

Empire Company Limited**Third Quarter 2021**

March 10, 2021 — 12:30 p.m. E.T.

Length: 68 minutes

"While Cision has used commercially reasonable efforts to produce this transcript, it does not represent or warrant that this transcript is error-free. Cision will not be responsible for any direct, indirect, incidental, special, consequential, loss of profits or other damages or liabilities which may arise out of or result from any use made of this transcript or any error contained therein."

« Bien que Cision ait fait des efforts commercialement raisonnables afin de produire cette transcription, la société ne peut affirmer ou garantir qu'elle ne contient aucune erreur. Cision ne peut être tenue responsable pour toute perte de profits ou autres dommages ou responsabilité causé par ou découlant directement, indirectement, accessoirement ou spécialement de toute erreur liée à l'utilisation de ce texte ou à toute erreur qu'il contiendrait. »

CORPORATE PARTICIPANTS

Katie Brine

Empire Company Limited — Director Finance, Investor Relations

Michael Medline

Empire Company Limited — President & Chief Executive Officer

Michael Vels

Empire Company Limited — Chief Financial Officer

Pierre St-Laurent

Empire Company Limited — Chief Operating Officer, Full Service

CONFERENCE CALL PARTICIPANTS

Patricia Baker

Scotiabank — Analyst

Chris Li

Desjardins Capital Markets — Analyst

Irene Nattel

RBC Capital Markets — Analyst

Mark Petrie

CIBC World Markets — Analyst

Karen Short

Barclays Capital — Analyst

Vishal Shreedhar

National Bank Financial — Analyst

Peter Sklar

BMO Capital Markets — Analyst

Kenric Tyghe

ATB Capital Markets — Analyst

Michael Van Aelst

TD Securities — Analyst

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Empire Third Quarter, 2021 Conference Call. At this time, all lines are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. If at any time during this call you need assistance, please press star zero for the operator. This call is being recorded on Wednesday, March 10, 2021.

I would now like to turn the conference over to Katie Brine, Director Finance, Investor Relations. Please go ahead.

Katie Brine — Director Finance, Investor Relations, Empire Company Limited

Thank you, Joanna. Good afternoon and thank you all for joining us for our third quarter conference call. Today we will provide summary comments on our results and then open the call for questions. This call is being recorded and the audio recording will be available on the Company's website at www.empireco.ca. There is a short summary document outlining the points of our quarter available on our website.

Joining me on the call this afternoon are Michael Medline, President and Chief Executive Officer; Michael Vels, Chief Financial Officer; and Pierre St-Laurent, Chief Operating Officer, Full Service.

Today's discussion includes forward-looking statements. We caution that such statements are based on management's assumptions and beliefs and are subject to uncertainties and other factors that could cause actual results to differ materially. I refer you to our news release and MD&A for more information on these assumptions and factors.

I will now turn the call over to Michael Medline.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Thanks, Katie. Good afternoon, everyone.

I don't need to say much about our third quarter results, they stand for themselves; however, I do think many people are sorely underestimating how much stronger our business is now, regardless of any COVID benefits. Today I want to focus on our performance this quarter, including early results from Horizon and an update on e-commerce. Before I get into our results, I would like to cover three very important things.

First, I want to reiterate how proud I am of our frontline and back-office teammates. They've continued to serve our customers every day through this pandemic. COVID has unfortunately become our new normal, but we remain more vigilant than ever in keeping our customers and teammates safe.

Second, in recognition of Black History Month in February and the recent International Women's Day, I want to take a moment to reflect on these important annual celebrations. Remembering and celebrating the people and events in Black history is important and necessary. We must address and rectify long-term institutional bias and racism. We are engaging with marginalized teammates, listening, learning, and taking action to address anti-black racism and advance on a culture of inclusion. Our partnership with the BlackNorth Initiative remains very important to us. It is a guidepost for our actions.

While there has been some meaningful progress on advancing women in the workplace, there is still so much to be done. For us, progression and representation of women continues to be a key focus. It is embedded in our leadership selection and development processes, which is making a real difference. For example, store-level programs have led to increases in women in historically male dominated roles. At Empire we don't limit our diversity, equity, and inclusion growth journey to a single month or day, it's ongoing. I'm so proud of our DE&I team and all our teammates who are supporting our DE&I growth journey.

Now on to our third quarter results. We're extremely pleased with our performance this quarter. We're delivering on both our top and bottom lines. We have a strong balance sheet and have continued to strengthen it through the last year. And even through the pandemic, with more demands than ever on our team, we are seeing the real start of financial benefits from Project Horizon. Sales were up 12% this quarter with same-store sales up 10.7%. We continue to see substantial gains in our national market share and market share growth in every region of the country as our sales growth outpaces competitors.

There are a few reasons sales remain elevated and our market share continued to grow. One, the latest COVID lockdown did bring a surge of sales in certain regions when initially announced. Two, the strong improvements in our store operations and merchandising have enhanced our winning customer value proposition. Three, our strategic investments, including Farm Boy, FreshCo, and Voilà, as well as our store renovation program, are outperforming. We are very proud of these investments. And lastly, this quarter encompasses our busiest time of the year, the holiday season. Our team delivered strong results, outperforming the market in this important period.

Our gross margin dollars were positively impacted by increased sales but, in addition, gross margin rate was 25.7%, up a truly impressive 134 basis points over last year. The strong improvement in margin is in large part due to early Project Horizon results. This includes tremendous progress we've made with our promotional optimization program. The program is powered by collaboration between our merchants and our advanced analytics team. Together, they have designed new processes and tools to improve promotional planning and already this program is embedded in the day-to-day business of our merchandising organization. However, algorithms alone do not make the best decisions and are no substitute for good judgment. Together, our great merchants, equipped with improved data, form a powerful combination that is driving our compelling customer value proposition. A smaller portion of the margin improvement comes from continued sales mix shift toward our full-service banners.

I believe our strong margin performance this quarter shows that you don't need to send unilateral letters to your suppliers to do well in this business. We try to treat our supplier partners with respect and transparency. We believe this values-driven approach garners better results for both sides. This doesn't mean we're not tough, we are, but we negotiate the right way. I am extremely proud of our merchants who put these values into practice every day.

