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Empire Company Ltd.

Third Quarter Results Conference Call

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CORPORATE PARTICIPANTS

Stewart Mahoney
Empire Company Limited —Vice President Treasury and Investor Relations

François Vimard
Empire Company Limited — Chief Financial Officer

Marc Poulin
Empire Company Limited — President and Chief Executive Officer

CONFERENCE CALL PARTICIPANTS

Perry Caicco
CIBC — Analyst

Michael Van Aelst
TD Newcrest — Analyst

Peter Sklar
BMO Capital Markets — Analyst

Jim Durran
Barclays Capital — Analyst

Chris Li
Bank of America Merrill Lynch — Analyst

Keith Howlett
Desjardins Securities — Analyst

Patricia Baker
Scotiabank — Analyst

Vishal Shreedhar
National Bank — Analyst

PRESENTATION

Operator

Good afternoon. My name is Candace (phon), and I will be your conference Operator today. At this time, I would like to welcome everyone to the Empire Company Third Quarter Results Conference Call.

All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. And if you would like to ask a question during that time, simply press *, then the number 1 on your telephone keypad. And if you would like to withdraw your question, please press the # key. Thank you.

I'll now turn the call over to Stewart Mahoney, Vice President Treasury and Investor Relations with Empire Company. You may begin.

Stewart Mahoney — Vice President Treasury and Investor Relations, Empire Company Limited

Thank you. Thank you, Candace, and good afternoon, everyone. Thank you for joining us today. Our comments today will focus primarily on the financial results for the third quarter ended February 1. Following our comments, we will then be open to your questions. This call is being recorded in live audio on our website at www.empireco.ca.

Joining me on the call this afternoon are Marc Poulin, President and Chief Executive Officer; François Vimard, Chief Financial Officer; and Clinton Keay, Executive Vice President Finance.

Today's discussion includes forward-looking statements. We want to caution you that such statements are based on management's assumptions and beliefs.

These forward-looking statements are subject to uncertainties and other factors that could cause actual results to differ materially from such statements. I refer to you to our news release and MD&A for more information on these assumptions and factors.

I will now turn the call over to François, who will provide a review of Empire's consolidated financial results. Marc will then discuss Sobeys.

François Vimard — Chief Financial Officer, Empire Company Limited

Thank you, Stewart, and good afternoon, everyone. Our third quarter results include the first full quarter of operations from the recently acquired Canada Safeway.

Consolidated sales in the third quarter were 6.02 billion compared to $4.29 billion in the third quarter last year, an increase of 1.73 billion or 40.4 percent. Excluding sales of 1.62 billion related to the acquisition of Canada Safeway, sales increased by 115.4 million, or 2.7 percent.

Sobeys same-store sales growth was negative 0.2 percent in the quarter. Same-store sales were impacted by low food inflation, which we pegged around 0.5 percent lower than the published CPI. And also by increased competitive square footage in the market, ongoing competitive intensity, and a severe ice storm in Ontario during the third quarter of fiscal 2014.

Consolidated EBITDA in the third quarter was 188.9 million compared to 195.6 million in the third quarter last year. EBITDA in the quarter was impacted by increased inventory shrink primarily associated with new standards we have rolled out in our fresh department, as well as shrink associated with the new and innovative merchandising program, part of the Sobeys' strategy to help Canadians to Eat Better, Feel Better, and Do Better.

Also by a highly promotional environment, a weaker Canadian dollar relative to the US dollar, ongoing drug regulatory reform which impacts generic prescription reimbursement rates, and increased selling and administrative expenses, which were primarily due to transaction costs associated with the Canada Safeway acquisition, offset by $83.2 million in EBITDA related to the Canada Safeway acquisition during the quarter.

After adjusting for items which are considered not indicative of underlying business operating performance, third quarter adjusted EBITDA amounted to 277.4 million compared to 201.8 million in the third quarter last year, or 75.6 million, 37.5 percent increase.

Finance costs, net of finance income, for the third week ended February 1, 2014, were 49.7 million, an increase of 37.2 million compared to 12.5 million recorded in the same period last year. The increase was primarily a result of higher interest expense of 33.8 million due to the increased debt level this quarter as a result of financing from the Canada Safeway acquisition.

Empire recorded adjusted net earnings from continuing operations net of non-controlling interest of $77.3 million, or $0.84 per diluted share, for the 13 weeks ended February 1, 2014, compared to 75.8 million, $1.11 per diluted share, recorded in the third quarter last year based on 92.1 million shares this year outstanding versus 68.1 million shares last year.

