

Safeway Inc. is one of the largest food and drug retailers in North America. As of January 1, 2000, the Company operated 1,659 stores in the Western, Southwestern, Rocky Mountain, Midwestern and Mid-Atlantic regions of the United States and in western Canada.

In support of its stores, Safeway has an extensive network of distribution, manufacturing and food processing facilities.

Safeway also holds a 49% interest in Casa Ley, S.A. de C.V., which at January 1, 2000 operated 86 food and general merchandise stores in western Mexico.

Percentage of Stores with Specialty Departments

	1999	1995
Bakery	91%	76%
Deli	94	91
Floral	89	93
Pharmacy	65	55

Manufacturing and Processing Facilities

	Year-end 1999	
	U.S.	Canada
Milk Plants	7	3
Bread Baking Plants	6	2
Ice Cream Plants	4	2
Cheese and Meat Packaging Plants	1	2
Soft Drink Bottling Plants	4	–
Fruit and Vegetable Processing Plants	2	3
Other Food Processing Plants	4	1
Pet Food Plant	1	–
	<u>29</u>	<u>13</u>

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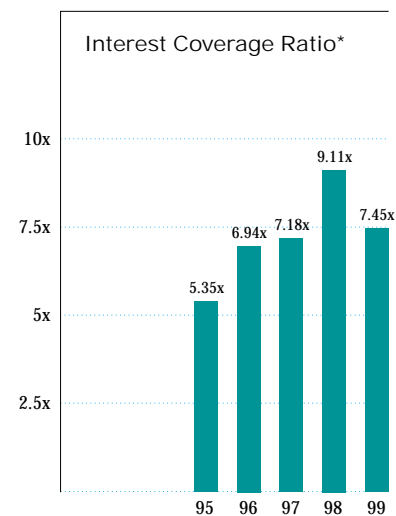
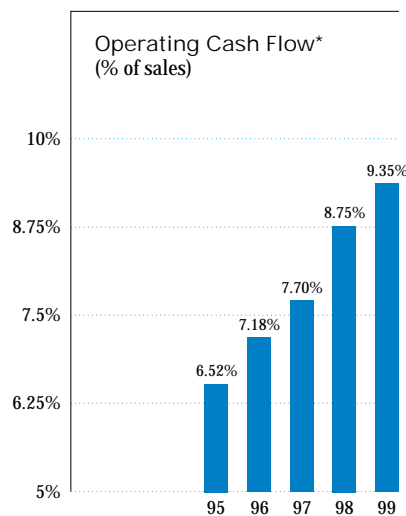
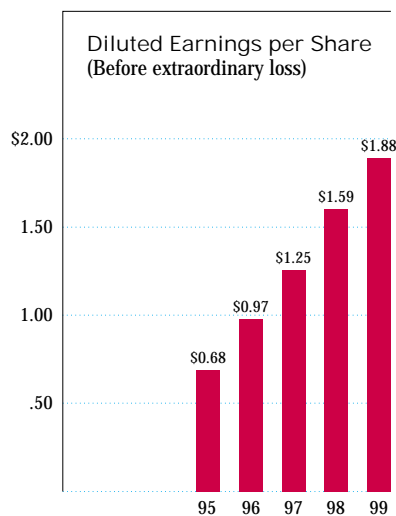
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FINANCIAL HIGHLIGHTS

	52 Weeks 1999	52 Weeks 1998	53 Weeks 1997
(Dollars in millions, except per-share amounts)			
For the Year:			
Sales	\$28,859.9	\$24,484.2	\$22,483.8
Gross profit	8,510.7	7,124.5	6,414.7
Operating profit	1,997.9	1,601.7	1,279.7
Income before extraordinary loss	970.9	806.7	621.5
Net income	970.9	806.7	557.4
Diluted earnings per share:			
Income before extraordinary loss	\$ 1.88	\$ 1.59	\$ 1.25
Net income	1.88	1.59	1.12
Capital expenditures (Note 1)	1,485.6	1,189.7	829.4
At Year-End:			
Common shares outstanding (in millions) (Note 2)	493.6	490.3	476.2
Retail square feet (in millions)	70.8	61.6	53.2
Number of stores	1,659	1,497	1,368

Note 1: Defined on page 15 under "Capital Expenditure Program."

Note 2: Net of 65.4 million, 60.6 million and 61.2 million shares held in treasury in 1999, 1998 and 1997, respectively.



* Defined on page 20

Safeway had another year of outstanding operating and financial results in 1999. Once again we were one of the industry's leading performers, posting record earnings and, on a pro forma basis, reducing our expense-to-sales ratio for an unprecedented seventh straight year. We also accelerated our capital spending program and completed two more acquisitions.

Unfortunately, as many of you know, these achievements were not reflected in our stock price. The supermarket industry, typically a "stable" sector, seemed to be out of favor in 1999 as investors found other sectors more attractive.

Fortunately history has shown that, over time, the financial markets tend to reward companies with strong earnings, solid economic fundamentals and sound management. We believe Safeway is widely regarded as such a company.

Operating Results

As indicated in the following highlights, we continued to make good progress in 1999.

Net income rose 20% to \$970.9 million (\$1.88 per share) from \$806.7 million (\$1.59 per share) in 1998.

Total sales increased 18% to \$28.9 billion, primarily due to the acquisitions described below. Bolstered by a strong fourth quarter, comparable-store sales for the year were up 2.2%, while identical-store sales (which exclude replacement stores) increased 1.7%. The corresponding fourth-quarter sales gains were 3.7% and 2.9%, respectively.

On a pro forma basis, our gross profit margin improved by 51 basis points in 1999. The increase reflects continuing improvements in buying practices and product mix.

On a pro forma basis, operating and administrative expense as a percentage of sales fell 30 basis points, largely as a result of increased sales and ongoing efforts to reduce or control costs. Our O&A expense-to-sales ratio has declined for seven consecutive years.

Operating cash flow as a percentage of sales reached an all-time high of 9.35%.

Our interest coverage ratio (operating cash flow divided by interest expense) remained a very strong 7.45 times despite the additional debt incurred to finance acquisitions and the stock repurchase program, described below.

Share Repurchases

During the fourth quarter of 1999, we repurchased 17.9 million shares of Safeway common stock for \$651 million. Due to the timing of the repurchases, this had only a minor impact on earnings per share in 1999.

We also recently completed an odd lot buyback program to reduce administrative expenses. More than 27% of targeted stockholders responded to the offer, opting either to tender their holdings or to round them up to at least 100 shares.

Store Modernization

Capital spending in 1999 increased to \$1.5 billion. We opened 67 new stores, closed 54 older ones and expanded or remodeled 251 existing stores, resulting in a 3.1% net addition to total retail square footage, exclusive of acquisitions. During 2000 we expect to invest more than \$1.6 billion and open 70 to 75 new stores while completing some 250 remodels, growing square footage 3.5% to 4.0%.

Additional Acquisitions

We acquired two more companies during 1999. In April we completed the acquisition of Carr-Gottstein Foods Co.,



Alaska's leading retailer. On the acquisition date, Carrs operated 49 stores and the state's largest food warehouse and freight network, which should significantly enhance the efficiency of our combined operations. We have operated our own stores in Alaska since 1960.

In September we acquired Randall's Food Markets, Inc., a Texas-based supermarket chain that, at the close of the transaction, operated 117 stores in the Houston, Dallas/Fort Worth and Austin areas under the Randalls and Tom Thumb banners. Like the Dominick's merger in 1998, the combination with Randall's extends our geographic reach into new operating areas.


Over the past three years, we have completed four mergers, acquiring almost 600 stores with combined sales of more than \$11 billion. Acquisitions continue to be a key element of our long-range growth strategy.

Outlook

We are pleased with our operating results in 1999, particularly the strong sales trend in the fourth quarter that has continued into the current year. As we roll out and refine a series of new sales-building initiatives in the months ahead, and as we continue to analyze acqui-

sition possibilities and other opportunities to grow our business, we are excited about Safeway's future.

Success requires a team effort. All of us at Safeway work hard to exceed our customers' expectations. In addition, many of our people are actively involved in their communities, giving tirelessly of themselves to improve the quality of life for their families and neighbors. With our employees' ongoing support and enthusiasm, we are confident we will continue "taking care of business" in 2000 and beyond.



Steven A. Burd
Chairman, President and Chief Executive Officer
February 25, 2000

Taking *Care* of *Business*

Every day, in hundreds of cities and towns across the U.S. and Canada, we work hard to take care of our customers, our stockholders, our employees and the communities we serve. We do this best by “taking care of business.”

As a multi-regional food and drug retailer committed to continuous improvement, we strive to combine the best practices found in our divisions and apply them throughout the company. We believe this creates a better shopping experience for our customers, greater value for our investors, enhanced training and advancement potential for our employees, and increased financial and in-kind support for our communities.

As we see it, balancing the diverse needs of our various stakeholders is not merely good corporate citizenship, it’s a business imperative.



Our customers are the central focus of everything we do, from the location and design of our stores to the assortment and display of the products we sell. Through daily interaction with shoppers, supplemented by extensive consumer research and cutting-edge technology, we stay close to our customers so we can anticipate and respond to their changing needs. We aren't satisfied until they are.

To achieve and sustain a competitive advantage in our business, we must differentiate ourselves from other retailers. It's not enough to earn our customers' trust and confidence. We must also provide them with a shopping experience they cannot duplicate elsewhere. Our goal is to delight and surprise shoppers by consistently delivering superior quality, selection, value and service in attractive, conveniently located stores. As we continue to gain market share in most of our operating areas, we believe we are making good progress toward this goal.

“Getting to know our *customers* enables me to *serve* their families' health care needs better—and often more *cost-effectively*.”

JOE KIM, PHARMACIST, DOMINICK'S STORE #4135

“I enjoy dealing with our *stockholders* and try to deliver the same *great* service we provide in the stores.”

RASHIDA SUMINSKI, INVESTOR RELATIONS SPECIALIST, SAFEWAY CORPORATE HEADQUARTERS

Just as we must continuously win our customers' loyalty in the marketplace, we must also earn our investors' confidence in the financial arena.

To improve communications with the financial community, in July we held a conference for supermarket industry analysts and institutional investors. During the conference we reiterated our commitment to increasing sales, reducing costs, managing capital effectively and pursuing acquisitions. We also reviewed our financial performance and discussed our growth strategy.

To further enhance communications with investors, we are expanding the financial content of our web site to include more useful, timely information about the company. We also announced a share repurchase program under which we bought back \$651 million of an authorized \$1 billion of our common stock. In addition, we recently completed an odd lot buyback program to reduce administrative expenses.



“Safeway lets us know *how* we’re doing and how we can contribute to the company’s *success*.”

JOHN CHAVEZ, TRUCK DRIVER, THE VONS COMPANIES, INC.



With more than 193,000 employees across North America, communicating our vision, values and priorities throughout the organization is one of our greatest challenges. It's also one of our biggest opportunities.

During the year we launched several initiatives to improve internal communications and training. Knowledgeable, well informed employees take pride in their work and enjoy their jobs. Of equal importance, motivated employees are highly productive and helpful to our customers. To attract and retain such people, we try to cultivate an environment in which work is challenging, satisfying and fun.

As we build more new stores and remodel existing ones, we create greater career advancement opportunities for our employees. Excluding acquisitions, we added almost 1,400 new retail jobs during 1999.

In addition to their pay and benefits, many of our people share in the company's success as stockholders. More than 25% of eligible employees participated in our payroll-deduction stock purchase plan in 1999.



“I’m *proud* of the active role my company plays in community activities and local *fundraising* programs.”

KATHY LUSSIER, PUBLIC AFFAIRS DIRECTOR, RANDALL'S FOOD MARKETS, INC.

In 1999 we made cash and in-kind contributions of more than \$80 million to non-profit organizations throughout the communities we serve. The primary recipients of our donations are food banks, educational institutions and local charities.

During the year we donated some \$50 million worth of merchandise to food banks and various programs to assist the hungry in the U.S. and Canada. We also contributed more than \$20 million to local schools through innovative fundraising programs. In addition, we supported hundreds of local civic, charitable and cultural organizations throughout our operating areas.

Since becoming a corporate sponsor of Easter Seals in 1985, the company and its employees have raised over \$63 million to help people with disabilities lead more productive, independent lives.

Many Safeway employees lend their time, energy and talents to community organizations and causes. We encourage and support these efforts through our Community Pride program, augmenting our employees' good work with financial contributions from the company.

During the past seven years, Safeway has consistently ranked among the industry's leaders in the following key measures of financial performance:*

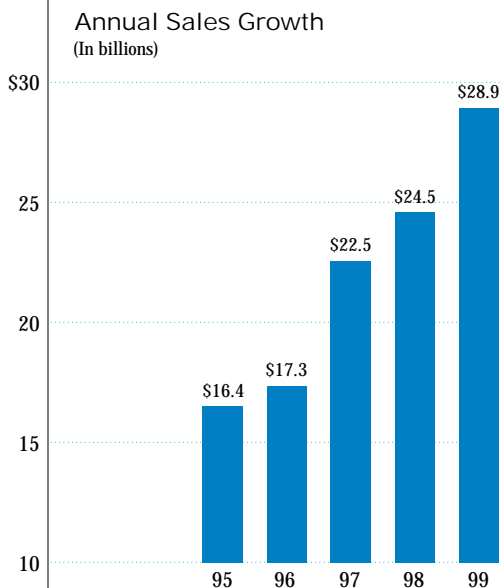
- Sales growth
- Expense ratio reduction
- Working capital management
- Operating cash flow margin
- Earnings per share growth

We have achieved these results by focusing on the three priorities detailed on the following pages.

*Based on latest available information

INCREASING SALES

Generating strong sales growth is an ongoing priority at Safeway. Since 1992 we have focused primarily on improved store standards, enhanced service and competitive pricing to drive top-line growth. During 1999 we began developing and implementing several new sales-building initiatives. With the Randall's acquisition, our fourth in the past three years, we have expanded our sales base and extended our geographic reach.