Mike will speak more on SG&A in a moment, but I would like to highlight how we have kept our commitment to offer our frontline and distribution centre teammates a lockdown bonus, even while much of the industry did not do so. To us, it was certainly the right thing to do. In Q3 this investment was \$9 million. Our initial estimate of up to \$5 million only included Manitoba and select regions of Ontario. In Q4, based on current estimates, we expect the lockdown bonus to be up to \$4 million.

Next, a few updates on e-commerce. It has been another impressive quarter for our e-commerce business as we continue to hear how much customers love Voilà. This quarter, Empire's e-commerce businesses grew 315% over last year. With the continued expansion of Voilà, arrival of winter, and further lockdowns, we saw an impressive increase over the second quarter as well.

Today I can share updated projections on the financial impact of Voilà. As we previously publicly disclosed, our expectation was that Voilà would dilute EPS in fiscal 2021 by \$0.20. However, we now expect our team will over-deliver on this estimate with full-year EPS dilution of \$0.18 in fiscal 2021. Our initial \$0.20 estimate did not include the full costs for store pick, but the revised estimate of \$0.18 actually does, so it's even better than it looks. This reduced dilution is a direct result of the team's outstanding efforts to ramp up the business quickly to meet customer demand, while maintaining cost discipline.

As we have said in the past, Voilà is a strategic, long-term investment. Our partnership with Ocado provides us with the best and most customer-friendly grocery e-commerce platform on earth. While we are seeing dilution now, this investment will pay off. When we achieve scale, we expect to have the most profitable approach to grocery e-commerce in Canada and it will be exclusive to us.

To wrap up, I would like to highlight how we have continuously demonstrated that when we set targets for ourselves, we meet them. Our results prove this time and time again. Our team is working hard to drive our core business and to execute our strategic growth agenda. We will review our first full year of Horizon in June. For now, while we are only nine months into our three-year growth strategy, we already have material benefits kicking in. With two years still to go, we are highly optimistic.

People sometimes forget that our operational and merchandising execution is so much better than it used to be. We proved what we can do by delivering Sunrise on time and exceeding targets. We continue to prove this with our strategic investments, like Voilà and Farm Boy, both of which are outperforming. There's a reason we are outperforming the competition and it ain't all COVID.

With that, over to Mike.

Michael Vels — Chief Financial Officer, Empire Company Limited

Thanks, Michael. Good afternoon, everyone. I'll provide some additional colour on our results, of course, and some comments on our fourth quarter, our cash flows, and an update on capital expenditures.

Next quarter, as everyone knows, we'll start to comp the elevated sales we saw at the beginning of the pandemic. Last year we started to see significantly higher sales starting on February 28th. The following week saw customers stock up in preparation for possible stay-at-home requirements. As a result, we saw an unprecedented 18% same-store sales in the fourth quarter last year with very volatile weekly sales comps ranging between negative 1% and positive 52%. The last half of Q4 last year drove the lion's share of that comp increase.

We've not seen this level of buying as elevated since then as shoppers' buying patterns evolved through COVID. As a result, our sales compared to last year this early in the quarter are in no way an indication of where our total sales comps will end up at the end of next quarter. Because of this volatility, even a negative same-store sales number for the fourth quarter will not automatically indicate weaker sales, just an anomalous outcome because of the highly unusual quarter last year. In the first five weeks of the fourth quarter ending last week, our same-store sales were 9% compared to last year. As I said, this increase is unlikely to be sustained through the fourth quarter as a result of the significant COVID-driven sales last year.

As Michael said, we had strong gross margins this quarter, with a 134 basis point increase from last year. Going into the fourth quarter, we continue to be satisfied with our margin rate discipline and the impact of Horizon benefits that are improving our margin. Of course, it's always our goal to keep pushing on efficient translation of sales to the bottom line, as we pursue our EBITDA margin goals. The rate of improvement in the third quarter, however, may not be entirely repeatable in the fourth quarter, as we're also lapping an increase in margin rates last year that were caused by inventory shortages that did not allow our suppliers to supply all promotional items and, as a result, we had a higher percentage of

sales at regular prices. On the other hand, we do expect to continue to reflect Horizon benefits and positive impacts of our higher margin service counters coming back into service since last year.

This quarter there were some significant items in SG&A that increased our SG&A as a percentage of sales. Some of these impacts will recur into the fourth quarter, but not necessarily into fiscal 2022. There's a lot going on in our SG&A line, including our new e-commerce business, store conversions, higher volumes, and COVID impact on labour wages.

First, accounting accruals for our store distribution centre and backstage teammate compensation continued to be higher this quarter and they will be in the fourth quarter as well. We do not expect to see these expenses at the same levels in fiscal 2022.

Second, COVID costs, including the lockdown bonuses, are an increase from last year. These costs for the fourth quarter, estimated at between \$15 million and \$20 million, will be less than the COVID cost for the fourth quarter last year of \$80 million.

Third, the new Voilà business now has its full back-office SG&A and supply chain costs reflected in the company's SG&A compared to last year. Voilà launched to customers June 22nd, a little over halfway through our first quarter last year. Fourth, both expenses associated with the closure of stores and conversion to FreshCo stores in Western Canada, and Farm Boy stores in Ontario, are recorded in the third quarter.

And finally, right-of-use asset depreciation on IFRS 16 is higher than last year, reflecting an increase in occupancy costs.

As I said, there are a number of items impacting SG&A with COVID costs and impacts and investments in Horizon initiatives. Another example of these costs that have been elevated and where we will continue to invest is in marketing, where we have invested to reposition our full service and discount banners with our customers and of course invested in awareness of our new e-commerce platform.

Another investment that will also begin in the fourth quarter is our extremely exciting investment in sponsorship of our Canadian athletes. In 2019 we announced our partnership with the Canadian Olympic Committee as the first ever Official Grocer of Team Canada. With the delay of the Summer Olympics, we now have both the Summer and Winter Games in the same fiscal year, which we of course did not fully expect. This is a once-in-a-generation opportunity to grow our brands with Canadians during two Olympics in one year and we intend to take full advantage of this exclusive chance.