With respect to our overall consolidated financial condition at the end of the third quarter, Empire's consolidated ratio of funded debt to total capital was 40.6 percent with cash and cash equivalents of 284.6 million.

Now I would like to make a few remarks on Empire investment and other operation, largely comprised of equity interest in Crombie REIT and Genstar. Total adjusted net earnings for continuing operations were 5.6 million in the quarter compared to 5.2 million last year.

At the end of the third quarter, the fair value of our 41.6 percent equity accounted ownership interest in Crombie REIT, 39.3 fully diluted, was 681 million on a carrying value of 336 million. For detailed information on Crombie REIT performance, please see their latest quarterly release dated February 27th.

On the residential property side, Genstar contributed equity earnings to Empire of 8.4 million at the third quarter compared to 6.7 million last year.

Now I would like to turn to Marc.

Marc Poulin — President and Chief Executive Officer, Empire Company Limited

Thanks, Francois, and good afternoon, everyone. Our growth in consolidated sales of 40.4 percent and adjusted EBITDA of 37.5 percent from the third quarter last year largely reflects the initial impact of the Canada Safeway acquisition, and the continued launch of our new innovative commercial programs as part of the Company's strategy to help Canadians Eat Better, Feel Better, and Do Better in what remains a highly competitive marketplace.

The market environment in the third quarter remained challenging. Promotional activity was—we can describe as intense.

We continued to be price competitive this quarter and try to protect our market share, and we followed up on the development and rollout of new commercial programs aligned with our Better Food For All movement. This impacted our gross margin performance in the quarter.

Sobeys recorded gross profit for the 13 weeks ended February 1, 2014, of $1.47 billion, an increase of 491.6 million or 50.2 percent compared to 980.2 million in the same quarter last year. The increase in gross profit is largely a result of a 483.3 million gross profit contribution related to the Canada Safeway acquisition, which is net of the one-time inventory adjustment of 17.1 million, and $6.3 million of cost reductions as a result of synergies realized during the quarter related to the acquisition.

Gross margin increased 158 basis points to 24.51 percent in the third quarter compared to 22.93 percent for the quarter ended February 2, 2013. The increase is primarily a result of the Canada Safeway acquisition. Excluding the impact related to Canada Safeway, gross margin would have been 22.53 percent of sales, a decrease of 40 basis points compared to the prior year.

Overall gross profit and gross margins were impacted in the quarter by the following factors: increased shrink primarily associated with new standard rollouts in our fresh department, as well as shrink associated with the new and innovative merchandising programs launched as part of Sobeys' strategy to help Canadians Eat Better, Feel Better, and Do Better; a highly promotional environment; a weaker Canadian dollar relative to the US dollar, which affected the Canadian dollar cost of US purchases; and ongoing drug regulatory reform, which impacted generic prescription reimbursement rates.

We are working diligently to successfully integrate the Canada Safeway business, and are focused on continuing to secure operational efficiencies and reducing costs across the network. I'll provide here some highlights of our progress.

On Safeway integration. The technical integration of Safeway and Sobeys is underway, which primarily involves the adoption of SAP functionality into the Safeway IT infrastructure. This includes the conversion of transactional systems with finance, payroll, store's merchandising, and distribution.

This integration, when complete, will allow us to fully leverage Sobeys' national SAP platform. Everything's on track, and our synergy work progressed in each functional area and it's really going as planned.

Overall, we remain confident in our ability to secure $200 million in annual run rate cost synergies over a three-year period, and we'll continue to update each of you in every one of the quarters in the process.

On cost reduction. Over the past number of years we have implemented shared services models where our transactional accounting, general accounting, and master data management function have been centralized, eliminating duplication of these services across the country.

We intend to continue to leverage our centralized shared services model by continuing to eliminate unnecessary or duplicate costs. Most recently, we have communicated to employees in two regional offices, Calgary and Rouyn in Quebec, that we are moving roles to shared services, which will result in the elimination of roles within those two offices.

Over the past six years, we have driven efficiencies in our distribution network through the development of automated distribution centres, one in Vaughan, Ontario, and one in Terrebonne, Quebec.

We are moving forward with an expansion of the Vaughan facility to handle frozen and dairy for our source in the Ontario province. When the expansion is completed in 2016, distribution of produce and meat categories will be consolidated into one of Sobeys' existing conventional distribution centres, either Milton or Whitby. The remaining distribution centres will then close.