Through internal growth and acquisitions, sales have increased at an annual compound rate of 13.1% during the past five years.

We continued to exchange best marketing practices among recently acquired operations and core Safeway divisions.

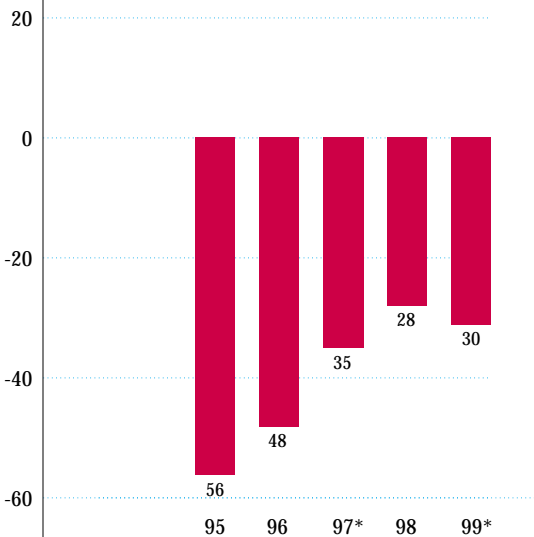
We operated 1,074 stores with pharmacies at year-end 1999, ranking us among the top 10 drug retailers in North America.

We introduced 185 new items under the Safeway SELECT brand of premium quality private-label products.

Further progress in category management enabled us to meet our customers' needs more effectively.

Pro forma operating and administrative expense as a percentage of sales declined again in 1999, continuing a seven-year trend. The ongoing improvement reflects concerted efforts throughout the company to streamline support functions, simplify work practices and maintain labor cost parity. No other major food and drug retailer has come close to Safeway in the magnitude of expense reduction, measured as a percentage of sales, since 1992.

Improvement in Annual Operating and Administrative Expense Margin (In basis points)



Our O&A expense margin improved for the seventh consecutive year, declining 30 basis points in 1999.

* Pro forma as defined on page 18

We made further improvements in cost of goods sold by applying best practices in product procurement, distribution and category management.

We converted Carrs, and all remaining Vons and Dominick's applications, to Safeway's accounting and merchandising systems.

We began consolidating corporate administrative functions at Carrs and Randall's into Safeway's operations, and continued the process at Dominick's.

We negotiated competitive labor agreements in several key markets.

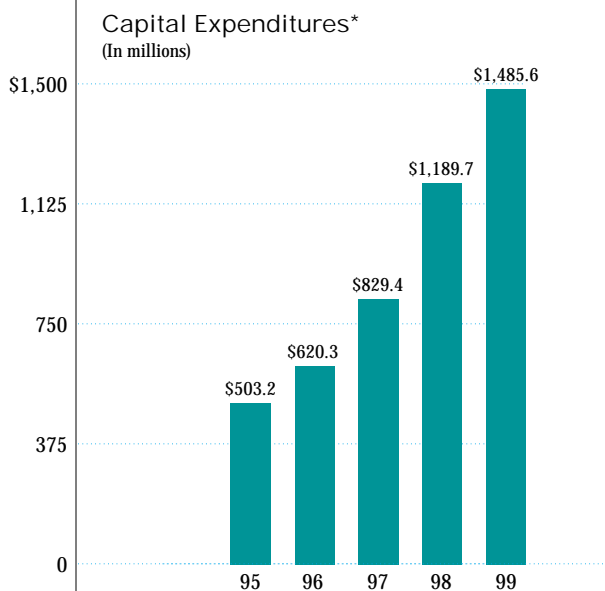
Capital spending increased to \$1.5 billion in 1999, up from \$1.2 billion in 1998. As shown on the chart below, we have invested more than \$4.6 billion over the past five years to keep our store system and support facilities up to date. During this period, a significant majority of our capital investments have exceeded targeted rates of return. In 1999 we maintained a strong interest coverage ratio despite the additional debt incurred to finance the Carrs and Randall's acquisitions and the stock repurchase program.

We opened 67 new stores, expanded or remodeled 251 existing stores and acquired 149 stores.

Through capital expenditures and acquisitions, we increased total retail square footage by 15%.

We maintained negative working capital for the sixth consecutive year by managing inventory and payables effectively.

We replaced \$290 million of higher rate long-term debt at Carrs and Randall's with lower rate borrowings.



Capital investments have increased steadily since 1993, reflecting strong operating results.

* Defined on page 15

Safeway Inc. (“Safeway” or the “Company”) is one of the largest food and drug chains in North America, with 1,659 stores at year-end 1999.

The Company’s U.S. retail operations are located principally in northern California, southern California, Oregon, Washington, Alaska, Colorado, Arizona, Texas, the Chicago metropolitan area, and the Mid-Atlantic region. The Company’s Canadian retail operations are located principally in British Columbia, Alberta and Manitoba/Saskatchewan. In support of its retail operations, the Company has an extensive network of distribution, manufacturing and food processing facilities.

In addition, Safeway has a 49% interest in Casa Ley, S.A. de C.V. (“Casa Ley”), which operates 86 food and general merchandise stores in Western Mexico.

Acquisition of Randall’s Food Markets, Inc.

(“Randall’s”) In September 1999, Safeway acquired all of the outstanding shares of Randall’s in exchange for \$1.3 billion consisting of \$754 million of cash and 12.7 million shares of Safeway stock (the “Randall’s Acquisition”). On the acquisition date, Randall’s operated 117 stores in Texas. The Randall’s Acquisition was accounted for as a purchase. Safeway funded the cash portion of the acquisition, and subsequent repayment of approximately \$403 million of Randall’s debt, through the issuance of senior notes. Randall’s sales for its last full fiscal year prior to the acquisition were \$2.6 billion.

Acquisition of Carr-Gottstein Foods Co. (“Carrs”) In April 1999, Safeway completed its acquisition of all of the outstanding shares of Carrs for approximately \$106 million in cash (the “Carrs Acquisition”). On the acquisition date, Carrs operated 49 stores. The Carrs Acquisition was accounted for as a purchase. Safeway funded the acquisition, and subsequent repayment of approximately \$239 million of Carrs’ debt, with issuance of commercial paper. Carrs’ sales for its last full fiscal year prior to the acquisition were \$602 million.

Stores Safeway’s average store size is approximately 43,000 square feet. Safeway’s primary new store prototype is 55,000 square feet and is designed to accommodate changing consumer needs and to achieve certain operating efficiencies. The Company determines the size of a new store based on a number of considerations, including the needs of the community the store serves, the location and site plan, and the estimated return on capital invested.

Most stores offer a wide selection of both food and general merchandise and feature a variety of specialty departments such as bakery, delicatessen, floral and pharmacy.

Safeway continues to operate a number of smaller stores which also offer an extensive selection of food and general merchandise, and generally include one or more specialty departments. These stores remain an important part of the Company’s store network in smaller communities and certain other locations where larger stores may not be feasible because of space limitations and/or community needs or restrictions.

The following table summarizes Safeway’s stores by size at year-end 1999:

	Number of Stores	Percent of Total
Less than 30,000 square feet	341	20%
30,000 to 50,000	794	48
More than 50,000	524	32
Total stores	<u>1,659</u>	<u>100%</u>

Store Ownership At year-end 1999, Safeway owned approximately one-third of its stores and leased its remaining stores. In recent years, the Company has preferred ownership because it provides control and flexibility with respect to financing terms, remodeling, expansions and closures.

Merchandising Safeway’s operating strategy is to provide value to its customers by maintaining high store standards and a wide selection of high quality products at competitive prices. To provide one-stop shopping for today’s busy shoppers, the Company emphasizes high quality produce and meat, as well as specialty departments, including in-store bakery, delicatessen, floral and pharmacy.

Safeway has developed a line of more than 1,100 premium corporate brand products since 1993 under the “Safeway SELECT” banner. The award-winning Safeway SELECT line is designed to offer premium quality products that the Company believes are equal or superior in quality to comparable best-selling nationally advertised brands, or are unique to the category and not available from national brand manufacturers.

The Safeway SELECT line of products includes carbonated soft drinks; unique salsas; the Indulgence line of cookies and other sweets; the Verdi line of fresh and frozen pastas, pasta sauces and olive oils; Artisan fresh-baked breads; Twice-the-Fruit yogurt; NutraBalance Pet Food; Ultra laundry detergents and dish soaps; and Softly paper products. The Safeway SELECT line also includes an extensive array of ice cream, frozen yogurt and sorbets; Healthy Advantage items such as low-fat ice cream and low-fat cereal bars; and Gourmet Club frozen entrees and hors d'oeuvres.

In addition, Safeway has repackaged over 2,500 corporate brand products primarily under the Safeway, Lucerne and Mrs. Wright's labels.

Manufacturing and Wholesale The principal function of manufacturing operations is to purchase, manufacture and process private label merchandise sold in stores operated by the Company. As measured by sales dollars, approximately one-half of Safeway's private label merchandise is manufactured in company-owned plants, and the remainder is purchased from third parties.

Safeway's Canadian subsidiary has a wholesale operation that distributes both national brands and private label products to independent grocery stores and institutional customers.

Safeway operated the following manufacturing and processing facilities at year-end 1999:

	U.S.	Canada
Milk plants	7	3
Bread baking plants	6	2
Ice cream plants	4	2
Cheese and meat packaging plants	1	2
Soft drink bottling plants	4	—
Fruit and vegetable processing plants	2	3
Other food processing plants	4	1
Pet food plant	1	—
Total	<u>29</u>	<u>13</u>

In addition, the Company operates laboratory facilities for quality assurance and research and development in certain of its plants and at its corporate offices.

Distribution Each of Safeway's 12 retail operating areas is served by a regional distribution center consisting of one or more facilities. Safeway has 16 distribution/warehousing centers (13 in the United States and three in Canada), which collectively provide the majority of all products to Safeway stores. Safeway's distribution centers in northern California and British Columbia are operated by third parties. During 1999, Safeway acquired three distribution centers through its acquisitions of Carrs and Randall's.

Capital Expenditure Program

A component of the Company's long-term strategy is its capital expenditure program. The Company's capital expenditure program funds, among other things, new stores, remodels, manufacturing plants, distribution facilities, and information technology advances. Over the last several years, Safeway management has significantly strengthened its program to select and approve new capital investments, resulting in continuing strong returns on investment.

The table below reconciles cash paid for property additions reflected in the Consolidated Statements of Cash Flows to Safeway's broader definition of capital expenditures, and also details changes in the Company's store base over the last three years:

(Dollars in millions)	1999	1998	1997
Cash paid for property additions	\$1,333.6	\$1,075.2	\$758.2
Less: Purchases of previously leased properties	(37.2)	(35.7)	(28.2)
Plus: Present value of all lease obligations incurred	179.5	117.4	91.3
Mortgage notes assumed in property acquisitions	9.7	32.8	0.9
Vons first quarter expenditures	—	—	7.2
Total capital expenditures	<u>\$1,485.6</u>	<u>\$1,189.7</u>	<u>\$829.4</u>
Capital expenditures as a percent of sales	5.1%	4.9%	3.7%
Stores opened (Note 1)	67	46	37
Stores closed or sold	54	30	37
Remodels (Note 2)	251	234	181
Total retail square footage at year-end (in millions)	70.8	61.6	53.2

Note 1: Excludes acquisitions.

Note 2: Defined as store projects (other than maintenance) generally requiring expenditures in excess of \$200,000.

Improved operations and lower project costs have kept the return on capital projects at a high level, allowing Safeway to increase capital expenditures to \$1.5 billion in 1999 and open 67 stores and remodel 251 stores. In 2000, Safeway expects to spend more than \$1.6 billion and open 70 to 75 new stores and complete approximately 250 remodels.

Performance-Based Compensation

The Company has performance-based compensation plans that cover approximately 13,000 management and professional employees. Performance-based compensation plans set overall bonus levels based upon both operating results and working capital management. Individual bonuses are based on job performance. Certain employees are covered by capital investment bonus plans which measure the performance of capital projects based on operating performance over several years.

Market Risk from Financial Instruments

Safeway manages interest rate risk through the strategic use of fixed and variable interest rate debt and, to a limited extent, interest rate swaps. As of year-end 1999, the Company had effectively converted \$200.0 million of its floating rate debt to fixed interest rate debt through interest rate swap agreements. Under one swap agreement, Safeway pays interest of 6.2% on the \$100.0 million notional amount and receives a variable interest

rate based on Federal Reserve rates quoted for commercial paper. This agreement expires in 2007. Additionally, the Company assumed two interest rate swap agreements, with notional amounts of \$50.0 million each, as part of the Randall's Acquisition. Under these swap agreements, Safeway pays interest of 5.30% and 5.49%, respectively, on the \$50 notional amounts and receives a variable interest rate based on Federal Reserve rates quoted for commercial paper. These swap agreements expire in 2001.

The Company does not utilize financial instruments for trading or other speculative purposes, nor does it utilize leveraged financial instruments. The Company does not consider the potential losses in future earnings, fair values and cash flows from reasonable possible near-term changes in interest rates and exchange rates to be material.

