



# IFRS 16 Investor Education Session

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Katie Brine, Director Finance & Investor Relations  
Phone: 905-238-7124 x2092  
Email: [katie.brine@sobeys.com](mailto:katie.brine@sobeys.com)

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## Forward-Looking Information

This document contains forward-looking statements which are presented for the purpose of assisting the reader to contextualize the Empire Company Limited's ("Empire" or the "Company") financial position and understand management's expectations regarding the impact of IFRS 16 Leasing standard. These forward-looking statements may not be appropriate for other purposes. Forward-looking statements are identified by words or phrases such as "estimates", "plans", "predicts", "anticipates", "forecasts" and other similar expressions or the negative of these terms.

By its nature, forward-looking information requires the Company to make assumptions and is subject to inherent risks, uncertainties and other factors which may cause actual results to differ materially from forward-looking statements made. For more information on risks, uncertainties and assumptions that may impact the Company's forward-looking statements, please refer to the Company's materials filed with the Canadian securities regulatory authorities, including the "Risk Management" section of Empire's fiscal 2019 annual MD&A.

## Non-GAAP Financial Measures & Financial Metrics

There are measures and metrics included in this IFRS 16 investor education presentation, such as EBITDA, adjusted EBITDA, adjusted earnings per share, same-store sales, and free cash flow that do not have a standardized meaning under generally accepted accounting principles ("GAAP") and therefore may not be comparable to similarly titled measures and metrics presented by other publicly traded companies. The Company includes these measures and metrics because it believes certain investors use these measures and metrics as a means of assessing financial performance.

For a complete description of Empire's non-GAAP financial measures and financial metrics, please see Empire's MD&A for the fiscal year ended May 4, 2019.

# Key Messages

## No Impact on:

- Business strategy
- Business operations
- Cash flow generation

## Key Changes:

- IFRS 16 introduces a balance sheet recognition and measurement model for lessees, eliminating the distinction between operating and financing leases
- Presentation of financial statements:
  - For historical operating leases where the Company is the lessee, leases will be recognized on the Balance Sheet
  - On the Statement of Earnings, straight-line lease expense is replaced with depreciation for right-of-use (ROU) asset and finance expense on lease liability
  - Classification of amounts on the Cash Flow Statement will change
- Additional financial statement disclosure requirements

## Empire's Approach

- Elected to use the modified retrospective approach
  - Applied standard from the beginning of May 5, 2019 for fiscal 2020
  - No restatement of prior year financial information
  - Recognized an equity adjustment in equity at the beginning of fiscal 2020
  - Publishes additional disclosures as per the new standard; exempt from certain disclosures required by paragraph 28 of IAS 8 on a change in accounting policy

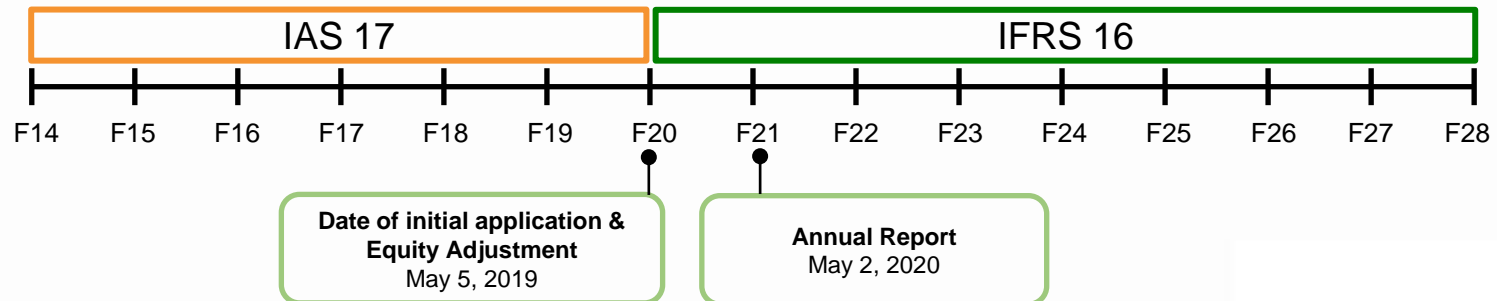


Illustration: 15 year lease term, annual payments of \$100K (increase by 7.5% every 5 years) and incremental borrowing rate (IBR) 4%

