5 related to Loblaw's acquisition of franchisee stores (see note 3).

(2) Weston Foods reorganized its remaining operations subsequent to the disposition of the U.S. fresh bakery business in the first quarter of 2009 resulting in a write-down of goodwill related to the biscuits, cookies, cones and wafers business.

(3) Year end 2010 includes the customer relationships acquired of $28 and $66 in connection with Weston Food's acquisition of ACE and Keystone respectively, the negative impact of foreign currency translation of $2 (2009 – nil) and amortization of $2 (2009 – nominal).

The intangible assets acquired as part of the acquisition of ACE of $35 consist of $28 for customer relationships and $7 for brands subject to amortization over their estimated useful lives of 20 and 30 years, respectively.

The intangible asset acquired as part of the acquisition of Keystone of $66 consists of customer relationships subject to amortization over 20 years.

The trademark and brand names recorded by Loblaw are indefinite life intangible assets relating to the acquisition of T&T. The remaining intangible assets are definite life intangible assets and are being amortized over their estimated useful lives ranging from 10 to 30 years.

During the fourth quarters of 2010 and 2009, the Company performed its annual goodwill and indefinite life intangible assets impairment tests and determined that there was no impairment to the carrying values of goodwill and indefinite life intangible assets.

## 15. OTHER ASSETS

The components of other assets as at December 31, 2010 and December 31, 2009 were as follows:

| | 2010 | 2009 |
|---|---|---|
| WHL's unrealized equity forward receivable (note 26) | **$ 421** | $ 446 |
| Accrued benefit plan asset (note 16) | **427** | 381 |
| Franchise investments and other receivables | **203** | 225 |
| Unrealized cross currency swaps receivable (note 26) | **172** | 142 |
| Other | **67** | 72 |
| Other assets | **$ 1,290** | $ 1,266 |

## 16. EMPLOYEE FUTURE BENEFITS

### Pension and Other Benefit Plans

The Company sponsors a number of pension plans, including funded defined benefit pension plans, defined contribution pension plans and supplemental unfunded arrangements providing pension benefits in excess of statutory limits. Certain obligations of the Company to these supplemental pension arrangements are secured by standby letters of credit issued by major Canadian chartered banks. The Company's defined benefit pension plans are predominantly non-contributory and these benefits are, in general, based on career average earnings.

In Canada, a national defined contribution pension plan for salaried employees was introduced by the Company during 2006. All eligible salaried employees were given the option to join this plan and convert their past accrued pension benefits or to remain in their existing defined benefit pension plans. All new salaried employees participate only in the national defined contribution pension plan.

The Company also offers other employee benefit plans comprised of post-retirement and post-employment benefit plans which are generally unfunded and non-contributory. Post-retirement benefit plans include health care, life insurance and dental benefits during retirement, while post-employment benefit plans include long term disability benefits and the continuation of health and dental benefits while on disability. Employees eligible for post-retirement benefits are those who retire at certain retirement ages having met certain service requirements and employees eligible for post-employment benefits are those on long term disability leave. The majority of post-retirement health care plans for current and future retirees include a limit on the total benefits payable by the Company.

The Company also contributes to various multi-employer pension plans.

The accrued benefit plan obligations and the fair value of the benefit plan assets were determined using a September 30 measurement date for accounting purposes.

### Funding of Pension and Other Benefit Plans

The most recent actuarial valuations of the Canadian defined benefit pension plans for funding purposes ("funding valuations") were performed as at December 31, 2007 and December 31, 2009. The Company is required to file funding valuations at least every three years; accordingly, the next funding valuations will be performed as at December 31, 2010 and 2012, respectively. The most recent funding valuations of the United States defined benefit pension plans were as at January 1, 2010. The Company is required to file United States funding valuations every year; accordingly, the next required funding valuations will be as at January 1, 2011.

Total cash paid or payable by the Company for 2010, consisting of contributions to funded defined benefit pension plans, defined contribution pension plans, multi-employer pension plans and benefits paid directly to beneficiaries of the supplemental unfunded defined benefit pension plans and other benefit plans, were $231 (2009 – $217).

**Pension and Other Benefit Plans Status**

Information on the Company's defined benefit pension plans and other benefit plans, in aggregate, was as follows:

| | | | **2010** | | | 2009 |
|---|---|---|---|---|---|---|
| | **Pension Benefit Plans** | **Other Benefit Plans[(1)]** | **Total** | Pension Benefit Plans | Other Benefit Plans[(1)] | Total |
| **Benefit Plan Assets** | | | | | | |
| Fair value, beginning of year | **$ 1,372** | **$ 8** | **$ 1,380** | $ 1,311 | $ 21 | $ 1,332 |
| Actual return on plan assets | **111** | | **111** | 58 | 1 | 59 |
| Employer contributions | **126** | **25** | **151** | 130 | 13 | 143 |
| Employee contributions | **3** | | **3** | 3 | | 3 |
| Benefits paid | **(95)** | **(32)** | **(127)** | (123) | (27) | (150) |
| Other, including impact of foreign currency translation | **(3)** | | **(3)** | (7) | | (7) |
| Fair value, end of year | **$ 1,514** | **$ 1** | **$ 1,515** | $ 1,372 | $ 8 | $ 1,380 |
| **Accrued Benefit Plan Obligations** | | | | | | |
| Balance, beginning of year | **$ 1,566** | **$ 340** | **$ 1,906** | $ 1,483 | $ 343 | $ 1,826 |
| Current service cost | **50** | **28** | **78** | 48 | 34 | 82 |
| Interest cost | **89** | **19** | **108** | 89 | 20 | 109 |
| Benefits paid | **(95)** | **(32)** | **(127)** | (123) | (27) | (150) |
| Actuarial loss (gain) | **174** | **23** | **197** | 70 | (28) | 42 |
| Contractual termination benefits[(2)] | **3** | | **3** | | | |
| Plan amendments | | | | 8 | | 8 |
| Other, including impact of foreign currency translation | **(3)** | **(1)** | **(4)** | (9) | (2) | (11) |
| Balance, end of year | **$ 1,784** | **$ 377** | **$ 2,161** | $ 1,566 | $ 340 | $ 1,906 |
| **Deficit of Plan Assets Versus Plan Obligations** | **$ (270)** | **$ (376)** | **$ (646)** | $ (194) | $ (332) | $ (526) |
| Unamortized past service costs | **7** | **(2)** | **5** | 8 | (2) | 6 |
| Unamortized net actuarial loss | **622** | **96** | **718** | 505 | 73 | 578 |
| Net accrued benefit plan asset (liability) | **$ 359** | **$ (282)** | **$ 77** | $ 319 | $ (261) | $ 58 |
| **Recorded on the consolidated balance sheets as follows:** | | | | | | |
| Other assets (note 15) | **$ 427** | | **$ 427** | $ 381 | | $ 381 |
| Other liabilities (note 19) | **(68)** | **$ (282)** | **(350)** | (62) | $ (261) | (323) |
| Net accrued benefit plan asset (liability) | **$ 359** | **$ (282)** | **$ 77** | $ 319 | $ (261) | $ 58 |

(1) Other benefit plans include post-retirement and post-employment benefit plans.

(2) Contractual termination benefits resulted from distribution centre closures in 2010.

### Funded Status of Plans in Deficit

Included in the accrued benefit plan obligations and the fair value of benefit plan assets at year end are the following amounts in respect of plans with accrued benefit plan obligations in excess of benefit plan assets:

| | **2010** | | 2009 | |
|---|---|---|---|---|
| | **Pension Benefit Plans** | **Other Benefit Plans[1]** | Pension Benefit Plans | Other Benefit Plans[1] |
| Fair Value of Benefit Plan Assets | **$ 1,495** | **$ 1** | $ 1,293 | $ 8 |
| Accrued Benefit Plan Obligations | **(1,765)** | **(377)** | (1,489) | (340) |
| Deficit of Plan Assets versus Plan Obligations | **$ (270)** | **$ (376)** | $ (196) | $ (332) |

(1) Other benefit plans include post-retirement and post-employment benefit plans.

### Asset Allocations

The benefit plan assets are held in trust and at September 30 consisted of the following asset categories:

| Percentage of Plan Assets | **2010** | | 2009 | |
|---|---|---|---|---|
| Asset Category | **Pension Benefit Plans** | **Other Benefit Plans[1]** | Pension Benefit Plans | Other Benefit Plans[1] |
| Equity securities | **57%** | | 54% | |
| Debt securities | **41%** | | 44% | 98% |
| Cash and cash equivalents | **2%** | **100%** | 2% | 2% |
| Total | **100%** | **100%** | 100% | 100% |

(1) Other benefit plans include post-employment benefit plans.

Pension benefit plan assets include securities issued by Loblaw having a fair value of $4 (2009 – $3) as at September 30, 2010. Pension benefit plan assets do not include any GWL securities. Other benefit plan assets do not include any GWL or Loblaw securities.

## Pension and Other Benefit Plans Cost

The total net cost for the Company's benefit plans and multi-employer pension plans was as follows:

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | **Pension Benefit Plans** | **Other Benefit Plans[(1)]** | Pension Benefit Plans | Other Benefit Plans[(1)] |
| Current service cost, net of employee contributions | **$ 47** | **$ 28** | $ 45 | $ 34 |
| Interest cost on plan obligations | **89** | **19** | 89 | 20 |
| Actual return on plan assets | **(111)** | | (58) | (1) |
| Actuarial loss (gain) | **174** | **23** | 70 | (28) |
| Contractual termination benefits[(2)] | **3** | | | |
| Plan amendments | | | 8 | |
| Defined benefit plan cost, before adjustments to recognize the long term nature of employee future benefit costs | **202** | **70** | 154 | 25 |
| Excess (shortfall) of actual return over expected return on plan assets | **21** | | (34) | |
| (Shortfall) excess of amortized net actuarial loss (gain) over actual actuarial loss (gain) on accrued benefit obligation | **(141)** | **(23)** | (44) | 32 |
| Excess (shortfall) of amortized past service costs over actual past service costs | **1** | | (6) | |
| Net defined benefit plan cost | **83** | **47** | 70 | 57 |
| Defined contribution plan cost | **19** | | 17 | |
| Multi-employer pension plan cost | **61** | | 57 | |
| Net benefit plan cost | **$ 163** | **$ 47** | $ 144 | $ 57 |

(1) Other benefit plans include post-retirement and post-employment benefit plans.
(2) Contractual termination benefits resulted from distribution centre closures in 2010.

## Plan Assumptions

The significant annual weighted average actuarial assumptions used in calculating the Company's accrued benefit plan obligations as at the measurement date of September 30 and the net defined benefit plan cost for the year were as follows:

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | **Pension Benefit Plans** | **Other Benefit Plans[(1)]** | Pension Benefit Plans | Other Benefit Plans[(1)] |
| **Accrued Benefit Plan Obligations** | | | | |
| Discount rate | **5.0%** | **4.8%** | 5.7% | 5.5% |
| Rate of compensation increase | **3.5%** | | 3.5% | |
| **Net Defined Benefit Plan Cost** | | | | |
| Discount rate | **5.7%** | **5.5%** | 6.0% | 5.9% |
| Expected long term rate of return on plan assets | **6.7%** | **5.0%** | 7.3% | 5.0% |
| Rate of compensation increase | **3.5%** | | 3.5% | |

(1) Other benefit plans include post-retirement and post-employment benefit plans.

The growth rate of health care costs, primarily drug and other medical costs for other benefit plans, for the net benefit plan cost was estimated at 9.0% (2009 – 9.5%) and is assumed to gradually decrease to 5.0% by 2015 (2009 – 5.0% by 2015), remaining at that level thereafter.

**Sensitivity of Key Assumptions**

The following table outlines the key assumptions for 2010 and the sensitivity of a 1% change in each of these assumptions on the accrued benefit plan obligations and on the benefit plan cost for defined benefit pension plans and other benefit plans. The table reflects the impact on the current service and interest cost components for the discount rate and expected growth rate of health care costs assumptions.

The sensitivity analysis provided in the table is hypothetical and should be used with caution. The sensitivities of each key assumption have been calculated independently of any changes in other key assumptions. Actual experience may result in changes in a number of key assumptions simultaneously. Changes in one factor may result in changes in another, which could amplify or reduce the impact of such assumptions.

| | | Pension Benefit Plans | | Other Benefit Plans(1) | |
|---|---|---|---|---|---|
| | | Accrued Benefit Plan Obligations | Benefit Plan Cost(2) | Accrued Benefit Plan Obligations | Benefit Plan Cost(2) |
| Expected long term rate of return on plan assets | | | **6.7%** | | **5.0%** |
| Impact of: | 1% increase | **n/a** | **$ (14)** | **n/a** | **–** |
| | 1% decrease | **n/a** | **$ 14** | **n/a** | **–** |
| Discount rate | | **5.0%** | **5.7%** | **4.8%** | **5.5%** |
| Impact of: | 1% increase | **$ (228)** | **$ (7)** | **$ (42)** | **$ (2)** |
| | 1% decrease | **$ 263** | **$ 7** | **$ 48** | **$ 2** |
| Expected growth rate of health care costs(3) | | | | **8.0%** | **9.0%** |
| Impact of: | 1% increase | **n/a** | **n/a** | **$ 37** | **$ 4** |
| | 1% decrease | **n/a** | **n/a** | **$ (32)** | **$ (4)** |

n/a – not applicable

(1) Other benefit plans include post-retirement and post-employment benefit plans.