The table below presents principal amounts and related weighted average rates by year of maturity for the Company's debt obligations at year-end 1999 and 1998 (dollars in millions):

January 1, 2000	2000	2001	2002	2003	2004	Thereafter	Total
Commercial paper:							
Principal	-	-	\$ 2,358.1	-	-	-	\$ 2,358.1 ⁽²⁾
Weighted average interest rate	-	-	6.81%	-	-	-	6.81%
Bank borrowings:							
Principal	\$ 129.7	-	\$ 75.7	-	-	-	\$ 205.4 ⁽²⁾
Weighted average interest rate	6.27%	-	5.18%	-	-	-	5.87%
Long-term debt:⁽¹⁾							
Principal	\$ 427.4	\$ 548.6	\$ 637.2	\$ 377.2	\$ 700.0	\$ 1,225.2	\$ 3,915.6 ⁽²⁾
Weighted average interest rate	5.89%	6.80%	7.03%	6.19%	7.43%	7.25%	6.93%

January 2, 1999	1999	2000	2001	2002	2003	Thereafter	Total
Commercial paper:							
Principal	-	-	-	\$ 1,745.1	-	-	\$ 1,745.1 ⁽²⁾
Weighted average interest rate	-	-	-	5.99%	-	-	5.99%
Bank borrowings:							
Principal	\$ 161.8	-	-	\$ 89.1	-	-	\$ 250.9 ⁽²⁾
Weighted average interest rate	5.80%	-	-	5.57%	-	-	5.72%
Long-term debt:⁽¹⁾							
Principal	\$ 118.0	\$ 427.5	\$ 549.6	\$ 37.8	\$ 377.6	\$ 1,015.9	\$ 2,526.4 ⁽²⁾
Weighted average interest rate	8.97%	5.93%	6.88%	8.95%	6.28%	7.22%	6.89%

⁽¹⁾ Primarily fixed rate debt

⁽²⁾ Carrying value approximates fair value

FIVE-YEAR SUMMARY FINANCIAL INFORMATION

	52 Weeks 1999	52 Weeks 1998	53 Weeks 1997	52 Weeks 1996	52 Weeks 1995
(Dollars in millions, except per-share amounts)					
Results of Operations					
Sales	<u>\$28,859.9</u>	<u>\$24,484.2</u>	<u>\$22,483.8</u>	<u>\$17,269.0</u>	<u>\$16,397.5</u>
Gross profit	<u>8,510.7</u>	7,124.5	6,414.7	4,774.2	4,492.4
Operating and administrative expense	<u>(6,411.4)</u>	(5,466.5)	(5,093.2)	(3,872.1)	(3,754.6)
Goodwill amortization	<u>(101.4)</u>	(56.3)	(41.8)	(10.4)	(10.4)
Operating profit	<u>1,997.9</u>	1,601.7	1,279.7	891.7	727.4
Interest expense	<u>(362.2)</u>	(235.0)	(241.2)	(178.5)	(199.8)
Equity in earnings of unconsolidated affiliates (Note 1)	<u>34.5</u>	28.5	34.9	50.0	26.9
Other income, net	<u>3.8</u>	1.7	2.9	4.4	2.0
Income before income taxes and extraordinary loss	<u>1,674.0</u>	1,396.9	1,076.3	767.6	556.5
Income taxes	<u>(703.1)</u>	(590.2)	(454.8)	(307.0)	(228.2)
Income before extraordinary loss	<u>970.9</u>	806.7	621.5	460.6	328.3
Extraordinary loss, net of tax benefit of \$41.1 and \$1.3	<u>-</u>	-	(64.1)	-	(2.0)
Net income	<u>\$ 970.9</u>	<u>\$ 806.7</u>	<u>\$ 557.4</u>	<u>\$ 460.6</u>	<u>\$ 326.3</u>
Diluted earnings per share:					
Income before extraordinary loss	<u>\$ 1.88</u>	\$ 1.59	\$ 1.25	\$ 0.97	\$ 0.68
Extraordinary loss	<u>-</u>	-	(0.13)	-	-
Net income	<u>\$ 1.88</u>	<u>\$ 1.59</u>	<u>\$ 1.12</u>	<u>\$ 0.97</u>	<u>\$ 0.68</u>
Financial Statistics					
Comparable-store sales increases (Note 2)	2.2%	4.1%	2.3%	5.8%	5.4%
Identical-store sales increases (Note 2)	1.7%	3.7%	1.3%	5.1%	4.6%
Gross profit margin	29.49%	29.10%	28.53%	27.65%	27.40%
Operating and administrative expense margin (Note 3)	22.57%	22.56%	22.84%	22.48%	22.96%
Operating profit margin	6.9%	6.5%	5.7%	5.2%	4.4%
Capital expenditures (Note 4)	\$ 1,485.6	\$ 1,189.7	\$ 829.4	\$ 620.3	\$ 503.2
Depreciation	594.2	475.1	414.0	328.1	319.3
Total assets	14,900.3	11,389.6	8,493.9	5,545.2	5,194.3
Total debt	6,956.3	4,972.1	3,340.3	1,984.2	2,190.2
Stockholders' equity	4,085.8	3,082.1	2,149.0	1,186.8	795.5
Weighted average shares outstanding – diluted (in millions)	515.4	508.8	497.7	475.7	481.2
Other Statistics					
Randall's stores acquired	117	-	-	-	-
Carrs stores acquired	32	-	-	-	-
Dominick's stores acquired	-	113	-	-	-
Vons stores acquired	-	-	316	-	-
Stores opened	67	46	37	30	32
Stores closed or sold	54	30	37	37	35
Total stores at year-end	1,659	1,497	1,368	1,052	1,059
Remodels completed (Note 5)	251	234	181	141	108
Total retail square footage at year-end (in millions)	70.8	61.6	53.2	40.7	40.1

Note 1. Includes equity in Vons' earnings through the first quarter of 1997.

Note 2. Defined as stores operating the entire year in both the current year and the previous year. Comparable stores include replacement stores while identical-stores do not. 1997 and 1996 sales increases exclude British Columbia stores, which were closed during a labor dispute in 1996.

Note 3. Includes goodwill amortization.

Note 4. Defined in the table on page 15 under "Capital Expenditure Program."

Note 5. Defined as store projects (other than maintenance) generally requiring expenditures in excess of \$200,000.

Stock Repurchase

In October 1999, Safeway announced that its Board of Directors had authorized a stock repurchase program under which Safeway may acquire up to \$1.0 billion of its common stock. The purpose of this program is, in part, to replace treasury stock issued in connection with the Randall's Acquisition. By the end of the year, the Company incurred \$651.0 million in short-term debt to repurchase 17.9 million shares of common stock. Due to the timing of the repurchases, the net impact of the reduced shares outstanding and the related interest expense increased annual earnings by only two-tenths of a cent per share.

Acquisition of Randall's Food Markets, Inc. ("Randall's")

In September 1999, Safeway acquired all of the outstanding shares of Randall's in exchange for \$1.3 billion consisting of \$754 million of cash and 12.7 million shares of Safeway stock (the "Randall's Acquisition"). On the acquisition date, Randall's operated 117 stores in Texas. The Randall's Acquisition was accounted for as a purchase. Safeway funded the cash portion of the acquisition, and subsequent repayment of approximately \$403 million of Randall's debt, through the issuance of senior notes. Randall's sales for its last full fiscal year prior to the acquisition were \$2.6 billion.

Acquisition of Carr-Gottstein Foods Co. ("Carrs")

In April 1999, Safeway completed its acquisition of all of the outstanding shares of Carrs for approximately \$106 million in cash (the "Carrs Acquisition"). On the acquisition date, Carrs operated 49 stores. The Carrs Acquisition was accounted for as a purchase. Safeway funded the acquisition, and subsequent repayment of approximately \$239 million of Carrs' debt, with the issuance of commercial paper. Carrs' sales for its last full fiscal year prior to the acquisition were \$602 million.

Acquisition of Dominick's Supermarkets, Inc. ("Dominick's")

In November 1998, Safeway completed its acquisition of all of the outstanding shares of Dominick's for approximately \$1.2 billion in cash (the "Dominick's Acquisition"). The Dominick's Acquisition was accounted for as a purchase. Safeway funded the Dominick's Acquisition, including repayment of approximately \$560 million in debt and lease obligations, with a combination of bank borrowings and commercial paper.

Merger with The Vons Companies, Inc. ("Vons")

In April 1997, Safeway completed a merger with Vons pursuant to which the Company issued 83.2 million shares of Safeway common stock for all of the shares of Vons common stock that Safeway did not already own (the "Vons Merger"). The Vons Merger was accounted for as a purchase.

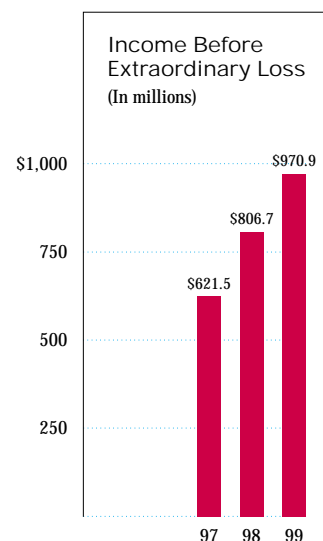
In connection with the Vons merger, Safeway repurchased 64.0 million shares of its common stock from a partnership affiliated with KKR & Co., L.L.C. at \$21.50 per share, for an aggregate purchase price of \$1.4 billion. Safeway funded the purchase through bank borrowings.

Results of Operations

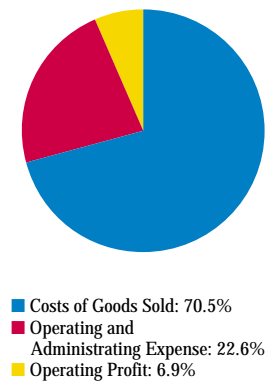
Safeway's net income was \$970.9 million (\$1.88 per share) in 1999, \$806.7 million (\$1.59 per share) in 1998 and \$557.4 million (\$1.12 per share) in 1997. In 1997, income before an extraordinary item related to debt refinancing was \$621.5 million (\$1.25 per share).

Safeway's recent acquisitions have affected its operating results. Safeway's 1999 income statement includes Dominick's and Vons' operating results for a full year, Carrs' operating results for 40 weeks and Randall's operating results for one quarter. Safeway's 1998 income statement includes Vons' operating results for the full year and Dominick's operating results for eight weeks. Safeway's 1997 income statement includes Vons' operating results since the second quarter plus the effect of Safeway's 34.4% equity interest in Vons in the first quarter of 1997. In order to facilitate an understanding of the Company's operations, this financial review presents certain pro forma information as if the Dominick's, Carrs and Randall's Acquisitions had been effective for the comparable period of 1998. See Note B to the Company's 1999 Consolidated Financial Statements.

During the second quarter of 1997, Safeway was engaged in a 75-day labor dispute affecting 74 stores in the Alberta, Canada operating area. The Company estimates that the strike reduced 1997 net income by approximately \$0.04 per share.



Portions of
1999 Sales Dollar



Sales Strong store operations helped to increase identical-store sales (stores operating the entire year in both 1999 and 1998, excluding replacement stores) 1.7% in 1999, while comparable-store sales, which include replacement stores, increased 2.2%. In 1998, identical-store sales increased 3.7% while comparable-store sales increased 4.1%. Total sales for the 52 weeks of 1999 were \$28.9 billion, compared to

\$24.5 billion for the 52 weeks of 1998 and \$22.5 billion for the 53 weeks of 1997. Total sales increases are attributed to comparable-store sales increases, the Vons Merger in 1997, the Dominick's Acquisition in 1998, and the Carrs and Randall's Acquisitions in 1999.

Gross Profit Safeway's continuing improvement in buying practices and product mix helped to increase gross profit to 29.49% of sales, from 29.10% in 1998 and 28.53% in 1997. On a pro forma basis, gross profit increased 51 basis points from 28.98% in 1998. Application of the LIFO method resulted in increases in cost of goods sold of \$1.2 million in 1999 and \$7.1 million in 1998, and a decrease of \$6.1 million in 1997.

Operating and Administrative Expense Operating and administrative expense, including amortization of goodwill, was 22.57% of sales in 1999 compared to 22.56% in 1998 and 22.84% in 1997. Safeway's operating and administrative expense-to-sales ratio increased in 1999 because Dominick's, Carrs and Randall's operating and administrative expense ratio had historically been higher than Safeway's. Increased sales and ongoing efforts to reduce or control expenses improved this expense ratio in 1998. Annual goodwill amortization has increased to \$101.4 million in 1999 from \$56.3 million in 1998 and \$41.8 million in 1997. On a pro forma basis, operating and administrative expense declined 30 basis points from 22.87% in 1998.

Interest Expense Interest expense was \$362.2 million in 1999, compared to \$235.0 million in 1998 and \$241.2 million in 1997. Interest expense increased in 1999 primarily because of the debt incurred to finance the Dominick's, Carrs and Randall's Acquisitions and, to a lesser extent, debt incurred to refinance the repurchase of Safeway stock. Interest expense in 1998 included debt incurred in connection with the Dominick's Acquisition, which was partially offset by the paydown of certain other indebtedness.

During 1997, Safeway recorded an extraordinary loss of \$64.1 million (\$0.13 per share) for the redemption of \$589.0 million of Safeway's public debt, \$285.5 million of Vons' public debt, and \$40.0 million of medium-term notes, which was financed with \$600 million of new public senior debt securities and the balance with commercial paper.

As of year-end 1999, the Company had effectively converted \$200.0 million of its floating rate debt to fixed interest rate debt through interest rate swaps agreements. Under one swap agreement, Safeway pays interest of 6.2% on the \$100.0 million notional amount and receives a variable interest rate based on Federal Reserve rates quoted for commercial paper. This agreement expires in 2007. Additionally, the Company assumed two interest rate swap agreements, with notional amounts of \$50.0 million each, as part of the Randall's Acquisition. Under these swap agreements, Safeway pays interest of 5.30% and 5.49%, respectively, on the \$50 million notional amounts and receives a variable rate based on Federal Reserve rates quoted for commercial paper. These swap agreements expire in 2001. Interest rate swap agreements, and a cap agreement that expired in 1999, increased interest expense by \$1.7 million in 1999, \$2.8 million in 1998 and \$3.3 million in 1997.

Equity in Earnings of Unconsolidated Affiliates

Safeway's investment in affiliates consists of a 49% ownership interest in Casa Ley, S.A. de C.V. ("Casa Ley"), which operates 86 food and general merchandise stores in western Mexico. Through the first quarter of 1997, Safeway also held a 34.4% interest in Vons. Safeway records its equity in earnings of unconsolidated affiliates on a one-quarter delay basis.

Income from Safeway's equity investment in Casa Ley increased to \$34.5 million in 1999, from \$28.5 million in 1998 and \$22.7 million in 1997. Casa Ley's financial results have been improving since 1995, when Mexico suffered from the adverse effects of high interest rates and inflation.