While we continue to assess the manufacturing assets that we acquired as part of the Canada Safeway purchase, we have made the decision to close the ice cream and cheese manufacturing facility in Winnipeg. This facility is undercapacity, and as there is a similar facility in Edmonton, we'll be able to consolidate the ice cream volume production in the Edmonton facility, and therefore significantly improve our efficiencies.

And we are making good progress on noncore asset sales. As you may know, on February 133, 2014, we announced that Sobeys entered into a binding purchase agreement with the Overwaitea Food Group and with Federated Co-op Limited to purchase 22 of the 23 retail store required to be divested as part of the Canada Safeway acquisition, as well as seven additional stores in British Columbia.

The sales are expected to occur during the Company's fourth quarter of fiscal 2014 and the first quarter of fiscal 2015. Sobeys has also signed a binding letter of intent with another retailer for the sale of one retail store which is also required to be divested as part of the Canada Safeway acquisition.

Total proceeds from the transaction with Overwaitea Food Group and Federated Co-op will be approximately 430 million, plus the value of inventory on closing, subject obviously to customary closing adjustments. Proceeds will be used to repay bank borrowing.

We will continue to assess our other noncore assets as a means to reduce our debt, and are committed to making our operations more efficient. And we will continue to make important decisions to reduce costs within our business.

As we have said before, the Canada Safeway acquisition represents a highly strategic opportunity for Sobeys to leverage its existing asset base and effectively create a new platform for growth.

Notwithstanding the significant focus we've put on the effective integration of Canada Safeway, we are also advancing our business by improving our overall customer value proposition through our Better Food For All movement. Certainly costs were incurred in the quarter related to the launch of new innovative programs. This is nonetheless very important for the future growth of the Company.

I invite all of you to visit our new Sobeys Extra stores in Burlington, Ancaster, Aurora to get a taste of this offering. Since last October, we also opened new concept stores in Winnipeg, Calgary, St. Catharines, London, and Flamborough.

In closing, we know that any period of heightened promotional activity will generate quarter-to-quarter volatility. I mean this is simply the nature of this business. We have experienced it many times before, and we know that in the future we'll experience periods like that, but we are a long-term player, and over time we are confident that we will continue to profitably grow the business, remaining committed on long-term growth prospects for the business.

We are now happy to respond to your questions.

Q&A

Operator

And at this time, if you would like to ask a question, please press *, then the number 1 on your telephone keypad.

And your first question comes from Peter (sic) (Perry) Caicco with CIBC. Your line is now open.

Perry Caicco — CIBC

It's Perry Caicco calling. Can you tell us about what the same-stores sales trend at Safeway might be; maybe the trend over the last few quarter and recently? And to what extent you think you can impact those and how fast?

Marc Poulin

Clearly the trend on the sales coming in to the acquisition was a little below what we would have liked. And we are clearly taking advantage of what opportunities we have through direct merchandising programs to address some concerns we have in some categories, and we’re diligently working on the overall picture from a Safeway point of view.

So it's not only a question of integration, but we're also dynamically running the business.

Perry Caicco

And on the topic of synergies, I know you've affirmed the target. How do you see the synergies tracking over the course of the remainder of this fiscal year into next fiscal year?

François Vimard

Clearly, Perry, like we said, I think we’re going to reach a run rate of 100 million at the end of the first year which should be Q3 next year, so you should see a ramp up. You saw 6.3 million this quarter. Part of that also because of some accounting rules we had to reserve against inventory, so it already that internal generation of pure net synergy, but you should see the ramp-up to get to a run rate by Q3 next year will be at that $100 million.

Perry Caicco

And lastly, the SG&A costs at the core Sobeys business seemed quite high. I'm just wondering, you mentioned that you're obviously spending on some of your new programs, such as the Better Food For All, but I'm wondering if you could indicate what exactly has driven the SG&A up. Are there any sort of one-time items in there specific to the core business that seems to have elevated the expenses in this quarter?

François Vimard

Yeah. Let me clarify a bit on the SG&A side because I think people through the press release were a bit confused about some numbers, so let me clarify that. If you exclude the—because as we said on the Sobeys side, purely the food (phon) business generated 267 million of EBITDA and Safeway 83.2, so if you subtract you arrive at an EBITDA for the Sobeys business.