Key Highlights	ROU Asset	Lease Liability
<b>Calculation</b>	Term: 6 years (retrospective) Payment: \$100K + 7.5% in year 6 IBR: 4%	Term: 9 years (remaining lease payments) Payment: \$108K + 7.5% in year 11 IBR: 4%
<b>Value at date of application</b>	\$721,950	< \$850,657
<b>Equity Adjustment: May 5, 2019</b>		\$128,707

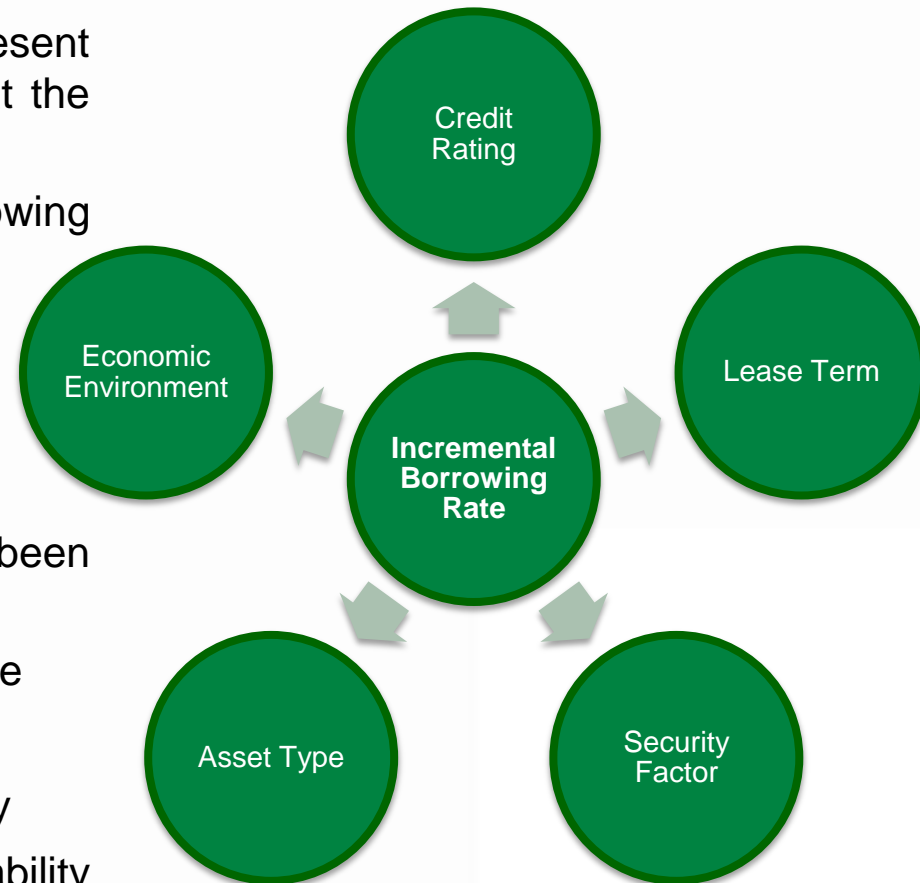
## IFRS 16 Lease Liability & Right-Of-Use Asset

### Lease Liability

- Lease Liability is measured as the present value of the remaining lease payments at the date of initial application, May 5, 2019
- Discount rate used is incremental borrowing rate as of May 5, 2019
- Rate for each lease is dependent on lease term