Equity in earnings of unconsolidated affiliates included Safeway's share of Vons earnings of \$12.2 million in the first quarter of 1997.

Liquidity and Financial Resources

Net cash flow from operations was \$1,488.4 million in 1999, \$1,252.7 million in 1998 and \$1,221.6 million in 1997. Net cash flow from operations increased in 1999 and 1998 largely due to increased net income.

Cash flow used by investing activities was \$2,064.3 million in 1999, \$2,186.4 million in 1998 and \$607.7 million in 1997. The change in cash flow used by investing activities in 1999 and 1998 is primarily due to the Randall's and Dominick's Acquisitions as well as increased capital expenditures. Safeway opened 67 new stores and remodeled 251 stores in 1999. In 1998, Safeway opened 46 new stores and remodeled 234 stores. The Company completed a new distribution center in Maryland and opened a new manufacturing plant in California during 1998.

Cash flow from financing activities was \$636.0 million in 1999 primarily due to borrowings related to the Randall's and Carrs Acquisitions. Cash flow from financing activities was \$903.4 million in 1998, reflecting borrowings related to the Dominick's Acquisition. Cash flow used by financing activities was \$614.6 million in 1997 primarily due to Safeway's reduction of total debt.

Net cash flow from operations as presented on the Statement of Cash Flows is an important measure of cash generated by the Company's operating activities. Operating cash flow, as defined below, is similar to net cash flow from operations because it excludes certain non-cash items. However, operating cash flow also excludes interest expense and income taxes. Management believes that operating cash flow is relevant because it assists investors in evaluating Safeway's ability to service its debt by providing a commonly used measure of cash available to pay interest. Operating cash flow also facilitates comparisons of Safeway's results of operations with companies having different capital structures. Other companies may define operating cash flow differently, and as a result, such measures may not be comparable to Safeway's operating cash flow. Safeway's computation of operating cash flow is as follows:

(Dollars in millions)	1999	1998	1997
Income before income taxes and extraordinary loss	\$1,674.0	\$ 1,396.9	\$1,076.3
LIFO expense (income)	1.2	7.1	(6.1)
Interest expense	362.2	235.0	241.2
Depreciation and amortization	695.6	531.4	455.8
Equity in earnings of unconsolidated affiliates	(34.5)	(28.5)	(34.9)
Operating cash flow	<u>\$2,698.5</u>	<u>\$ 2,141.9</u>	<u>\$1,732.3</u>
As a percent of sales	<u>9.35%</u>	<u>8.75%</u>	<u>7.70%</u>
As a multiple of interest expense	<u>7.45x</u>	<u>9.11x</u>	<u>7.18x</u>

Total debt, including capital leases, increased to \$6.96 billion at year-end 1999 from \$4.97 billion at year-end 1998 and \$3.34 billion at year-end 1997, primarily due to the Randall's, Carrs and Dominick's Acquisitions, the Vons Merger and the Safeway stock repurchase. Annual debt maturities over the next five years are set forth in Note C of the Company's 1999 consolidated financial statements.

Based upon the current level of operations, Safeway believes that operating cash flow and other sources of liquidity, including borrowings under Safeway's commercial paper program and bank credit agreement, will be adequate to meet anticipated requirements for working capital, capital expenditures, interest payments and scheduled principal payments for the foreseeable future. There can be no assurance, however, that the Company's business will continue to generate cash flow at or above current levels. The bank credit agreement is used primarily as a backup facility to the commercial paper program.

Year 2000

In 1997, the Company established a year 2000 project group to coordinate the Company's year 2000 compliance efforts. Before the end of calendar year 1999, the year 2000 project group determined what modifications or replacements to the computer-based systems and applications were necessary to achieve compliance; implemented the modifications; conducted the tests necessary to verify that the modified systems were operational; and transitioned the compliant systems into the Company's regular operations. The Company also examined its relationships with key outside vendors and others with whom the Company has significant business relationships to determine, to the extent practical, the degree of such parties' year 2000 compliance.

The Company spent approximately \$30 million, and Randall's spent \$2.6 million prior to the acquisition, to address year 2000 issues, which included costs of modifications, testing and consultants' fees. The cost of the year 2000 compliance efforts were funded from current operations and did not significantly impact the Company's operational decisions during the time the year 2000 issues were being addressed. The Company has not experienced any material adverse effects on its liquidity or results of operations relating to the year 2000 issues associated with its systems or those of key outside vendors or others with whom the Company has significant business relationships.

Forward-Looking Statements

This Annual Report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. Such statements relate to, among other things, capital expenditures, acquisitions, operating improvements, the effect of our share repurchase program on earnings per share and cost reductions and are indicated by words or phrases such as "continuing," "on-going," "expects," and similar words or phrases. The following factors are among the principal factors that could cause actual results to differ materially from the forward-looking statements: general business and economic conditions in our operating regions, including the rate of inflation, population, employment and job growth in our markets; pricing pressures and competitive factors, which could include pricing strategies, store openings and remodels; results of our programs to reduce costs; the ability to integrate any companies we acquire and achieve operating improvements at those companies; increases in labor costs and relations with union bargaining units representing our employees; opportunities or acquisitions that we pursue; and the availability and terms of financing. Consequently, actual events and results may vary significantly from those included in or contemplated or implied by such statements.

SAFEWAY INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

(In millions, except per-share amounts)	52 Weeks 1999	52 Weeks 1998	53 Weeks 1997
Sales	\$ 28,859.9	\$ 24,484.2	\$ 22,483.8
Cost of goods sold	(20,349.2)	(17,359.7)	(16,069.1)
Gross profit	8,510.7	7,124.5	6,414.7
Operating and administrative expense	(6,411.4)	(5,466.5)	(5,093.2)
Goodwill amortization	(101.4)	(56.3)	(41.8)
Operating profit	1,997.9	1,601.7	1,279.7
Interest expense	(362.2)	(235.0)	(241.2)
Equity in earnings of unconsolidated affiliates	34.5	28.5	34.9
Other income, net	3.8	1.7	2.9
Income before income taxes and extraordinary loss	1,674.0	1,396.9	1,076.3
Income taxes	(703.1)	(590.2)	(454.8)
Income before extraordinary loss	970.9	806.7	621.5
Extraordinary loss related to early retirement of debt, net of income tax benefit of \$41.1	-	-	(64.1)
Net income	\$ 970.9	\$ 806.7	\$ 557.4
Basic earnings per share:			
Income before extraordinary loss	\$ 1.95	\$ 1.67	\$ 1.35
Extraordinary loss	-	-	(0.14)
Net income	\$ 1.95	\$ 1.67	\$ 1.21
Diluted earnings per share:			
Income before extraordinary loss	\$ 1.88	\$ 1.59	\$ 1.25
Extraordinary loss	-	-	(0.13)
Net income	\$ 1.88	\$ 1.59	\$ 1.12
Weighted average shares outstanding – basic	498.6	482.8	462.3
Weighted average shares outstanding – diluted	515.4	508.8	497.7

See accompanying notes to consolidated financial statements.

SAFEWAY INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(In millions)	Year-end 1999	Year-end 1998
Assets		
Current assets:		
Cash and equivalents	\$ 106.2	\$ 45.7
Receivables	292.9	200.1
Merchandise inventories, net of LIFO reserve of \$81.5 and \$80.2	2,444.9	1,856.0
Prepaid expenses and other current assets	208.1	218.1
Total current assets	<u>3,052.1</u>	<u>2,319.9</u>
Property:		
Land	996.2	794.1
Buildings	2,502.3	2,069.9
Leasehold improvements	1,784.3	1,498.3
Fixtures and equipment	3,852.4	3,282.6
Property under capital leases	591.4	379.2
	<u>9,726.6</u>	<u>8,024.1</u>
Less accumulated depreciation and amortization	<u>(3,281.9)</u>	<u>(2,841.5)</u>
Total property, net	6,444.7	5,182.6
Goodwill, net of accumulated amortization of \$314.4 and \$211.0	4,786.6	3,348.0
Prepaid pension costs	405.6	369.6
Investment in unconsolidated affiliate	131.6	115.2
Other assets	79.7	54.3
Total assets	<u>\$14,900.3</u>	<u>\$11,389.6</u>

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)	52 Weeks 1999	52 Weeks 1998	53 Weeks 1997
Cash Flow from Operations:			
Net income	\$ 970.9	\$ 806.7	\$ 557.4
Reconciliation to net cash flow from operations:			
Extraordinary loss related to early retirement of debt, before income tax benefit	-	-	105.2
Depreciation and amortization	695.6	531.4	455.8
Amortization of deferred finance costs	4.8	1.6	1.7
Deferred income taxes	244.7	59.4	55.9
LIFO expense (income)	1.2	7.1	(6.1)
Equity in earnings of unconsolidated affiliates	(34.5)	(28.5)	(34.9)
Net pension income	(35.1)	(18.3)	(4.1)
Contributions to Canadian pension plan	(0.9)	(6.8)	(10.0)
Decrease in accrued claims and other liabilities	(8.4)	(17.5)	(13.9)
(Gain) loss on property retirements	(30.6)	13.3	(12.4)
Changes in working capital items:			
Receivables	(31.9)	(5.5)	25.8
Inventories at FIFO cost	(283.1)	(48.0)	37.5
Prepaid expenses and other current assets	23.0	(36.9)	2.7
Payables and accruals	(27.3)	(5.3)	61.0
Net cash flow from operations	<u>1,488.4</u>	<u>1,252.7</u>	<u>1,221.6</u>
Cash Flow from Investing Activities:			
Cash paid for property additions	(1,333.6)	(1,075.2)	(758.2)
Proceeds from sale of property	143.5	47.6	75.6
Net cash used to acquire Randall's	(729.8)	-	-
Net cash used to acquire Carrs	(94.4)	-	-
Net cash used to acquire Dominick's	-	(1,144.9)	-
Net cash acquired in merger with Vons	-	-	55.3
Other	(50.0)	(13.9)	19.6
Net cash flow used by investing activities	<u>(2,064.3)</u>	<u>(2,186.4)</u>	<u>(607.7)</u>

(In millions)	52 Weeks 1999	52 Weeks 1998	53 Weeks 1997
Cash Flow from Financing Activities:			
Additions to short-term borrowings	\$ 204.9	\$ 251.7	\$ 414.5
Payments on short-term borrowings	(237.0)	(299.9)	(287.5)
Additions to long-term borrowings	3,840.7	2,722.3	4,254.3
Payments on long-term borrowings	(2,520.0)	(1,789.9)	(3,553.5)
Purchase of treasury stock	(651.0)	-	(1,376.0)
Net proceeds from exercise of warrants and stock options	22.9	34.5	43.9
Premiums paid on early retirement of debt	-	-	(97.7)
Other	(24.5)	(15.3)	(12.6)
Net cash flow from (used by) financing activities	<u>636.0</u>	<u>903.4</u>	<u>(614.6)</u>
Effect of changes in exchange rates on cash	0.4	(1.2)	(1.8)
Increase (decrease) in cash and equivalents	<u>60.5</u>	<u>(31.5)</u>	<u>(2.5)</u>
Cash and Equivalents:			
Beginning of year	45.7	77.2	79.7
End of year	<u>\$ 106.2</u>	<u>\$ 45.7</u>	<u>\$ 77.2</u>
Other Cash Flow Information:			
Cash payments during the year for:			
Interest	\$ 351.4	\$ 241.0	\$ 263.6
Income taxes, net of refunds	378.2	468.7	214.6
Noncash Investing and Financing Activities:			
Stock issued for acquisition of Randall's Food Markets, Inc.	546.4	-	-
Stock issued for acquisition of The Vons Companies, Inc.	-	-	1,693.0
Tax benefit from stock options exercised	77.0	85.2	42.4
Capital lease obligations entered into	24.8	34.2	37.3
Mortgage notes assumed in property additions	9.7	32.8	0.9

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In millions)	Common Stock		Additional Paid-in Capital	Treasury Stock		Unexercised Warrants Purchased	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity	Comprehensive Income
	Shares	Amount		Shares	Cost					
Balance, year-end 1996	442.8	\$ 4.4	\$ 748.1			\$ (322.7)	\$ 745.0	\$ 12.0	\$ 1,186.8	\$ 452.3
Net income	-	-	-			-	557.4	-	557.4	\$ 557.4
Translation adjustments	-	-	-			-	-	(11.4)	(11.4)	(11.4)
Equity in Vons' pre-merger earnings due to timing of recording earnings	-	-	-			-	12.6	-	12.6	-
Shares issued for acquisition of Vons	83.2	0.8	1,692.2			-	-	-	1,693.0	-
Treasury stock purchased	-	-	-	(64.0)	\$(1,376.0)	-	-	-	(1,376.0)	-
Options and warrants exercised	11.4	0.1	26.8	2.8	59.4	-	-	-	86.3	-
Stock bonuses	-	-	0.3	-	-	-	-	-	0.3	-
Balance, year-end 1997	537.4	5.3	2,467.4	(61.2)	(1,316.6)	(322.7)	1,315.0	0.6	2,149.0	\$ 546.0
Net income	-	-	-	-	-	-	806.7	-	806.7	\$ 806.7
Translation adjustments	-	-	-	-	-	-	-	(20.3)	(20.3)	(20.3)
Dominick's options converted	-	-	27.0	-	-	-	-	-	27.0	-
Options and warrants exercised	13.5	0.2	105.5	0.6	14.0	-	-	-	119.7	-
Warrants canceled	-	-	-	-	-	196.7	(196.7)	-	-	-
Balance, year-end 1998	550.9	5.5	2,599.9	(60.6)	(1,302.6)	(126.0)	1,925.0	(19.7)	3,082.1	\$ 786.4
Net income	-	-	-	-	-	-	970.9	-	970.9	\$ 970.9
Translation adjustments	-	-	-	-	-	-	-	8.2	8.2	8.2
Shares issued for acquisition of Randall's	-	-	272.8	12.7	273.6	-	-	-	546.4	-
Randall's options converted	-	-	29.3	-	-	-	-	-	29.3	-
Treasury stock purchased	-	-	-	(17.9)	(651.0)	-	-	-	(651.0)	-
Options and warrants exercised	8.1	0.1	91.4	0.4	8.4	-	-	-	99.9	-
Balance, year-end 1999	559.0	\$ 5.6	\$ 2,993.4	(65.4)	\$(1,671.6)	\$ (126.0)	\$ 2,895.9	\$ (11.5)	\$ 4,085.8	\$ 979.1

See accompanying notes to consolidated financial statements.