(2) Discount rate and expected growth rate of health care costs sensitivity is for current service and interest costs only.

(3) Gradually decreasing to 5.0% by 2015 (2009 – 5.0% by 2015) for the accrued benefit plan obligation and the benefit plan cost and remaining at that level thereafter.

## 17. SHORT TERM DEBT

Included in short term debt are GWL's Series B Debentures, due on demand, of $336 (2009 – $300) (see note 18).

Loblaw has an $800 committed credit facility expiring in March 2013 provided by a syndicate of third-party lenders which contains certain financial covenants (see note 23). This facility is a potential source of Loblaw's short term funding requirements and permits borrowings having up to a 180-day term. Interest is based on a floating rate, primarily the bankers' acceptance rate and an applicable margin based on Loblaw's credit rating. As at December 31, 2010 and 2009, Loblaw had not drawn on the committed credit facility.

## 18. LONG TERM DEBT

The components of long term debt as at December 31, 2010 and December 31, 2009 were as follows:

| | 2010 | 2009 |
|---|---|---|
| **George Weston Limited** | | |
| Debentures | | |
| Series B, current rate 1.79%, due on demand(i) | **$ 336** | $ 300 |
| Series A, 7.00%, due 2031(i) | **466** | 466 |
| Notes | | |
| 6.45%, due 2011 | **300** | 300 |
| 5.05%, due 2014 | **200** | 200 |
| 7.10%, due 2032 | **150** | 150 |
| 6.69%, due 2033 | **100** | 100 |
| **Loblaw Companies Limited** | | |
| Notes | | |
| 7.10%, due 2010(ii) | | 300 |
| 6.50%, due 2011 | **350** | 350 |
| 5.40%, due 2013 | **200** | 200 |
| 6.00%, due 2014 | **100** | 100 |
| 4.85%, due 2014(iii) | **350** | 350 |
| 7.10%, due 2016 | **300** | 300 |
| 5.22%, due 2020(iii) | **350** | |
| 6.65%, due 2027 | **100** | 100 |
| 6.45%, due 2028 | **200** | 200 |
| 6.50%, due 2029 | **175** | 175 |
| 11.40%, due 2031 | | |
| Principal | **151** | 151 |
| Effect of coupon repurchase | **(81)** | (67) |
| 6.85%, due 2032 | **200** | 200 |
| 6.54%, due 2033 | **200** | 200 |
| 8.75%, due 2033 | **200** | 200 |
| 6.05%, due 2034 | **200** | 200 |
| 6.15%, due 2035 | **200** | 200 |
| 5.90%, due 2036 | **300** | 300 |
| 6.45%, due 2039 | **200** | 200 |
| 7.00%, due 2040 | **150** | 150 |
| 5.86%, due 2043 | **55** | 55 |
| Private placement notes | | |
| 6.48%, due 2013 (U.S. $150) | **150** | 158 |
| 6.86%, due 2015 (U.S. $150) | **150** | 158 |
| Long term debt secured by mortgage | | |
| 5.49%, due 2018 (note 13) | **93** | 96 |
| Guaranteed investment certificates, due 2011 – 2015 (1.55% – 3.15%)(iv) | **18** | |
| VIE loans payable(v) (note 30) | **202** | 163 |
| Capital lease obligations(v) (note 20) | **132** | 64 |
| Other | **1** | 1 |
| Total long term debt | **6,198** | 6,020 |
| Less – amount due within one year | **(733)** | (343) |
| – amount due on demand (note 17) | **(336)** | (300) |
| | **$ 5,129** | $ 5,377 |

The schedule of repayment of long term debt, inclusive of VIE and other debt, based on maturity, excluding the amount due on demand, is as follows: 2011 – $733; 2012 – $77; 2013 – $419; 2014 – $682; 2015 – $182; thereafter – $3,769.

*(i)* During 2010, GWL issued an additional $36 (2009 – $37) of Series B Debentures due on demand, which are at a current weighted average interest rate of 1.79%. The Series A, 7.00% and Series B Debentures are secured by a pledge of 9.6 million Loblaw common shares.

*(ii)* During 2010, Loblaw's $300 7.10% Medium Term Notes ("MTN") due May 11, 2010 matured and was repaid.

*(iii)* During 2010, Loblaw issued $350 principal amount of unsecured MTN, Series 2-B pursuant to its MTN, Series 2 program. The Series 2-B notes pay a fixed rate of interest of 5.22% payable semi-annually commencing on December 18, 2010 until maturity on June 18, 2020. During 2009, Loblaw issued $350 principal amount of unsecured MTN, Series 2-A which pay a fixed rate of interest of 4.85% payable semi-annually. The Series 2-A and 2-B notes are subject to certain covenants and are unsecured obligations of Loblaw and rank equally with all the unsecured indebtedness of Loblaw that has not been subordinated. The Series 2-A and 2-B notes may be redeemed at the option of Loblaw, in whole at any time or in part from time to time, upon not less than 30 days and not more than 60 days notice to the holders of the notes.

*(iv)* During the third quarter of 2010, PC Bank began accepting deposits under a new Guaranteed Investment Certificate ("GIC") program. The GICs, which are sold through independent brokers, are issued with fixed terms ranging from 12 to 60 months and are non-redeemable prior to maturity. Individual balances up to $100,000 are Canada Deposit Insurance Corporation insured. As at year end 2010, $18 was recorded as long term debt on the consolidated balance sheet of which $5 was due within one year.

*(v)* Pursuant to the requirements of AcG 15, the consolidated balance sheet as at year end 2010 includes $221 (2009 – $181) of loans payable and capital lease obligations of VIEs consolidated by the Company, $39 (2009 – $37) of which is due within one year.

During 2009, GWL's $250 5.90% MTN due February 5, 2009 and Loblaw's $125 5.75% MTN due January 22, 2009 matured and were repaid.

During 2009, GWL repurchased the 12.70% Promissory Notes, due 2030, for an aggregate purchase price of $73. As a result, GWL recorded a loss of $49 in interest expense and other financing charges (see note 6).

Subsequent to the end of 2010, Loblaw's $350 6.50% MTN due January 19, 2011 matured and was repaid.

See note 27 for the fair value of long term debt.

## 19. OTHER LIABILITIES

The components of other liabilities as at December 31, 2010 and December 31, 2009 were as follows:

| | **2010** | 2009 |
|---|---|---|
| Accrued benefit plan liability (note 16) | **$ 350** | $ 323 |
| Accrued insurance liabilities | **68** | 83 |
| Asset retirement obligation | **12** | 11 |
| Stock-based compensation liability (note 24) | **63** | 26 |
| Unrealized interest rate swap liability (note 26) | **24** | 31 |
| Deferred vendor allowances | **40** | 48 |
| Other | **98** | 95 |
| Other liabilities | **$ 655** | $ 617 |

Included in other above is the Loblaw liability associated with the preferred shares issued by T&T (see note 3).

Total accrued insurance liabilities were $91 (2009 – $111), of which $68 (2009 – $83) was included in other liabilities and $23 (2009 – $28) in accounts payable and accrued liabilities. Included in total accrued insurance liabilities of $91 (2009 – $111) were $52 (2009 – $69) of United States workers' compensation liabilities. The related cost and accrued workers' compensation liabilities are based on actuarial valuations which are dependent on assumptions determined by management. The discount rate used in determining the 2010 workers' compensation cost and liability was 4.0% (2009 – 4.0%). The total workers' compensation liability is equal to the ultimate actuarial loss estimate less any actual losses paid to date. Any change in the workers' compensation liability is recognized immediately in operating income.

The United States workers' compensation cost associated with the workers' compensation liability was $5 in 2010 (2009 – $3).

## 20. LEASES

### As Lessee

Future minimum lease payments relating to the Company's operating leases are as follows:

| | Payments due by year | | | | | | **2010** | 2009 |
|---|---|---|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | 2014 | 2015 | Thereafter | **Total** | Total |
| Operating lease payments | $ 229 | $ 209 | $ 186 | $ 163 | $ 134 | $ 645 | **$ 1,566** | $ 1,555 |
| Sub-lease income | (37) | (34) | (31) | (26) | (18) | (76) | **(222)** | (255) |
| Net operating lease payments | $ 192 | $ 175 | $ 155 | $ 137 | $ 116 | $ 569 | **$ 1,344** | $ 1,300 |

### As Lessor

Fixed assets on the consolidated balance sheets include cost of Loblaw properties which are currently leased to third parties of $885 (2009 – $755) and related accumulated depreciation of $230 (2009 – $211). Rental income for 2010 from these operating leases totaled $47 (2009 – $47) before income taxes and minority interest.

### Capital Leases

Capital lease obligations of $132 (2009 – $64) are included on the consolidated balance sheets as at year end (see note 18). The amount due within one year is $40 (2009 – $8).

## 21. CAPITAL SECURITIES ($ except where otherwise indicated)

Loblaw has 9.0 million 5.95% non-voting Second Preferred Shares, Series A outstanding (authorized – 12.0 million), which entitle the holder to a fixed cumulative preferred cash dividend of $1.4875 per share per annum which will, if declared, be payable quarterly. The Second Preferred Shares, Series A, are classified as capital securities and included in liabilities on the consolidated balance sheets. During 2010, the Board of Loblaw declared dividends of $1.4875 (2009 – $1.4875) per second preferred share which are included as a component of interest expense and other financing charges on the consolidated statements of earnings (see note 6).

On April 1, 2009, the 10.6 million GWL 5.15% non-voting preferred shares, Series II authorized and outstanding, which were presented as capital securities and included in current liabilities, were redeemed for cash of $25.00 per share, or $265 million in aggregate, plus accrued and unpaid dividends to but excluding April 1, 2009.

## 22. SHARE CAPITAL

The components of share capital as at December 31, 2010 and December 31, 2009 were as follows:

| | **2010** | 2009 |
|---|---|---|
| Common share capital | **$ 133** | $ 133 |
| Preferred shares, Series I | **228** | 228 |
| Preferred shares, Series III | **196** | 196 |
| Preferred shares, Series IV | **197** | 197 |
| Preferred shares, Series V | **196** | 196 |
| Share capital | **$ 950** | $ 950 |

**Common Share Capital (authorized – unlimited)**

The common shares issued and outstanding during the year were as follows:

| | **2010** | | 2009 | |
|---|---|---|---|---|
| | **Number of Common Shares** | **Common Share Capital** | Number of Common Shares | Common Share Capital |
| Issued and outstanding, beginning and end of year | **129,073,662** | **$ 133** | 129,073,662 | $ 133 |
| Weighted average outstanding | **129,073,662** | | 129,073,662 | |

**Preferred Shares, Series I (authorized – 10.0 million) ($)**

GWL has 9.4 million 5.80% non-voting Preferred Shares, Series I outstanding, with a face value of $235 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.45 per share per annum which will, if declared, be payable quarterly. GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**Preferred Shares, Series III (authorized – 10.0 million) ($)**

GWL has 8.0 million 5.20% non-voting Preferred Shares, Series III outstanding, with a face value of $200 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.30 per share per annum which will, if declared, be payable quarterly. On or after July 1, 2010, GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares as follows:

On or after July 1, 2010 at $26.00 per share, together with all accrued and unpaid dividends to the redemption date;
On or after July 1, 2011 at $25.75 per share, together with all accrued and unpaid dividends to the redemption date;
On or after July 1, 2012 at $25.50 per share, together with all accrued and unpaid dividends to the redemption date;
On or after July 1, 2013 at $25.25 per share, together with all accrued and unpaid dividends to the redemption date; and
On or after July 1, 2014 at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**Preferred Shares, Series IV (authorized – 8.0 million) ($)**
GWL has 8.0 million 5.20% non-voting Preferred Shares, Series IV outstanding, with a face value of $200 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.30 per share per annum which will, if declared, be payable quarterly. On or after October 1, 2010, GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares as follows:

On or after October 1, 2010 at $26.00 per share, together with all accrued and unpaid dividends to the redemption date;
On or after October 1, 2011 at $25.75 per share, together with all accrued and unpaid dividends to the redemption date;
On or after October 1, 2012 at $25.50 per share, together with all accrued and unpaid dividends to the redemption date;
On or after October 1, 2013 at $25.25 per share, together with all accrued and unpaid dividends to the redemption date; and
On or after October 1, 2014 at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**Preferred Shares, Series V (authorized – 8.0 million) ($)**
GWL has 8.0 million 4.75% non-voting Preferred Shares, Series V outstanding, with a face value of $200 million, which entitle the holder to a fixed cumulative preferred cash dividend of $1.1875 per share per annum which will, if declared, be payable quarterly. On or after July 1, 2011, GWL may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares as follows:

On or after July 1, 2011 at $26.00 per share, together with all accrued and unpaid dividends to the redemption date;
On or after July 1, 2012 at $25.75 per share, together with all accrued and unpaid dividends to the redemption date;
On or after July 1, 2013 at $25.50 per share, together with all accrued and unpaid dividends to the redemption date;
On or after July 1, 2014 at $25.25 per share, together with all accrued and unpaid dividends to the redemption date; and
On or after July 1, 2015 at $25.00 per share, together with all accrued and unpaid dividends to the redemption date.

At any time after issuance, GWL may, at its option, give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by GWL on a share-for-share basis on a date specified by GWL.