### Right-Of-Use Asset

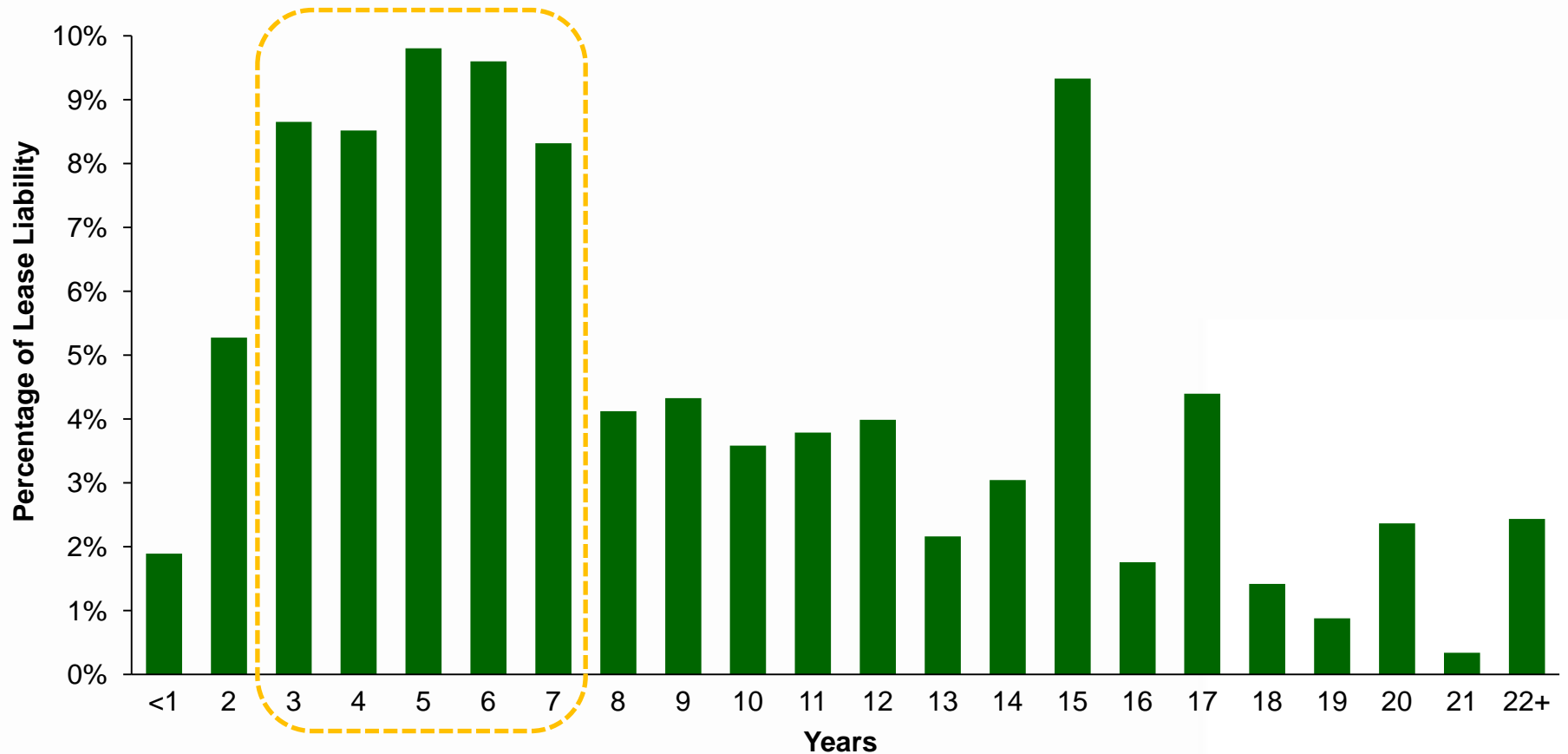
- Measured as if IFRS 16 had always been applied (retrospective)
- Reflects the ROU asset depreciation profile
- Used the incremental borrowing rate as of May 5, 2019 on transition for the Company
- Future ROU asset will equal lease liability upon recognition for new leases