And like Marc said, on the gross profit side we did generate 22.6, 53 percent of gross margin on the Sobeys side, which is 40 basis points lower than the Q3 last year. And net, if you look at EBITDA, the SG&A went down by 10 basis points to generate that EBITDA.

So on the core business, excluding Safeway, our SG&A was down 10 basis points, not as much as it was in Q2. And like Marc said, we're still working on many activities to continue to reduce SG&A, but the trend wasn't up. It was down on the core business of Sobeys.

On the Safeway side because of the prospectus and the way the accounting was done on a GAAP basis, there were around 425 basis points that were moved from margin to SG&A, so margin went up by 425 points, but SG&A also went up by 425 points. So that's why if you merge the two you see how the SG&A went up, but when you re-class, I would say, or separate the two between Sobeys and Safeway, you can see how the gap is more on the gross profit than on the SG&A.

Perry Caicco

And sorry, what are the items that you've had to reclassify at Safeway.

François Vimard

Because on a GAAP basis I would say distribution cost, for example, manufacturing cost, even some advertising expenses were all net of the gross profit when Safeway was reporting the numbers in the past, and now they are in SG&A.

Perry Caicco

Okay. Thank you.

François Vimard

Okay.

Operator

And your next question comes from Michael Van Aelst. Your line is now open.

Michael Van Aelst — TD Newcrest

Yes. Thanks. Just continuing on the lines of Safeway, when they were reporting their results for the last few quarters, we saw the EBITDA trends at the Canadian business declining progressively more, I guess, as calendar 2013 went on. Can you give us an idea of how Safeway's

EBITDA may have trended year over year for the 13-week period that you reported it for, and give us an idea of what the seasonality might be across your four quarters?

François Vimard

Yeah. So clearly it's really down because the key pressure they have on their EBITDA it comes from two sides. First on the pharmacy side, as you can imagine, because of the strength of their pharmacy, they are more impacted than the rest of our Sobeys business on the pharmacy side, and because of two elements. The first element clearly is the generic cost, as you know, and the generic reduction in terms of revenue it can get, but also the fact that in BC there were a change in term of some regulation coming from the Pharmacy Association. And then we can't incent any more script count—script revenues.

So people, I would say, moved some of their scripts to other pharmacies because they don't get the incentive of 7 Air Miles anymore from our pharmacy. So those two elements in fact impacted our pharmacy numbers for sure on the Safeway side.

And one element also you have to consider. Clearly there's some seasonality in their business, like it is in our business. Q3 is always a softer quarter for us than the three other quarters. So there's some element also in that.

So if you want to understand the full EBITDA level for Safeway you have to take that consideration. But clearly their EBITDA numbers were softer than last year mainly impacted by pharmacy and impacted also by some impact coming from the softness on their sales and also the currency in terms of the US dollar going up. So...

Michael Van Aelst

Are you able to tell us whether the EBITDA—the degree to which EBITDA was down at Canada Safeway for that 13-week period?

François Vimard

Sorry, I didn't understand your question there, Mike.

Michael Van Aelst

Are you able to quantify the percentage decrease in EBITDA Canada Safeway for that 13-week period?

François Vimard

Yeah. We were able to.

Michael Van Aelst

Are you able to disclose it to us, though?

François Vimard

No. It's not something we want to—because it's overall business we want to talk about.

Michael Van Aelst

Okay. Second question is on the procurement savings that are part of your synergy target. Typically procurement is a big part of the synergy numbers, and it's been reported pretty widely in the press that you've been looking for a 1 percent reduction in your prices from suppliers. It sounds like there's a big pushback there, and I'm wondering if you can give us any kind of an update as to how procurement savings are coming along?

Marc Poulin

Well, the discussions with our suppliers are ongoing. We are pleased with what we're seeing so far.

I think suppliers are realizing that we have a lot to offer in terms of partnering with them to drive our mutual business. And to be honest, we believe that everything is on plan in that regard.

Michael Van Aelst

All right. Thank you.

Operator

Question comes from Peter Sklar. Your line is now open.

Peter Sklar — BMO Capital Markets

Thank you. I'm just wondering if we could go back to the shrink issue that you had talked about at Sobeys. Can you just elaborate a little bit further why it occurred, what was the financial impact, and how do you see that unfolding? Is it also going to have an impact in the fourth quarter and future quarters?

Marc Poulin

Well, we launched a number of new programs under the Better Food For All movement, and it was not only supported from an advertising point of view, but as you launch new programs at store level, before these programs become fruitful you do incur additional shrink. So that's clearly an element that impacted the quarter.