**Dividends**

The declaration and payment of dividends and the amounts thereof are at the discretion of the Board of Directors, which takes into account the Company's financial results, capital requirements, available cash flow and other factors the Board of Directors considers relevant from time to time. Over the long term, GWL's objective is for its common dividend payment ratio to be in the range of 20% to 25% of the prior year's basic net earnings per common share from continuing operations, adjusted as appropriate for items which are not regarded to be reflective of ongoing operations, giving consideration to the year end cash position, future cash flow requirements and investment opportunities. 2010 includes the special one-time common share dividend of $7.75 per common share which was declared in the fourth quarter of 2010 and subsequently paid on January 25, 2011. During 2010, the Board of Directors declared dividends as follows:

| ($) | | **2010** | 2009 |
|---|---|---|---|
| Common shares | | **$ 9.19** | $ 1.44 |
| Preferred shares | – Series I | **$ 1.45** | $ 1.45 |
| | – Series II | | $ 0.32 |
| | – Series III | **$ 1.30** | $ 1.30 |
| | – Series IV | **$ 1.30** | $ 1.30 |
| | – Series V | **$ 1.19** | $ 1.19 |

**Normal Course Issuer Bid ("NCIB")**

In 2010, GWL and Loblaw renewed their Normal Course Issuer Bid ("NCIB") programs to purchase on the Toronto Stock Exchange ("TSX") or enter into equity derivatives to purchase up to 5% of its common shares outstanding. In accordance with the requirements of the TSX, any purchases must be at the then market prices of such shares. GWL did not purchase any shares under its NCIB during 2010 or 2009. Loblaw did not purchase any shares under its NCIB during 2010. During 2009, Loblaw purchased for cancellation 1,698,400 of its common shares at a price of $33.14. In 2011, GWL and Loblaw each intend to renew their NCIB programs.

## 23. CAPITAL MANAGEMENT

The Company defines capital as net debt(1) and shareholders' equity.

The Company's objectives when managing capital are to:

- ensure sufficient liquidity to support its financial obligations and execute its operating and strategic plans;
- maintain financial capacity and access to capital to support future development of the business;
- minimize the cost of its capital while taking into consideration current and future industry, market and economic risks and conditions; and
- utilize short term funding sources to manage its working capital requirements and long term funding sources to match the long term nature of the fixed assets of the business.

The following ratios are used by the Company to monitor its capital:

| | **2010** | 2009 |
|---|---|---|
| Interest coverage | **3.6x** | 2.6x |
| Net debt(1) to EBITDA(1) | **0.23x** | 0.18x |
| Net debt(1) to equity | **0.08** | 0.04 |

(1) See non-GAAP financial measures in the Company's Management's Discussion and Analysis ("MD&A") beginning on page 61.

These ratios are also calculated from time to time on an alternative basis by management to approximate the methodology of debt rating agencies and other market participants.

**Net Debt**[1]

The Company manages debt on a net basis. The following table details the net debt calculation used in the net debt[1] to EBITDA[1] and the net debt[1] to equity ratios:

| | 2010 | 2009 |
|---|---|---|
| Bank indebtedness | **$ 4** | $ 2 |
| Short term debt | **336** | 300 |
| Long term debt due within one year | **733** | 343 |
| Long term debt | **5,129** | 5,377 |
| Certain other liabilities | **35** | 36 |
| Fair value of financial derivatives related to the above | **(352)** | (327) |
| | **5,885** | 5,731 |
| Less: Cash and cash equivalents | **1,528** | 1,535 |
| Short term investments | **3,234** | 3,371 |
| Security deposits | **435** | 348 |
| Fair value of financial derivatives related to the above | **187** | 178 |
| | **5,384** | 5,432 |
| Net debt[1] | **$ 501** | $ 299 |

(1) See non-GAAP financial measures in the Company's MD&A beginning on page 61.

Capital securities are excluded from the calculation of net debt[1]. For the purpose of calculating net debt[1], fair values of financial derivatives are not credit value adjusted in accordance with EIC 173 (see note 2). As at year end 2010, the credit value adjustment was $4 (2009 – $4).

**EBITDA**[1]

The following table reconciles earnings from continuing operations before minority interest, income taxes, interest expense and other financing charges and depreciation and amortization ("EBITDA") used in the net debt[1] to EBITDA[1] ratio to Canadian GAAP measures reported in the audited consolidated financial statements:

| | 2010 | 2009 |
|---|---|---|
| Net earnings from continuing operations | **$ 452** | $ 127 |
| Add impact of the following: | | |
| Minority interest | **273** | 260 |
| Income taxes | **370** | 259 |
| Interest expense and other financing charges | **388** | 363 |
| Operating income | **1,483** | 1,009 |
| Depreciation and amortization[2] | **709** | 645 |
| EBITDA[1] | **$ 2,192** | $ 1,654 |

(1) See non-GAAP financial measures in the Company's MD&A beginning on page 61.
(2) Includes depreciation of $43 (2009 – $44) included in cost of inventories sold.

During the fourth quarter of 2010, Loblaw filed a Short Form Base Shelf Prospectus ("Prospectus") allowing for the potential issuance of up to $1.0 billion of unsecured debentures and/or preferred shares subject to the availability of funding by capital markets. As at year end 2010, no amounts have been drawn on the Prospectus.

**Covenants and Regulatory Requirements**
The committed credit facility which Loblaw entered into during 2008, the U.S. $300 fixed rate private placement notes which Loblaw issued during 2008, Loblaw's MTNs and certain of Loblaw's letters of credit contain certain financial and non-financial covenants. Certain agreements include maintaining an interest coverage ratio as well as a leverage ratio, which Loblaw measures on a quarterly basis. These ratios are defined in the respective agreements. As at December 31, 2010, Loblaw was in compliance with the covenants under these agreements.

Loblaw is also subject to externally imposed capital requirements from the Office of the Superintendent of Financial Institutions ("OSFI"), as the primary regulator of PC Bank, and the Central Bank of Barbados, as the primary regulator of Glenhuron, both wholly owned subsidiaries of the Company. PC Bank's capital management objectives are to maintain a consistently strong capital position while considering the Bank's economic risks generated by its credit card loan portfolio and to meet all regulatory capital requirements as defined by OSFI. PC Bank is subject to the Basel II regulatory capital management framework which includes a Tier 1 capital ratio of 7% and a total capital ratio of 10%. PC Bank has met all applicable capital targets as at year end 2010. Glenhuron is currently regulated under Basel I. Under Basel I, Glenhuron's assets are risk weighted and the minimum ratio of capital to risk weighted assets is 8.0%. Glenhuron's ratio of capital to risk weighted assets met the minimum requirements under Basel I as at year end 2010.

In addition, a wholly owned subsidiary of the Company that engages in insurance related activities exceeded the minimum regulatory capital and surplus requirements as at year end 2010.

## 24. STOCK-BASED COMPENSATION ($ except table)

The following table summarizes the Company's cost recognized in operating income related to its stock-based compensation plans, RSU plans, and GWL's and Glenhuron's equity derivatives:

| ($ millions) | **2010** | 2009 |
|---|---|---|
| Stock option plans/share appreciation right plan expense | **$ 43** | $ 7 |
| Restricted share unit plan expense | **19** | 14 |
| Equity derivative contracts income (note 26) | **(42)** | (9) |
| Net stock-based compensation expense | **$ 20** | $ 12 |

The Company maintains various types of stock-based compensation plans, which are described below.

**Stock Option and Share Appreciation Right Plans**
GWL maintains a stock option plan for certain employees. Under this plan, GWL may grant options for up to 7 million of its common shares; however, these stock option plans limit the number of common shares available for stock option grants to a maximum of 5% of outstanding common shares at any time. Stock options have up to a 7-year term, vest 20% or 33% cumulatively on each anniversary date of the grant and are exercisable at the designated common share price, which is 100% of the market price of GWL's common shares on the last trading day prior to the effective date of the grant. Each stock option is exercisable into one common share of GWL at the price specified in the terms of the option agreement, or option holders may elect to receive in cash the share appreciation value equal to the excess of the market price at the date of exercise over the specified option price. Subsequent to the end of 2010, the right to receive a cash payment in lieu of exercising an option for shares was removed.

In 2010 and 2009, GWL did not issue common shares or receive cash consideration on the exercise of stock options.

GWL also maintains a share appreciation right plan for certain senior United States employees. There were no rights outstanding at year end 2010.

Loblaw maintains a stock option plan for certain employees. Under this plan, Loblaw may grant options for up to 13.7 million common shares, which is Loblaw's guideline for the number of stock option grants up to a maximum of 5% of outstanding common shares at any time. Stock options have up to a 7-year term, vest 20% or 33% cumulatively on each anniversary date of the grant and are exercisable at the designated common share price, which is 100% of the market price of Loblaw's common shares on the last trading day prior to the effective date of the grant. Each stock option is exercisable into one common share of Loblaw at the price specified in the terms of the option agreement, or option holders may elect to receive in cash the share appreciation value equal to the excess of the market price at the date of exercise over the specified option price. Subsequent to the end of 2010, the right to receive a cash payment in lieu of exercising an option for shares was removed.

In 2010 and 2009, Loblaw did not issue common shares or receive cash consideration on the exercise of stock options.

GWL's stock option and share appreciation right transactions were as follows:

| | **2010** | | 2009 | |
|---|---|---|---|---|
| | **Options/ Rights (number of shares)** | **Weighted Average Exercise Price/Share** | Options/ Rights (number of shares) | Weighted Average Exercise Price/Share |
| Outstanding options/rights, beginning of year | **1,761,345** | **$ 79.07** | 1,616,344 | $ 81.94 |
| Granted | **300,573** | **$ 74.49** | 236,988 | $ 59.65 |
| Exercised | **(129,917)** | **$ 63.26** | (22,527) | $ 46.24 |
| Forfeited/cancelled | **(398,558)** | **$ 93.73** | (69,460) | $ 90.09 |
| Outstanding options, end of year(1,2) | **1,533,443** | **$ 75.71** | 1,761,345 | $ 79.07 |
| Options exercisable, end of year(2) | **674,062** | **$ 86.88** | 883,822 | $ 91.15 |
| Share appreciation value paid ($ millions)(3) | **$ 1** | | $ | |

(1) Options outstanding of 1,533,443 (2009 – 1,669,345) represented approximately 1.2% (2009 – 1.3%) of GWL's issued and outstanding common shares, which was within GWL's guideline of 5%.
(2) Included in the outstanding balance in 2009 are 92,000 share appreciation rights at a weighted average exercise price of $101.03. Included in the exercisable balance in 2009 are 84,000 share appreciation rights at a weighted average exercise price of $100.08. There were no share appreciation rights outstanding at year end 2010.
(3) The share appreciation value paid by GWL in 2009 was nominal.

The following table summarizes information about GWL's stock options outstanding:

| | | | **2010** | | |
|---|---|---|---|---|---|
| | **Outstanding Options** | | | **Exercisable Options** | |
| Range of Exercise Prices ($) | **Number of Options Outstanding** | **Weighted Average Remaining Contractual Life (years)** | **Weighted Average Exercise Price/Share** | **Number of Exercisable Options** | **Weighted Average Exercise Price/Share** |
| $46.24 – $59.56 | **342,592** | **5** | **$ 54.04** | **56,575** | **$ 53.55** |
| $62.71 – $75.62 | **768,118** | **4** | **$ 71.55** | **323,528** | **$ 72.19** |
| $81.05 – $111.02 | **422,733** | **3** | **$ 100.81** | **293,959** | **$ 109.47** |

Loblaw's stock option transactions were as follows:

| | **2010** | | 2009 | |
|---|---|---|---|---|
| | **Options (number of shares)** | **Weighted Average Exercise Price/Share** | Options (number of shares) | Weighted Average Exercise Price/Share |
| Outstanding options, beginning of year | **9,207,816** | **$ 40.14** | 7,892,660 | $ 43.29 |
| Granted | **2,571,203** | **$ 36.52** | 2,787,970 | $ 31.13 |
| Exercised | **(603,787)** | **$ 29.68** | (127,513) | $ 29.00 |
| Forfeited/cancelled | **(1,854,367)** | **$ 46.48** | (1,345,301) | $ 40.99 |
| Outstanding options, end of year(1) | **9,320,865** | **$ 38.56** | 9,207,816 | $ 40.14 |
| Options exercisable, end of year | **2,938,014** | **$ 46.33** | 2,940,474 | $ 50.15 |
| Share appreciation value paid ($ millions) | **$ 6** | | $ 1 | |

(1) Options outstanding of 9,320,865 (2009 – 9,207,816) represented approximately 3.3% (2009 – 3.3%) of Loblaw's issued and outstanding common shares, which was within Loblaw's guideline of 5%.

The following table summarizes information about Loblaw's stock options outstanding:

| | **2010** | | | | |
|---|---|---|---|---|---|
| | **Outstanding Options** | | | **Exercisable Options** | |
| Range of Exercise Prices ($) | **Number of Options Outstanding** | **Weighted Average Remaining Contractual Life (years)** | **Weighted Average Exercise Price/Share** | **Number of Exercisable Options** | **Weighted Average Exercise Price/Share** |
| $28.95 – $31.77 | **3,878,261** | **5** | **$ 29.97** | **972,010** | **$ 29.56** |
| $31.78 – $46.72 | **2,705,513** | **6** | **$ 36.40** | **55,194** | **$ 36.26** |
| $46.73 – $69.75 | **2,737,091** | **3** | **$ 52.88** | **1,910,810** | **$ 55.16** |

**Restricted Share Unit Plans**

GWL and Loblaw both maintain a RSU plan for certain senior employees. The RSUs entitle employees to a cash payment after the end of each performance period, of up to 3 years, following the date of the award. The RSU payment will be an amount equal to the weighted average price of a GWL or Loblaw common share on the last three trading days preceding the end of the performance period for the RSUs multiplied by the number of RSUs held by the employee.