EBITDA margin in the third quarter increased by 90 basis points over last year due to the 134 basis point increase in gross margin, partially offset by the impacts of SG&A. The effective tax rate for the quarter of 26.4% was in line with the statutory rate and, excluding the effect of any unusual transactions or tax rates on property sales, we estimate that the effective income tax rate for fiscal 2021 will be between 26% and 28%. The earnings per share, as Michael said, includes \$0.04 per share of Voilà dilution compared to \$0.01 last year and \$0.04 per share of FreshCo and Farm Boy conversion and store closure costs compared to none last year.

We are very pleased with Voilà's consistent growth in order volumes week over week. Voilà sales have increased by approximately 100% from Q2 and our total e-commerce sales are up by 350% compared to last year. This increased pace of sales has reduced our expected EPS dilution estimate from \$0.20 to \$0.18 for fiscal 2021, even after accounting for the launch of our store pick solution, which has an expected dilutive impact of approximately \$0.01 for fiscal 2021.

Equity earnings increased year over year, principally due to higher earnings from Crombie REIT, which continues to perform well in spite of COVID headwinds, primarily due to their high-quality portfolio, a significant amount of which is anchored by Empire grocery banners. Their rent collection rates are high at 98% in their fourth quarter and continuing through January. Crombie REIT started their calendar 2021 with record committed occupancy of 96.4% and a strong property development strategy.

Cash flow generation continues to be strong. At the beginning of this quarter, we fully retired two debt facilities. This, combined with continued strong EBITDA, improved our funded debt to EBITDA to 3.3 times compared to 4.1 times last year. The Company's credit metrics and financial profile continue to improve due to stronger operating performance and stable financial leverage.

As of this week, we've repurchased approximately 2.8 million shares so far for consideration of \$100 million. We intend to complete the current NCIB up to 5 million shares. And when that NCIB is completed, we plan to renew it with the TSX at a higher level of share repurchases.

Year to date we've spent approximately \$450 million in capital investments and we continue to expect to spend between \$650 million and \$675 million for fiscal 2021. About half of this investment is being spent on renovations and new stores, including the expansion of FreshCo in the West and Farm Boy in Ontario. \$65 million of the total will be spent on Voilà, including CFC 2 construction and rollout of the in-store picking solution.

We renovated 19 locations across our network this quarter and we are on track to renovate 30% of our Empire store network over the course of Horizon. This is a significant disciplined program with our strongest returns. Our renovation program is meeting, if not exceeding, sales forecasts and business case. If you look at the earnings presentation document on our website, we put some of the before and after pictures of recent renovations, which have improved our customer experience and provided new assortment in many stores, which is garnering significant enthusiasm from our customers.

In January we announced that we have reached the halfway mark of our Western Canada discount expansion plans. We opened our 23rd store last week and have plans to open another three to five stores in the fourth quarter, for a target achievement of 10 to 15 stores in fiscal 2021. Next quarter will be the two-year anniversary of our first FreshCo stores opening in the West.

Farm Boy opened their 36th store last month. They are on track to open a total of eight stores, including one relocation, in fiscal 2021. Approximately two years since the acquisition, we now have 42 confirmed locations and plans for more.

In March, we opened our first Voilà spoke in Etobicoke, Ontario. Spokes are cross-dock facilities that allow us to get closer to our customers and improve efficiencies at our CFCs, for example, by improving a key efficiency metric such as drops per van. The spoke reduces the distance to our customers and increases the amount of deliveries our customers can make in a shift. This particular spoke will relieve long-term capacity constraints and it had a very smooth start-up.

In December, through our Crombie development partner, we completed our part of the construction of the CFC building in Montreal on time and Ocado began their build of the internal grid. We expect to start testing the system and bringing in products in the second half of calendar 2021. Our target launch date remains early calendar 2022.

As you can see, there's lots on the go. We have detailed plans built by our leadership teams singularly focused on our Horizon targets and managed by our disciplined PMO teams. We've managed to restart all of our initiatives that were previously delayed due to COVID and expect to exit fiscal 2021 with momentum on these critical activities. We are really encouraged by our early success on new capabilities and tools such as Artificial Intelligence and Advanced Analytics and the new processes in our merchandising and operations groups. Our Horizon progress is on track and there is so much more to come.

And with that, Katie, I'll hand the call back to you and take questions.

Katie Brine — Director Finance, Investor Relations, Empire Company Limited

Thank you, Mike. Joanna, you may open the line for questions at this time.

Q & A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press the star followed by the one on your touchtone phone. You will hear a three-tone prompt acknowledging your request. If you are using a speakerphone, please lift the handset before pressing any keys.

Your first question comes from Patricia Baker at Scotiabank. Please go ahead.

Patricia Baker — Analyst, Scotiabank

Good afternoon. Thank you very much for taking my questions. Michael, I'd like to talk a little bit more on the promotional optimization. I mean it certainly provided you with a win in Q3 and it sounds like it's going to be a gift that keeps on giving. So, the way that I look at it here, there are two elements. There's the data and the analysis of that data. And then of course, as you referred to in your opening remarks, there's the team that works with those tools to deliver the promotional effectiveness. Now the data has always been there at Sobeys. I recall, when you first joined the Company, you said you were really impressed by the amount of data. So obviously part of what's happening here is that the mining of the data has improved significantly. But I just want to get your impression. If you look at the teams that are managing the promotions and, as you indicated, also using their judgment, do the results that we saw in Q3 demonstrate that the teams are as agile as you want them to be? And how would you compare them to where they were a year ago Is there more to come? And does successful promotion just build on the next promotion so that you just keep getting better and better?

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Great question and one I think about all the time, especially today. We just had a presentation, we have many presentations, but we had one at our board today on promotional optimization and it was led by merchants at many levels of the Company. I think four different levels were represented. We swim in data and we always have. What we've done is we've cleaned up the data so it's incredibly usable. I want to compliment our technology team. They're just killing it. And we're putting tons of pressure on them and they're responding.

