

2. Overview

Loblaws, a subsidiary of George Weston Limited, is Canada's largest food distributor and a leading provider of general merchandise, drugstore and financial products and services. Through its various operating banners, including 672 corporate stores and 405 franchised stores, Loblaws is committed to providing Canadians across the country with a one-stop destination in meeting their food and everyday household needs. For 50 years, the Company has supplied the Canadian market with innovative products and services through a portfolio of store formats across Canada.

Corporate owned store banners include *Atlantic Superstore*, *Dominion* (in Newfoundland and Labrador), *Extra Foods*, *Loblaws*, *Maxi*, *Maxi & Cie*, *Provigo*, the *Real Canadian Superstore* and *Zehrs* and wholesale outlets operating as *Cash & Carry*, *Presto* and *The Real Canadian Wholesale Club*. The Company's franchised and associated stores operate under the trade names *Atlantic SaveEasy*, *Fortinos*, *no frills*, *SuperValu*, *Valu-mart* and *Your Independent Grocer*. The store network is supported by 26 Company-operated and 2 third-party warehouse facilities located across Canada as well as temporary storage facilities when required.

The Company offers a strong control label program, including the *President's Choice*, *no name* and *Joe Fresh Style* brands. In addition, the Company makes available to consumers *President's Choice Financial* services and products, including the *President's Choice Financial MasterCard*®, and *PC Financial* auto, home, travel and pet insurance, *PC Mobile* phone service, as well as a loyalty program known as *PC points*.

The Company competes in the retail industry in Canada, which is a changing and competitive market. Consumer needs drive industry changes, which are impacted by changing demographic and economic trends such as changes in disposable income, ethnic diversity, nutritional awareness and time availability. Over the past several years, consumers have demanded more choice, value and convenience. Customer satisfaction is central to the success of the Company's business.

The Company competes with non-traditional competitors as well as traditional supermarkets. Recent industry changes have seen the expansion of non-traditional competitors, such as mass merchandisers, warehouse clubs, drugstores, limited assortment stores, discount stores, convenience stores and specialty stores, all of which continue to increase their offerings of products typically associated with traditional supermarkets. Over the past several years, there has been an increase in the number of retail outlets that traditionally exclusively featured food, general merchandise or drugstore items that now offer a selection of these items, resulting in what is commonly referred to in the industry as "channel blurring". This evolution of the retail landscape presents a number of issues for traditional grocers: the need to reposition conventional supermarkets to either expand or, conversely, better focus their offerings; the reality of lower prices offered by discount retailers; and the need to reduce operating and labour costs in order to maintain earnings in light of lower prices and increased competition.

Management's Discussion and Analysis

Since the beginning of 2005 and throughout 2006, the financial performance of the Company has been uncharacteristically poor. 2006 was a year of challenge and change for the Company as it evolves through its continued transformation into a company that will be truly competitive over the long term. The past year saw a number of significant changes in the operations of the Company, including the change in senior leadership. Galen G. Weston was appointed Executive Chairman of the Company's Board of Directors (the "Board"), Mark Foote became President and Chief Merchandising Officer and Allan L. Leighton joined the Board as Deputy Chairman. Early in 2007, Dalton Philips joined the Company as Chief Operating Officer and William M. Wells will be joining the Company as Chief Financial Officer, effective April 2007. A 100 Day Review of the Company commenced in the latter half of 2006 which focused on key drivers of the business such as fresh food presentation, maximizing employee engagement, the performance of retailing basics and customer satisfaction. The results of this review provided key inputs into management's future business priorities and vision for the organization.