The following is a summary of GWL's and Loblaw's RSU activity during the year:

| | GWL | | Loblaw | |
|---|---|---|---|---|
| | **2010** | 2009 | **2010** | 2009 |
| Outstanding RSUs, beginning of year | **152,555** | 151,769 | **973,351** | 829,399 |
| Granted | **49,056** | 62,706 | **381,712** | 453,680 |
| Cash settled | **(34,148)** | (59,423) | **(198,389)** | (204,943) |
| Cancelled | **(4,093)** | (2,497) | **(111,328)** | (104,785) |
| Outstanding RSUs, end of year | **163,370** | 152,555 | **1,045,346** | 973,351 |
| RSUs cash settled ($ millions) | **$ 2** | $ 4 | **$ 8** | $ 7 |

**Director Deferred Share Unit Plans**
Members of GWL's and Loblaw's Boards of Directors who are not management may elect annually to receive all or a portion of their annual retainer(s) and fees in the form of DSUs, the value of which is determined by the market price of GWL or Loblaw common shares at the time the director's annual retainer(s) or fees are earned. Upon termination of Board service, the common shares due to the director, as represented by the DSUs, will be purchased on the open market on the director's behalf. As at year end 2010, GWL had 105,015 (2009 – 83,974) and Loblaw had 147,358 (2009 – 110,303) DSUs outstanding. During 2010, a compensation cost of $5 million (2009 – $3 million) related to these plans was recognized in operating income.

**Executive Deferred Share Unit Plan**
Under this plan, executives may elect to defer up to 100% of the STIP bonus earned in any year into the EDSU plan, subject to an overall cap of three times the executive's base salary. All EDSUs held by an executive will be paid out in cash by December 15 of the year following the year in which the executive's employment ceases for any reason. An election to participate in the plan in any year must be made before the beginning of the year and is irrevocable. The number of EDSUs granted in respect of any year will be determined by dividing the STIP bonus that is subject to the EDSU plan election by the value of the GWL or Loblaw common shares on the date the STIP bonus would otherwise be payable. For this purpose, and for purposes of determining the value of an EDSU upon conversion of the EDSUs into cash, the value of the EDSUs will be calculated by using the weighted average of the trading prices of GWL or Loblaw common shares on the Toronto Stock Exchange for the five trading days prior to the valuation date. As at year end 2010, GWL had 2,129 (2009 – nil) and Loblaw had 29,143 (2009 – nil) EDSUs outstanding. During 2010, $1 million (2009 – nil) related to these plans was recognized in operating income.

**Employee Share Ownership Plans**
GWL and Loblaw maintain ESOPs which allow employees to acquire GWL and Loblaw common shares through regular payroll deductions of up to 5% of their gross regular earnings. GWL and Loblaw contribute an additional 25% (2009 – 25%) of each employee's contribution to the respective plans. The ESOPs are administered through a trust which purchases GWL and Loblaw common shares on the open market on behalf of employees. During 2010, a compensation cost of $7 million (2009 – $7 million) related to these plans was recognized in operating income.

## 25. ACCUMULATED OTHER COMPREHENSIVE LOSS

The following tables provide further detail regarding the composition of accumulated other comprehensive loss for the years ended December 31, 2010 and December 31, 2009:

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | **Foreign Currency Translation Adjustment** | **Available-for-Sale Assets** | **Cash Flow Hedges** | **Total** |
| Balance, beginning of year | **$ (103)** | **$ (3)** | **$ 14** | **$ (92)** |
| Foreign currency translation adjustment | **(28)** | | | **(28)** |
| Net unrealized loss on available-for-sale financial assets(1) | | **(8)** | | **(8)** |
| Reclassification of loss on available-for-sale financial assets(2) | | **8** | | **8** |
| Net gain on derivatives designated as cash flow hedges(3) | | | **1** | **1** |
| Reclassification of gain on derivatives designated as cash flow hedges(4) | | | **(6)** | **(6)** |
| Balance, end of year | **$ (131)** | **$ (3)** | **$ 9** | **$ (125)** |

(1) Net of income taxes of nil and minority interest of $4.
(2) Net of income taxes of nil and minority interest of $5.
(3) Net of income taxes recovered of $1 and minority interest of a nominal amount.
(4) Net of income taxes of $3 and minority interest of $3.

| | December 31, 2009 | | | |
|---|---|---|---|---|
| | Foreign Currency Translation Adjustment | Available-for-Sale Assets | Cash Flow Hedges | Total |
| Balance, beginning of year | $ (334) | $ 10 | $ 2 | $ (322) |
| Cumulative impact of implementing new accounting standards(1) (note 2) | | | (1) | (1) |
| Foreign currency translation adjustment | 35 | | | 35 |
| Reclassification of cumulative foreign currency translation loss to net earnings | 196 | | | 196 |
| Net unrealized loss on available-for-sale financial assets(2) | | (14) | | (14) |
| Reclassification of loss on available-for-sale financial assets(3) | | 1 | | 1 |
| Net gain on derivatives designated as cash flow hedges(4) | | | 4 | 4 |
| Reclassification of loss on derivatives designated as cash flow hedges(5) | | | 9 | 9 |
| Balance, end of year | $ (103) | $ (3) | $ 14 | $ (92) |

(1) Net of income taxes recovered of $1 and minority interest of $1.
(2) Net of income taxes recovered of $1 and minority interest of $9.
(3) Net of income taxes recovered of $3 and minority interest of $1.
(4) Net of income taxes of $8 and minority interest of $3.
(5) Net of income taxes recovered of $10 and minority interest of $1.

During 2010, the change in the foreign currency translation adjustment of $28 resulted from the appreciation of the Canadian dollar relative to the U.S. dollar.

During 2009, the Company reversed a cumulative foreign currency translation loss of $196 into operating income associated with the U.S. net investment summarized as follows:

- A loss of $34 was reversed after the sale of the U.S. fresh bakery business on January 21, 2009, when Dunedin and certain of its affiliates became integrated foreign subsidiaries.
- A loss of $52 was reversed related to a reduction in the Company's U.S. net investment in self-sustaining foreign operations.
- An additional loss of $110 associated with the Company's net investment in the U.S. fresh bakery business was reversed and included in the results of discontinued operations.

The remaining decrease in 2009 in the foreign currency translation adjustment of $35 resulted primarily from the depreciation of the Canadian dollar relative to the U.S. dollar in the period prior to the sale of the U.S. fresh bakery business, partially offset by the appreciation of the Canadian dollar thereafter.

An estimated gain of $2 (2009 – $5), net of income taxes and minority interest, recorded in accumulated other comprehensive loss related to interest rate swaps as at year end 2010 is expected to be reclassified to net earnings during the next 12 months.

A gain of $3 (2009 – $3), net of income taxes and minority interest, recorded in accumulated other comprehensive loss related to cross currency swaps will be reclassified to net earnings over the next 12 months but will be partially offset by the losses reclassified from accumulated other comprehensive loss to net earnings on available-for-sale assets. Remaining amounts on the cross currency swaps will be reclassified to net earnings over periods of up to 3 years.

## 26. FINANCIAL DERIVATIVE INSTRUMENTS

A summary of the Company's outstanding derivative instruments is as follows:

| | Notional Amounts Maturing in | | | | | | **2010** | 2009 |
|---|---|---|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | 2014 | 2015 | Thereafter | **Total** | Total |
| Cross currency swap receivable | $ 56 | $ 166 | $ 75 | $ 145 | $ 236 | $ 528 | **$ 1,206** | $ 1,149 |
| Cross currency swap payable | | | $ 148 | | $ 148 | | **$ 296** | $ 296 |
| Interest rate swaps receivable | $ 200 | | | | | | **$ 200** | $ 250 |
| Interest rate swaps payable | | | $ 150 | | | | **$ 150** | $ 150 |
| Equity swaps and forwards | $ 84 | $ 82 | | | $ 92 | | **$ 258** | $ 273 |
| Equity forward associated with the forward sale of Loblaw common shares | | | | | | $ 807 | **$ 807** | $ 771 |
| Foreign exchange forwards | $ 66 | | | | | | **$ 66** | $ 5 |
| Electricity forward contract | $ 8 | | | | | | **$ 8** | $ 17 |

Notional amounts do not represent assets or liabilities and are therefore not recorded on the consolidated balance sheet. The notional amounts are used in order to calculate the payments to be exchanged under the contracts.

**Cross Currency Swaps**

Glenhuron entered into cross currency swaps (see note 28) to exchange U.S. dollars for $1,206 (2009 – $1,149) Canadian dollars, which mature by 2017. Cross currency swaps totaling $200 (2009 – $250) are designated in a cash flow hedge and the remaining undesignated $1,006 (2009 – $899) are classified as held-for-trading financial assets. Currency adjustments receivable or payable arising from these swaps are settled in cash on maturity. As at year end 2010, a cumulative unrealized foreign currency exchange rate receivable of $161 (2009 – $123) was recorded in other assets (see note 15), and a receivable of $15 (2009 – $40) was recorded in prepaid expenses and other assets.

In 2008, Loblaw entered into fixed cross currency swaps to exchange $296 Canadian dollars for U.S. $300, which mature by 2015. A portion of these cross currency swaps are designated in a cash flow hedge to manage the foreign exchange related to a part of Loblaw's fixed rate U.S. dollar private placement notes (see note 18). As at year end 2010, a cumulative unrealized foreign currency exchange rate receivable of $11 (2009 − $19) was recorded in other assets (see note 15).

**Interest Rate Swaps**

Glenhuron maintains interest rate swaps (see note 28) that convert a notional $200 (2009 – $250) of floating rate available-for-sale cash and cash equivalents, short term investments and security deposits to average fixed rate investments at 4.74% (2009 – 5.11%), which are part of a hedging relationship that matures in 2011. As at year end 2010, the fair value of these interest rate swaps of $7 (2009 – $15) was recorded in other assets and the unrealized fair value gain of $4 (2009 – $9) was deferred, net of income taxes and minority interest, in accumulated other comprehensive loss. When realized, these unrealized gains are reclassified to net earnings.

Loblaw also maintains a notional $150 (2009 – $150) in interest rate swaps, on which it pays a fixed rate of 8.38% that are not part of a hedging relationship. As at year end 2010, the fair value of these interest rate swaps of $24 (2009 − $31) was recorded in other liabilities (see note 19).

**Equity Swaps and Forwards ($, except where otherwise indicated)**

As at year end 2010, GWL had cumulative outstanding equity swaps in its common shares of 1.7 million (2009 – 1.7 million) at an average forward price of $103.17 (2009 – $103.17). Subsequent to the end of 2010, GWL elected to adjust the forward price of these equity swaps by $7.75 to an average forward price of $95.42 as a result of the special one-time common share dividend of $7.75 per common share declared in the fourth quarter of 2010 (see note 22).

As at year end 2010, Glenhuron had cumulative outstanding equity forwards to buy 1.5 million (2009 – 1.5 million) Loblaw common shares at a cumulative average forward price of $56.26 (2009 – $66.25), including $0.04 (2009 – $10.03) per common share of interest expense and dividends that has been recognized in net earnings from continuing operations and will be paid at each reset date.

These swaps and forwards provide for settlement of net amounts owing between the respective company and its counterparty in cash or common shares. As at year end 2010, the fair value of GWL's swaps of $32 million (2009 – $61 million) was recorded in accounts payable and accrued liabilities. Cumulative interest, dividends and the unrealized market loss on Glenhuron's forwards of $24 million (2009 – $48 million) was recorded in accounts payable and accrued liabilities. During 2010, a fair value gain of $42 million (2009 – $9 million) was recorded in operating income related to these equity swaps and forwards (see note 24). During 2010, Glenhuron paid $16 million to its counterparty to settle the interest and dividends accrued on outstanding equity forwards. During 2009, Glenhuron paid $55 million to terminate equity forwards representing 3.3 million Loblaw common shares, which led to the extinguishment of a corresponding portion of the associated liability.

In 2001, WHL entered into an equity forward sale agreement based on 9.6 million Loblaw common shares at an original forward price of $48.50 per Loblaw common share which, under the terms of the agreement, had increased to a forward price of $84.09 (2009 – $80.28) per Loblaw common share as at year end 2010. The forward matures in 2031 and will be settled in cash as follows: WHL will receive the forward price and will pay the market value of the underlying Loblaw common shares at maturity. As at year end 2010, the fair value of this equity forward sale agreement based on 9.6 million Loblaw common shares of $421 million (2009 – $446 million) was recorded in other assets (see note 15). During 2010, a fair value loss of $62 million (2009 – a fair value gain of $13 million) was recorded in interest expense and other financing charges related to this forward (see note 6).

**Commodity Derivatives**
The Company uses commodity futures, options and forward contracts to manage its anticipated exposure to fluctuations in commodity prices.