Note A: The Company and Significant Accounting Policies

The Company Safeway Inc. (“Safeway” or the “Company”) is one of the largest food and drug chains in North America, with 1,659 stores as of year-end 1999. Safeway’s U.S. retail operating areas are located principally in northern California, southern California, Oregon, Washington, Alaska, Colorado, Arizona, Texas, the Chicago metropolitan area and the Mid-Atlantic region. The Company’s Canadian retail operations are located principally in British Columbia, Alberta and Manitoba/Saskatchewan. In support of its retail operations, the Company has an extensive network of distribution, manufacturing and food processing facilities.

As discussed in Note B, in September 1999 the Company acquired all of the outstanding shares of Randall’s Food Markets, Inc. (“Randall’s”) in exchange for \$1.3 billion consisting of \$754 million of cash and 12.7 million shares of Safeway stock (the “Randall’s Acquisition”). The acquisition was accounted for as a purchase and Randall’s operating results have been consolidated with Safeway’s since the beginning of the fourth quarter of 1999.

Also discussed in Note B, in April 1999 Safeway completed its acquisition of all of the outstanding shares of Carr-Gottstein Foods Co. (“Carrs”) for approximately \$106 million in cash (the “Carrs Acquisition”). The Carrs acquisition was accounted for as a purchase. Safeway’s 1999 income statement includes 40 weeks of Carrs’ operating results.

In November 1998 the Company acquired Dominick’s Supermarkets, Inc. (“Dominick’s”), by purchasing all of the outstanding shares of Dominick’s for a total of approximately \$1.2 billion in cash (the “Dominick’s Acquisition”). The Dominick’s Acquisition was accounted for as a purchase. Dominick’s operating results have been consolidated with Safeway’s since approximately midway through the fourth quarter of 1998.

In April 1997 Safeway completed a merger with The Vons Companies, Inc. (“Vons”) pursuant to which the Company issued 83.2 million shares of Safeway common stock for all of the shares of Vons common stock that it did not already own for an aggregate purchase price of

\$1.4 billion (the “Vons Merger”). The Vons Merger was accounted for as a purchase. Beginning in the second quarter of 1997, Safeway’s consolidated financial statements include Vons’ financial results.

In addition to these operations, the Company has a 49% ownership interest in Casa Ley, S.A. de C.V. (“Casa Ley”), which operates 86 food and general merchandise stores in western Mexico.

Basis of Consolidation The consolidated financial statements include Safeway Inc., a Delaware corporation, and all majority-owned subsidiaries. All significant inter-company transactions and balances have been eliminated in consolidation. The Company’s investment in Casa Ley is reported using the equity method. Prior to the Vons Merger in the second quarter of 1997, the Company’s investment in Vons was reported using the equity method.

Fiscal Year The Company’s fiscal year ends on the Saturday nearest December 31. The last three fiscal years consist of the 52-week period ending January 1, 2000, the 52-week period ended January 2, 1999 and the 53-week period ended January 3, 1998.

Revenue Recognition Revenue is recognized at the point of sale for retail sales. Vendor allowances and credits that relate to the Company’s buying and merchandising activities are recognized as earned.

Use of Estimates The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Translation of Foreign Currencies Assets and liabilities of the Company’s Canadian subsidiaries and Casa Ley are translated into U.S. dollars at year-end rates of exchange, and income and expenses are translated at average rates during the year. Adjustments resulting from translating financial statements into U.S. dollars are reported, net of applicable income taxes, as a separate

component of comprehensive income in the Statements of Stockholders' Equity.

Merchandise Inventories Merchandise inventory of \$1,823 million at year-end 1999 and \$1,326 million at year-end 1998 is valued at the lower of cost on a last-in, first-out ("LIFO") basis or market value. Such LIFO inventory had a replacement or current cost of \$1,905 million at year-end 1999 and \$1,406 million at year-end 1998. Liquidations of LIFO layers did not have a significant effect on the results of operations. All remaining inventory is valued at the lower of cost on a first-in, first-out ("FIFO") basis or market value. The FIFO cost of inventory approximates replacement or current cost.

Property and Depreciation Property is stated at cost. Depreciation expense on buildings and equipment is computed on the straight-line method using the following lives:

Stores and other buildings	7 to 40 years
Fixtures and equipment	3 to 15 years

Property under capital leases and leasehold improvements are amortized on a straight-line basis over the shorter of the remaining terms of the lease or the estimated useful lives of the assets.

Self-Insurance The Company is primarily self-insured for workers' compensation, automobile, and general liability costs. The self-insurance liability is determined actuarially, based on claims filed and an estimate of claims incurred but not yet reported. The present value of such claims was accrued using a discount rate of 6.0% in 1999 and 5.5% in 1998. The current portion of the self-insurance liability of \$103.2 million at year-end 1999 and \$107.3 million at year-end 1998 is included in Other Accrued Liabilities in the consolidated balance sheets. The long-term portion of \$243.2 million at year-end 1999 and \$265.5 million at year-end 1998 is included in Accrued Claims and Other Liabilities. Claims payments were \$123.6 million in 1999, \$98.2 million in 1998 and \$100.0 million in 1997. The total undiscounted liability was \$391.9 million at year-end 1999 and \$413.1 million at year-end 1998.

Income Taxes The Company provides a deferred tax expense or benefit equal to the change in the deferred tax liability during the year in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes." Deferred income taxes represent tax credit carryforwards and future net tax effects resulting from temporary differences between the financial statement and tax basis of assets and liabilities using

enacted tax rates in effect for the year in which the differences are expected to reverse.

Statement of Cash Flows Short-term investments with original maturities of less than three months are considered to be cash equivalents.

Off-Balance Sheet Financial Instruments As discussed in Note E, the Company has entered into interest rate swap agreements to limit the exposure of certain of its floating interest rate debt to changes in market interest rates. Interest rate swap agreements involve the exchange with a counterparty of fixed and floating rate interest payments periodically over the life of the agreements without exchange of the underlying notional principal amounts. The differential to be paid or received is recognized over the life of the agreements as an adjustment to interest expense.

The Company's counterparties are major financial institutions.

Fair Value of Financial Instruments Generally accepted accounting principles require the disclosure of the fair value of certain financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate fair value. Safeway estimated the fair values presented below using appropriate valuation methodologies and market information available as of year-end. Considerable judgment is required to develop estimates of fair value, and the estimates presented are not necessarily indicative of the amounts that the Company could realize in a current market exchange. The use of different market assumptions or estimation methodologies could have a material effect on the estimated fair values. Additionally, these fair values were estimated at year-end, and current estimates of fair value may differ significantly from the amounts presented.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and equivalents, accounts receivable, accounts payable and short-term debt The carrying amount of these items approximates fair value.

Long-term debt Market values quoted on the New York Stock Exchange are used to estimate the fair value of publicly traded debt. To estimate the fair value of debt issues that are not quoted on an exchange, the Company uses those interest rates that are currently available to it for issuance of debt with similar terms and remaining maturities. At year-end 1999 and 1998, the estimated fair value of debt approximated carrying value.

Off-balance sheet instruments The fair value of interest rate swaps are the amount at which they could be settled based on estimates obtained from dealers. At year-end 1999, net unrealized gains on such agreements were \$4.7 million compared to an unrealized loss of \$7.0 million at year-end 1998. Since the Company intends to hold these agreements as hedges for the term of the agreements, the market risk associated with changes in interest rates should not be significant.

Impairment of Long-Lived Assets When Safeway decides to close a store or other facility, the Company accrues estimated future losses, if any, which may include lease payments or other costs of holding the facility, net of estimated future income in accordance with the provisions of SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of." The operating costs, including depreciation, of stores or other facilities to be sold or closed are expensed during the period they remain in use. Safeway had an accrued liability of \$87.3 million at year-end 1999 and \$84.6 million at year-end 1998 for such estimated future losses, which is included in Accrued Claims and Other Liabilities in the Company's consolidated balance sheets.

Goodwill Goodwill is \$4.8 billion at year-end 1999 and \$3.3 billion at year-end 1998, and is being amortized on a straight-line basis over its estimated useful life of 40 years. If it became probable that the projected future undiscounted cash flows of acquired assets were less than the carrying value of the goodwill, Safeway would recognize an impairment loss in accordance with the provisions of SFAS No. 121.

Goodwill amortization was \$101.4 million in 1999, \$56.3 million in 1998 and \$41.8 million in 1997. Goodwill and related amortization have increased due to the acquisitions of Randall's, Dominick's and Carrs and the Vons Merger discussed in Note B.

Stock-Based Compensation Safeway accounts for stock-based awards to employees using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." The disclosure requirements of SFAS No. 123, "Accounting for Stock-Based Compensation," are set forth in Note F.

New Accounting Standards In June 1998 the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," which was amended by SFAS 137, which defines derivatives, requires that derivatives be carried at

fair value, and provides for hedge accounting when certain conditions are met. This statement is effective for Safeway beginning in the first quarter of 2001. Although the Company has not fully assessed the implications of this new statement, the Company believes adoption of this statement will not have a material impact on its financial statements.

During the first quarter of 1999, the Company adopted SOP 98-5, "Reporting on the Costs of Start-Up Activities," which requires that costs incurred for start-up activities, such as store openings, be expensed as incurred. This SOP did not have a material impact on Safeway's financial statements.

Note B: Acquisitions

In September 1999, Safeway acquired all of the outstanding shares of Randall's in exchange for \$1.3 billion consisting of \$754 million of cash and 12.7 million shares of Safeway stock. The Randall's Acquisition was accounted for as a purchase and resulted in goodwill of approximately \$1.3 billion which will be amortized over 40 years. Safeway used proceeds from the issuance of subordinated debt to fund the cash portion of the acquisition.

In April 1999, Safeway acquired Carrs by purchasing all of the outstanding shares of Carrs for approximately \$106 million in cash. The Carrs Acquisition was accounted for as a purchase and resulted in goodwill of approximately \$213 million which will be amortized over 40 years. Safeway funded the acquisition, and subsequent repayment of approximately \$239 million of Carrs' debt, with issuance of commercial paper.

In November 1998 Safeway completed its acquisition of all of the outstanding shares of Dominick's for a total of approximately \$1.2 billion in cash. The Dominick's Acquisition was accounted for as a purchase and resulted in additional goodwill of \$1.6 billion which is being amortized over 40 years. Safeway funded the Dominick's Acquisition, including the repayment of approximately \$560 million of debt and lease obligations, with a combination of bank borrowings and commercial paper.

The following unaudited pro forma combined summary financial information is based on the historical consolidated results of operations of Safeway, Dominick's, Carrs and Randall's as if the Dominick's, Carrs and Randall's Acquisitions had occurred as of the beginning of each year presented. This pro forma financial information is presented for informational purposes only and may not be indicative of what the actual consolidated results of operations would have been if the acquisitions had been effective as of the beginning of the years presented. Pro forma adjustments were applied to the respective historical financial statements to account for the Dominick's, Carrs and Randall's

Acquisitions as purchases. Under purchase accounting, the purchase price is allocated to acquired assets and liabilities based on their estimated fair values at the date of acquisition, and any excess is allocated to goodwill.

For Randall's and Carrs, such allocations are subject to final determination based on real estate, leasehold and equipment valuation studies, and a review of the books, records and accounting policies of Randall's and Carrs, which are expected to be complete before the end of the third quarter and first quarter of fiscal 2000, respectively. Accordingly, the final allocations may be different from the amount reflected herein, although management does not expect such differences to be material.

(in millions, except per-share amounts)	Pro Forma	
	1999	1998
Sales	\$30,801.8	\$29,474.1
Net income	\$ 957.6	\$ 706.2
Diluted earnings per share:		
Net income	\$ 1.82	\$ 1.42

Note C: Financing

Notes and debentures were composed of the following at year-end (in millions):

	1999	1998
Commercial paper	\$2,358.1	\$1,745.0
Bank credit agreement, unsecured	75.7	89.1
9.30% Senior Secured		
Debentures due 2007	24.3	24.3
6.85% Senior Notes due 2004, unsecured	200.0	200.0
7.00% Senior Notes due 2007, unsecured	250.0	250.0
7.45% Senior Debentures		
due 2027, unsecured	150.0	150.0
5.75% Senior Notes due 2000, unsecured	400.0	400.0
5.875% Senior Notes due 2001, unsecured	400.0	400.0
6.05% Senior Notes due 2003, unsecured	350.0	350.0
6.50% Senior Notes due 2008, unsecured	250.0	250.0
7.00% Senior Notes due 2002, unsecured	600.0	-
7.25% Senior Notes due 2004, unsecured	400.0	-
7.50% Senior Notes due 2009, unsecured	500.0	-
9.35% Senior Subordinated Notes		
due 1999, unsecured	-	66.7
10% Senior Subordinated Notes		
due 2001, unsecured	79.9	79.9
9.65% Senior Subordinated Debentures		
due 2004, unsecured	81.2	81.2
9.875% Senior Subordinated Debentures		
due 2007, unsecured	24.2	24.2
10% Senior Notes due 2002, unsecured	6.1	6.1
Mortgage notes payable, secured	75.6	115.9
Other notes payable, unsecured	98.8	102.7
Medium-term notes, unsecured	25.5	25.5
Short-term bank borrowings, unsecured	129.7	161.8
	6,479.1	4,522.4
Less current maturities	(557.1)	(279.8)
Long-term portion	\$5,922.0	\$4,242.6

Commercial Paper The amount of commercial paper borrowings is limited to the unused borrowing capacity under the bank credit agreement. Commercial paper is classified as long-term because the Company intends to and has the ability to refinance these borrowings on a long-term basis through either continued commercial paper borrowings or utilization of the bank credit agreement, which matures in 2002. The weighted average interest rate on commercial paper borrowings was 5.37% during 1999 and 6.79% at year-end 1999.