We talk about our data analytics team led by Mohit Grover. They're aces. But we're not hiring hundreds of people here. You don't need to. You just need fantastic superstars in data analytics. But the biggest thing that I've seen, and I don't think they notice it, is that our merchants have just embraced this and they're excited about it and now they're the ones driving to have more and more analytics and to make good decisions on behalf of our customers, so our offers to our customers are sharper and smarter and more appealing. And it's not just margins. This is a sales game. We want to win our customers over and take market share. And the merchants, I don't think they notice how much better they are than a year ago. It's incredible. They're speaking a different language.

But we're in early days. So, you saw the difference it can make to our Company. It was a big portion of the 134 basis points that we saw. And these are just early days. This reminds me, I'm aging myself, it might be the early days of Sunrise when people didn't see what was coming. But we saw it. And this, the way we do things, our leadership, especially from Pierre St-Laurent, Mohit Grover, and Bruce Burrows, and the technology driving these analytics, this is our biggest opportunity. And now that they love it,

they're going hunting for it. So, this is our biggest opportunity, always was going to be, but we couldn't have done any of this before Sunrise.

Patricia Baker — Analyst, Scotiabank

No. Absolutely. You mentioned that the merchants embrace this and they're speaking a different language. I'm just curious, are they speaking a more return-oriented language than they would have been a year or two ago?

Pierre St-Laurent — Chief Operating Officer, Full Service, Empire Company Limited

They have very powerful dashboards in front of them now. They know, in a very short time, this promotion or the level of effectiveness of the promotion. So, we're hearing them talking about red promos and yellow promos, but we have less and less red promo now. We have more green promo. And it's not only good for us, but it's also good for our supplier partners. Everybody wants to have a meaningful and effective promotion and they want to maximize the impact on customers, and our merchants had very good conversations with suppliers to increase the effectiveness and how meaningful our promotions are for customers. So that's the different language we're hearing now and it's very encouraging for the future.

Patricia Baker — Analyst, Scotiabank

Thank you very much, Pierre and Michael.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Thank you, Patricia.

Operator

Thank you. The next question comes from Chris Li at Desjardins. Please go ahead.

Chris Li — Analyst, Desjardins Capital Markets

Good afternoon. Maybe first one to Michael. Just listening to your opening remarks, it sounds like the benefits from Horizon were a bigger driver of the gross margin improvement this quarter more so than the sales mix impact. I guess first question, is that correct? And then number two is can you maybe quantify for us a little bit just how much of the impact was from each factor, please?

Michael Vels — Chief Financial Officer, Empire Company Limited

Thanks, Chris. I think Michael said it was a significant amount. COVID is still a significant effect on the numbers and that mix shift has been significant. So, I think in order it would be mix and Horizon benefits.

But when I add other, call it, strategic decisions in like Farm Boy, discount, renovations, you know, this is not only about advanced analytics, if I started adding in some of those items and then, I think, ascribe some of our share gains that we've made to those initiatives, then I would say, yeah, in total, between sales and gross margin rates, Horizon was probably a greater driver. So, I guess what I'm saying is that it is very hard to specifically separate out sales impacts. We can separate out gross margin rate impacts a little better. But I wouldn't get fixated on just the one thing we're doing. We're doing many things. We've been doing them quite well, even coming out of Sunrise, and we feel good about material amounts of this quarter's result being repeatable in future quarters.

Chris Li — Analyst, Desjardins Capital Markets

Great. That's very helpful. And then my other question is, just conceptually speaking, as the industry cycles through very strong comps, how do you strike the balance between not chasing after unprofitable sales versus ensuring that you're not losing the share that you have fought so hard to gain this past year?

Michael Medline — President & Chief Executive Officer, Empire Company Limited

We're going to see some negative comps probably in the next tiny bit because we're comping over some big periods, but how do you make sure you don't chase them but keep your market share?

Pierre St-Laurent — Chief Operating Officer, Full Service, Empire Company Limited

I think that's the main KPI going forward. We need to look at market share more than our usual KPIs like comp sales versus last year. So, as long as we continue to gain market share in the healthy way with no empty calorie sales, we would be satisfied. So, I think the team is behind the new KPIs for the next year because we don't want to change the good behaviour we saw recently. But we believe that we did really well during COVID, and we believe that customers will continue to shop our stores based on the good job we did, so we're confident for the next year for sure. But yes, we won't have the same sales, especially over the next two, three weeks. We had big panic buying. We won't see the same level of sales. But I think we will continue to see healthy sales and margin by measuring through good KPIs.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

I think, Pierre, that's perfect. That's exactly right. And a lot of retailers, you know, you hear, and it's always danger, they chase sales or then they chase margin. We're working, and we're helped by a fantastic team, but also with way more use of data and smarts and category reset, that we don't talk like that anymore. We believe we can grow our market share and grow our margins.

Chris Li — Analyst, Desjardins Capital Markets

Perfect. And maybe just one very last question. How much were the full costs for the store pick that were not initially included in your \$0.20 Voilà dilution estimate?

Michael Vels — Chief Financial Officer, Empire Company Limited

It was about \$0.01 per share.

Chris Li — Analyst, Desjardins Capital Markets

Okay. Thanks very much.

Operator

Thank you. The next question comes from Irene Nattel at RBC Capital Markets. Please go ahead.

Irene Nattel — Analyst, RBC Capital Markets

Thanks, and good morning, everyone. I guess we're now almost nine months since you rolled out Voilà in the GTA and I was just wondering if you could talk about what you're seeing in terms of consumer purchasing patterns, sort of how often are they ordering, basket sizes, retention rates, anything that you can tell us there.

Michael Vels — Chief Financial Officer, Empire Company Limited

First of all, week-over-week sales, I think, in virtually every week since we spoke to you last, have increased. And that's a combination of our new customer accounts and basket size increases as well. Our retention rates are excellent. And our efficiency statistics, I mentioned on the call, drops per van, the number of picks generated inside the facility by our robots, our substitution rates, our on-time delivery rates, are all at or above our targets.