As at year end 2010, the fair value of Weston Foods' commodity futures of $16 (2009 – negative $5) was recorded in accounts receivable. During 2010, a fair value gain of $21 (2009 – $23) was recorded in operating income relating to futures which were not designated in a cash flow hedge. As at year end 2010, the fair value of the commodity options of $3 (2009 – nominal amount) was recorded in accounts receivable and a fair value gain of $3 (2009 – $5) was recorded in operating income.

Loblaw entered into an electricity forward contract to minimize price volatility and to maintain a portion of its electricity costs at approximately 2006 rates. This electricity forward contract has an initial term of five years and expires in December 2011. As at year end 2010, the fair value of this forward contract of $1 (2009 – $3) was recorded in other liabilities. During 2010, a gain of $2 (2009 – loss of $10) was recorded in operating income.

Loblaw from time to time enters into exchange traded futures contracts and options contracts to minimize cost volatility on fuel prices. Futures contracts establish a fixed cost on a portion of Loblaw's fuel exposure and option contracts typically provide protection against a range of cost outcomes. As at year end 2010, Loblaw did not hold any outstanding fuel exchange traded future or option contracts (2009 – nil). During 2010, a gain of $1 (2009 – $4) was recorded in operating income.

**Foreign Exchange Forwards**
During 2010, Loblaw entered into forward contracts to hedge a portion of its U.S. dollar fixed asset and inventory purchases. As at year end 2010, the fair value of the foreign exchange forward contracts of $1 (2009 –nil) was recorded in accounts payable and accrued liabilities. During 2010, a loss of $2 (2009 – nil) was recorded in operating income.

## 27. FAIR VALUES OF FINANCIAL INSTRUMENTS

**Derivative Instruments**
The fair value of derivative instruments is the estimated amount that the Company would receive or pay to terminate the instrument at the reporting date. The fair values have been determined by reference to prices available from the markets on which the instruments trade and prices provided by counterparties where available, or are estimated using industry standard valuation models. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, credit spreads, foreign exchange rates, and forward and spot prices for currencies.

**Other Financial Instruments**
The fair values of cash and cash equivalents, short term investments, security deposits, accounts receivable, accounts payable and accrued liabilities and short term borrowings approximate their carrying values given their short term maturities. The fair values of long term debt and capital securities were estimated based on the Company's current incremental borrowing rate for similar types of borrowing arrangements or where applicable, quoted market prices.

The following tables provide a comparison of carrying and fair values for each classification of financial instruments as at December 31, 2010 and December 31, 2009 and an analysis of financial instruments carried at fair value by fair value hierarchy level.

The different fair value hierarchy levels have been defined as follows:

- Fair value level 1: determined using quoted prices (unadjusted) in active markets for identical assets or liabilities
- Fair value level 2: determined using inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)
- Fair value level 3: determined using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

**As at December 31, 2010**

| | Financial derivatives designated in a cash flow hedge | Financial instruments required to be classified as held-for-trading | Financial instruments designated as held-for-trading | Available-for-sale instruments measured at fair value | Loans and receivables | Other financial liabilities | Total carrying amount | Total fair value |
|---|---|---|---|---|---|---|---|---|
| Cash and cash equivalents, short term investments and security deposits | | | $ 5,050 | $ 147 | | | $ 5,197 | $ 5,197 |
| Derivatives included in accounts receivable | | $ 19 | | | | | 19 | 19 |
| Other receivables | | | 21 | | $ 780 | | 801 | 801 |
| Derivatives included in other assets | $ 64 | 554 | | | | | 618 | 618 |
| Total financial assets | $ 64 | $ 573 | $ 5,071 | $ 147 | $ 780 | | $ 6,635 | $ 6,635 |
| Fair value level 1 | | $ 19 | | | | | | $ 19 |
| Fair value level 2 | $ 64 | 551 | $ 5,050 | $ 147 | | | | 5,812 |
| Fair value level 3 | | 3 | 21 | | | | | 24 |
| Total fair value | $ 64 | $ 573 | $ 5,071 | $ 147 | | | | $ 5,855 |
| Short term borrowings | | | | | | $ 340 | $ 340 | $ 340 |
| Derivatives included in accounts payable and accrued liabilities | | $ 56 | | | | | 56 | 56 |
| Other accounts payable and accrued liabilities | | | | | | 4,661 | 4,661 | 4,661 |
| Long term debt | | | | | | 5,862 | 5,862 | 6,405 |
| Derivatives included in other liabilities | | 26 | | | | 7 | 33 | 33 |
| Certain other liabilities | | | | | | 35 | 35 | 35 |
| Capital securities | | | | | | 221 | 221 | 252 |
| Total financial liabilities | | $ 82 | | | | $ 11,126 | $ 11,208 | $ 11,782 |
| Fair value level 1 | | | | | | | | |
| Fair value level 2 | | $ 82 | | | | | | $ 82 |
| Fair value level 3 | | | | | | | | |
| Total fair value | | $ 82 | | | | | | $ 82 |

The equity investment in Loblaw franchises is measured at a cost of $85 because quoted market prices in an active market are not available. These investments are classified as available-for-sale.

As at December 31, 2009

| | Financial derivatives designated in a cash flow hedge | Financial instruments required to be classified as held-for-trading | Financial instruments designated as held-for-trading | Available-for-sale instruments measured at fair value | Loans and receivables | Other financial liabilities | Total carrying amount | Total fair value |
|---|---|---|---|---|---|---|---|---|
| Cash and cash equivalents, short term investments and security deposits | | | $ 5,062 | $ 192 | | | $ 5,254 | $ 5,254 |
| Derivatives included in accounts receivable | | $ (5) | | | | | (5) | (5) |
| Other receivables | | | 13 | | $ 843 | | 856 | 856 |
| Derivatives included in other assets | $ 83 | 562 | | | | | 645 | 645 |
| Total financial assets | $ 83 | $ 557 | $ 5,075 | $ 192 | $ 843 | | $ 6,750 | $ 6,750 |
| Fair value level 1 | | $ (5) | | | | | | $ (5) |
| Fair value level 2 | $ 83 | 561 | $ 5,062 | $ 192 | | | | 5,898 |
| Fair value level 3 | | 1 | 13 | | | | | 14 |
| Total fair value | $ 83 | $ 557 | $ 5,075 | $ 192 | | | | $ 5,907 |
| Short term borrowings | | | | | | $ 302 | $ 302 | $ 302 |
| Derivatives included in accounts payable and accrued liabilities | | $ 109 | | | | | 109 | 109 |
| Other accounts payable and accrued liabilities | | | | | | 3,507 | 3,507 | 3,507 |
| Long term debt | | | | | | 5,720 | 5,720 | 6,066 |
| Derivatives included in other liabilities | | 34 | | | | 7 | 41 | 41 |
| Certain other liabilities | | | | | | 36 | 36 | 36 |
| Capital securities | | | | | | 220 | 220 | 244 |
| Total financial liabilities | | $ 143 | | | | $ 9,792 | $ 9,935 | $ 10,305 |
| Fair value level 1 | | | | | | | | |
| Fair value level 2 | | $ 143 | | | | | | $ 143 |
| Fair value level 3 | | | | | | | | |
| Total fair value | | $ 143 | | | | | | $ 143 |

The equity investment in Loblaw franchises is measured at a cost of $75 because quoted market prices in an active market are not available. These investments are classified as available-for-sale.

The financial instruments classified as fair value level 3 are as follows:

- The retained interest from the securitization of PC Bank receivables, for which a reconciliation and sensitivity analysis are included in note 10.
- The fair value of the Loblaw embedded foreign currency derivative of $3 included in other assets (2009 – $1), of which the fair value gain of $2 (2009 – $4) was recognized in operating income. A 100 basis point increase (decrease) in foreign currency exchange rates would result in a $1 gain (loss) in fair value.

There were no significant transfers between the fair value hierarchy levels during 2010 and 2009.

During 2010, the net unrealized and realized loss on held-for-trading financial assets designated as held-for-trading, recognized in net earnings from continuing operations before income taxes and minority interest was $32 (2009 – $120). In addition, the net unrealized and realized gain on held-for-trading financial assets and financial liabilities, including non-financial derivatives, required to be classified as held-for-trading, recognized in net earnings from continuing operations before income taxes and minority interest was $53 (2009 – $108).

### 28. FINANCIAL RISK MANAGEMENT

The Company is exposed to the following risks as a result of holding and issuing financial instruments: credit risk, market risk and liquidity risk. The following is a description of those risks and how the exposures are managed.

**Credit Risk**

The Company is exposed to credit risk resulting from the possibility that counterparties may default on their financial obligations. Exposure to credit risk relates to derivative instruments, cash equivalents, short term investments, security deposits, pension assets held in the Company's defined benefit plans, PC Bank's credit card receivables and other receivables from Weston Foods' customers and Loblaw's vendors, independent franchisees, associated stores and independent accounts.

The Company may be exposed to losses if a counterparty to the Company's financial or non-financial derivative agreements fails to fulfill its obligations. Potential counterparty risk and losses are limited to the net amounts recoverable under such derivative agreements with any specific counterparty. These risks are further reduced by entering into agreements with counterparties that have a minimum long term "A" credit rating from a recognized credit rating agency and by placing risk adjusted limits on exposure to any single counterparty for financial derivative agreements. Internal policies, controls and reporting processes are in place and require ongoing assessment and corrective action, if necessary, with respect to derivative transactions.

Credit risk associated with cash equivalents, short term investments and security deposits results from the possibility that a counterparty may default on the repayment of a security. Policies and guidelines that require issuers of permissible investments to have a minimum long term "A" credit rating from a recognized credit rating agency and that specify minimum and maximum exposures to specific industries, issuers and types of investment instruments mitigate credit risk. These investments are purchased and held directly in custody accounts and have limited exposure to third-party money market portfolios and funds.

Credit risk from PC Bank's credit card receivables, receivables from Weston Foods' customers and suppliers and Loblaw's independent franchisees, associated stores and independent accounts results from the possibility that customers may default on their payment obligations. PC Bank manages the credit card receivable risk by employing stringent credit scoring techniques, actively monitoring its credit card portfolio and reviewing techniques and technology that can improve the effectiveness of the collection process. In addition, these receivables are dispersed among a large, diversified group of credit card customers.

Receivables from Weston Foods' customers and Loblaw's independent franchisees, associated stores and independent accounts are actively monitored and counterparties are assessed for credit risk on an ongoing basis.

The Company's maximum exposure to credit risk as it relates to derivative instruments is approximated by the positive fair market value of the derivatives on the balance sheet (see note 27).

See note 11 for additional information on the credit quality performance of credit card receivables and other receivables from Weston Foods' customers, Loblaw's independent franchisees, associated stores and independent accounts.

**Market Risk**

Market risk is the risk of loss that may arise from changes in factors such as foreign currency exchange rates, commodity prices, interest rates and common share prices and the impact these factors may have on other counterparties.

***Foreign Currency Exchange Rate Risk***

As at year end 2010, the Company had $1.5 billion (2009 – $1.5 billion) in cash and cash equivalents, $3.2 billion (2009 – $3.4 billion) in short term investments and $435 (2009 – $348) in security deposits, of which $2.2 billion (2009 – $2.2 billion) is denominated in U.S. dollars and is held primarily by Dunedin and certain of its affiliates and Glenhuron.

The Company's consolidated financial statements are expressed in Canadian dollars, however a portion of the Company's (excluding Loblaw's) net assets are denominated in U.S. dollars through both its net investment in self-sustaining foreign operations in the United States, and its net investment in integrated foreign subsidiaries held by Dunedin and certain of its affiliates. The U.S. dollar denominated net assets are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. As a result, the Company is exposed to foreign currency translation gains and losses. Those gains and losses arising from the translation of the U.S. dollar denominated assets of the integrated foreign subsidiaries are included in operating income, while for the self-sustaining operations in the United States, foreign currency translation gains and losses are recorded in accumulated other comprehensive loss.

Accordingly, operating income includes $56 (2009 – $225) of foreign currency translation losses due to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates. The Company estimates that based on the U.S. net assets held in integrated subsidiaries at the end of 2010, an appreciation (depreciation) in the Canadian dollar of $0.01 relative to the U.S. dollar would have a negative (positive) impact on operating income of $9 (2009 – $12).

Unrealized foreign currency translation losses (2009 – gains) associated with the effect of foreign currency translation on the Company's (excluding Loblaw's) U.S. net investment held in self-sustaining foreign operations increased accumulated other comprehensive loss by $28 during 2010 (2009 – decreased by $35).

Revenues and expenses of these integrated and self-sustaining foreign operations are translated into Canadian dollars at the foreign currency exchange rates that approximate the rates in effect at the dates when such items are recognized. An appreciating Canadian dollar relative to the U.S. dollar will negatively impact year-over-year changes in reported sales, operating income and net earnings, while a depreciating Canadian dollar relative to the U.S. dollar will have the opposite impact.

Loblaw is exposed to foreign currency exchange rate variability, primarily on U.S. dollar denominated cash and cash equivalents, short term investments and security deposits held by Glenhuron, foreign denominated and foreign currency based purchases in accounts payable and accrued liabilities, and U.S. dollar private placement notes included in long term debt. Loblaw and Glenhuron have cross currency swaps and foreign exchange forward contracts that partially offset their respective exposure to fluctuations in foreign currency exchange rates. Loblaw designates a portion of the cross currency swaps in a cash flow hedge of the exposure to fluctuations in the foreign currency exchange rate on a portion of its U.S. dollar denominated cash equivalents, short term investments and security deposits. The remaining undesignated cross currency swaps partially offset fluctuations in the foreign currency exchange rate on the remaining U.S. dollar denominated cash and cash equivalents, short term investments and security deposits and the U.S. dollar private placement notes.