**Weighted average discount rate on transition is 4.4%**

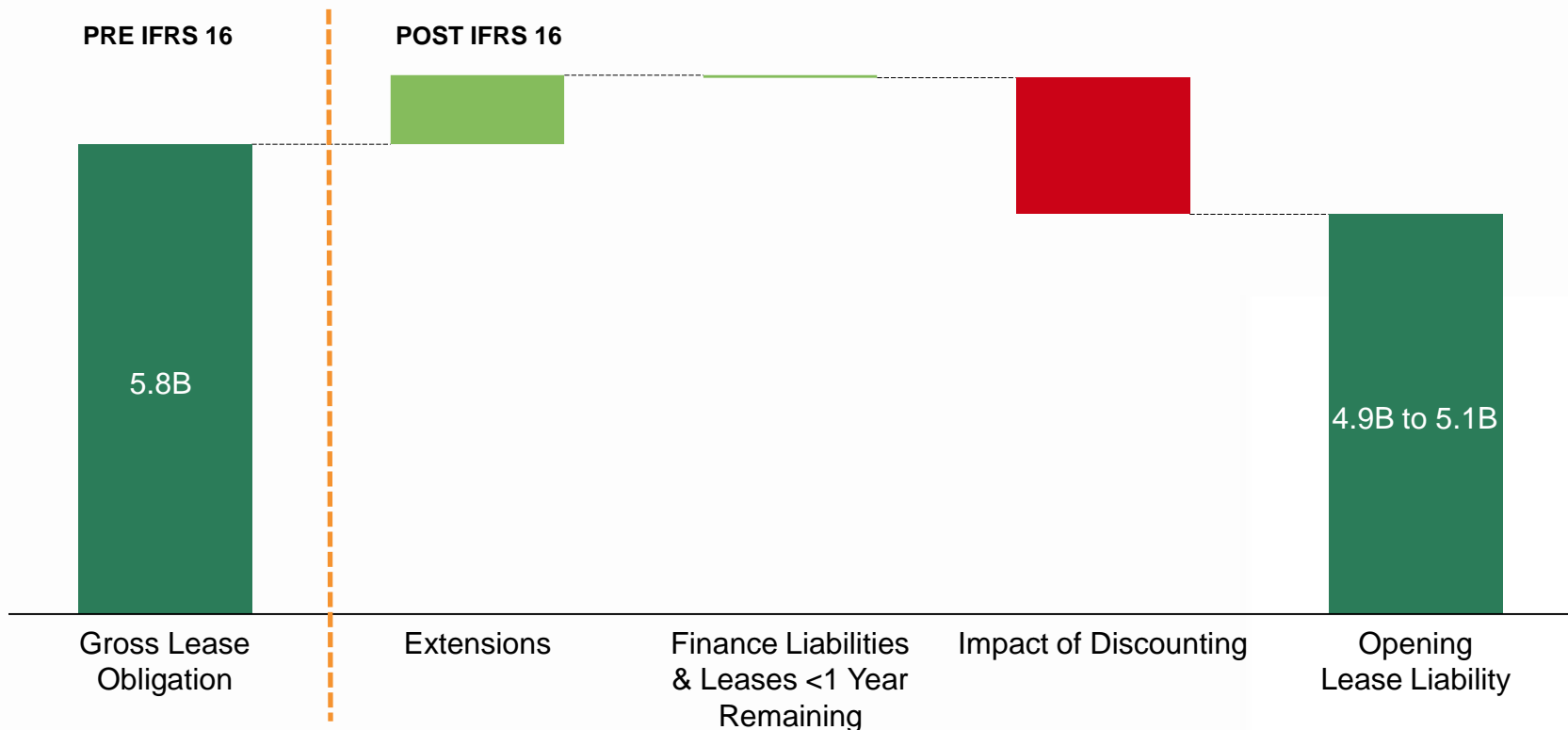
## Lease Term

- The following illustrates the Company's remaining lease term, with nearly 50% of the leases having remaining term between 3-7 years