So it's super hard to go through every one of those statistics and probably not smart competitively to do it, but I think the only item that we are planning to change materially going forward is that we added about a 1,000 articles to our assortment since the last time we spoke to you; and as we move forward, we still have significantly more room to add assortments in that facility. And we intend to do so as soon as the supply chain can make it and when negotiations that we have in place for some more specialty items are completed. We added a pretty cool line of Oliver & Bonacini pre-made meals and I think they sold out in an afternoon. It's that type of innovation and that type of excitement that's really going to generate a lot of long-term success and something that Sarah and her team are working on with a significant amount of urgency.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

The three things that I look at most and I'm happy, in fact we're over-performing in, are our retention rate of existing customers, tracking new customers, and basket size. So, there's no bad news there. It's all good.

Irene Nattel — Analyst, RBC Capital Markets

That's great. Thank you. Can we get an update, if possible, on just how the Compliments re-launch is doing and sort of whether you're continuing to see rising penetration and how that's playing into e-commerce as well?

Pierre St-Laurent — Chief Operating Officer, Full Service, Empire Company Limited

On private label, we continue to outperform our total growth, which is a good sign. Once again, like I already said before, penetration rate is a KPI, but not my favourite. My favourite is to make sure that private label would play a meaningful role in every single category. So, in some categories there's a lot of opportunity for us and others, less. And the good news is that now the team has rebuilt the category for private label. If you remember, we did category resets in the past. Now we're doing the exact same thing with private label. So, we'll have more relevancy for private label items, and we'll have better cost of goods, and then private label will play the main role they have to play in generating more operating profit at meaningful prices for customers.

Irene Nattel — Analyst, RBC Capital Markets

That is great. Thank you.

Operator

Thank you. The next question comes from Mark Petrie at CIBC. Please go ahead.

Mark Petrie — Analyst, CIBC World Markets

Good afternoon. Actually, just a couple of follow-ups, and appreciate all the comments. With regards to the dilution on Voilà, obviously you're moving in the right direction there. I mean, if I heard right, it sort of sounds like \$0.03 likely for Q4. Can we extrapolate that kind of \$0.01 a quarter pace of improvement as to when you might reach breakeven? Or what are the other variables there?

Michael Vels — Chief Financial Officer, Empire Company Limited

Yeah, I don't think I'd do that, Mark. The most significant element of moving to accretion for that CFC is going to be sales increases, for sure. And as I mentioned, things like assortment size, basket size, customer retention, all that sort of thing is going to go into that. We are going to also start incurring costs from CFC 2 next year and our intention, once we've solidified our plans, is to provide a more granular estimate of what we anticipate our total e-commerce impact will be for next year. But I think it's fair to say that as Voilà continues to bed down, their efficiency ratios now become either at or better than target and are repeatable week to week. We're converting the sales to earnings and really what we need to do over the next year is just keep doing what we've been doing and cover the fixed costs. So, you're right

that it's going to consistently improve, in our opinion, but just taking a linear earnings per share number I don't think is going to get it done. So, we're going to provide a little more information on that probably in the next quarter.

Mark Petrie — Analyst, CIBC World Markets

Okay. Thanks. Yeah, I was just referring to CFC 1 and sort of putting CFC 2 aside. And just on that topic, I think you've said in the past, but just to confirm, you expect CFC 2 to be less dilutive than CFC 1, at least incrementally, simply because you're now leveraging some of the infrastructure that's in place.

Michael Vels — Chief Financial Officer, Empire Company Limited

To the extent that we don't have to repeat the infrastructure, you're 100% right.

Mark Petrie — Analyst, CIBC World Markets

Yeah. Okay. And then actually I just wanted to ask specifically just, again, follow up on the private label side. Pierre, how far are you through that sort of category management exercise, specifically as it relates to private label? And then I don't know, Mike, if you can help us just, you know, was that also a factor in terms of gross margin in Q3? Obviously, it's embedded in the Horizon number, but just curious to any comments.

Pierre St-Laurent — Chief Operating Officer, Full Service, Empire Company Limited

Good question. I think it's in the plan for this year. I think most of the benefit will be in fiscal 2022 and fiscal 2023. So, we're at the early stage of capturing benefits, but there's a lot of the job done so far. We're doing it in waves like we did with category resets. It's a very good method and we're leveraging from our past experience with category resets, following the same type of process. So now we're in wave one and then we'll do wave two and wave three like we did for category resets. But most of the benefit will come in fiscal 2022 and fiscal 2023 and they're significant. But in this quarter, it's not material.

Mark Petrie — Analyst, CIBC World Markets

Okay. Thanks. And actually, sorry, just to come back to Voilà, I had one other question, which was with regards to adding more SKUs. Like I think that is something that customers are definitely looking for. So, what is the impediment to doing that? I mean you mentioned negotiations with suppliers, but is it strictly sort of ramp up on customers and then also the supplier constraints? Or what is the impediment to doing that today?

Michael Vels — Chief Financial Officer, Empire Company Limited

Well, there's no impediment to stopping us from doing it, for sure. We're very picky about making sure that if we introduce an item into our assortment that our suppliers are going to be able to deliver it consistently on time so our efficiency rates stay up in terms of no substitutions and on-time and full. And just with COVID, not all of the suppliers have been quite as flexible. And that's improving day by day and we're encouraged by the progress. That's really it, Mark. There's no other reason over and above that.

Mark Petrie — Analyst, CIBC World Markets

Okay. Appreciate the comments. All the best.

Operator

The next question comes from Karen Short at Barclays. Please go ahead.

Karen Short — Analyst, Barclays Capital

Hi. Thanks very much. Just a couple questions. In terms of the comp in the quarter to date, I was wondering if you could give a little colour on basket and traffic in terms of the comp, but then also talk a little bit about variation by province. And then I know some parts of GTA have started to reopen, so is there any colour you could give on how that's trended since a little bit more of a reopening in some of the regions that you operate in? And then I had one other.

