

RETAIL SECTOR WEEKLY

Key Retail News and Commentary

Inside this issue:

Heard in the Grocery Aisle	2
The Global World of Sports and Footwear	3
Upcoming Reporting Dates	3
Specialty Items	4
Health & Beauty Aids	4
Rating Changes & Outlooks	4
Bankruptcy Blotter	5
FYI for the DIY	5
Hi Tech Entertainment	5
Management on the Move	6
Options and Resources	6
Off the Rack	7
Mass Merchant Musings	7
General Retail News	8
Second Quarter Scorecard	8

Value of American's Life Dropping

It's not just the American dollar that's losing value. A government agency has decided that an American life isn't worth what it used to be. The "value of a statistical life" is \$6.9 million in today's dollars, the Environmental Protection Agency reckoned in May – a drop of nearly \$1 million from just five years ago.

The Associated Press discovered the change after a review of cost-benefit analyses over more than a dozen years.

Though it may seem like a harmless bureaucratic recalculation, the devaluation has real consequences.

When drawing up regulations, government agencies put a value on human life and then weigh the costs versus the lifesaving benefits of a proposed rule. The less a life is worth to the government, the less the need for a regulation, such as tighter restrictions on pollution.

Consider, for example, a hypothetical regulation that costs \$18 billion to enforce but will prevent 2,500 deaths. At \$7.8 million per person (the old figure), the lifesaving benefits outweigh the
(continued on page 2)

Whole Foods: Retailer of the Week

We are **downgrading Whole Foods Market** from a low risk, 'B' credit to a **moderate risk, 'C' credit** on Whole Foods Market, but maintaining its **stable outlook**. The grocer is still a solid credit despite reduced profitability and the weak Wild Oats stores. Management is currently focused on integrating the acquired stores. CEO John Mackey stated that he is pleased with the pace of the integration. Whole Foods is looking to help its lagging legacy store base by upgrading or relocating existing supermarkets. In addition, the company continues to aggressively expand the size of its store portfolio. GCS speculates that the slowing economy and the increased organic offerings by more traditional grocers is having on negative impact on Whole Foods' performance. The equity markets have certainly punished the firm's common share price over the past few years as its growth has moderated. While Whole Foods has taken some debt and seen a reduction in its bottom line, the organic grocer is not a credit worry at this point because it has a decent balance sheet and a revolver with increased availability.

OPERATING PERFORMANCE: 6 MONTHS ENDED APRIL 13, 2008

\$ in millions, 28 weeks ended	4/13/2008	YOY Var.	4/8/2007	4/9/2006
Revenue	\$4,323.80	29.80%	\$3,333.90	\$2,978.40
Comparable Store Sales	8.10%		6.60%	12.50%
Operating Profit	\$149.60	-6.30%	\$159.60	\$173.40
Net Profit	\$79.10	-20.70%	\$99.70	\$110.10
Gross Margin	34.20%	(47 bps)	34.70%	34.90%
SG&A Burden*	30.60%	90 bps	29.70%	29.00%
Operating Margin	3.45%	(134 bps)	4.79%	4.90%
Return on Sales	1.82%	(117 bps)	2.99%	2.90%
EBITDAR / (Interest + Rent)	3.16x	(37 bps)	3.53x	4.32x

* - direct store expenses, GSA expenses, and pre-opening & relocating expenses.

(continued on page 8)

Remember...

People, even more than things, have to be restored, renewed, revived, reclaimed and redeemed; never throw out anyone.

Value of American's Life Dropping

(continued from page 1)

costs. But at \$6.0 million per person, the rule costs more than the lives its saves, so it may not be adopted.

Some environmentalists accuse the Bush administration of changing the value to avoid tougher rules – a charge the EPA denies.

Agency officials say they were just following what science told them.

The EPA figure is not based on people's earning capacity, or their potential contributions to society, or how much they are loved and needed by their friends and family – some of the factors used in insurance and wrongful-death lawsuits.

Instead, economist calculate the value based on what people are willing to pay to avoid certain risks, and on how much extra employers pay their workers to take on additional risks. Most of the data is drawn from payroll statistics; some comes from opinion surveys. According to the EPA, people shouldn't thin of the number as a price tag on a life.