Bank Credit Agreement Safeway's total borrowing capacity under the bank credit agreement is \$3.0 billion. Of the \$3.0 billion credit line, \$2.0 billion matures in 2002 and has two one-year extension options, and \$1.0 billion is renewable annually through 2004. The restrictive covenants of the bank credit agreement limit Safeway with respect to, among other things, creating liens upon its assets and disposing of material amounts of assets other than in the ordinary course of business. Safeway is also required to meet certain financial tests under the bank credit agreement. At year-end 1999, the Company had total unused borrowing capacity under the bank credit agreement of \$520 million.

U.S. borrowings under the bank credit agreement carry interest at one of the following rates selected by the Company: (i) the prime rate; (ii) a rate based on rates at which Eurodollar deposits are offered to first-class banks by the lenders in the bank credit agreement plus a pricing margin based on the Company's debt rating or interest coverage ratio (the "Pricing Margin"); or (iii) rates quoted at the discretion of the lenders. Canadian borrowings denominated in U.S. dollars carry interest at one of the following rates selected by the Company: (a) the Canadian base rate or (b) the Canadian Eurodollar rate plus the Pricing Margin. Canadian borrowings denominated in Canadian dollars carry interest at one of the following rates selected by the Company: (i) the Canadian prime rate or (ii) the rate for Canadian bankers acceptances plus the Pricing Margin.

The weighted average interest rate on borrowings under the bank credit agreement was 5.59% during 1999 and 5.18% at year-end 1999.

Senior Secured Indebtedness The 9.30% Senior Secured Debentures due 2007 are secured by a deed of trust which created a lien on the land, buildings and equipment owned by Safeway at its distribution center in Tracy, California.

Senior Unsecured Indebtedness In September 1999, Safeway issued senior unsecured debt facilities consisting of 7.00% Notes due 2002, 7.25% Notes due 2004, and 7.5% Notes due 2009.

In 1998 Safeway issued senior unsecured debt securities consisting of 5.75% Notes due 2000, 5.875% Notes due 2001, 6.05% Notes due 2003, and 6.5% Notes due 2008.

In 1997 Safeway issued senior unsecured debt securities consisting of 6.85% Senior Notes due 2004, 7.00% Senior Notes due 2007, and 7.45% Senior Debentures due 2027. The Company used the proceeds from this debt to redeem a portion of the Senior Subordinated Indebtedness, described below.

Senior Subordinated Indebtedness The 10% Senior Subordinated Notes due 2001, 9.65% Senior Subordinated Debentures due 2004, and 9.875% Senior Subordinated Debentures due 2007 are subordinated in right of payment to, among other things, the Company's borrowings under the bank credit agreement, the 9.30% Senior Secured Debentures, the Senior Unsecured Indebtedness, and mortgage notes payable.

Mortgage Notes Payable Mortgage notes payable at year-end 1999 have remaining terms ranging from one to 19 years, have a weighted average interest rate of 8.64% and are secured by properties with a net book value of approximately \$298 million.

Other Notes Payable Other notes payable at year-end 1999 have remaining terms ranging from one to 10 years and a weighted average interest rate of 7.28%.

Redemptions During 1997, the Company redeemed \$588.5 million of the Senior Subordinated Indebtedness, \$285.5 million of Vons' public debt, and \$40.0 million of medium-term notes using proceeds from the Senior Unsecured Indebtedness and commercial paper program. In connection with this redemption, Safeway recorded an extraordinary loss of \$64.1 million (\$0.13 per share). The extraordinary loss represents the payment of redemption premiums and the write-off of deferred finance costs, net of the related tax benefits.

Annual Debt Maturities As of year-end 1999, annual debt maturities were as follows (in millions):

2000	\$ 557.1
2001	548.6
2002	3,071.0
2003	377.2
2004	700.0
Thereafter	1,225.2
	<u>\$6,479.1</u>

Letters of Credit The Company had letters of credit of \$89.3 million outstanding at year-end 1999 of which \$46.3 million were issued under the bank credit agreement. The letters of credit are maintained primarily to support performance, payment, deposit, or surety obligations of the Company. The Company pays commitment fees ranging from 0.15% to 1.00% on the outstanding portion of the letters of credit.

Note D: Lease Obligations

Approximately two-thirds of the premises that the Company occupies are leased. The Company had approximately 1,600 leases at year-end 1999, including approximately 220 which are capitalized for financial reporting purposes. Most leases have renewal options, some with terms and conditions similar to the original lease, others with reduced rental rates during the option periods. Certain of these leases contain options to purchase the property at amounts that approximate fair market value.

As of year-end 1999, future minimum rental payments applicable to non-cancelable capital and operating leases with remaining terms in excess of one year were as follows (in millions):

	Capital Leases	Operating Leases
2000	\$ 91.0	\$ 325.8
2001	97.9	302.7
2002	77.0	306.2
2003	72.6	289.1
2004	77.9	264.4
Thereafter	460.9	2,482.5
Total minimum lease payments	877.3	<u>\$3,970.7</u>
Less amounts representing interest	(400.1)	
Present value of net minimum lease payments	477.2	
Less current obligations	(41.8)	
Long-term obligations	<u>\$435.4</u>	

Future minimum lease payments under non-cancelable capital and operating lease agreements have not been reduced by minimum sublease rental income of \$241.8 million.

Amortization expense for property under capital leases was \$38.5 million in 1999, \$22.3 million in 1998 and \$21.1 million in 1997. Accumulated amortization of property under capital leases was \$132.3 million at year-end 1999 and \$136.1 million at year-end 1998.

The following schedule shows the composition of total rental expense for all operating leases (in millions). In general, contingent rentals are based on individual store sales.

	1999	1998	1997
Property leases:			
Minimum rentals	\$280.3	\$208.7	\$206.0
Contingent rentals	18.6	19.2	12.3
Less rentals from subleases	(13.2)	(12.0)	(13.4)
	<u>285.7</u>	<u>215.9</u>	<u>204.9</u>
Equipment leases	42.9	22.4	19.3
	<u>\$328.6</u>	<u>\$238.3</u>	<u>\$224.2</u>

Note E: Interest Expense

Interest expense consisted of the following (in millions):

	1999	1998	1997
Bank credit agreement	\$ 19.4	\$ 10.8	\$ 36.9
Commercial paper	87.4	83.7	43.8
9.30% Senior Secured Debentures	2.3	2.3	5.3
6.85% Senior Notes	13.7	13.7	4.1
7.00% Senior Notes	17.5	17.5	5.2
7.45% Senior Debentures	11.2	11.2	3.4
5.75% Senior Notes	23.0	3.5	-
5.875% Senior Notes	23.5	3.6	-
6.05% Senior Notes	21.2	3.2	-
6.50% Senior Notes	16.3	2.5	-
7.00% Senior Notes	12.8	-	-
7.25% Senior Notes	8.8	-	-
7.5% Senior Notes	11.4	-	-
9.35% Senior Subordinated Notes	1.3	6.2	12.3
10% Senior Subordinated Notes	8.0	8.0	19.3
9.65% Senior Subordinated Debentures	7.8	7.8	17.8
9.875% Senior Subordinated Debentures	2.4	2.4	8.2
10% Senior Notes	0.6	0.6	4.3
Vons Debentures	-	-	10.2
Mortgage notes payable	7.3	12.1	22.0
Other notes payable	16.0	9.5	9.9
Medium-term notes	2.1	2.1	4.4
Short-term bank borrowings	4.9	10.6	8.8
Obligations under capital leases	46.1	27.8	26.0
Amortization of deferred finance costs	4.8	1.6	1.7
Interest rate swap and cap agreements	1.7	2.8	3.3
Capitalized interest	(9.3)	(8.5)	(5.7)
	<u>\$362.2</u>	<u>\$235.0</u>	<u>\$241.2</u>

As of year-end 1999, the Company had effectively converted \$200.0 million of its floating rate debt to fixed interest rate debt through interest rate swap agreements. Under one swap agreement, Safeway pays interest of 6.2% on the \$100.0 million notional amount and receives a variable interest rate based on Federal Reserve rates quoted for commercial paper. This agreement expires in 2007.

Additionally, the Company assumed two interest rate swap agreements, with notional amounts of \$50.0 million each, as part of the Randall's Acquisition. Under these swap agreements, Safeway pays interest of 5.30% and 5.49%, respectively, on the \$50 million notional amounts and receives a variable rate based on Federal Reserve rates quoted for commercial paper. These swap agreements expire in 2001. Interest rate swap agreements, and a cap agreement that expired in 1999, increased interest expense by \$1.7 million in 1999, \$2.8 million in 1998 and \$3.3 million in 1997. At year-end 1999, the net unrealized gain on interest rate swap agreements was \$4.7 million compared to an unrealized loss of \$7.0 million at year-end 1998.

The Company is not subject to credit risk because the notional amounts do not represent cash flows. The Company is subject to risk from nonperformance of the counterparties to the swap agreements in the amount of any interest differential to be received. Because the Company monitors the credit ratings of its counterparties, which are limited to major financial institutions, Safeway does not anticipate nonperformance by the counterparties.

Because the Company intends to hold these agreements as hedges for the term of the agreements, the market risk associated with changes in interest rates should not be significant.

Note F: Capital Stock

Shares Authorized and Issued Authorized preferred stock consists of 25 million shares of which none was outstanding during 1999, 1998 or 1997. Authorized common stock consists of 1.5 billion shares at \$0.01 par value. Common stock outstanding at year-end 1999 was 493.6 million shares (net of 65.4 million shares of treasury stock) and 490.3 million shares at year-end 1998 (net of 60.6 million shares of treasury stock).

Stock Option Plans Under Safeway's stock option plans, the Company may grant incentive and non-qualified options to purchase common stock at an exercise price equal to or greater than the fair market value at the grant date, as determined by the Compensation and Stock Option Committee of the Board of Directors. Options generally vest over seven years. Vested options are exercisable in part or in full at any time prior to the expiration date of 10 to 15 years from the date of the grant. Options to purchase 16.9 million shares were available for grant at year-end 1999.

Activity in the Company's stock option plans for the three-year period ended January 1, 2000 was as follows:

	Options	Weighted Average Exercise Price
Outstanding, year-end 1996	38,773,156	\$ 5.07
1997 Activity:		
Granted	3,981,766	26.25
Converted Vons options	7,578,098	7.34
Canceled	(962,522)	10.01
Exercised	<u>(8,373,270)</u>	5.06
Outstanding, year-end 1997	40,997,228	7.53
1998 Activity:		
Granted	4,987,038	40.28
Converted Dominick's options	922,701	19.70
Canceled	(848,482)	14.61
Exercised	<u>(6,680,083)</u>	3.90
Outstanding, year-end 1998	39,378,402	12.15
1999 Activity:		
Granted	6,455,276	43.17
Converted Randall's options	1,069,432	15.54
Canceled	(1,325,892)	37.81
Exercised	<u>(5,070,905)</u>	4.95
Outstanding, year-end 1999	<u>40,506,313</u>	17.44
Exercisable, year-end 1997	<u>25,887,094</u>	4.75
Exercisable, year-end 1998	<u>24,447,905</u>	5.79
Exercisable, year-end 1999	<u>23,775,488</u>	7.84
Weighted average fair value of options granted during the year:		
1997	\$ 12.43	
1998	17.06	
1999	20.83	

The following table summarizes stock option information at year-end 1999:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number of Options	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number of Options	Weighted-Average Exercise Price
\$ 1.57 to \$ 3.22	7,701,712	6.95 years	\$ 2.91	7,661,712	\$ 2.91
3.25 to 6.28	7,122,251	6.46	4.55	6,637,323	4.53
6.31 to 9.44	7,017,977	4.51	7.18	4,988,185	7.14
9.67 to 26.41	7,145,707	7.34	18.28	3,364,247	17.17
26.72 to 41.25	7,266,509	8.67	35.43	998,500	34.75
42.06 to 60.94	4,252,157	9.26	50.09	125,521	46.74
1.57 to 60.94	<u>40,506,313</u>	7.06	17.44	<u>23,775,488</u>	7.84

Additional Stock Plan Information The Company accounts for its stock-based awards using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and its related interpretations. Accordingly, no compensation expense has been recognized in the financial statements for employee stock option awards granted at fair market value.

SFAS No. 123, "Accounting for Stock-Based Compensation," requires the disclosure of pro forma net income and earnings per share as if the Company had adopted the fair value method as of the beginning of fiscal 1995. Under SFAS 123, the fair value of stock-based awards to employees is calculated through the use of option pricing models, even though such models were developed to estimate the fair value of freely tradable, fully transferable options without vesting restrictions, which significantly

differ from the Company's stock option awards. These models also require subjective assumptions, including future stock price volatility and expected time to exercise, which greatly affect the calculated values. The Company's calculations were made using the Black-Scholes option pricing model with the following weighted average assumptions: seven to nine years expected life; stock volatility of 31% in 1999, 1998 and 1997; risk-free interest rates of 5.79% in 1999, 5.26% in 1998 and 6.29% in 1997; and no dividends during the expected term.