During 2010, Loblaw's unrealized foreign currency translation loss of $12 (2009 – $25) before income taxes and minority interest, related to cash and cash equivalents, short term investments and security deposits classified as available-for-sale was recognized in accumulated other comprehensive loss and was partially offset by the unrealized foreign currency translation gain of $12 (2009 – $28) before income taxes and minority interest relating to the designated cross currency swaps also deferred in accumulated other comprehensive loss. The unrealized foreign currency translation loss of $40 (2009 – $121) on the designated held-for-trading cash and cash equivalents, short term investments and security deposits is partially offset in operating income by the unrealized foreign currency translation gain of $40 (2009 – $117) relating to the cross currency swaps which are not designated in a cash flow hedge.

During 2010, Loblaw realized a foreign currency translation loss of $39 (2009 – $14) relating to cross currency swaps that matured or were terminated.

During 2010, Loblaw recognized in operating income an unrealized foreign currency translation gain of $16 (2009 – $45) related to U.S. $300 fixed rate private placement notes. This was partially offset by both the effective portion of the designated cross currency swaps that was reclassified from other comprehensive (loss) income to operating income and the fair value gain on the cross currency swaps that are not designated in a hedging relationship. At the inception of the cash flow hedge, a nominal amount of ineffectiveness was recognized in operating income.

***Commodity Price Risk***
Weston Foods costs are directly impacted by fluctuations in the prices of commodity-linked raw materials such as wheat flours, sugars, vegetable oils, cocoa powders and chocolate. Loblaw is also exposed to commodity prices as a result of the direct link between commodities and the cost of consumer products. In addition, both Weston Foods and Loblaw are exposed to increases in the prices of electricity, natural gas and fuel in operating, in the case of Weston Foods, its bakeries and distribution centres, and, in the case of Loblaw, its stores and distribution centres. Both Weston Foods and Loblaw use purchase commitments and financial and non-financial derivative instruments in the form of futures contracts, option contracts and forward contracts to manage their current and anticipated exposure to fluctuations in commodity prices. The Company estimates that a 10% increase (decrease) in relevant commodity prices, with all other variables held constant, would result in a net gain (loss) of $8 in net earnings before income taxes and minority interest.

***Interest Rate Risk***
Interest rate risk arises from the issuance of short term debt and equity derivatives, net of cash and cash equivalents, short term investments and security deposits. The Company is exposed to changes in short term interest rates which are offset partly by Glenhuron's and Loblaw's interest rate swaps. Interest rate swaps are transactions in which interest flows are exchanged with a counterparty on a specified notional amount for a pre-determined period based on agreed-upon fixed and floating interest rates. The Company estimates that a 100 basis point increase (decrease) in interest rates, with all other variables held constant, could result in a decrease (increase) of $51 in interest expense and other financing charges.

***Common Share Price Risk***

GWL and Loblaw issue stock-based compensation to employees in the form of stock options and RSUs based on their respective underlying common shares. Consequently, operating income is negatively impacted when the common share prices increase and positively impacted when the common share prices decline. The equity derivatives provide a partial offset to fluctuations in stock-based compensation cost. The equity derivatives allow for settlement in cash, common shares or net settlement. These derivatives change in value as the market prices of the respective underlying common shares change and provide a partial offset to fluctuations in stock-based compensation cost, including RSU plan expense. The partial offset between stock-based compensation costs, including RSU plan expense, and the equity derivatives is more effective when the market price of the respective underlying common shares exceeds the exercise price of the employee stock options. When the market price of the respective underlying common shares is lower than the exercise price of the employee stock options, these equity derivatives provide a partial offset only to the RSU plan expense. The amount of net stock-based compensation cost recorded in operating income is mainly dependent upon the number of unexercised stock options and RSUs, their vesting schedules relative to the number of respective underlying common shares on the equity derivatives, and the level of fluctuations in the market price of the respective underlying common shares. A one dollar increase (decrease) in the market value of the respective underlying shares of the equity derivatives, with all other variables held constant, would result in a gain (loss) of $3 in net earnings before income taxes and minority interest.

In addition, the obligation of WHL under the equity forward sale agreement based on 9.6 million Loblaw common shares, which matures in 2031, is secured by the underlying Loblaw common shares. If the market value of the underlying Loblaw common shares exceeds the obligation of WHL under this forward, a portion of the proceeds from a future sale of these shares may be used to satisfy the obligation under this forward contract upon termination or maturity. At maturity, if the forward price is greater than the market price of the Loblaw shares, WHL will receive a cash amount equal to the difference. If the forward price is less than the market price of the Loblaw shares, WHL will pay a cash amount equal to the difference. A one dollar increase (decrease) in the market value of the underlying shares of the equity forward, with all other variables held constant, would result in a loss (gain) of $10 in net earnings before income taxes and minority interest. Any cash paid under the forward contract could be offset by the sale of Loblaw common shares.

**Liquidity Risk**

Liquidity risk is the risk that the Company cannot meet a demand for cash or fund its obligations as they come due. Liquidity risk also includes the risk of not being able to liquidate assets in a timely manner at a reasonable price.

The Company mitigates liquidity risk by maintaining appropriate levels of cash and cash equivalents and short term investments, committed lines of credit as required, actively monitoring market conditions and by diversifying its sources of funding and maturity profile of its debt and capital obligations.

Should Loblaw's or PC Bank's financial performance and condition deteriorate or downgrades in Loblaw's current credit ratings occur, Loblaw's or PC Bank's ability to obtain funding from external sources may be restricted. In addition, credit and capital markets are subject to inherent risks that may negatively affect Loblaw's access and ability to fund its financial and other liabilities.

Should GWL's financial performance and condition deteriorate or downgrades in GWL's current credit ratings occur, GWL's ability to obtain funding from external sources may be restricted. In addition, credit and capital markets are subject to inherent risks that may negatively affect GWL's access and ability to fund its financial and other liabilities.

The following are the undiscounted contractual maturities of significant financial liabilities as at December 31, 2010:

| | 2011 | 2012 | 2013 | 2014 | 2015 | Thereafter[5] | Total |
|---|---|---|---|---|---|---|---|
| Interest rate swaps payable[1] | $ 13 | $ 13 | $ 5 | | | | $ 31 |
| Equity swaps and forwards[2] | 84 | 82 | | | $ 92 | | 258 |
| Long term debt including fixed interest payments[3] | 1,032 | 343 | 683 | $ 910 | 383 | $ 7,144 | 10,495 |
| Foreign exchange forward contracts | 66 | | | | | | 66 |
| Other liabilities[4] | | | | 35 | | | 35 |
| | $ 1,195 | $ 438 | $ 688 | $ 945 | $ 475 | $ 7,144 | $ 10,885 |

(1) Based on the pay fixed interest which will be partially offset by the floating interest received.
(2) Based on the average cost base as at December 31, 2010.
(3) Based on the maturing face values and annual interest for each instrument as well as annual payment obligations for VIEs, mortgages and capital leases.
(4) Contractual amount of Loblaw's obligation related to certain other liabilities.
(5) Loblaw's capital securities and their related dividends have been excluded as Loblaw is not contractually obligated to pay these amounts.

The Company's bank indebtedness, short term debt and accounts payable and accrued liabilities are short term in nature, which are due within the next 12 months and thus not included above.

## 29. CONTINGENCIES, COMMITMENTS AND GUARANTEES

The Company is involved in, and potentially subject to, various claims by third parties arising out of the normal course and conduct of its business including, but not limited to, product liability, labour and employment, regulatory and environmental claims. In addition, the Company is involved in and potentially subject to regular audits from federal, provincial and state tax authorities relating to income, capital and commodity taxes and as a result of these audits may receive assessments and reassessments. Although such matters cannot be predicted with certainty, management currently considers the Company's exposure to such claims and litigation, to the extent not covered by the Company's insurance policies or otherwise provided for, not to be material to these consolidated financial statements, with the exception of the items disclosed in the Legal Proceedings section below.

As at year end 2010, the Company has committed approximately $96 (2009 – $76) with respect to capital investment projects such as the construction, expansion and renovation of buildings and the purchase of real property.

The Company establishes letters of credit used in connection with certain obligations mainly related to real estate transactions, benefit programs, purchase orders and performance guarantees. The aggregate gross potential liability related to these letters of credit is approximately $445 (2009 – $406), a portion of which is recorded on the consolidated balance sheets. Additionally, Loblaw has a guarantee on behalf of PC Bank in the amount of U.S. $180. Other letters of credit related to the financing program for Loblaw's independent franchisees and securitization of PC Bank's credit card receivables have been identified as guarantees and are discussed further in the Guarantees section below.

### Guarantees

The Company has provided to third parties the following significant guarantees as defined pursuant to AcG 14, "Disclosure of Guarantees".

***Independent Funding Trusts***
Certain independent franchisees of Loblaw obtain financing through a structure involving independent funding trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. These trusts are administered by a major Canadian chartered bank.

The gross principal amount of loans issued to Loblaw's independent franchisees by the independent funding trusts as at year end 2010 was $405 (2009 – $390) including $202 (2009 – $163) of loans payable by VIEs consolidated by the Company. Loblaw has agreed to provide credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trust representing not less than 15% (2009 – 15%) of the principal amount of the loans outstanding. This standby letter of credit has never been drawn upon. This credit enhancement allows the independent funding trust to provide financing to Loblaw's independent franchisees. As well, each independent franchisee provides security to the independent funding trust for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and Loblaw has not, within a specified time period, assumed the loan, or the default is not otherwise remedied, the independent funding trust would assign the loan to Loblaw and draw upon this standby letter of credit. Loblaw has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit.

During 2010, the $475, 364-day revolving committed credit facility that is the source of funding to the independent trusts was renewed. This facility has a further 12-month repayment term upon maturity. The financing structure has been reviewed and Loblaw determined there were no additional VIEs to consolidate as a result of this financing. In accordance with Canadian GAAP, the financial statements of the independent funding trust are not consolidated with those of the Company.

***Letters of Credit***
Letters of credit for the benefit of independent trusts with respect to the credit card receivables securitization program of PC Bank have been issued by major Canadian chartered banks. These standby letters of credit could be drawn upon in the event of a major decline in the income flow from or in the value of the securitized credit card receivables. Loblaw has agreed to reimburse the issuing banks for any amount drawn on the standby letters of credit. The aggregate gross potential liability under these arrangements, which represents 9% (2009 – 9%) on a portion of the securitized credit card receivables amount, is approximately $48 (2009 – $116) (see note 10).

***Lease Obligations***
In connection with historical dispositions of certain of its assets, the Company has assigned leases to third parties. The Company remains contingently liable for these lease obligations in the event any of the assignees are in default of their lease obligations. The estimated amount for minimum rent, which does not include other lease related expenses such as property tax and common area maintenance charges, is in aggregate $26 (2009 – $41).

***Indemnification Provisions***
The Company from time to time enters into agreements in the normal course of its business, such as service and outsourcing arrangements and leases, and in connection with business or asset acquisitions or dispositions. These agreements by their nature may provide for indemnification of counterparties. These indemnification provisions may be in connection with breaches of representations and warranties or with future claims for certain liabilities, including liabilities related to tax and environmental matters. Indemnities were provided to the purchasers of the Company's dairy and bottling operations sold in 2008 and the U.S. fresh bakery business sold in 2009. The terms of these indemnification provisions vary in duration and may extend for an unlimited period of time. The indemnification provisions could result in future cash outflows and statement of earnings charges. The Company is unable to reasonably estimate its total maximum potential liability as certain indemnification provisions do not provide for a maximum potential amount and the amounts are dependent on the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time. Historically, the Company has not made any significant payments in connection with these indemnification provisions.

**Legal Proceedings**

In 2007, pursuant to a transaction whereby Domtar was combined with the fine paper business of Weyerhaeuser Inc., Domtar common shares were exchanged for an equal number of either exchangeable shares of Domtar (Canada) Paper Inc. or common shares of New Domtar. The Company elected to receive exchangeable shares of Domtar (Canada) Paper Inc. in exchange for its Domtar common shares. The Share Purchase Agreement governing the June 1998 sale by GWL of E.B. Eddy Paper, Inc. to Domtar (the "SPA") contains a price adjustment clause. The SPA provides, subject to certain limited exceptions, that if any person subsequently acquired more than 50% of the outstanding voting shares of Domtar, the price adjustment clause applies. GWL believes that a price adjustment in the amount of $110 is payable to it by Domtar and it has demanded payment of such amount from Domtar. Domtar's position is that the purchase price adjustment does not apply because of the application of an exception contained in the SPA. GWL has commenced an action against Domtar for $110. The parties have exchanged legal pleadings.

The Company is the subject of various legal proceedings and claims that arise in the ordinary course of business. The outcome of all of these proceedings and claims is uncertain. However, based on information currently available, these proceedings and claims, individually and in the aggregate, are not expected to have a material impact on the Company.

**Income Taxes**

During 2010, GWL received a reassessment from the Canada Revenue Agency ("CRA") challenging GWL's characterization of a gain reported in a previous tax return filing. Should the CRA be successful in its assertion, the maximum exposure to the Company's net earnings would be approximately $62. GWL intends to vigorously defend its filing position. No amount has been recorded in the Company's financial statements.