At the same time that EPA was trimming the value of life, the Department of Transportation twice raised its life value figure. But its number is still lower than the EPA's.

EPA traditionally has put the highest value on life of any government agency and still does, despite efforts by administrations to bring uniformity to that figure among all departments.

From 1996 to 2003, EPA kept the value of a statistical life generally around \$7.8 million to \$7.96 million in current dollars. In 2004, for a major air pollution rule, the agency lowered the value to \$7.15 million in current dollars. Just how the EPA came up with that figure is complicated and involves two dueling analyses.

One of those big studies came up with a value of \$8.8 million in current dollars, while the other study put the number between \$2 million and \$3.3 million. The author of the second study said her figure was lower because it emphasized differences in pay for various risky jobs, not just risky industries as a whole. EPA took portions of each study and essentially split the difference – a decision two of the agency's advisory boards faulted or questioned.

If this does not sound Orwellian, I don't know what does. Whatever happened to the government providing for the national security as its prime objective and the states for most everything else and politicians working for the good of the country not the good of their party. In the public specter, bigger is definitely not better.

Heard in the Grocery Aisle

Meijer will build a new store to replace its oldest supercenter store in Grand Rapids, MI. The new store will open in 2010.

Kroger associates who are members of UFCW local 1995 in Tennessee and Alabama ratified the new labor agreement we reported two weeks ago.

Seeing opportunity in the down economy, **Aldi Inc.** plans to open 100 more discount grocery stores in 2008. Aldi currently operates over 900 stores in the U.S.

Stop & Shop held Affordable Food Summits at several NYC area locations in response to rising food prices. Speakers included an economist and a food bank representative, *Newsday* reported.

Penn Traffic launched a new branding and advertising campaign, *Supermarket News* reported. The "Big Smiles, Fresh Food, Low Prices" effort is a component of the company's ongoing strategic turnaround plan.

Feedback?

Questions?

Suggestions?

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[RETURN TO FIRST PAGE](#)

The Global World of Sports and Footwear

Sport Chalet, Inc. expanded its senior credit facility with Bank of America to \$70 million from \$40 million.

Academy Sports & Outdoors, which intends to open four stores in Alabama over the next 12 months, will exit its store in Birmingham's Wildwood Centre when the lease expires.

Dick's Sporting Goods will shutter **Golf Galaxy's** headquarters in Minnesota, nearly two years after DKS paid \$225 million for the golf specialty chain. Dick's will integrate the back-office functions for the current 75 Golf Galaxy stores with those of its own banner and will likely take the amalgamation further, executives suggest.

Sporting Goods Intelligence reports that **Executive Compensation** was down 8.8% compared to the prior year for 62 public sporting goods retail company executives who had at least two years at their present employer. That compared favorably with the pre-tax profits of the 15 retailers in the survey, which dropped 56.9% from last year's levels. Dick's CEO Ed Stack remained atop the list of earners at \$9.5 million, though he took a 15% decrease in compensation. Foot Locker CEO Matt Serra and PacSun CEO Sally Frame Kasaks topped the \$3 million mark. Five executives topped the \$2 million level: Dick's CMO Gwen Manto, Golf Galaxy CEO Randy Zanatta, Dick's COO Bill

Columbo, Foot Locker U.S. chief Rick Mina and Lululemon CEO Bob Meers. Another 16 retail executives topped the \$1 million mark. Last year, only 20 retail executives had two commas in their compensation package.

G-III Apparel acquired certain assets of **Wilsons Leather Outlet** stores for \$22.3 million cash. The acquisition, which includes 116 outlet store locations, \$18.5 million in inventory, control of Wilsons' distribution center and the Wilsons name and related trademarks, should be accretive in FY09.

NexCen Brands has reportedly named Darius Billings, director of retail brand marketing and merchandising, to oversee a rebranding of The Athlete's Foot that will see the 242-door (U.S.) chain move toward calling itself, 'taf' as it undergoes an interior makeover.

National Sporting Goods Association reported that U.S. consumer purchases of used sporting goods topped the \$1 billion mark, hitting \$1.08 billion in 2007. Used outdoor sports equipment (camping, fishing and shooting sports) purchases grew 11% last year to \$669 million. Meanwhile, the second largest used sporting goods category, exercise equipment, saw sales rise 6% in 2007 to slightly more than \$208 million. The dollar total represents more than 850,000 used treadmills and stationary bicycles, the trade group reported.