# Opening Lease Liability

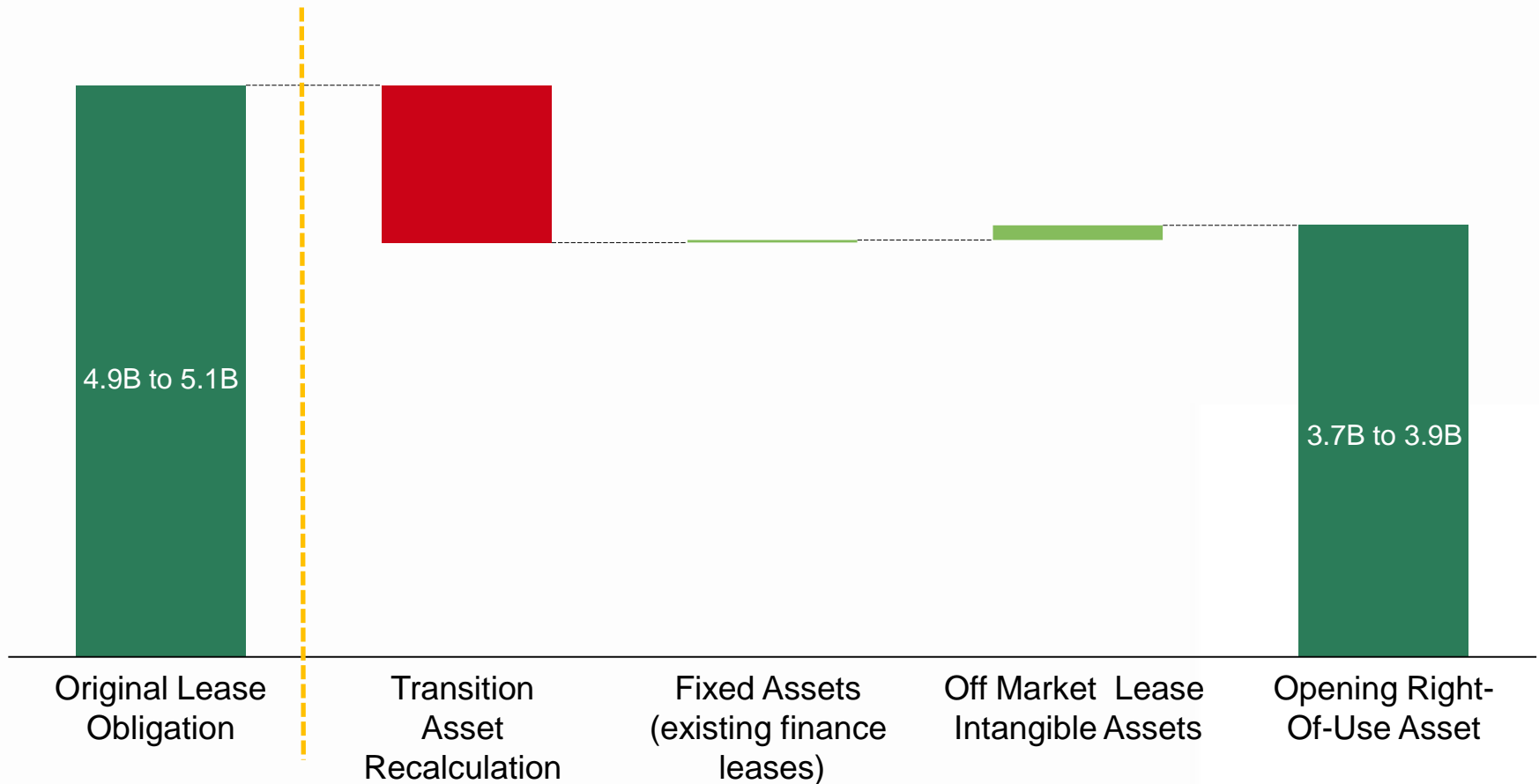
- The following table depicts the reconciliation of the Company's existing annual operating lease commitment disclosure to the lease liability balance on transition
- Opening lease liability balance as of May 5, 2019 on the balance sheet will be in the range of \$4.9 billion to \$5.1 billion





## Opening Right-of-Use Asset

- Opening right of use asset balance as of May 5, 2019 on the balance sheet will be in the range of \$3.7 billion to \$3.9 billion



## Income Statement Impact

Non-GAAP Measure (\$millions)	Expected IFRS 16 Impact on Item	Forecasted Impact on Q1 Fiscal 2020 Net Earnings	Explanation
Occupancy expense	↓	+ \$130	Occupancy expense decreases as net rental expense is captured in depreciation and finance expense
Depreciation expense - ROU	↑	- \$85	Depreciation expense increases as there is new depreciation for ROU assets
Intangible Amortization	↓	+ \$2	Off-market lease intangibles included in ROU assets (adjusted in 'Adjusted operating income')
Operating Income	↑	+ \$45	Rental expense removed from operating income and included in interest expense
Net Finance Expense	↑	- \$47	Interest expense on lease liability offset by interest income on lease receivables for finance subleases
Net Earnings	Depends	+ / - \$3	Dependent on time left on leases in portfolio and tax rate
Adjusted Net Earnings	Depends	+ / - \$5	Dependent on time left on leases in portfolio and tax rate. Difference from net earnings related to inclusion of historical Safeway acquisition off market lease intangibles in ROU asset and draw down included in depreciation go forward.