## 30. VARIABLE INTEREST ENTITIES

Pursuant to AcG 15, Loblaw consolidates all VIEs for which it is the primary beneficiary. AcG 15 defines a VIE as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. AcG 15 requires the primary beneficiary to consolidate VIEs and considers an entity to be the primary beneficiary of a VIE if it holds variable interests that expose it to a majority of the VIEs' expected losses or that entitle it to receive a majority of the VIEs' expected residual returns or both. Loblaw has identified the following significant VIEs:

**Franchisees**

Loblaw enters into various forms of franchise agreements that generally require the franchisee to purchase inventory from Loblaw and pay certain fees in exchange for services provided by Loblaw and for the right to use certain trademarks and licenses owned by Loblaw. Franchisees generally lease the land and building from Loblaw, and when eligible, may obtain financing through a structure involving independent trusts to facilitate the purchase of the majority of their inventory and fixed assets, consisting mainly of fixtures and equipment (see note 29). These trusts are administered by a major Canadian chartered bank. Under the terms of certain franchise agreements, Loblaw may also lease equipment to franchisees. Franchisees may also obtain financing through operating lines of credit with traditional financial institutions or through issuing preferred shares or notes payable to Loblaw. Loblaw monitors the financial condition of its franchisees and provides for estimated losses or write-downs on its accounts and notes receivable or investments when appropriate.

As at year end 2010, 214 (2009 – 166) of Loblaw's franchised stores met the criteria for a VIE and were consolidated pursuant to AcG 15.

**Warehouse and Distribution Agreements**
Loblaw has warehouse and distribution agreements with third-party entities to provide to Loblaw distribution and warehousing services from dedicated facilities. Loblaw has no equity interest in these third-party entities; however, the terms of the agreement with the third-party entities are such that Loblaw has determined that the third-party entities meet the criteria for a VIE that requires consolidation by Loblaw. The impact of the consolidation of the warehouse and distribution entities was not material.

Accordingly, the Company has included the results of these independent franchisees and these third-party entities that provide distribution and warehousing services in its consolidated financial statements. The consolidation of these VIEs by the Company does not result in any change to its tax, legal or credit risks, nor does it result in the Company assuming any obligations of these third parties.

**Independent Trusts**
Loblaw has also identified that it holds variable interests, by way of standby letters of credit in independent trusts which are used to securitize credit card receivables for PC Bank. In these securitizations, PC Bank sells a portion of its credit card receivables to the independent trust in exchange for cash. Although these independent trusts have been identified as VIEs, it was determined that Loblaw is not the primary beneficiary and therefore these VIEs are not subject to consolidation by the Company. The Company's maximum exposure to loss as a result of its involvement with these independent trusts is disclosed in note 29.

## 31. RELATED PARTY TRANSACTIONS

The Company's majority shareholder, Wittington Investments, Limited ("Wittington"), and its affiliates are related parties. The Company, in the normal course of business, has routine transactions with these related parties, including the rental of office space at market prices from Wittington. In 2010, rental payments to Wittington amounted to approximately $3 (2009 – $3).

From time to time, the Company, Wittington and its affiliates may enter into agreements to make elections that are permitted or required under applicable income tax legislation with respect to affiliated corporations. These elections and accompanying agreements did not have a material impact on the Company in 2010.

## 32. SEGMENT INFORMATION

The Company has two reportable operating segments: Weston Foods and Loblaw. The Weston Foods operating segment is a leading fresh and frozen baking company in Canada and is engaged in frozen baking and biscuit manufacturing in the United States. The Loblaw operating segment, which is operated by Loblaw and its subsidiaries, is Canada's largest food distributor and a leading provider of drugstore, general merchandise and financial products and services.

The accounting policies of the reportable operating segments are the same as those described in the Company's summary of significant accounting policies. The Company measures each reportable operating segment's performance based on operating income. Neither reportable operating segment is reliant on any single external customer.

| | **2010** | 2009 |
|---|---|---|
| **Sales** | | |
| Weston Foods | **$ 1,624** | $ 1,686 |
| Loblaw | **30,997** | 30,735 |
| Intersegment | **(613)** | (601) |
| Consolidated | **$ 32,008** | $ 31,820 |
| **Operating income** | | |
| Weston Foods | **$ 278** | $ 123 |
| Loblaw | **1,261** | 1,197 |
| Other(1) | **(56)** | (311) |
| Consolidated | **$ 1,483** | $ 1,009 |
| **Depreciation and Amortization** | | |
| Weston Foods | **$ 54** | $ 56 |
| Loblaw | **655** | 589 |
| Consolidated | **$ 709** | $ 645 |
| **Total Assets** | | |
| Weston Foods | **$ 1,868** | $ 1,674 |
| Loblaw | **16,091** | 15,151 |
| Other(2) | **2,895** | 3,318 |
| Consolidated | **$ 20,854** | $ 20,143 |
| **Fixed Assets and Goodwill Purchases** | | |
| Weston Foods | **$ 189** | $ 40 |
| Loblaw | **1,291** | 1,127 |
| Consolidated | **$ 1,480** | $ 1,167 |

(1) Operating income for 2010 includes a loss of $56 (2009 – $225) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates, which are integrated foreign subsidiaries for accounting purposes. 2009 operating income also includes a loss of $86 related to the reversal of cumulative foreign currency translation losses.

(2) Other includes cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates.

The Company operates primarily in Canada and the United States.

| | **2010** | 2009 |
|---|---|---|
| **Sales (excluding intersegment)** | | |
| Canada | **$ 31,378** | $ 31,126 |
| United States | **630** | 694 |
| Consolidated | **$ 32,008** | $ 31,820 |
| **Fixed Assets and Goodwill** | | |
| Canada | **$ 10,624** | $ 9,974 |
| United States | **329** | 241 |
| Consolidated | **$ 10,953** | $ 10,215 |

# Three Year Summary

## CONSOLIDATED INFORMATION[1]

For the years ended December 31[2]

| ($ millions except where otherwise indicated) | **2010** | 2009 | 2008 |
|---|---|---|---|
| **Operating Results** | | | |
| Sales | **32,008** | 31,820 | 32,088 |
| EBITDA[3] | **2,192** | 1,654 | 1,808 |
| Operating income | **1,483** | 1,009 | 1,198 |
| Interest expense and other financing charges[4] | **388** | 363 | 360 |
| Net earnings from continuing operations | **452** | 127 | 647 |
| Net earnings[5] | **452** | 1,035 | 834 |
| **Financial position** | | | |
| Working capital | **2,131** | 3,813 | 1,165 |
| Fixed assets | **9,584** | 9,020 | 8,542 |
| Goodwill and intangible assets | **1,571** | 1,296 | 1,145 |
| Total assets | **20,854** | 20,143 | 19,563 |
| Net debt[3] | **501** | 299 | 3,251 |
| Shareholders' equity | **6,132** | 6,942 | 5,910 |
| **Cash Flows** | | | |
| Cash flows from operating activities of continuing operations | **1,741** | 1,987 | 956 |
| Fixed asset purchases | **1,304** | 1,011 | 807 |
| **Per Common Share ($)** | | | |
| Basic net earnings from continuing operations | **3.16** | 0.64 | 4.65 |
| Basic net earnings | **3.16** | 7.68 | 6.10 |
| Common dividend rate at year end[6] | **9.19** | 1.44 | 1.44 |
| Cash flows from operating activities of continuing operations | **13.14** | 15.05 | 7.04 |
| Fixed asset purchases | **10.10** | 7.83 | 6.25 |
| Book value | **41.17** | 47.44 | 39.45 |
| Market value at year end | **84.20** | 66.92 | 59.90 |
| **Financial Ratios** | | | |
| EBITDA margin (%)[3] | **6.8** | 5.2 | 5.6 |
| Operating margin (%) | **4.6** | 3.2 | 3.7 |
| Return on average net assets (%)[3] | **13.3** | 9.3 | 11.2 |
| Return on average common shareholders' equity (%) | **7.1** | 1.5 | 13.4 |
| Interest coverage | **3.6x** | 2.6x | 3.2x |
| Net debt[3] to EBITDA[3] | **0.23x** | 0.18x | 1.80x |
| Net debt[3] to equity | **0.08** | 0.04 | 0.53 |
| Cash flows from operating activities of continuing operations to net debt[3] | **3.48** | 6.65 | 0.29 |
| Price/net earnings from continuing operations ratio at year end | **26.6** | 104.6 | 12.9 |
| Market/book ratio at year end | **2.0** | 1.4 | 1.5 |

(1) For financial definitions and ratios refer to the Glossary beginning on page 126.
(2) 2008 was a 53-week year.
(3) See non-GAAP financial measures beginning on page 61.
(4) 2010 includes a non-cash charge of $62 (2009 – non-cash income of $13) related to the fair value adjustment of WHL's forward sale agreement for 9.6 million Loblaw common shares (see note 6 to the consolidated financial statements).
(5) 2009 net earnings include a gain on disposal of $939 ($901, net of tax) recorded in discontinued operations.
(6) 2010 includes the special one-time common share dividend of $7.75 per common share which was declared in the fourth quarter of 2010 and subsequently paid on January 25, 2011 (see note 22 to the consolidated financial statements).

## SEGMENT INFORMATION[1]

For the years ended December 31[2]

| ($ millions except where otherwise indicated) | | 2010 | 2009 | 2008 |
|---|---|---|---|---|
| **OPERATING RESULTS** | | | | |
| **Sales** | Weston Foods | **1,624** | 1,686 | 2,197 |
| | Loblaw | **30,997** | 30,735 | 30,802 |
| | Intersegment | **(613)** | (601) | (911) |
| | Consolidated | **32,008** | 31,820 | 32,088 |
| **EBITDA**[3] | Weston Foods | **332** | 179 | 214 |
| | Loblaw | **1,916** | 1,786 | 1,594 |
| | Other[4] | **(56)** | (311) | |
| | Consolidated | **2,192** | 1,654 | 1,808 |
| **Operating Income** | Weston Foods | **278** | 123 | 154 |
| | Loblaw | **1,261** | 1,197 | 1,044 |
| | Other[4] | **(56)** | (311) | |
| | Consolidated | **1,483** | 1,009 | 1,198 |
| **FINANCIAL POSITION** | | | | |
| **Fixed Assets** | Weston Foods | **461** | 461 | 497 |
| | Loblaw | **9,123** | 8,559 | 8,045 |
| | Consolidated | **9,584** | 9,020 | 8,542 |
| **Total Assets** | Weston Foods | **1,868** | 1,674 | 2,892 |
| | Loblaw | **16,091** | 15,151 | 14,083 |
| | Discontinued Operations | | | 2,588 |
| | Other[5] | **2,895** | 3,318 | |
| | Consolidated | **20,854** | 20,143 | 19,563 |
| **CASH FLOWS** | | | | |
| **Fixed Asset Purchases** | Weston Foods | **24** | 40 | 57 |
| | Loblaw | **1,280** | 971 | 750 |
| | Consolidated | **1,304** | 1,011 | 807 |
| **FINANCIAL RATIOS** | | | | |
| **EBITDA Margin** (%)[3] | Weston Foods | **20.4** | 10.6 | 9.7 |
| | Loblaw | **6.2** | 5.8 | 5.2 |
| | Consolidated | **6.8** | 5.2 | 5.6 |
| **Operating Margin** (%) | Weston Foods | **17.1** | 7.3 | 7.0 |
| | Loblaw | **4.1** | 3.9 | 3.4 |
| | Consolidated | **4.6** | 3.2 | 3.7 |
| **Return on Average Net Assets** (%)[3] | Weston Foods | **38.1** | 19.2 | 22.6 |
| | Loblaw | **12.1** | 11.8 | 10.4 |
| | Consolidated | **13.3** | 9.3 | 11.2 |

(1) For financial definitions and ratios refer to the Glossary beginning on page 126.
(2) 2008 was a 53-week year.
(3) See non-GAAP financial measures beginning on page 61.
(4) Operating income for 2010 includes a loss of $56 (2009 – $225) related to the effect of foreign currency translation on a portion of the U.S. dollar denominated cash and short term investments held by Dunedin and certain of its affiliates, which are integrated foreign subsidiaries for accounting purposes. 2009 operating income also includes a loss of $86 related to the reversal of cumulative foreign currency translation losses.
(5) Other includes cash and cash equivalents and short term investments held by Dunedin and certain of its affiliates.

# Glossary

**Basic net earnings per common share from continuing operations**
Net earnings from continuing operations available to common shareholders divided by the weighted average number of common shares outstanding during the year.

**Book value per common share**
Common shareholders' equity divided by the number of common shares outstanding at year end.

**Cash flows from operating activities of continuing operations per common share**
Cash flows from operating activities of continuing operations less preferred dividends paid divided by the weighted average number of common shares outstanding during the year.

**Cash flows from operating activities of continuing operations to net debt**
Cash flows from operating activities of continuing operations divided by net debt (see non-GAAP financial measures beginning on page 61).

**Common shareholders' equity**
Total shareholders' equity less preferred shares outstanding.

**Control label**
A brand and associated trademark that is owned by Loblaw for use in connection with its own products and services.

**Conversion**
A store that changes from one Loblaw banner to another Loblaw banner.

**Corporate stores sales per average square foot**
Sales by corporate stores divided by the average corporate stores' square footage at year end.