Did You Know...?

The Pending Home Sales Index, a forward-looking index released by the National Association of Realtors, fell 4.7% to a rating of 84.7 in May, compared with an upwardly revised reading of 88.9 in April. The index remains 14% below last year's figure of 98.5.

Upcoming Reporting Dates

Company	Event	Date
99 Cents Only Stores	Quarterly Results	Aug 7, 2008
Abbott	Quarterly Results	Jul 16, 2008
Amazon.com	Quarterly Results	Jul 23, 2008
AmerisourceBergen	Quarterly Results	Jul 24, 2008
Bebe Stores	Quarterly Results	Aug 21, 2008
Cabela's	Quarterly Results	Jul 31, 2008
Charlotte Russe	Quarterly Results	Jul 23, 2008
Crane	Quarterly Results	Jul 28, 2008
Ethan Allen	Quarterly Results	Jul 23, 2008
Express Scripts	Quarterly Results	Jul 30, 2008
Ingram Micro	Quarterly Results	Jul 24, 2008
Loblaw Companies	Quarterly Results	Jul 25, 2008
McKesson Corporation	Quarterly Results	Jul 23, 2008
Mothers Work	Quarterly Results	Jul 29, 2008
Nash Finch	Quarterly Results	Jul 17, 2008
Office Depot	Quarterly Results	Jul 30, 2008
PC Mail	Quarterly Results	Jul 29, 2008
Rent A Center	Quarterly Results	Jul 29, 2008
Safeway	Quarterly Results	Jul 17, 2008
Shoppers Drug Mart	Quarterly Results	Jul 16, 2008
Staples	Quarterly Results	Sep 3, 2008
West Marine	Quarterly Results	Jul 24, 2008

[RETURN TO FIRST PAGE](#)

Specialty Items

Finlay Enterprises was delisted from Nasdaq Global Market on July 11, and now trades on the OTC Bulletin Board under the same ticker: FNLY.

Tuesday Morning Corp. sales were \$885.3 million for the year ended June 30, down 4.2% from to \$924.2 million last year. Comps fell 7.6%. The company issued earnings guidance of (\$0.05) to (\$0.08) per share for the fourth quarter and \$0.33 to \$0.36 per share for the year.

Limited Brands is opening six **Bath & Body Works** stores in Canada. In Ontario, there will be two stores in Toronto and one each in

Guelph, Mississauga, and London. In Alberta, there will be a store in West Edmonton Mall.

O'Reilly Automotive has acquired over 90% of the issued and outstanding shares of **CSK Auto Corp.** and completed a short-form merger of its indirect wholly-owned subsidiary with and into CSK, with CSK continuing as the surviving corporation and an indirect wholly owned subsidiary of O'Reilly.

Hurt by the downturn in the economy, **Jennifer Convertibles** posted a \$711,000 loss in its fiscal third quarter, on revenue of \$28.4 million, which was down 12.6% versus prior year.

Did You Know...?

Private equity funds continue to raise large amounts at a staggering pace despite continuing difficulties in the credit markets and a dearth of buyouts. The industry raised \$161.9 billion in the three months to June 30th, the second-highest quarterly total ever.

Health & Beauty Aids

Sales of health and wellness products reached \$102.8 billion last year, representing growth of 15 percent according to a Natural Marketing Institute report issued last week.

Walgreens lowered their projected store growth target from 9% this year, to 6% in FY2010, to 5% beginning in FY2011. The reduction will reduce capex by \$500 million over the next three years. That translates to 500 net new stores this year, 495 in fiscal 2009, 425 in fiscal 2010 and 365 in fiscal 2011.

McKesson's will offer their RxOwnership program to help prospective independent pharmacy owners with business planning and consulting.

Rite Aid Corp. has completed its refinancing including a \$350 million senior secured term loan due 2014 and \$470 million of new 10.375% senior secured notes due 2016. Proceeds will be used to fund tender offers for existing debt.

Cardinal Health will consolidate its businesses into two segments: Healthcare Supply Chain Services and Clinical and Medical Products. There will also be an All Other segment. Cardinal expects to cut 600 positions, and incur a charge of approximately \$63 million in FY09 related to the reorganization.