## Cash Flow Impact

- IFRS 16 changes cash flow statement presentation; however actual cash flows will remain unchanged
- The Company will classify the cash payments for both the principal and interest portion of the lease liability within financing activities
  - Results in an increase in operating cash flows, and will introduce new 'cash paid' disclosure for base rent costs; historically all lease expense disclosure was based on the calculated straight-line expense
- Management included additional disclosures of fiscal 2019 net cash rent paid for leases affected by IFRS 16 in the MD&A to facilitate comparatives.
- Impacts on the cash flow statement for fiscal 2019 impacted by IFRS 16 would have been:

(\$ millions)	Q1	Q2	Q3	Q4	Full Year 2019
Increased cash from operating activities	122.1	123.6	125.9	129.0	500.6
Decreased cash from financing activities	(122.1)	(123.6)	(125.9)	(129.0)	(500.6)
Total Cash Flow Impact	0	0	0	0	0
Total Free Cash Flow Impact	0	0	0	0	0

## Stakeholder Impact

- Rating agencies continue to develop post IFRS 16 methodologies, no expected significant impact.
- No significant impact on existing banking covenants.
- Existing metric updates:
  - EBITDA – we will disclose IFRS 16 impacts in fiscal 2020 for reference
  - Free cash flow definition will be updated to exclude net lease cash payments made

## Summary

- IFRS 16 does not impact the business – accounting and measurement changes only
  - No effect on our cash generating ability
  - Not expecting any material change related to debt ratings or financing costs
- Continue to estimate that adoption of IFRS 16 will not have a material effect on earnings per share in fiscal 2020
- First quarter F2020 results release date is September 12, 2019 including IFRS 16 results



## Appendices

## Financial Statements and MD&A Information

- Additional disclosure are provided in the financial statements and Management's Discussion and Analysis for the year ended May 4, 2019, to provide visibility to the expected IFRS 16 impacts
- See the following for references to the relevant information:
- **Financial Statements:**
  - Page 24: Note 9 – Existing finance lease assets
  - Page 26: Note 11 – Off-market lease intangible
  - Page 30: Note 15 – Finance lease obligations
  - Page 31: Note 16 – Deferred lease obligations
  - Page 38: Note 24 – Gross and net obligations for operating leases and the minimum lease expense disclosures
- **Management's Discussion and Analysis:**
  - Page 22 to 24:
    - Expected range of impact on the consolidated balance sheets is provided for the lease liability and right-of-use assets
    - Transition balance sheet impacts
    - Cash rent paid for leases impacted by IFRS 16 in fiscal 2019
    - Summary of IFRS 16 impacts on various Key Performance Indicators and financial ratios

# Financial Statements and MD&A Information




- As per page 22 in the Management's Discussion and Analysis, changes to the balance sheet are estimated as follows:

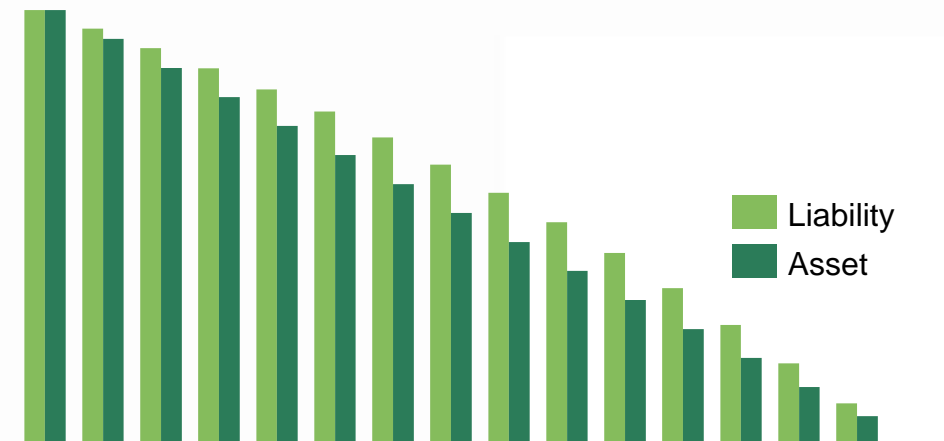
	(\$ in millions unless otherwise stated)	
Asset increases (decreases):		
Current assets, excluding lease receivables	\$	(43.4)
Fixed assets		(22.3)
Intangible assets		(126.7)
Deferred tax assets		(43.1)
Lease receivable		520.0 to 570.0
Right-of-use assets		3.7 to 3.9 billion
<b>Total asset estimated increase</b>	<b>\$</b>	<b>4.0 to 4.2 billion</b>
Liability (increases) decreases:		
Provisions	\$	32.1
Debt		29.1
Other liabilities		164.4
Deferred tax liabilities		34.5
Lease Liabilities		(4.9) to (5.1) billion
<b>Total liability estimated increase</b>	<b>\$</b>	<b>(4.6) to (4.8) billion</b>
<b>Retained earning estimated decrease</b>	<b>\$</b>	<b>0.5 to 0.9 billion</b>



# IFRS 16 Key Principles: Balance Sheet

- Brings the characterization of leased assets in line with owned assets
- Eliminates the classification of leases as either operating or financing leases for lessee
- Results in a significant gross-up for the balance sheet
  - Lease liability represents obligation of future lease payments
  - ROU asset represents the initial measurement of the lease liability<sup>1</sup>
- At inception, leased asset and liability are equal
- Carrying amount of the asset decreases more quickly than the liability – net liability
  - ROU asset depreciates evenly
  - Lease liability decreases by cash payments including interest

	IAS 17		IFRS 16
	Finance Leases	Operating Leases	All Leases
Assets			
Liabilities	\$\$		\$\$\$\$
Off Balance Sheet Rights / Obligations		 \$\$\$\$	

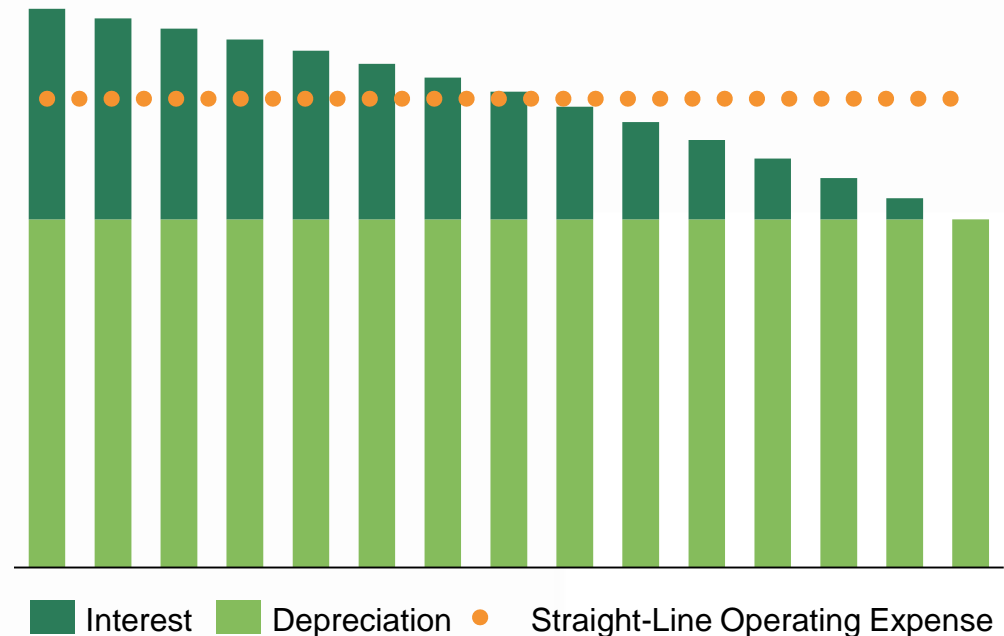


Note 1: ROU asset equal lease liability (present value of future lease payments) and adjustments for lease incentives received, initial direct cost, etc.