The Company's calculations are based on a single option valuation approach and forfeitures are recognized as they occur. However, the impact of outstanding non-vested stock options granted prior to 1995 has been excluded from the pro forma calculation; accordingly, the pro forma results presented below are not indicative of future period pro forma results. Had compensation cost for Safeway's stock option plans been determined based on the fair value at the grant date for awards in 1999, 1998 and 1997, consistent with the provisions of SFAS No. 123, the Company's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

	1999	1998	1997
Net income (in millions):			
As reported	\$970.9	\$806.7	\$557.4
Pro forma	951.5	794.8	553.5
Basic earnings per share:			
As reported	\$ 1.95	\$ 1.67	\$ 1.21
Pro forma	1.91	1.65	1.20
Diluted earnings per share:			
As reported	\$ 1.88	\$ 1.59	\$ 1.12
Pro forma	1.85	1.56	1.11

Note G: Taxes on Income

The components of income tax expense are as follows (in millions):

	1999	1998	1997
Current:			
Federal	\$333.7	\$398.8	\$303.6
State	62.3	80.0	57.5
Foreign	62.4	52.0	37.8
	<u>458.4</u>	<u>530.8</u>	<u>398.9</u>
Deferred:			
Federal	188.9	44.4	40.4
State	38.1	12.2	8.4
Foreign	17.7	2.8	7.1
	<u>244.7</u>	<u>59.4</u>	<u>55.9</u>
	<u>\$703.1</u>	<u>\$590.2</u>	<u>\$454.8</u>

Extraordinary losses are presented net of related tax benefits. Therefore, 1997 income tax expense excludes the \$41.1 million tax benefit on an extraordinary loss related

to the early retirement of debt. Tax benefits from the exercise of employee stock options of \$77.0 million in 1999, \$85.2 million in 1998 and \$42.4 million in 1997 were credited directly to paid-in capital and, therefore, are excluded from income tax expense.

The reconciliation of the provision for income taxes at the U.S. federal statutory income tax rate to the Company's income taxes is as follows (dollars in millions):

	1999	1998	1997
Statutory rate	35%	35%	35%
Income tax expense using federal statutory rate	\$585.9	\$488.9	\$376.7
State taxes on income net of federal benefit	65.2	59.9	42.8
Taxes provided on equity in earnings of unconsolidated affiliates at rates below the statutory rate	(12.1)	(10.0)	(9.4)
Taxes on foreign earnings not permanently reinvested	8.3	7.9	8.9
Nondeductible expenses and amortization	32.9	17.6	13.6
Difference between statutory rate and foreign effective rate	16.6	11.1	10.6
Other accruals	6.3	14.8	11.6
	<u>\$703.1</u>	<u>\$590.2</u>	<u>\$454.8</u>

Significant components of the Company's net deferred tax liability at year-end were as follows (in millions):

	1999	1998	1997
Deferred tax assets:			
Workers' compensation and other claims	\$ 144.7	\$ 158.5	\$ 138.8
Accruals not currently deductible	111.3	106.6	80.3
Accrued claims and other liabilities	28.9	48.0	48.8
Employee benefits	46.1	34.7	18.4
U.S. operating loss carryforward	-	12.1	-
Other assets	42.7	51.5	14.6
	<u>\$ 373.7</u>	<u>\$ 411.4</u>	<u>\$ 300.9</u>
Deferred tax liabilities:			
Property	\$ (387.8)	\$ (315.7)	\$ (280.8)
Prepaid pension costs	(165.4)	(166.4)	(161.3)
LIFO inventory reserves	(171.3)	(125.7)	(106.0)
Investments in unconsolidated affiliates	(5.8)	(16.7)	(15.3)
Cumulative translation adjustments	(4.9)	(3.8)	(16.2)
Other liabilities	(17.6)	-	(18.3)
	<u>(752.8)</u>	<u>(628.3)</u>	<u>(597.9)</u>
Net deferred tax liability	<u>\$ (379.1)</u>	<u>\$ (216.9)</u>	<u>\$ (297.0)</u>

Note H: Employee Benefit Plans and Collective Bargaining Agreements

Retirement Plans The Company maintains defined benefit, non-contributory retirement plans for substantially all of its employees not participating in multi-employer pension plans.

In connection with the Randall's Acquisition and the Vons Merger, the Company assumed the obligations of Randall's and Vons' retirement plans. The actuarial assumptions for the existing Randall's and Vons retirement plans are comparable to the existing plans of the Company. Randall's and Vons' retirement plans have been combined with Safeway's for financial statement presentation.

The following tables provide a reconciliation of the changes in the retirement plans' benefit obligation and fair value of assets over the two-year period ending January 1, 2000 and a statement of the funded status as of year-end 1999 and 1998 (in millions):

	1999	1998
Change in benefit obligation:		
Beginning balance	\$1,165.7	\$1,056.8
Service cost	54.4	52.5
Interest cost	81.6	69.7
Plan amendments	17.5	18.2
Actuarial (gain) loss	(129.4)	65.1
Acquisition of Randall's	28.1	-
Benefit payments	(87.3)	(79.8)
Change in assumption	(23.4)	(0.5)
Currency translation adjustment	12.5	(16.3)
Ending balance	<u>\$1,119.7</u>	<u>\$1,165.7</u>

	1999	1998
Change in fair value of plan assets:		
Beginning balance	\$1,766.1	\$1,662.6
Actual return on plan assets	432.4	193.2
Acquisition of Randall's	27.6	-
Employer contributions	0.9	6.8
Benefit payments	(87.3)	(79.8)
Currency translation adjustment	13.7	(16.7)
Ending balance	<u>\$2,153.4</u>	<u>\$1,766.1</u>

	1999	1998
Funded status:		
Fair value of plan assets	\$ 2,153.4	\$ 1,766.1
Projected benefit obligation	(1,119.7)	(1,165.7)
Funded status	1,033.7	600.4
Adjustment for difference in book and tax basis of assets	(165.1)	(165.1)
Unamortized prior service cost	97.2	95.5
Unrecognized gain	(560.2)	(161.2)
Prepaid pension cost	<u>\$ 405.6</u>	<u>\$ 369.6</u>

The following table provides the components of 1999, 1998 and 1997 net pension income for the retirement plans (in millions):

	1999	1998	1997
Estimated return on assets	\$162.7	\$141.5	\$118.3
Service cost	(54.4)	(52.5)	(42.5)
Interest cost	(81.6)	(69.7)	(60.1)
Amortization of prior service cost	(15.4)	(14.3)	(11.6)
Amortization of unrecognized gains	23.8	13.3	-
Net pension income	<u>\$ 35.1</u>	<u>\$ 18.3</u>	<u>\$ 4.1</u>

Prior service costs are amortized on a straight-line basis over the average remaining service period of active participants. Actuarial gains and losses are amortized over the average remaining service life of active participants when the accumulation of such gains and losses exceeds 10% of the greater of the projected benefit obligation and the fair value of plan assets.

The actuarial assumptions used to determine year-end plan status were as follows:

	1999	1998	1997
Discount rate used to determine the projected benefit obligation:			
United States Plans	7.8%	6.5%	7.0%
Canadian Plan	7.5	6.3	6.3
Combined weighted average rate	7.7	6.5	6.8
Expected return on plan assets:			
United States Plan	9.0%	9.0%	9.0%
Canadian Plans	8.0	8.0	8.0
Rate of compensation increase:			
United States Plan	5.0%	5.0%	5.0%
Canadian Plans	5.0	4.5	4.5

Retirement Restoration Plan The Retirement Restoration Plan provides death benefits and supplemental income payments for senior executives after retirement. The Company recognized expense of \$5.4 million in 1999, \$5.0 million in 1998 and \$4.3 million in 1997. The aggregate projected benefit obligation of the Retirement Restoration Plan was approximately \$48.4 million at year-end 1999 and \$53.8 million at year-end 1998.

Multi-Employer Pension Plans Safeway participates in various multi-employer pension plans, covering virtually all Company employees not covered under the Company's non-contributory pension plans, pursuant to agreements between the Company and employee bargaining units which are members of such plans. These plans are generally defined benefit plans; however, in many cases, specific benefit levels are not negotiated with or known by the employer-contributors. Contributions of \$144 million in 1999, \$119 million in 1998 and \$130 million in 1997 were made and charged to expense.

Under U.S. legislation regarding such pension plans, a company is required to continue funding its proportionate share of a plan's unfunded vested benefits in the event of withdrawal (as defined by the legislation) from a plan or plan termination. Safeway participates in a number of these pension plans, and the potential obligation as a participant in these plans may be significant. The information required to determine the total amount of this contingent obligation, as well as the total amount of accumulated benefits and net assets of such plans, is not readily available. During 1988 and 1987, the Company sold certain operations. In most cases, the party acquiring the operation agreed to continue making contributions to the plans. Safeway is relieved of the obligations related to these sold operations to the extent the acquiring parties continue to make contributions. Whether such sales could result in withdrawal under ERISA and, if so, whether such withdrawals could result in liability to the Company, is not determinable at this time.

Collective Bargaining Agreements At year-end 1999, Safeway had more than 193,000 full and part-time employees. Approximately 90% of Safeway's employees in the United States and Canada are covered by collective bargaining agreements negotiated with local unions affiliated with one of 12 different international unions. There are approximately 400 such agreements, typically having three-year terms, with some agreements having terms up to five years. Accordingly, Safeway negotiates a significant number of these agreements every year.

Note I: Investment in Unconsolidated Affiliates
At year-end 1999, Safeway's investment in unconsolidated affiliate consists of a 49% ownership interest in Casa Ley, which operates 86 food and general merchandise stores in western Mexico. Income from Safeway's equity investment in Casa Ley, recorded on a one-quarter delay basis, was \$34.5 million in 1999, \$28.5 million in 1998 and \$22.7 million in 1997.

Through April 8, 1997, Safeway also owned 15.1 million common shares, or 34.4% of the total shares outstanding of Vons. Vons is now a wholly-owned subsidiary of Safeway, and as of the beginning of the second quarter of 1997, Safeway's consolidated financial statements include Vons' financial position and results of operations. Safeway's share of Vons' earnings was \$12.2 million for the first quarter of 1997.

Note J: Related-Party Transactions
The Company holds an 80% interest in Property Development Associates ("PDA"), a partnership formed in 1987 with a company controlled by an affiliate of KKR, to purchase, manage and dispose of certain Safeway facilities which are no longer used in the retail grocery business. The financial statements of PDA are consolidated with those of the Company, and a minority interest of \$19.9 million and \$23.9 million at year-end 1999 and 1998, respectively, is included in accrued claims and other liabilities in the accompanying consolidated balance sheets. Safeway paid PDA \$2.7 million in 1999, \$1.9 million in 1998 and \$1.5 million in 1997 for reimbursement of expenses related to management and real estate services provided by PDA.

Note K: Commitments and Contingencies

Legal Matters In July 1988, there was a major fire at the Company's dry grocery warehouse in Richmond, California. Through February 10, 2000, in excess of 126,000 claims for personal injury and property damage arising from the fire have been settled for an aggregate amount of approximately \$123.9 million. The Company's loss as a result of the fire damage to its property and settlement of the above claims was substantially covered by insurance.

As of February 10, 2000, there were still pending approximately 2,600 claims against the Company for personal injury (including punitive damages), and approximately 290 separate active claims for property damage, arising from the smoke, ash and embers generated by the fire. A substantial percentage of these claims have been asserted in lawsuits against the Company filed in the Superior Court for Alameda County, California. There can be no assurance that the pending claims will be settled or otherwise disposed of for amounts and on terms comparable to those settled to date.

On July 10, 1998, Safeway was served with a new case filed in the Superior Court for Alameda County, California, authored by the same attorney who had filed a previous class action relating to the Richmond warehouse fire that was dismissed and affirmed on appeal. The July 1998 action, as amended, alleges that Safeway committed fraud and breach of contract in connection with settlements involving the Richmond warehouse fire. The case purports to be filed on behalf of approximately 21,500 individual plaintiffs. Plaintiffs seek damages according to proof, plus interest and punitive damages. On March 5, 1999, the court sustained the Company's demurrer to plaintiffs' fraud claim. On May 20, 1999, the court granted the Company's motion for judgment on the pleadings on plaintiffs' contract claim. Plaintiffs filed a notice of appeal, and the appeal is pending. The Company believes that the claims in this case are without merit and that the judgment of the trial court will be affirmed.

The Company has received notice from its insurance carrier denying coverage for the claims asserted in the two purported class action suits described above. Safeway strongly disagrees with the insurance carrier's denial of coverage. Safeway continues to believe that coverage under its insurance policy will be sufficient and available for resolution of all remaining personal injury and property damage claims arising out of the fire.

On September 13, 1996, a class action lawsuit entitled *McC Campbell, et al. v. Ralphs Grocery Company, et al.*, was filed in the Superior Court of San Diego County, California against Vons and two other grocery store chains operating in southern California. The complaint alleged, among other things, that Vons and the other defendants conspired to fix the retail price of eggs in southern California, in violation of the California Cartwright Act, and that they engaged in unfair competition. The court subsequently certified a class of retail purchasers of white chicken eggs by the dozen in southern California from September 1992 to October 1997. A jury trial commenced in July 1999, and plaintiffs asked the jury to award damages against Vons (before trebling) of \$36.8 million. On September 2, 1999, the jury returned a verdict in favor of Vons and the other defendants. On October 15, 1999, the court denied plaintiffs' motion for judgment notwithstanding the verdict or a new trial, and also denied their motion for judgment on the unfair competition claim. On November 1, 1999, judgment was entered in favor of defendants, and plaintiffs appealed. The appeal is pending. The Company believes that plaintiffs have no meritorious grounds for an appeal and expects the judgment to be affirmed.

Safeway acquired Dominick's in November 1998. At that time, there was pending against Dominick's a class action lawsuit that had been filed in the U.S. District Court for the Northern District of Illinois in March 1995, alleging gender discrimination and seeking compensatory and punitive damages in an unspecified amount. The lawsuit also alleged national origin discrimination, but the court denied plaintiffs' class certification motion as to those claims. On December 20, 1999, the court granted the parties' request for preliminary approval of a proposed settlement agreement that provides for the Company, while denying all liability, to implement job posting programs and other similar forms of relief, to establish a \$7.7 million settlement fund to be available for distribution to eligible class members, and to pay attorneys' fees to current and former class counsel in the maximum amount of \$2.2 million. These amounts are included in Other Accrued Liabilities at year-end 1999. The court has scheduled a final fairness hearing on the proposed settlement for March 31, 2000.