Michael Vels — Chief Financial Officer, Empire Company Limited

It has increased across the board across the entire country. The rates of improvement would be different depending on which province you're in. So, in Atlantic, which has had less COVID cases and in many cases have been in quite the Atlantic bubble for most of the time, not all of it, those rates of improvement haven't been quite as high. In Québec and Ontario, depending on timing of lockdowns, they would probably, on average, have had the highest rates through the period, and then varying rates in the Western provinces depending on, again, the timing of their lockdowns and the impact on resulting behaviour. So that's, generally speaking, I think, as far as we're prepared to go. We're not going to quantify

the numbers in each province. They're actually also highly volatile. They go up and down depending on lockdowns and in what areas. In terms of the 9% year to date, there's obviously changes in Ontario and other places where lockdowns are being eased. We have no comment at this point as to what those trends will be and where they're going to go over the short term. I think it'd just be wrong for us to try and estimate that. We've given you at least the actual facts for just the early weeks in the quarter, but really can't provide any further at least numerical guidance on that at this point.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

The only thing, Karen, I'd add to what Mike said, which is completely accurate, is —the swings are on the margin, right? They don't swing way up and way down on lockdown. It's more like a margin. And so, I don't want you to go away thinking that we go from 20 to zero. That doesn't happen. It's just little things. And so, we're still seeing elevated full-service market share gains and all that, just little movements across the country where things change. I don't want to overstate it.

Karen Short — Analyst, Barclays Capital

Okay. Thanks. And then I don't know if you've given us this, if you have, I've missed this. What is the actual cost of the investment in the Olympics from, I guess, an expense perspective? And then how do you think about the return on that investment? Just curious.

Michael Vels — Chief Financial Officer, Empire Company Limited

So, I'll punt the question to Michael on the returns. And we're not disclosing the total cost of that. There's clearly media and sponsorship costs, but, at the same time, we're also not necessarily investing in some of the other media properties we might have otherwise done without the Olympics. So, it's not a straight add. We are becoming more efficient in some of our other marketing expenditures as well. But we're not providing the estimate for that.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

And on the return, look, so I have a lot of previous experiences in branding and the Olympics and that's why Empire has taken such a big stand in terms of sponsoring specialty sports because I think part of our rejuvenation has been on the brand and what we've done in terms of sponsorships. Hard to quantify, I can just say that being the exclusive grocery partner of the Olympics, and the Olympics are the biggest, as soon as we could grab that, we grabbed it, because I know how powerful that is and it's an exclusive platform. And for our people, I mean it's great for customers, it's great business, but it's also, for our people inside the company, very exciting to support our athletes. So, it has a big impact. Sometimes hard to quantify, because it's brand, et cetera, but we'll take full advantage of this exclusive opportunity.

Karen Short — Analyst, Barclays Capital

Yeah, no, I agree. It's a great opportunity. I was wondering if you had any metrics on top line potential as well because, obviously, there has been history on that in other categories.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

In Canada, no one had ever grabbed the Olympics before. It's a hot property in every other part of retail, except no one had ever done it in grocery, surprisingly, or none that I've ever remembered. And so, I think we have a huge opportunity. And of course, we have goals and we have a great marketing team that's all over it, merchandisers who are all over it and so that's built into our plans.

Karen Short — Analyst, Barclays Capital

Great. Thank you.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Thanks for a great question.

Operator

The next question comes from Vishal Shreedhar from National Bank. Please go ahead.

Vishal Shreedhar — Analyst, National Bank Financial

Hi. Thanks for taking my questions. Just to paint the same wall here and going back to gross margins, obviously we don't see that kind of performance on a regular basis in that sector, so with respect to the initiatives that you've implemented, wondering if you've had any customer feedback on kind of the movements that you've made on your promotion. Are you seeing any changes in net promoter score one way or the other to kind of gauge the customer's reception to these initiatives?

Pierre St-Laurent — Chief Operating Officer, Full Service, Empire Company Limited

That's a good question. I think, once again, the best indicator for us is market share. So that means the things we are doing are meaningful for customers. We're monitoring price perception and we're seeing positive movement. So, I think, overall, customers don't have the data we have to build a meaningful promotion, but their perception remains strong and we're seeing slight improvement. But the real KPI, once again, is the market share. And we're seeing good results in Q3, but it's not new. In Q2 we got good results also on margin and so it's just a continuous improvement. We accelerated both margin and market share gain in Q2. So, it's not something new in Q3, it's just a continuous improvement on what we've been working on for the past year or two and we're in the early stage of Horizon. So, we're expecting a continuous improvement again.

Vishal Shreedhar — Analyst, National Bank Financial

Okay. Thank you for that colour. And just a few quicker ones here. With respect to a sale, is management indifferent to a sale on Voilà or your existing store-based platform and maybe if you can expand upon why, if you do have a preference?

Michael Medline — President & Chief Executive Officer, Empire Company Limited

So far, we haven't had to make any choice. We'll take in both places like we are today. I mean right now, until we got to scale, it's probably slightly better to sell it in the store in terms of the bottom line, but as we get up to scale, that's going to get closer and closer that we're indifferent. We want just to thrill our customers. And most customers, like I'm an example, I shop bricks-and-mortar and I shop Voilà. And

most customers don't think of it, like they just think of it as shopping. They think of it as having opportunities to buy in different places. They don't usually choose one or the other.

Some customers during COVID may have chosen to go e-commerce more heavily at the bleakest times, but I don't see it, we don't make a choice. Wherever a customer feels most comfortable, we'd love to welcome them. And every indication I've ever seen is that when they become an e-commerce customer, the halo effect on your bricks-and-mortar go way up. Basket sizes are bigger in e-commerce, margins slightly better in bricks-and-mortar right now, but we'll take them any way we get them. Good question though and we think about that a lot.

Vishal Shreedhar — Analyst, National Bank Financial

Thanks for that colour. As you reflect on the pandemic and potential lasting changes to the consumer, I'm wondering if you can talk about your real estate strategy and if you foresee any changes, perhaps more suburban, perhaps lower real estate costs in urban centers that make those regions more appealing. Is there any insights that you can share or is it business as usual?