Stater Bros.' Super Rx pharmacies and pharmacies in **Dierbergs** supermarkets are both offering generics for \$4 for a 30-day supply and \$10 for a 90-day supply.

General Nutrition Corp. has partnered with **WebMD** on web content for both companies' web sites. The Live Well Topic Center will have consumer information on vitamins and supplements.

Jean Coutu Group Inc. is putting on hold plans to expand out of its Quebec home base into Ontario, preferring for the time being to invest in its core market.

Rating Changes & Outlooks

Company	Global Credit Services Credit Rating		Global Credit Services Outlook	
	Current	Prior	Current	Prior
WHOLE FOODS MARKET INC	C	A	STA	POS

Company	S&P Credit Rating		S&P Credit Outlook		GCS Credit Rating
	Current	Prior	Current	Prior	Current
WALGREEN COMPANY INC	A+		STABLE		B-
STAPLES INC	BBB	BBB+	STABLE	NM	B
LIMITED BRANDS INC	BBB-	BBB-	NEGATIVE	NM	C
OFFICE DEPOT INC	BB+	BB+	NM	NEGATIVE	D

[RETURN TO FIRST PAGE](#)

Bankruptcy Blotter

Creditors of **Goody's Family Clothing Inc.** are urging the court to deny the company a \$210 million loan with **General Electric Capital Corp.**, accusing the lenders and shareholders of trying to saddle Goody's with exorbitant costs while they decide whether to push for a liquidation.

The newly appointed Unsecured Creditors' Committee for **Whitehall Jewellers Holdings, Inc.** has objected to a proposed sale of the company's assets, claiming the early August schedule is too quick and will not bring an optimal return.

Linens 'n Things won court approval of a \$200 million trade credit program designed to enhance the flow of merchandise into its shops on favorable terms from its vendors. The program allows the company to tap a \$100 million letter of credit under its \$700 million DIP facility for the benefit of its suppliers.

In other news **Linens 'n Things** is requesting permission close an additional 87 stores,

bringing the total number of stores to be closed to 207. A joint venture of **Tiger Capital Group LLC** and **SB Capital Group LLC** won the right to run liquidation sales for the first round of 120 stores to be closed.

Steve & Barry's, which filed for Chapter 11 protection last week, reached a deal with its lenders to push back the sale of the company to August after the court balked at an initial plan to sell by the end of July. The company plans to auction its assets on August 12th.

Dawahare's clothing stores has been unable to raise the cash needed to continue operating and will shut down September 30th. The Lexington, Kentucky based chain has been in business for 101 years.

Delphi Corp. is asking the court to force an investor group led by Appaloosa Management to follow through on its \$2.55 billion equity investment in the company, claiming it's still the best hope for getting the struggling auto-parts company out of bankruptcy.

FYI for the DIY

ProBuild Holdings acquired **Big Buck Building Centers** of Racine, Wisconsin as the Denver-based company's foothold into the Chicago and Milwaukee markets.

Sherwin-Williams Co. reported that the City of Columbus has voluntarily dismissed with prejudice its lawsuit against former manufacturers of lead pigment. All ten public nuisances suits filed by Ohio cities since 2006 have been either voluntarily dismissed or rejected by courts.

Grainger subsidiary Lab Safety Supply has acquired library equipment, furniture and supplies distributor Highsmith, Inc. The acquisition is expected to add \$20-30 million to

LSS's sales in 2008, but is expected to be dilutive by \$.02 to \$.03 per share this year.

Fastenal Co.'s board has authorized an additional stock buyback by the company of up to one million shares of its common stock.

United Rentals, Inc. narrowed its full year 2008 earnings guidance to \$2.65 to \$2.75 per share, the low end of the previous range of \$2.65 to \$2.85. Revenue guidance was narrowed to \$3.3 billion to \$3.4 billion from \$3.3 billion to \$3.5 billion previously.

Lowe's will open three stores this month, in North Peoria, AZ, Shepherdsville, KY and North Winchester, VA.

Hi Tech Entertainment

Office Depot, Inc. warned that sales trends worsened late in the second quarter. Comps for the quarter were down around 10 percent, total sales were down slightly and EBIT margin down 400 to 450 basis points.