In April 1999, a lawsuit entitled Sanders, et al. v. Lucky Stores, Inc., et al. was filed in the California Superior Court, San Francisco County, against the Company and five other retail grocery store operations. The complaint alleges, among other things, that the Company conspired with the other defendants to fix the retail price of milk in six San Francisco Bay Area counties in violation of the California Cartwright Act and the California Unfair Competition Act. The plaintiffs purport to bring the lawsuit as a class action on behalf of all persons who reside, and who purchased milk from the defendants, in the Bay Area counties from April 1995 to the present. The complaint seeks unspecified damages, an injunction enjoining the defendants from fixing the price of milk and restitution of profits earned through the allegedly unlawful practices. If damages were to be awarded, they may be trebled under the applicable statute. On November 5, 1999, the defendants filed a

motion for summary judgment. Subsequently, plaintiffs began entering into settlement agreements with various defendants. On February 9, 2000, plaintiffs and the Company agreed in principle to a settlement whereby the action would be dismissed and the Company, without admitting liability, would pay \$15,000 in cash and make \$17,500 worth of product donations to local food banks. The settlement agreement must be documented and submitted to the court for approval.

Commitments The Company has commitments under contracts for the purchase of property and equipment and for the construction of buildings. Portions of such contracts not completed at year-end are not reflected in the consolidated financial statements. These unrecorded commitments were \$94.2 million at year-end 1999.

Note L: Segments

Safeway's retail grocery business, which represents more than 98% of consolidated sales and operates in the United States and Canada, is its only reportable segment.

The following table presents information about the Company by geographic area (in millions):

	U.S.	Canada	Total
1999			
Sales	\$25,535.3	\$3,324.6	\$28,859.9
Operating profit	1,815.4	182.5	1,997.9
Income before income taxes	1,499.0	175.0	1,674.0
Total assets	13,960.2	940.1	14,900.3
1998			
Sales	\$ 21,241.7	\$ 3,242.5	\$ 24,484.2
Operating profit	1,467.3	134.4	1,601.7
Income before income taxes	1,272.3	124.6	1,396.9
Total assets	10,541.9	847.7	11,389.6
1997			
Sales	\$ 19,075.9	\$ 3,407.9	\$ 22,483.8
Operating profit	1,169.6	110.1	1,279.7
Income before income taxes and extraordinary loss	978.4	97.9	1,076.3
Total assets	7,613.7	880.2	8,493.9

Note M: Computation of Earnings Per Share

(in millions, except per-share amounts)	1999		1998		1997	
	Diluted	Basic	Diluted	Basic	Diluted	Basic
Income before extraordinary loss	\$970.9	\$970.9	\$806.7	\$806.7	\$621.5	\$621.5
Extraordinary loss	-	-	-	-	(64.1)	(64.1)
Net income	\$970.9	\$970.9	\$806.7	\$806.7	\$557.4	\$557.4
Weighted average common shares outstanding	498.6	498.6	482.8	482.8	462.3	462.3
Common share equivalents	16.8		26.0		35.4	
Weighted average shares outstanding	515.4		508.8		497.7	
Earnings per common share and common share equivalent:						
Income before extraordinary loss	\$ 1.88	\$ 1.95	\$ 1.59	\$ 1.67	\$ 1.25	\$ 1.35
Extraordinary loss	-	-	-	-	(0.13)	(0.14)
Net income	\$ 1.88	\$ 1.95	\$ 1.59	\$ 1.67	\$ 1.12	\$ 1.21
Calculation of common share equivalents:						
Options and warrants to purchase common shares	37.7		48.0		58.6	
Common shares assumed purchased with potential proceeds	(20.9)		(22.0)		(23.2)	
Common share equivalents	16.8		26.0		35.4	
Calculation of common shares assumed purchased with potential proceeds:						
Potential proceeds from exercise of options and warrants to purchase common shares	\$986.8		\$913.9		\$597.4	
Common stock price used under the treasury stock method	\$47.26		\$41.60		\$25.75	
Common shares assumed purchased with potential proceeds	20.9		22.0		23.2	

Note N: Quarterly Information (Unaudited)

The summarized quarterly financial data presented below reflect all adjustments which, in the opinion of management, are of a normal and recurring nature necessary to present fairly the results of operations for the periods presented.

(in millions, except per-share amounts)	52 Weeks	Last 16 Weeks	Third 12 Weeks	Second 12 Weeks	First 12 Weeks
1999					
Sales	\$28,859.9	\$9,934.7	\$6,475.0	\$6,337.0	\$6,113.2
Gross profit	8,510.7	2,875.3	1,918.8	1,895.0	1,821.6
Operating profit	1,997.9	649.9	453.3	469.6	425.2
Income before income taxes	1,674.0	526.4	385.2	401.4	361.1
Net income	970.9	305.3	223.4	236.4	205.8
Earnings per share:					
Basic	\$ 1.95	\$ 0.60	\$ 0.45	\$ 0.48	\$ 0.42
Diluted	1.88	0.59	0.44	0.46	0.40
Price range, New York Stock Exchange	62⁷/₁₆ to 29⁷/₁₆	46⁷/₁₆ to 29⁷/₁₆	55 to 42¹¹/₁₆	56 to 43¹⁵/₁₆	62⁷/₁₆ to 50⁷/₁₆

(in millions, except per-share amounts)	52 Weeks	Last 16 Weeks	Third 12 Weeks	Second 12 Weeks	First 12 Weeks
1998					
Sales	\$ 24,484.2	\$ 7,922.6	\$ 5,589.0	\$ 5,583.3	\$ 5,389.3
Gross profit	7,124.5	2,288.1	1,650.1	1,622.2	1,564.1
Operating profit	1,601.7	511.8	377.8	380.9	331.2
Income before income taxes	1,396.9	441.6	335.5	334.4	285.4
Net income	806.7	255.0	193.7	193.2	164.8
Earnings per share:					
Basic	\$ 1.67	\$ 0.52	\$ 0.40	\$ 0.40	\$ 0.34
Diluted	1.59	0.50	0.38	0.38	0.33
Price range, New York Stock Exchange	61⁷/₁₆ to 30⁷/₁₆	61⁷/₁₆ to 37⁷/₁₆	46⁷/₁₆ to 37⁷/₁₆	40⁷/₁₆ to 34	37⁷/₁₆ to 30⁷/₁₆

Financial Statements Safeway Inc. is responsible for the preparation, integrity and fair presentation of its published financial statements. The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles and necessarily include amounts that are based on judgments and estimates made by management. Safeway also prepared the other information included in the annual report and is responsible for its accuracy and consistency with the financial statements.

The financial statements have been audited by Deloitte & Touche LLP, independent auditors, which was given unrestricted access to all financial records and related data, including minutes of all meetings of stockholders, the Board of Directors, and committees of the Board. Safeway believes that all representations made to the independent auditors during their audit were valid and appropriate. The report of Deloitte & Touche LLP is presented below.

Internal Control System Safeway maintains a system of internal control over financial reporting, which is designed to provide reasonable assurance to management and the Board of Directors regarding the preparation of reliable published financial statements. The system includes a documented organizational structure and division of responsibility; established policies and procedures including a code of conduct to foster a strong ethical

climate, which are communicated throughout Safeway; and the careful selection, training and development of employees. Internal auditors monitor the operation of the internal control system and report findings and recommendations to management and the Board, and corrective actions are taken to address control deficiencies and other opportunities for improving the system as they are identified. The Board, operating through its Audit Committee, which is composed entirely of outside directors, provides oversight to the financial reporting process.

There are inherent limitations in the effectiveness of any system of internal control, including the possibility of circumvention or overriding of controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to financial statement preparation. Furthermore, the effectiveness of an internal control system can change with circumstances. As of January 1, 2000, Safeway believes its system of internal controls over financial reporting was effective for providing reliable financial statements.



Steven A. Burd
Chairman, President and
Chief Executive Officer



David G. Weed
Executive Vice President
and Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

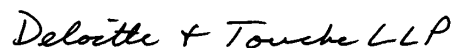
The Board of Directors and Stockholders of Safeway Inc:

We have audited the accompanying consolidated balance sheets of Safeway Inc. and subsidiaries as of January 1, 2000 and January 2, 1999, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three fiscal years in the period ended January 1, 2000. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit

also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Safeway Inc. and subsidiaries as of January 1, 2000 and January 2, 1999, and the results of their operations and their cash flows for each of the three fiscal years in the period ended January 1, 2000 in conformity with generally accepted accounting principles.



San Francisco, California
February 25, 2000

DIRECTORS AND PRINCIPAL OFFICERS

Directors

Steven A. Burd
Chairman, President
and Chief Executive Officer
Safeway Inc.

James H. Greene, Jr.
Member
KKR & Co., LLC

Paul Hazen
Chairman
Wells Fargo & Co.

Henry R. Kravis
Member
KKR & Co., LLC

Robert I. MacDonnell
Member
KKR & Co., LLC

Peter A. Magowan
Managing General Partner
and President
San Francisco Giants

George R. Roberts
Member
KKR & Co., LLC

Rebecca A. Stirn
Business Consultant

William Y. Tauscher
Private Investor
Former Chairman and
Chief Executive Officer
Vanstar Corporation

Director-Nominee

Hector Ley Lopez
General Director
Casa Ley, S.A. de C.V.

Executive Officers

Steven A. Burd
Chairman, President and
Chief Executive Officer

Richard W. Dreiling
Executive Vice President
Marketing and
Manufacturing Operations

Kenneth W. Oder
Executive Vice President
Labor Relations, Human Resources,
Law, Public Affairs and Information
Technology

Larree M. Renda
Executive Vice President
Retail Operations

David G. Weed
Executive Vice President
and Chief Financial Officer

David F. Bond
Senior Vice President
Finance and Control

David T. Ching
Senior Vice President and
Chief Information Officer

David F. Faustman
Senior Vice President
Labor Relations and Public Affairs

Dick W. Gonzales
Senior Vice President
Human Resources

Lyn C. Gordon
Senior Vice President
Strategic Development

Lawrence V. Jackson
Senior Vice President
Supply Operations

Melissa C. Plaisance
Senior Vice President
Finance and Investor Relations

Michael C. Ross
Senior Vice President
Secretary and General Counsel

Kenneth M. Shachmut
Senior Vice President
Corporate Reengineering

Donald P. Wright
Senior Vice President
Real Estate and Engineering

Other Principal Officers

Michael J. Bessire
Eastern Division President

Robert A. Diens
Seattle Division President

Bruce Everette
Northern California Division President

Robert H. Henry
Denver Division President

Thomas A. Mossey
Phoenix Division President

Lyle A. Waterman
Portland Division President

Thomas C. Keller
President
The Vons Companies, Inc.

Timothy J. Hakin
President
Dominick's Finer Foods, Inc.

Frank Lazaran
President
Randall's Food Markets, Inc.

Robert A. Gordon
Senior Vice President
Deputy General Counsel

Foreign Subsidiary

Canada Safeway Limited

Grant M. Hansen
President and Chief Operating Officer

Equity Affiliate

Casa Ley, S.A. de C.V. (Mexico)

Juan Manuel Ley Lopez
Chairman and Chief Executive Officer

Executive Offices

Mailing Address:
Safeway Inc.
P.O. Box 99
Pleasanton, CA 94566-0009

**Stock Transfer Agent
and Registrar**

First Chicago Trust Company
of New York
P.O. Box 2500
Jersey City, NJ 07303-2500
800-756-8200

Form 10-K

A copy of Safeway's 1999 Form 10-K filed with the Securities and Exchange Commission may be obtained by writing to the Investor Relations Department at our executive offices, or by calling 925-467-3790.

Independent Auditors

Deloitte & Touche LLP
San Francisco, California

Annual Meeting

The 2000 Annual Meeting of Stockholders will be held on May 9, 2000. A notice of the meeting, together with a proxy statement and a form of proxy, were mailed to stockholders with this annual report.

Stock Exchange Listing

The Company's common stock, which trades under the symbol SWY, and certain debentures and notes are listed on the New York Stock Exchange.

Internet Address

Safeway's web site on the Internet can be accessed at <http://www.safeway.com>.

Investor Inquiries

Communications regarding investor records, including changes of address or ownership, should be directed to the Company's transfer agent, First Chicago Trust Company of New York, at the address listed on the left. To inquire by phone, please call 800-756-8200.

Investors, security analysts and members of the media should direct their financial inquiries to our Investor Relations Department at 925-467-3832.

To obtain or access financial reports, please write to our Investor Relations Department, call 925-467-3790 or check our web site at <http://www.safeway.com>.

EEO-1 Report

As an equal opportunity employer, Safeway values and actively supports diversity in the workplace. A copy of the Company's 1999 summary EEO-1 report, filed with the federal Equal Employment Opportunity Commission, is available upon request at our executive offices.

Trustees and Paying Agents

5.75% Notes
5.875% Notes
6.05% Notes
6.50% Notes
6.85% Senior Notes
7.00% Notes
7.25% Notes
7.50% Notes
7.00% Senior Notes
7.45% Senior Debentures
9.65% Senior
Subordinated Debentures
10.00% Senior
Subordinated Notes

The Bank of New York
Bondholder Relations Department
Corporate Trust Operations
Fiscal Agencies Department
101 Barclay Street, 7-East
New York, NY 10286
800-548-5075

9.30% Senior Secured Debentures
The First National Bank of Chicago
Corporate Trust Investor Relations
One First National Plaza, Suite 0134
Chicago, IL 60670-0134
800-524-9472

9.35% Senior Subordinated Notes
9.875% Senior
Subordinated Debentures

Harris Trust and Savings Bank
P.O. Box 755
Chicago, IL 60690
312-461-2908

10.00% Senior Notes

Trustee

The Chase Manhattan Bank
Corporate Trust Administration
101 California Street, Suite 2725
San Francisco, CA 94111
415-954-9581

Paying Agent

Bankers Trust Company
Corporate Trust & Agency Group
4 Albany Street, 4th Floor
New York, NY 10006
212-250-6161



Safeway Inc.
P.O. Box 99
Pleasanton, CA 94566-0009