But long term, these programs will create differentiation that will make the business stronger. So obviously it's something that we feel is important, and as any manufacturer launches new programs they incur costs. The same thing at retail; when you launch a new program you do incur cost not only from a shrink point of view, but training and everything else. We also modified some standards in our merchandising programs how we—around some fresh programs, and experienced some difficulties in ensuring that the appropriate level of stock versus the sales and the new standards were aligned.

And obviously this is something that is operational in nature that we need to correct, and we're working diligently on doing so. But those were done for the benefit of our customers to make sure that we have the best offer that will long term generate healthier business.

Peter Sklar

And then, Marc, can you quantify the negative impact that the shrink issue had on earnings during the quarter?

François Vimard

We can't quantify, but I would say it's a big part of it, but we won't provide a specific number. But it's a big part of it.

Peter Sklar

And when is it going to work its way through? Is it going to be something that's going to also impact the fourth quarter?

François Vimard

It takes always some time to adjust those programs, as you know, Peter. Because it takes time to understand not only the new program because you have to understand that sales of the stores and how the customer react, all that stuff, but also retraining of some of our employees to be sure they understand the standard attached to it. So it’s going to take some time.

Peter Sklar

Okay. And if I could just switch back to you were talking before about the EBITDA at Safeway. Would the additional rent—you listed a bunch of items that negatively…

François Vimard

Yeah.

Peter Sklar

Impacted Safeway. Would there also have been the additional rent…

François Vimard

Yeah.

Peter Sklar

Related to the sale and leaseback?

François Vimard

Yeah. Clearly, Peter. And for me it was obvious because we disclose it pretty clearly in our prospectus that, as you know, we've sold $1 billion of assets to Crombie, and we have evaluated the rent attached to $1 billion around 57 million a year. So clearly you have that impact there EBITDA for the quarter, so for sure.

Peter Sklar

Yeah. So I believe that that sale and leaseback happened at the beginning of the quarter, so it would just be a quarter...

François Vimard

Yeah. That was done at the time of the transaction. So it was for the full quarter.

Peter Sklar

Yeah. Okay. And just my last question; on the 29 stores that are going to be sold in Q4 and Q1. I just want to know what the accounting treatment is in Q4. Will they be classified as discontinued? Or how are they...

François Vimard

Yeah. Some of them will be closed, so we hope they won't be on our balance sheet and we'll have the cash in the bank. And the others would be considered clearly as discontinued.

Peter Sklar

Sorry, I didn't hear. They will be…

François Vimard

As discontinued, yeah, clearly.

Peter Sklar

Okay. Thank you.

Operator

Your next call comes from Jim Durran. Your line is now open.

Jim Durran — Barclays Capital

Good afternoon. Just wanted to start off with the inventory adjustment of 17.1 million; so was it related to actual product that you're no longer going to be selling or a reduction in the value of that inventory and you're still going to sell it?

François Vimard

Jim, I don't want to go into detail of the accounting rules, but I'm going to try to simplify that. When we acquired the business, as per the rule of IFRS, we have to evaluate the inventory at the fair market value. And so that fair market value was evaluated for those inventory we acquired with Safeway, which they include because they had inventory at store level and in DC, so there's some cost that has to be, I would say, put in the value of those products when we acquired.

So it was just at the time of the acquisition we did that. And as you can imagine, because we turn our inventory around almost every month, so the first month of that quarter we sold that inventory, so that 17 million came and impacted us. But going forward that will be a no issue because then we're going to evaluate inventory as we always did.

Jim Durran

So...

François Vimard

So it's not specific product. It's all the inventory we bought from Safeway…

Jim Durran

Yeah.

François Vimard

That was evaluated at fair market value the day we acquired the business, and that inventory was sold the first period of that quarter.

Jim Durran

And so when you provided disclosure that Safeway's EBITDA was 83.2 million, the inventory adjustment was not included in that number? Or...

François Vimard

No because we kept that number at the corporate level not to impact specifically the Safeway business.

Jim Durran

But if I'm going to look at what the true earnings power was of Safeway Canada in the quarter and then look at it as a way to sort of project the next subsequent quarters…

François Vimard

Yeah.

Jim Durran

Truthfully the profit of the business before the inventory adjustment would have been 100.3 or 100.4 million, not the 83.2 then.