Best Buy Inc. laid out some detail of its five year plan to double revenue to \$80 billion. The company will focus on growing market share,

expanding digital services and international expansion. BBY may also take its Pacific Sales Kitchen and Bath Centers chain national

Amazon.com Inc. hosted hiring open houses for several hundred full-time hourly positions in its Goodyear and Phoenix, Arizona fulfillment centers.

[RETURN TO FIRST PAGE](#)

Management on the Move

Ann Navarra, co-owner of So. California furniture retailer **Jerome's**, will retire at the end of July. She's worked for the family-owned company in the early 1970s.

Kevin Layden, who helped steer **Future Shop Ltd.** through its purchase by **Best Buy Co. Inc.**, has quit as COO of Best Buy International after just a few months in that role.

Ahold shuffled management of its U.S. subsidiaries.

- **Lawrence Benjamin**, COO of Ahold USA, has been nominated to the Ahold Corporate Executive Board pending shareholder approval.
- **Carl Schlicker** was appointed President and CEO of Stop & Shop/Giant-Landover.
- **Sander van der Laan** was appointed President and CEO of Giant-Carlisle.
- **Jose Alvarez** has been appointed EVP Global Business Development.

Blockbuster names **Rebeca Johnson** Chief Marketing Officer. Johnson was previously at Brinker International and Frito-Lay.

Joel Waller, the former CEO of Wilsons The Leather Experts, is joining **GIII Apparel** as president of its outlet store unit.

Collective Brands taps **LuAnn Via** as the new Payless ShoeSource President, CEO. She was most recently group divisional president for the Lane Bryant and Cacique retail chains owned by Charming Shoppes.

Charming Shoppes President and CEO Dorrit J. Bernhas has resigned, and will be replaced on an interim basis by Chairman **Alan Roskamm** until a permanent CEO can be found. Separately, the company appointed **Brian P. Woolf** President of the Lane Bryant brand, replacing LuAnn Via.

Also, **M. Jeannine Strandjord** has rejoined **Charming Shoppes** board of directors.

Strandjord stepped down during the recent proxy contest but was unanimously elected again after the recent death of board member **William O. Albertini**.

Safeway appointed **Christiane Pelz** as VP Investor Relations. Pelz was formerly with investor relations agency Lippert/Heilshorn & Assoc.

Thomas M. Bazzone resigned as EVP of **Michaels Stores, Inc.**

Rebecca Roedell, EVP and CFO of **Sharper Image Corp.** has resigned.

Carpet One Floor & Home appointed **Scott Wheeler** COO. Wheeler has had executive positions at Flooring America and Avalon Carpet Tile & Flooring.

Genesco Inc. adds the CEO title to President **Robert J. Dennis**, effective as of Aug 1.

PC Mall, Inc. named **Brandon H. LaVerne** CFO. He had been Interim CFO for the past year.

OfficeMax named **Deborah O'Connor** SVP Finance and CAO. O'Connor was SVP and Controller at ServiceMaster.

Walgreens promoted three:

- **Hal F. Rosenbluth**, President of Walgreens Health and Wellness division, was named a corporate SVP.
- **Michael Nameth**, EVP for pharmacy benefit management and specialty pharmacy at Walgreens Health Services division, was promoted to corporate divisional VP for Walgreens.
- **Mark A. Wattley**, VP and legal counsel of human resources for Walgreens Health Services, was promoted to a corporate divisional VP for Walgreens.

United Rentals, Inc. board member **Gerald Tsai, Jr.** passed away on July 9, 2008.

Did You Know...?

U.S. initial jobless claims fell to their lowest level since April in the latest week, but continuing unemployment claims reached a level not seen since December 2003.

Options and Resources

Feedback and Questions: Should you have any feedback to provide us or questions to ask, please email us at inbox@globalcreditservices.com.

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[RETURN TO FIRST PAGE](#)

Off the Rack

Stage Stores said it expects to meet or exceed its second quarter guidance of comp store sales down 3.0% and earnings of \$0.23 per diluted share.

Cache Inc. increased second quarter guidance to earnings of \$0.14 to \$0.15 per share, up from \$0.12 to \$0.14 prior guidance.

dELiA's is out with its latest CCS.com catalog. The 108-page effort offers over 650 new items for the action sports/skateboard set.