**Diluted net earnings per common share from continuing operations**
Net earnings from continuing operations available to common shareholders divided by the weighted average number of common shares outstanding during the year minus the dilutive impact of outstanding stock option grants and certain other liabilities.

**Dividend rate per common share at year end**
Dividend per common share declared in the fourth quarter multiplied by four.

**DRIP**
Loblaw Dividend Reinvestment Plan.

**EBITDA**
Operating income before depreciation and amortization (see non-GAAP financial measures beginning on page 61).

**EBITDA Margin**
EBITDA divided by sales (see non-GAAP financial measures beginning on page 61).

**Fixed asset purchases per common share**
Fixed asset purchases divided by the weighted average number of common shares outstanding during the year.

**Gross margin**
Sales less cost of inventories sold including inventory shrinkage divided by sales.

**Interest coverage**
Operating income divided by interest expense and other financing charges adding back interest capitalized to fixed assets.

**Major expansion**
Expansion of a store that results in an increase in square footage that is greater than 25% of the square footage of the store prior to the expansion.

**Market/book ratio at year end**
Market price per common share at year end divided by book value per common share at year end.

**Minor expansion**
Expansion of a store that results in an increase in square footage that is less than or equal to 25% of the square footage of the store prior to the expansion.

**Net debt**
Bank indebtedness, short term debt, long term debt due within one year, long term debt, certain other liabilities and the fair value of certain financial derivative liabilities less cash and cash equivalents, short term investments, security deposits and the fair value of certain financial derivative assets (see non-GAAP financial measures beginning on page 61).

**Net debt to EBITDA**
Net debt divided by EBITDA (see non-GAAP financial measures beginning on page 61).

**Net debt to equity**
Net debt divided by total shareholders' equity adding back GWL's capital securities (see non-GAAP financial measures beginning on page 61).

**New store**
A newly constructed store, conversion or major expansion.

**Operating income**
Net earnings from continuing operations before minority interest, income taxes, interest expense and other financing charges and gain on disposal of business.

**Operating margin**
Operating income divided by sales.

**Price/earnings from continuing operations ratio at year end**
Market price per common share at year end divided by basic net earnings per common share from continuing operations for the year.

**Renovation**
A capital investment in a store resulting in no change to the store square footage.

**Retail sales**
Combined sales of stores owned by Loblaw and those owned by Loblaw's independent franchisees.

**Retail square footage**
Retail square footage includes corporate and independent franchised stores.

**Return on average common shareholders' equity**
Net earnings from continuing operations available to common shareholders divided by average total common shareholders' equity.

**Return on average net assets**
Operating income divided by average total assets excluding cash and cash equivalents, short term investments, security deposits, accounts payable and accrued liabilities and assets of discontinued operations (see non-GAAP financial measures beginning on page 61).

**Same-store sales**
Retail sales from the same physical location for stores in operation in that location in both periods being compared by excluding sales from a store that has undergone a conversion or major expansion in the period.

**Variable interest entity ("VIE")**
An entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest (see note 30 to the consolidated financial statements).

**Weighted average common shares outstanding**
The number of common shares outstanding determined by relating the portion of time within the year the common shares were outstanding to the total time in that year.

**Working capital**
Total current assets less total current liabilities.

**Year**
The Company's year end is December 31. Activities are reported on a fiscal year ending on the Saturday closest to December 31, usually 52 weeks in duration, but includes 53 weeks every 5 to 6 years. 2008 was a 53-week year.

# Corporate Directory

## Board of Directors

**W. Galen Weston**, O.C., B.A., LL.D.(1*)
Chairman and President of the Corporation; former Chairman, Loblaw Companies Limited; Chairman, Holt, Renfrew & Co., Limited, Brown Thomas Group Limited and Selfridges & Co. Ltd.; President, The W. Garfield Weston Foundation; Director, Associated British Foods plc; Member, Advisory Board of Columbia University.

**Allan L. Leighton**
Deputy Chairman of the Corporation; Deputy Chairman and President, Loblaw Companies Limited; Deputy Chairman, Selfridges & Co. Ltd.; Chairman, PANDORA A/S; former Chairman, Royal Mail Group (U.K. Postal Service); former President and Chief Executive Officer, Wal-Mart Europe; former Chief Executive, Asda Stores Ltd.; Director, Loblaw Companies Limited, BskyB plc, Selfridges & Co. Ltd., Holt, Renfrew & Co., Limited and Brown Thomas Group Limited.

**A. Charles Baillie**, O.C., B.A., M.B.A., LL.D.(2*,3)
Corporate Director; Chair, Alberta Investment Management Corporation; Retired Chairman and Chief Executive Officer, Toronto Dominion Bank; Director, Canadian National Railway Company and TELUS Corporation; Chancellor Emeritus, Queen's University; Chair, Art Gallery of Ontario's Board of Trustees.

**Warren Bryant,** B.S., M.B.A.(2,5)
Corporate Director; former Chairman, President and Chief Executive Officer, Longs Drug Stores; former Executive, Kroger Co.; Director, Dollar General Corporation and OfficeMax Incorporated.

**Robert J. Dart**, B. Comm., CA, F.C.A.(4,5)
Director, Vice Chairman and former President, Wittington Investments, Limited; former Senior Tax Partner, Price Waterhouse Canada; Director, Holt, Renfrew & Co., Limited and Brown Thomas Group Limited.

**Peter B.M. Eby**, B. Comm., M.B.A.(1,2,3*)
Corporate Director; former Vice-Chairman and Director, Nesbitt Burns Inc.; former Executive, Nesbitt Burns Inc. and its predecessor companies; Director, Leon's Furniture Limited, Sixty Split Corporation, R. Split II Corporation and TD Asset Management USA Funds Inc.

**Anne L. Fraser**, O.C., C.M., B.Sc., LL.D.(5*)
Corporate Director; Education Consultant, University of Victoria; Associate, Faculties of Education, Engineering, Law and Fine Arts, University of Calgary; President, EnerG Enterprises Inc.; Director, Pier 21 Foundation; active with The Victoria Foundation; former syndicated broadcaster, CBC.

**Anthony R. Graham**, LL.D.(1,3,4*)
President and Director, Wittington Investments, Limited; President and Chief Executive Officer, Sumarria Inc.; former Vice-Chairman and Director, National Bank Financial; Chairman and Director, President's Choice Bank; Director, Loblaw Companies Limited, Brown Thomas Group Limited, Holt, Renfrew & Co., Limited, Selfridges & Co. Ltd., De Bijenkorf B.V., Graymont Limited, Power Financial Corporation, Power Corporation of Canada, Grupo Calidra and Victoria Square Ventures Inc.

**John S. Lacey**, B.A.
Consultant to the Chairman of the Board; Chairman of the Advisory Board, Brookfield Special Situations Funds; former President and Chief Executive Officer, The Oshawa Group (now a part of Sobeys Inc.); Director, Loblaw Companies Limited, TELUS Corporation and Ainsworth Lumber Co. Ltd.

**Isabelle Marcoux**, B.A., LL.B.(2)
Vice-Chair, Board of Directors and Vice-President, Corporate Development, Transcontinental Inc.; Director, Rogers Communications Inc. and Power Corporation of Canada; Board Member, the Montreal Museum of Fine Arts and the Board of Trade of Metropolitan Montreal.

**J. Robert S. Prichard**, O.C., O.Ont., LL.B, M.B.A., LL.M., LL.D.(3,4)
Chair, Torys LLP and Metrolinx; past President and Chief Executive Officer, Metrolinx and Torstar Corporation; President Emeritus, University of Toronto; Director, Bank of Montreal, Onex Corporation and Toronto Community Foundation; Chairman, the Visiting Committee for Harvard Law School; Vice Chair, Canada's Science Technology & Innovation Council; Trustee, Hospital for Sick Children.

**Thomas F. Rahilly**, B.A., M.A., LL.B.(2,4,5)
Corporate Director; Retired Vice-Chairman, RBC Capital Markets.

(1) Executive Committee
(2) Audit Committee
(3) Governance, Human Resource, Nominating and Compensation Committee
(4) Pension Committee
(5) Environmental, Health and Safety Committee

* Chair of the Committee

## Corporate Officers (includes age and years of service)

**W. Galen Weston**, O.C. (70 and 39 years)
Chairman and President

**Allan L. Leighton** (57 and 5 years)
Deputy Chairman

**Paviter S. Binning** (50 and 1 year)
Chief Financial Officer

**Gordon A.M. Currie** (52 and 6 years)
Executive Vice President and Chief Legal Officer

**Robert G. Vaux** (62 and 13 years)
Executive Vice President, Corporate Development

**Robert A. Balcom** (49 and 17 years)
Senior Vice President, General Counsel – Canada and Secretary

**Manny DiFilippo** (51 and 19 years)
Senior Vice President, Risk Management and Audit Services

**J. Bradley Holland** (47 and 17 years)
Senior Vice President, Taxation

**Lucy J. Paglione** (51 and 27 years)
Senior Vice President, Pension and Benefits

**Jeremy Roberts** (48 and 2 years)
Senior Vice President, Finance

**Geoffrey H. Wilson** (55 and 24 years)
Senior Vice President, Financial Control and Investor Relations

**Gabriel R. Crozzoli** (48 and 7 years)
Vice President, Canadian Tax

**David Farnfield** (47 and 14 years)
Vice President, Commodities

**Lina Taglieri** (42 and 10 years)
Vice President, Controller

**Adam Walsh** (37 and 6 years)
Vice President, Legal Counsel

# Shareholder and Corporate Information

**Executive Office**
George Weston Limited
22 St. Clair Avenue East
Toronto, Canada M4T 2S7
Tel: 416.922.2500
Fax: 416.922.4395
www.weston.ca

**Stock Exchange Listing and Symbols**
The Company's common and preferred shares are listed on the Toronto Stock Exchange and trade under the symbols: "WN", "WN.PR.A", "WN.PR.C", "WN.PR.D" and "WN.PR.E".

**Common Shares**
At year end 2010, there were 129,073,662 common shares outstanding, 900 registered common shareholders and 48,349,064 common shares available for public trading.

The average 2010 daily trading volume of the Company's common shares was 120,237.

**Preferred Shares**
At year end 2010, there were 9,400,000 preferred shares Series I, 8,000,000 preferred shares Series III, 8,000,000 preferred shares Series IV and 8,000,000 preferred shares Series V outstanding and 35 registered preferred shareholders. All outstanding preferred shares were available for public trading.

The average 2010 daily trading volume of the Company's preferred shares was:

| | |
|---|---|
| Series I: | 7,181 |
| Series III: | 9,602 |
| Series IV: | 13,322 |
| Series V: | 10,359 |

**Common Dividend Policy**
The declaration and payment of common dividends and the amount thereof are at the discretion of the Board of Directors (the "Board") which takes into account the Company's financial results, capital requirements, available cash flow and other factors the Board considers relevant from time to time. Over the long term, the Company's objective is for its dividend payment ratio to be in the range of 20% to 25% of the prior year's basic net earnings per common share from continuing operations adjusted as appropriate for items which are not regarded to be reflective of ongoing operations giving consideration to the year end cash position, future cash flow requirements and investment opportunities.

**Common Dividend Dates**
The declaration and payment of quarterly common dividends are made subject to approval by the Board. The anticipated record and payment dates for 2011 are:

| Record Date | Payment Date |
|---|---|
| March 15 | April 1 |
| June 15 | July 1 |
| Sept. 15 | Oct. 1 |
| Dec. 15 | Jan. 1 |

**Normal Course Issuer Bid**
The Company has a Normal Course Issuer Bid on the Toronto Stock Exchange.

**Value of Common Shares**
For capital gains purposes, the valuation day (December 22, 1971) cost base for the Company, adjusted for the 4 for 1 stock split (effective May 27, 1986) and the 3 for 1 stock split (effective May 8, 1998), is $1.50 per share.
The value on February 22, 1994 was $13.17 per share.

**Registrar and Transfer Agent**
Computershare Investor Services Inc.
100 University Avenue
Toronto, Canada M5J 2Y1
Toll Free Tel: 1.800.564.6253 (Canada and U.S.A.)
International Tel: 514.982.7555 (direct dial)
Fax: 416.263.9394
Toll Free Fax: 1.888.453.0330

To change your address or eliminate multiple mailings, or for other shareholder account inquiries, please contact Computershare Investor Services Inc.

**Independent Auditors**
KPMG LLP
Chartered Accountants
Toronto, Canada

**Annual Meeting**
The George Weston Limited Annual Meeting of Shareholders will be held on Thursday, May 12, 2011, at 11:00 a.m. in Toronto, Ontario, Canada.

**Trademarks**
George Weston Limited and its subsidiaries own a number of trademarks. These trademarks are the exclusive property of George Weston Limited and its subsidiary companies. Trademarks where used in this report are in italics.

**Investor Relations**
Shareholders, security analysts and investment professionals should direct their requests to Mr. Geoffrey H. Wilson, Senior Vice President, Financial Control and Investor Relations at the Company's Executive Office or by e-mail at investor@weston.ca.

Additional financial information has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR). The Company holds an analyst call shortly following the release of its quarterly results. These calls are archived in the Investor Centre section of the Company's website.

This Annual Report includes selected information on Loblaw Companies Limited, a 62.9%-owned public reporting subsidiary company with shares trading on the Toronto Stock Exchange.

Ce rapport est disponible en français.

**Printing**: Transcontinental Printing www.transcontinental-printing.com.