# IFRS 16 Key Principles: Income Statement

- Replaces the straight-line operating lease expense with:
  - Depreciation charge for the lease asset, straight-lined over the term
  - Interest expense on the lease liability, reduces over the life of the lease
- EBITDA and Operating Profit increases as the rent expense is segregated
- Total expense before taxes over the term of the lease is equal to cash paid
- Total lease expense will be front-loaded even when cash rentals are constant

	IAS 17		IFRS 16
	Finance Leases	Operating Leases	All Leases
Revenue	\$	\$	\$
Operating Costs (excl. Depreciation & Amortization)	---	Single Expense	---
<b>EBITDA</b>			↑↑↑
Depreciation & Amortization	Depreciation	---	Depreciation
<b>Operating Profit</b>			↑↑
Finance Costs	Interest	---	Interest
<b>Profit Before Tax</b>			↔



## Impact on Key Performance Indicators & Financial Ratios

Non-GAAP Measure (\$millions unless otherwise noted)	Expected IFRS 16 Impact on Metric	Forecasted Impact on Q1 Fiscal 2020 Results	Explanations
Same Store Sales	↔	↔	No IFRS 16 impact to sales
Gross margin	↔	↔	No IFRS 16 impact to sales or cost of sales
EBITDA	↑	+ \$130	Lease expenses and finance sublease income will be excluded, will disclose EBITDA impact in fiscal 2020
EPS*	Depends	+/- \$0.01	Dependent on net earnings impact
Adjusted EPS*	Depends	+/- \$0.02	Dependent on adjusted net earnings impact
Free Cash Flow			Definition will be updated to include cash rental payments

\*Difference between EPS and Adjusted EPS is related to inclusion of historical Safeway acquisition off market lease intangibles in ROU asset and draw down included in depreciation go forward.

# IFRS 16 Key Principles: Balance Sheet & Income Statement

- IAS 17:**

- Operating leases are not on the Balance Sheet
- Leases are included in operating expense for rent paid

	0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	Total
<b>Balance Sheet Impact:</b>																	
ROU Asset	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Lease Liability	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
<b>Income Statement Impact:</b>																	
Rent Expense	-	100	100	100	100	100	108	108	108	108	108	116	116	116	116	116	1,615
Depreciation Expense	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Interest Expense	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
																	<b>1,615</b>

- IFRS 16:**

- Recognizes Right-Of-Use Asset and Lease Liability
- Replaces operating expense (rent) with depreciation and interest expense

	0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	Total
<b>Balance Sheet Impact:</b>																	
ROU Asset	1,203	1,123	1,043	963	882	802	722	642	562	481	401	321	241	160	80	-	
Lease Liability	1,203	1,152	1,098	1,042	983	922	851	776	698	616	531	434	332	226	116	-	
<b>Income Statement Impact:</b>																	
Rent Expense																	
Depreciation Expense		80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	1,203
Interest Expense		49	46	44	41	39	36	33	29	26	22	18	14	10	5	-	412
Earnings Impact		129	126	124	122	119	116	113	110	106	103	99	94	90	85	80	<b>1,615</b>

Note: Chart illustrates 15 year term, annual payments of \$100K (increase by 7.5% every 5 years) and IBR 4%

# IFRS 16 Key Principles: Cash Flow

- No effect on the total amount of cash flows reported.
- Affects the presentation of cash flows related to historical operating leases.

	IAS 17	IFRS 16	Effects on Cash Flow Statement
	Operating Leases	All Leases	
Operating Activities	Single Operating Lease Cash Flow		↑
Investing Activities			↔
Financing Activities		Principal Portion of Lease Cash Flow Interest Portion	↓
Total Cash Flow			↔

- Over the lease term, the cumulated impact on net result is the same under IAS 17 and IFRS 16. Difference between periods is due to decreasing interest expense.

Illustration: 15 year lease term, annual payments of \$100K (increase by 7.5% every 5 years) and IBR 4%