Men's Wearhouse decreased its guidance for second quarter to earnings per share to arrange of \$0.61 to \$0.65 from \$0.69 to \$0.73 provided at the end of May.

Mothers Work, Inc. narrowed its guided range for third quarter earnings per share to between \$0.66 and \$0.70 per share, from between \$0.61 and \$0.76 per share provided earlier.

The Wet Seal revised second quarter earnings guidance to a range of \$0.07 to \$0.09 per diluted share including a non-cash \$1.9mm interest charge. Without the charge, the earnings guidance would have increased to a range of \$0.09 to \$0.11 per diluted share from \$0.08 to \$0.10 per diluted share earlier.

The lawsuit brought against **Polo Ralph Lauren Corp.** by former retail employees in California was granted class certification in U.S. District Court for No. CA. The class consists of more than 5,300 former Polo sales associates and cashiers. Among the plaintiff's claims, Polo misclassified associates as exempt from premium overtime wages, detained them off the

clock for security searches, and failed to give adequate rest breaks.

Cato Corp. adjusted earnings guidance for the second quarter upward to a range of \$.42 to \$.44 per share versus \$.28 to \$.33 given previously and \$.39 last year. Management cited better than expected sell-throughs of regular price and markdown merchandise.

Aeropostale, Inc. also raised second quarter guidance based on a strong June. ARO now projects earnings of \$0.25 to \$0.26 per share, versus its previously issued guidance of \$0.22 to \$0.24 per share.

TJX Companies, Inc. raised its second quarter earnings outlook to \$.44 to \$.45 per share on the back of strong sales and margins in May and June.

Saks Inc. has adjusted its sales outlook for the second quarter and now expects "modestly negative" comps.

Ross Stores upped its projected earnings per share for the second quarter to \$.51 to \$.53 from the prior range of \$.43 to \$.47.

Nordstrom cited higher levels of markdowns and resulting lower gross profit margins, saying that earnings for the quarter will be at the low end or slightly below its guidance of \$.65 to \$.70 per share.

Lord & Taylor parent **NRDC Equity Partners LLC** is reportedly in talks to acquire **Hudson's Bay Co.** NRDC already owns 20% of the Canadian retail chain.

Mass Merchant Musings

Wal-Mart may add 40 to 50 Canadian supercenters, including new stores and conversions, *Bloomberg News* reported, citing an analyst report. The number exceeds Wal-mart management's own guidance estimate of 27 new stores.

Wal-Mart and **Carrefour**, along with investment fund TPG Capital plan to bid for control of Russian retailer **Lenta**. Neither Wal-Mart nor Carrefour, the world's second largest retailer,

has any retail outlets in Russia, but both have a representative office in the country.

On the strength of a solid June, **Wal-mart** updated its earnings guidance for the second quarter to a range of \$0.82 to \$0.84 per share.

Kmart announced the closing of four stores, including three Super Kmart supercenters, this fall. The closures would leave Kmart operating 52 Super Kmart stores.

[RETURN TO FIRST PAGE](#)

General Retail News

A study by Experian Consumer Research found that nearly 10% of the U.S. population could be considered **multi-channel shoppers**. Multi-channel shoppers are defined as those people who regularly participate in more than one method of shopping, including online, in-store, catalog, and phone order.

Strip center vacancies rose to 8.2% in Q2 from 7.3% in Q207, the highest level since 1995, according to data from the International Council of Shopping Centers (ICSC).

Second Quarter Scorecard

\$ in Millions. Quarter ended closest to 7/31/08	Sales			Comps	Net Income		
	2008	2007	Change		2008	2007	Change
Apparel							
Bebe Stores, Inc.	\$167.2	\$160.9	3.9%	-5.6%	tba	tba	tba
Cache, Inc.	\$74.1	\$71.1	4.2%	3.0%	tba	tba	tba
Mothers Work, Inc.	\$152.2	\$153.2	-0.7%	2.4%	tba	tba	tba
Mass Merchants							
99 Cents Only Stores	\$304.9	\$293.0	4.1%	-0.5%	tba	tba	tba
Sports & Footwear							
West Marine, Inc. (Stores)	\$198.6	\$218.7	-9.2%	tba	tba	tba	tba
Specialty							
Haverty Furniture	\$168.4	\$187.1	-10.0%	-12.7%	tba	tba	tba
Jennifer Convertibles	\$26.8	\$30.3	-11.6%	-19.8%	(\$0.6)	\$1.7	-135.3%
Tuesday Morning Corp.	\$196.5	\$219.4	-10.4%	-12.7%	tba	tba	tba
Home Centers							
Fastenal Company	\$604.2	\$519.7	16.3%	NA	\$76.2	\$60.3	26.4%