François Vimard

No. No, Jim. Like I said, that 17 million of impact we didn't put it—because it was based on—caused by the acquisition…

Jim Durran

Yeah.

François Vimard

We didn't want to put that in the Safeway number. We kept that at corporate level. So the 83—the real generation of EBITDA for Safeway during the quarter was 83.2.

Jim Durran

Okay. Thank you. On FX, obviously there's been some commentary by your competitors about success of passing through the Canadian dollar weakness into higher retail prices. Can you give us some idea as to how that's worked for you, both at regular price and promo price?

François Vimard

Well, on FX, as you note, especially as it relates to perishable, the market reacts sooner than it does on non-perishable items, so that's why some of it we've been able to pass through. But the reality is there's always a lag, and in times of decrease in Canadian dollars, especially this time around it was very impactful because everything we were purchasing was imported. On the produce department, for example, I mean it's—so it was not a great period to experience a decline in the Canadian dollar.

So that lag had an impact on gross margin before we could actually pass some of it to our customers. But that being said, I mean the market remains very competitive, and it's hard work to pass it down, so that's why we probably experienced a little bit more inflation this quarter than in the previous quarter. And I would say it’s mainly due to the ability to pass some of that, but I would be lying if I were to say it was neutral in the quarter. It's not the case at all.

Jim Durran

Okay. No, that’s good. That's helpful. And last question, François. Just on the interest expense in the quarter, excluding the fact that when you divest—get the divestiture proceeds you're going to reduce your debt. Is the $49-plus million in the quarter in your view a run rate for the interest expense related to the existing debt?

François Vimard

Yeah. There were some one-time costs, but limited, I would say. Maybe 2 million or 3 million was kind of one-time because of financing cost in the way we account for that, but yes, it is. But as you know also with the divestiture we announced in February 13 we're going to reduce our debt by another 400 million there, and like Marc said, we're looking at other potential noncore assets to dispose. So over the next few quarters you're going to see a reduction of our debt, which will impact our financing cost for sure.

Jim Durran

And so you'll presumably reduce the term revolving facility first, right, as the most expensive...

François Vimard

Yeah. The first one we still have outstanding is the 200 million bridge assets loan, so that's going to be the first one clearly, and then after that it's going to be to the term loan, clearly.

Jim Durran

And what's the effective rate on that term loan?

Stewart Mahoney

It's a little over 4 percent at this point, Jim.

Jim Durran

Okay. Great. Thanks, Stewart.

Operator

And your next question comes from Chris Li. Your line is now open.

Chris Li — Bank of America Merrill Lynch

Good afternoon. Sorry, just maybe a couple of follow-up ones on the Safeway question. So thanks for the clarification first on the 83 million of EBITDA, so I guess based on that, the 5.1 percent was really what the underlying EBITDA margin for the business. And I think based on the last filings, I think Safeway Canada was doing about 6.5 percent of EBITDA margin, even including the 57 million of incremental rent expenses. So I just want to make sure I heard you correctly. So the step down in margin is really mostly because of the former regulations and because of the weakness in the Canadian dollar that represented the bulk of that margin step down. Is that correct?

François Vimard

Yeah. The two additional elements that I mentioned, but you're right, those are the two key ones…

Chris Li

Okay.

François Vimard

But it is also because of the softness on the sales it did affect also their operating costs. And the key point also, like we said, there’s some similarity in their numbers, so their Q3 numbers is only a bit softer than the others, but you mentioned the two major ones.

Chris Li

Okay. And yeah, so I guess my other question is, understanding there's some seasonal impact, I guess from a modelling perspective, I mean is sort of the mid 5 percent is sort of what we should we be thinking about going forward on the Safeway business?

François Vimard

We don't, as you know, Chris, we don't give any forecasts, and we're going to work hard to be as high as possible.

Chris Li

Okay. And then just on the gross margin. Again, I just want to confirm the 483.3 million from Safeway; that also excludes the 17 million inventory adjustment?

François Vimard

Yeah. Yeah. Exactly.

Chris Li

Okay. So on that, the margin on Safeway was about almost 30 percent, which is I think a couple of hundred basis points higher than what that business did before. And I just want to make sure there's no sort of accounting reclassification that...

François Vimard

No. And like I said to Perry, it's because of the re-class we did between the US GAAP and the IFRS…

Chris Li

Okay.

François Vimard

So the gross margin increased by around 425 business point, but the SG&A also increased by 425 basis points.