Michael Medline — President & Chief Executive Officer, Empire Company Limited

That's what we're looking at right now. I mean we believe there will be lasting impacts, not only in our sector, which is grocery, that we do believe, we're quite happy to be heavily in full service right now while furiously expanding our discount FreshCo banners, but we're going to keep looking at this because there is going to be lasting impact. It's a question of how big that impact is. We're well set up for it, to be honest to you, and I don't think we have to change our strategy very much at all, but we're going through

that right now, our real estate team working with our operators are looking at that right now. But I don't think it will make a big difference. But you've got to keep looking at these things. I think you're absolutely right. We have to look at the trends. And so far, the trends are really helping us. I think they'll continue to help us. And then we have to look forward and really optimize.

Vishal Shreedhar — Analyst, National Bank Financial

Okay. Thanks a lot, and congrats to the team on the quarter.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Thanks, Vishal. Appreciate it.

Operator

Your next question comes from Peter Sklar at BMO Capital. Please go ahead.

Peter Sklar — Analyst, BMO Capital Markets

Hi. Just a couple of questions left. Michael, first of all, it's no secret that Loblaw was more aggressive on price, on the discount side. I'm just wondering, from your perspective, do you feel that pressure and do you have to adjust your promotional direction or is it just the shift is on automatic pilot and you just sailed through it, which is kind of noise in the backdrop?

Michael Medline — President & Chief Executive Officer, Empire Company Limited

That's got to be one of the best questions I've been asked. Look, you're never on automatic pilot. We watch like hawks everything that goes on in this industry. At the same time, playing our own game and kind of tuning out some of the noise on the sides has really been serving us well, as you can see in a quarter where I've never seen a quarter like this where we boosted our margins like this and grew market share and all the other things. And that's on top of COVID benefits.

So, we saw an increase. When you lose market share, you swing around a little bit and you try to do some things. Kudos to that, I guess. And we saw some more front-page promotional activity in certain areas in discount, which has lost market share, and we saw a real heavy marketing spend from competitors. But I think, you know, maybe we adjusted a tiny bit, but not very much. We think others are going to have to adjust around us a little bit. So that's the way we look at it. But we're not on autopilot. We're always looking. But I think we've got the right tactics and I think Pierre St-Laurent in full service and Mike Venton in discount and Sarah Joyce in Voilà, they know what they're doing.

Peter Sklar — Analyst, BMO Capital Markets

Okay. The other thing I wanted to ask you about, if I could just challenge you on one thing, is like you know how some of your competitors have been demanding additional price from the supply base and Empire is not. Like you're taking a more, I don't know if I'd call it responsible or businesslike relationship with your suppliers. But like if you look at Project Sunrise and like the category resets would have incorporated suppliers, it has. Like in that context, didn't you go back to suppliers and ask for price? So, I'm just wondering what your thoughts are when I put it to you that way.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Can you say it one more time?

Peter Sklar — Analyst, BMO Capital Markets

Well, you're saying that, unlike your competitors, you're not demanding price from your suppliers. You're not demanding a 2% price across the board, you're being much more responsible. But what I'm challenging you on, as part of Project Sunrise though, I would have thought you would have gone for some pretty aggressive price from your suppliers. So, isn't it true you really did have a go at your suppliers? Just wondering what your comment is when I put it to you that way.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

That's a great question. I've never hidden that we're tough, that we're going to negotiate. And I don't think we were a number of years ago. I think we got taken advantage of and we didn't know our own business well enough. You've seen how we've improved our bottom line and some of that is because we're fair, but tough.

But I think that the way to look at it, Peter, is there is, in our opinion, and there's other opinions I suppose, there's the right way to do business and there's the wrong way to do business. And we try as much as we can to be transparent, fair, but not everyone's happy. I got a few e-mails this week from suppliers that had lost some business, it's always quality and pricing and all that so we can be more competitive. And so not everybody's going to be happy with us. At the same time, there's a way to do it.

And I know our supplier partners understand that. They are into hard negotiation. They're darn good at it. We're good at it now. And that's the way we do it.

But we're trying to build the pie up, right? We're trying to work with them to thrill the customers, add more innovation, and take out some costs and pass it on to customers. And our way is better, in our opinion. And I think, if you look over the last four years, you'll see that our way is probably the better way. If you look at it, we've grown our margins and EBITDA margins while at the same time trying, as successfully as we can, to be fair, transparent, and be values based.

I gave a speech, it got a little bit of attention, at the Empire Club in October and I said it, which is that COVID showed us how we can work together better. We think we can grow the pie. But we're not going to give up being tough and negotiating tough. And we've been very clear on that. Our customers and our investors expect us to outperform and beat the competition. We just want to do it in a different way that we think is more successful. If others want to do a different way, it's up to them.

Peter Sklar — Analyst, BMO Capital Markets

Okay, that's a good answer. Thank you.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Thanks a lot. Boy, we got some good questions today.

Operator

The next question is from Kenric Tyghe at ATB Capital. Please go ahead. Kenric, your line is open.

You may proceed with your question.

Kenric Tyghe — Analyst, ATB Capital Markets

Thank you and good afternoon. No pressure, Michael, I guess I better keep the trend going. If I could just come at this a slightly different way to an earlier question, so you called out share and share gains and the like. Can you even directionally give any insight on just how much of a benefit full-service has been sort of through the pandemic with your one-stop type shop focus, but perhaps more importantly, how you see that evolving through 2021, both as your footprint evolves with increased discount, but also as consumer habits start to rebalance and we find whatever our new normal is. And I don't think normal is the normal of old, but we also know exactly what that's going to look like. Could you provide any insight directionally or otherwise on that? I mean how sticky is this? How well are you positioned on the rebalancing?

Michael Medline — President & Chief Executive Officer, Empire Company Limited

There's a mix here, a lot of mixing going on, which is, you know, COVID has been helpful to full service. At the same time, we stepped our game up appreciably over the year. Last year we would have done so anyway. If you look back at our investor calls since one year ago to almost a week, we've been pretty darn accurate in our projections of COVID impact generally, since the very beginning of the pandemic. And we've said we really like being in full service and in the new normal we expect we'll really

like being in full service. At the same time, as I said, we're expanding our great discount FreshCo business, which we always wanted to do.