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Whole Foods: Retailer of the Week

(continued from page 1)

In the first half of fiscal 2008, sales increased 29.8% to \$4.3 billion; however much of this rapid growth is the result of the acquisition of Wild Oats. When backing out the impact of the recently purchased stores, the top-line increased 17.3% to \$3.9 billion. After six months, same store sales increased 8.1%. As has been the case for several quarters, older locations continue to significantly lag newer supermarkets' same store sales figures. Locations that are more than 11 years old produced comps of 4.5% (see Comparable Store Sales). Whole Foods is looking to produce better same store sales figures by building large new stores, expanding older supermarkets, and revitalizing the former Wild Oats locations. As a reminder, Wild Oats will be entered into the firm's comps calculation during Q4 2008. The company has expects to open 13 stores in the second half of fiscal 2008. The company has signed 89 leases that will be used to house new or relocated stores. Whole Foods' gross margin declined 47 basis points to 34.2%, as a result of some price investments. CEO John Mackey has aimed to protect margins by expanding its private label program. In the past three years, management has improved private label penetration from 15% to 22%.

Whole Foods' SG&A burden expanded by 90 basis points to 30.6%. The grocer's overhead increased because of new stores and integration cost. In addition to building costs, new locations are expensive because of the advertising required to generate interest. In addition, newer stores tend not to generate adequate sales volume to support its operating expenses. During the second quarter, the firm has spent heavily to upgrade the IT systems and rebanner its acquired stores. As a result, Whole Foods' GSA expense line was up by about 60 basis points to 3.6%. The company expects that the GSA line will drop significantly during fiscal 2009. Whole Foods' bottom line fell 20.7% to \$79.1 million. The difference between the operating line and the net profit line is partially the result of interest expense. **When adjusting for the impact of Wild Oats, the firm's net**

[RETURN TO FIRST PAGE](#)

(continued on page 9)

Whole Foods: Retailer of the Week

(continued from page 8)

income would have been flat on a year-over-year basis. Despite disappointing results and a growing debt level, the firm's EBITDAR coverage remains a solid 3.2 times.

During the past few months, management has devoted significant time and money to revitalize its Wild Oats stores. Subsequent to the close of Q2 2008, four of the remaining 62 stores were closed. By the close of the quarter, Whole Foods had converted all of the acquired locations to its IT systems. The company expects to have rejuvenated most of the Wild Oats units by the end of fiscal 2008. Management has indicated that sales growth at the rebannered stores are significantly better than the results of the supermarkets using the Wild Oats name. Within the Wild Oats store base, Whole Foods has already made some changes at the supermarket management level. Overall, CEO Mackey seems upbeat on the future of the Wild Oats stores. Would we expect anything different?

LIQUIDITY AND FINANCIAL STRUCTURE

In mid-April, cash and equivalents totaling \$58.4 million provided Whole Foods with sufficient asset-side liquidity. The company finished the quarter with \$89.1 million of availability on its \$250 million bank line. The facility had \$81.0 million of direct borrowings and \$79.9 million of letters of credit outstanding against it. **Subsequent to the close of the quarter, the company expanded its \$250 million line by \$100 million** (see Bank Reference). Whole Foods continues to have a fully drawn \$700 million term loan. As a reminder, this loan was obtained to purchase Wild Oats.

Cash flow from operations of \$156.6 million failed to cover capital expenditures of \$267.3 million. The smaller cash flow number is the result of deteriorating operations and some working capital changes. While the company continues to add debt, the firm is not overly-leveraged. The firm's tangible net worth of \$722 million has fallen 46% over the past twelve months, primarily due to the approximately \$600 million of goodwill and intangibles being placed on the balance sheet at the time of the Wild Oats purchase.

[RETURN TO FIRST PAGE](#)