Chris Li

Okay. So on a like-for-like basis?

François Vimard

Yeah. Compared to what you saw before when the US were producing the numbers.

Chris Li

I understand. Okay. Thank you. I'll just get back into line. Thank you.

François Vimard

Thanks a lot.

Operator

Next question comes from Keith Howlett. Your line is now open.

Keith Howlett — Desjardins Securities

Yes. I just wanted to ask on the shrink program. Has that been being rolled out to the whole system? Or is it just in some stores?

Marc Poulin

No, it's an initiative that launched across what we called the Sobeys multi-format operation.

Stewart Mahoney

So all the Sobeys stores…

Marc Poulin

So all the Sobeys stores across the country and some Thrifty stores.

Keith Howlett

And would—in terms of the standards, is this to ensure sort of a higher degree of freshness or something of what's actually sold?

Marc Poulin

It's not something. It's a higher degree of freshness, yes.

Keith Howlett

Oh okay.

Marc Poulin

It's a better experience for the customer when purchasing products from our stores.

Keith Howlett

So is that in the nature of sort of a bit of a one-time thing as you adjust to the new standard? Or does that take time to sort of work itself into the system consistently?

Marc Poulin

It's clearly growing pains as we adapt those new standards. Some stores are adapting better than others and they need to—we need to readjust our production and ordering patterns so that—and some stores are doing a better job than others at doing so. So we clearly need to work the tools we have and go back in some cases to properly execute around those new standards.

Keith Howlett

And is it sort of the evenly pretty much across the seafood/meat/perishables/produce? Or is it mostly in say produce? Or mostly in fish?

Marc Poulin

Well, some departments are more impacted than others. It's not uniform, but it does impact the fresh side of the store by opposition to grocery, as you can imagine.

Keith Howlett

Great. Thanks. Thanks very much.

Marc Poulin

Pleasure.

Operator

Again, if you would like to ask a question, please press *, 1.

And your next question comes from Patricia Baker. Your line is now open.

Patricia Baker — Scotiabank

Yeah. Good afternoon. I know—most of my questions have been answered, but I just want to go back to this reclassification. And just I know you didn't want to give us last year's Safeway numbers, but if you went back and reclassified last year's Safeway numbers, would there have been a discernable change in trend either on COGS or SG&A comparing year over year?

François Vimard

I would say the key impact, and that's we've what said, is mainly on the gross profit side…

Patricia Baker

Okay.

François Vimard

Because of the impact of the pharmacy and the currency.

Patricia Baker

Okay. Yeah.

François Vimard

That's on the sales, so you're going to see it impact more on that than on the SG&A side.

Patricia Baker

Okay. And the SG&A just would have been it's simply just this reclassifications. Okay. That's a good clarification.

François Vimard

Yeah, yeah. Clearly, and if you look at our press release also we talk about, yeah, we're starting to invest a bit on the Safeway integration, so there's a 2.2 million of investment quoted for that, so there's some cost associated with that, but it's mainly on the gross profit.

Patricia Baker

Brilliant. Okay. Thank you.

Operator

Your next question comes from Jim Durran. Your line is now open.

Jim Durran

Sorry, I know everybody is sort of focused on the same thing, but if I look at the Sobeys' SG&A and it was up say 2 percent in the quarter and you've been largely flattish up to now, but you are talking about continued cost savings initiatives. And not necessarily being part of the synergy bucket, do you expect your SG&A to be up 2 plus percent in the coming quarters? Or do you see opportunities to contain that even more?

François Vimard

Yeah. You're talking about up 2 percent, but in terms of percentage of sales it was down 10 basis points…

Jim Durran

Yeah.

François Vimard

So just to be sure we're talking about the same thing. Clearly, and Marc mentioned, the many activities we have going on, so clearly our goal is continue to see a decrease in the G&A going forward.

Jim Durran

Great. Thank you.

Operator

Question comes from Vishal Shreedhar. Your line is now open.

Vishal Shreedhar — National Bank

Thank you very much. Just given the current EBITDA generation trends, do you feel comfortable with your debt reduction targets over the next few years? Or will you change views on potentially asset sales or something of that like?

François Vimard

No, no. We're pretty confident about that, clearly. As you saw from the divestiture of the store, we're getting more capital there than we were planning for, and from what we saw from other elements that we could sell, we're pretty confident about the target we have in terms of debt reduction.