My experience as a retailer, and we have a lot of studies and we can look at them, but my experience as a retailer is that once a retailer gets momentum, it's hard to stop them. So, customers start coming to your stores, you start winning them over, you get better things, you get the confidence. And I said it twice in my script today, but I want to say it again: the key to our success will not be COVID. It will be Project Horizon and executing. That will be what drives us.

Kenric Tyghe — Analyst, ATB Capital Markets

Thank you, Michael. Just one quick follow up, if I could squeeze it in here, one quick additional question rather. The launch of curbside pickup in Alberta last month, just in the context of CFC 3, the timing around CFC 3 being, I think, first half of 2023, could you just help us understand the thinking there, the evolution, and whether or not it's safe to say we won't see curbside pickup necessarily across the country but it's more opportunistic in markets where you've got a long lead time to your next CFC opening? I just want to make sure we're correctly thinking about your curbside launches in a very select number of markets.

Michael Vels — Chief Financial Officer, Empire Company Limited

Well, you didn't just ask a good question, you also provided a good answer. So that's right. And it's really store pick. At some point in time it's not just going to be a curbside pickup, which is really more of a COVID term, but store pick, ultimately, is going to fit into our e-commerce strategy in places where our

CFC will probably never service efficiently. And so that's why we're seeing Atlantic Canada being a focus for us.

In the West, to your specific question, it's going to be a while before that CFC is up and running and so we're going to provide customers with the Voilà experience in advance and they're going to be just thrilled when they convert into a CFC that's going to have a wider assortment and just the same high-quality Voilà service. So, it's a bit of a beachhead for a CFC that will ultimately be there. But even after it's there, we'll likely still use store pick in places where it's too remote or too thinly populated for the CFC to be effective. So, it's always going to be one of the arrows in our quiver, but it's not going to be the main one.

Kenric Tyghe — Analyst, ATB Capital Markets

Thank you. That's great colour and congrats. I'll leave it there.

Michael Medline — President & Chief Executive Officer, Empire Company Limited

Thank you so much.

Operator

Thank you. And the last question comes from Michael Van Aelst from TD. Please go ahead.

Michael Van Aelst — Analyst, TD Securities

Thank you. Good afternoon. I wanted to focus first on FreshCo and if you could give us an update as to how the conversions are performing on the more recent stores compared to the initial conversions and are you seeing improvements because of experience and the learnings or is that diluted by the possibility that you started with the higher-return stores.

Michael Vels — Chief Financial Officer, Empire Company Limited

Thanks, Michael. So, we didn't actually necessarily start with higher-return stores. That's an interesting way of looking at it. We spent a lot of time figuring out, at first —sorry, this isn't directly the answer to your question, so I apologize, but our initial plan was maybe only focus on BC. And then we decided that it made more sense to be present in more markets, which is why we ended up in Saskatchewan and BC, of course, now Alberta. So, we haven't actually tiered the rollout according to advantaged stores and disadvantaged stores. So that really wasn't part of the decision making. It was all about where it made more sense for the business to be given customer demographics and opportunity.

I'd point at two things in terms of how the recent stores are doing compared to the initial ones. From just an efficiency and a ramp-up and general store conditions, our recent stores have been way better than the first ones. And that makes a lot of sense because, if you think about it, we now have an experienced management team and an experienced group of franchise operators in the West who've learned from initial experience and they're just getting better and better and better every time they roll a store out. So, just because of that, those experiences have been better, our margins are improved, and we're being much more effective in terms of how we promote and how we price.

Offsetting that though is we haven't done the same grand openings that we did in our first stores. We haven't been able to because of COVID. So, it's been a quieter launch for many of the stores. Having said that, even with reduced marketing, because we didn't want to overcrowd the stores and have lineups like we did with our other grand openings, the results have been really good and we're comfortable with them. They're just now a slower ramp-up than the earlier stores, which had the big, splashy grand openings. On balance, though, I'd say, from a bottom line perspective, the more recent stores are having more efficient ramp-ups than the early ones.

Michael Van Aelst — Analyst, TD Securities

Okay. Great. And then on Voilà, you talked earlier about expectations to have the most profitable e-commerce approach in Canada once you hit scale. Can you give us an idea of the penetration level you figure you need to get to that scale? And when you're at that level, would you be expecting to have to cut your bricks-and-mortar square footage at the same time?

Michael Vels — Chief Financial Officer, Empire Company Limited

So, we don't have a real number, Michael, from a penetration perspective. For us, it's about winning the channel. We expect over index in the online channel. And at this stage we're in the business of tracking weekly sales increases and just pushing them as hard as we can.

The second question in Ontario is do we think that's going to cannibalize our bricks-and-mortar and are we going to have to change our layouts? We don't think so at this point. I think it's a large enough market and we're not going to have, at least in the next five years, I don't think we'll have the type of market shares or penetration rates that are going to require changes in bricks-and-mortar stores. But having said that, as we're rolling out newer stores, like Farm Boy for example, they're much more online proof than a larger conventional store, because they provide an experience and they provide assortment that's not 100% replicable in Voilà.

In Québec, we strongly feel, and so do our franchise partners, that there's going to be more of a halo effect. So, we're going to be providing existing IGA customers with a very, very much higher-quality option than they're currently getting online with an improved assortment and we actually think we're going to grow the total pie there. And the losers are not going to be our stores; they're going to be the competition.

Michael Van Aelst — Analyst, TD Securities

Great. Thank you.

Operator

Thank you. At this time, I will now turn the conference call back over to Katie Brine for closing comments.

Katie Brine — Director Finance, Investor Relations, Empire Company Limited

Thank you, Joanna. Ladies and gentlemen, we appreciate your continued interest in Empire. If there are any unanswered questions, please contact me by phone or email. We look forward to having you join us for our fourth quarter fiscal 2021 conference call on June 23rd. Talk soon.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and we ask that you please disconnect your lines. Enjoy the rest of your day.