Vishal Shreedhar

Okay. And just in terms of the way you go to market currently, just given the difficult backdrop, does the balance sheet you have right now impact that way that your merchandising strategy unfolds currently? Or is that not a factor?

François Vimard

Not at all. Because we were so successful in terms of the financing of the acquisition, I think we're in good position.

Vishal Shreedhar

Okay. Thank you. That's it.

Operator

Question comes from Keith Howlett. Your line is now open.

Keith Howlett

Yes. I just wanted to ask about the FreshCo stores, and I noticed you've got some stores with licensed fish and meat departments. I'm just wondering how that is working out and how you look at that going forward?

Marc Poulin

We're still very happy with the way the FreshCo banner is evolving. I wouldn't say that we're not challenged like everybody in the marketplace by the dynamic of what's happening in Ontario on the pricing front.

But that being said, overall, consumer acceptance of the FreshCo concept keeps on growing, and that we're extremely pleased with. We're clearly building a solid business on FreshCo.

Initiatives like the one you just mentioned are an element of that, and we will continue to offer those services in the markets where it warrants it, and allows us to basically differentiate our offering specifically in markets where ethnic meat and fish are required to be relevant to the consumer.

Keith Howlett

Thank you.

Operator

Next question comes from Chris Li. Your line is now open.

Chris Li

Hi. Do you subsidize your franchisees when you—in terms of pricing and promotions? And if so, do you expense that through your SG&A expense line?

François Vimard

We don't want to talk specifically about a program with our franchisee, but clearly we are always conservative the way we account for things. So clearly it's part of SG&A if we need to support in any way our franchises.

Marc Poulin

But it's also supported through gross margin on the wholesale line, so if we need to give price support for flyer activity, for example, this will also get—this will impact our wholesale gross margin line.

François Vimard

Yeah. It could be on both lines, you're right.

Chris Li

Okay. And then sorry if you covered this already, with respect to the impact of the weaker currency, I think some of your other competitors have recently talked about able to pass through some of the cost increases. Are you finding now are you able to pass on the cost increases from the weaker dollar?

Marc Poulin

As I said previously on the call, we've had some success. There's a lag clearly between the actual timings of things.

That being said, I don't want to make it look it's the nirvana of price increases in this country right now. It's very difficult to get price movement, even on commodities where everybody—the cost increase for everybody is not always, so it's unfortunately a market that's digesting significant additional square footage, everybody's fighting for their ground tooth and nail, and everybody's watching everybody. And nobody wants to be the first to blink, so these dynamics don't make for a market where it's easy to pass along any price increase…

Chris Li

Okay.

Marc Poulin

Any cost increase in pricing.

Chris Li

Okay. Just my last question is you mentioned, I think, in your opening remarks about eliminating some of the duplicate services in Calgary and in the market in Quebec, and also closing the ice cream facility in Winnipeg. Can you just remind us the timing of those two events and the charges that you expect to incur and what the expected cost savings will be?

Marc Poulin

Some announcements were done recently in Q4, and the decisions were taken recently. Some moves were done in the—like some reshuffling activity occurred as the business goes. So it—but I would say, for example, the ice cream facility announcement and the announcement in Rouyn are very recent events.

François Vimard

So some of those elements (phon) you're going to see some charge in Q4, and some require way more work because there are a lot of work to be done before being finalized, but being sure we're going to disclose it in a way you can understand that.

Chris Li

And then in terms of potential costs savings?

François Vimard

Savings? They're going to be good.

Chris Li

Any sort of number around what you mean by good?

François Vimard

It's supporting, Chris, like we said, supporting a reduction of our overall SG&A.

Chris Li

Okay.

François Vimard

And keeping a trend that we have done over the past few years.

Chris Li

Okay. Thanks. Thank you.

Operator

Question comes from Jim Durran. Your line is now open.

Jim Durran

I promise it's my last question. Tax rate. The tax rate in the quarter was low for the reasons mentioned. Is that an isolated quarter incident? Or is that going to carry on for a few quarters?

François Vimard

No. It is as you saw. It's pretty specific because of all the one-time and everything that happened during the quarter, but you should foresee, like we said in the past, a tax rate around 26 percent.

Jim Durran

Great. Thank you.

Operator

And we have no further questions at this time. I turn the call back to our presenters.

Stewart Mahoney

Thank you, Candace, and thank you, ladies and gentlemen. We appreciate your continued interest in Empire, and look forward to having you joining us for our Q4 conference call on June 26th.

Good-bye.

Operator

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

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