Global Credit SERVICES

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RETAIL SECTOR WEEKLY

Key Retail News and Commentary

Inside this issue:

Remember...

A discovery is said to be an accident meeting a prepared mind.

RETURN TO FIRST PAGE

Will CIT Rescue Deal Be Enough?

CIT Group Inc.'s $3 billion rescue package from bondholders may not be enough to protect the lender from seeking bankruptcy protection, the company said in a filing last week with the Securities and Exchange Commission, though the cash injection should help the company deal with $1 billion of debt maturing in August, and also provide some fresh funding for making new loans.

CIT is seeking to reduce its debt burden in a tender offer for $1 billion of its bonds. The company said in the filing that if it does not get enough of its outstanding floating-rate senior notes due August 17th tendered, it may need to file for bankruptcy protection, absent additional financing.

CIT has also drawn the ire of the Federal Deposit Insurance Corp., which has threatened to shut down its CIT Bank unit because of inadequate capital levels. The government judged that the company needs about $4 billion in additional regulatory capital including an extra $2.6 billion in tier-one capital, following a stress test. The FDIC issued a cease and desist order on CIT Bank to stop collecting "brokered deposits." These deposits are a key source of funding that comes from brokerage accounts, but have been viewed by regulators as volatile because of their short-term nature.

The lender is facing a worsening liquidity crisis as its customers are drawing down credit lines amid fears it may disappear. The government turned down the company's request for a second bailout following $2.3 billion in funds from the Troubled Asset Relief Program it previously received. While the government hasn't judged CIT to pose a systemic risk should it tumble, it could damage efforts to revive employment because it lends to around 1 million small and medium businesses.

(continued on page 2)

Retailer of the Week: Walgreen Co.

We are maintaining our low risk, 'B' credit rating and negative outlook (indicating that a downgrade to 'C' territory is likely in the future) on Walgreen. While revenue growth has been assisted by a growing store count, the low single-digit same stores sales growth and margin pressure are more indicative of the challenges facing retailers in today's economy. Deteriorating economic conditions and the increasingly blurred lines between traditional drugstore chains and the likes of big box mass merchants and supermarket chains have caused Walgreen and other players to be become more creative in cementing their presence on the average consumer's to-do list.

Walgreen has become more focused in recent quarters on driving cash flow. Beginning in Q4 2009, we can expect to see a much more modest pace of new store openings at the retailer. The P&L statement stands to benefit from this strategic change, as news stores do require a bit of time before they become sustainably profitable. Beyond looking to enhancing profits, which is a key ingredient to cash flow, capital spending requirements will be lighter over the next few years. Finally, working capital improvements, most notably on the inventory front have begun to help the organization's cash flow. The balance sheet remains stable; even as debt as doubled on a year-over-year basis, Walgreen locked in this capital at rates that other, lesser-quality credits couldn't dream of obtaining.

As of May 2009, Walgreen operated a total of 7,361 locations that included 6,857 drugstores, 373 worksite facilities, 112 home care facilities, 17 specialty pharmacies, and 2 mail service facilities. These figures do not include 343 convenient care clinics operated by Take Care Health Systems, Inc. In February 2009, the company agreed to purchase 12 Rite Aid locations in San Francisco and eastern Idaho. Furthermore, in March 2009, Walgreen agreed to acquire script

(continued on page 8)

Will CIT Rescue Deal Be Enough?

(continued from page 1)

Analysts at CreditSights previously have said the company may need about $6 billion to avoid bankruptcy protection.

Last week, CIT struck an agreement with a group of creditors that will provide it with $3 billion in 2½ year loans, a development that gives it a little breathing room to restructure its finances. Under the terms of the loan from bondholders, CIT has to get creditors to approve a restructuring plan by October 1st, according to the filing.

In CIT's tender offer for the floating-rate notes, it is asking investors to swap those securities for 82.5 cents on the dollar before July 31st. Those who tender after that date will only get 80 cents. Some of the same CIT bondholders that came up with the new loan already have agreed to support the tender offer.

People involved in the rescue process say bondholders' longer-term vision for CIT depends on some forbearance from the Federal Reserve and FDIC officials. Without it, bondholders will be hard-pressed to continue to provide support for the lender. Indeed, $1.7 billion in debt payments is due by year's end, and CIT must pay off an additional $8 billion in 2010.

The bondholders hope that by taking steps to stabilize its finances, CIT will be able to transfer more assets from a holding company to its bank in Utah. It can than raise customer deposits to fund those assets.

First, CIT needs an exemption from the Federal Reserve and a nod from the FDIC. Earlier this year, the regulators allowed a transfer to $5.7 billion in student loans by CIT, but more recently they have seemed reluctant to grant additional transfers. Bondholders hope, however, that with a private-sector deal in hand, the regulators will take a second look and allow more transfers. Even though CIT's long-term plans center around the regulatory waiver, no imminent action is expected on that front, according to a report from The Wall Street Journal.

CIT has to find a way to borrow funds cheaply, such that it can lend at a profit. At an initial interest rate of 13%—more than the 10.5% rate mentioned in initial news reports—the emergency loan is coming at a high cost to CIT. One goal of the debt swap is to reduce credit concerns about CIT, potentially allowing it to borrow more cheaply.

Health & Beauty Aids

Mass merchants (53% mentioned) and drug stores (41%) were the channels where women more frequently shopped for cosmetics and beauty needs, according to NPD Group findings reported in *Drug Store News*. Specialty stores (27%) and department stores (15%) lagged behind.

Shoppers Drug Mart Corp. noted that prescription sales rose 9.8% in the second quarter, while front-end sales rose 7.4%. Prescription same-store sales were up 5.6% and front-end same-store sales rose 5.8%, helped by the Easter shift.

Rite Aid Corp. received a commitment from GE Capital for a $290 million loan as part of RAD's $1 billion revolver.

Options and Resources

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RETURN TO FIRST PAGE

Bankruptcy Blotter

A federal watchdog in **Filene's Basement Inc.'s** bankruptcy case is objecting to the $1 million expense reimbursement that a **Men's Wearhouse Inc**. subsidiary (K & G Acquisition Corp.) is trying to collect after watching the budget retailer's assets slip away at auction. U.S. Trustee **Roberta A. DeAngelis** called the $1 million price tag "unreasonably high".

Eddie Bauer Holdings Inc. received court permission to sells its assets to **Golden Gate Capital** for $286 million. Eddie Bauer and term loan lenders engineered a settlement that affords the term loan lenders $135 million from the sale proceeds, subject to some restrictions. The unsecured creditors support the agreement, according to attorneys for the term loan lenders. The sale to Golden Gate is expected to close by August 15.

Ritz Camera Centers Inc. won bankruptcy-court permission to turn over its remaining stores to **RCI Acquisition LLC**, a company led by Ritz CEO David Ritz, despite objections from creditor **Canon U.S.A. Inc**. that the official took advantage of his "position and power" to effect the sale. The total deal was valued at $48.8 million, according to **Alex Goldman**, a spokesman for the buyer, including $16.25 million in cash, a $7.8 million secured note and up to $13.1 million in liabilities.

Bi-Lo LLC is expected to complete a five-year business plan that company officials say will be the foundation for the grocer's emergence from bankruptcy. Company officials said their options include retention of all or part of the grocer's business, a merger or consolidation, and a sale or distribution of its operations to a creditor or other interested party. Operations at the company's more than 200 stores have continued uninterrupted since Bi-Lo filed its voluntary Chapter 11 bankruptcy petition in March.

KB Toys Inc. won bankruptcy-court approval to auction off its intellectual property at an auction scheduled for August 6th. KB Toys filed for bankruptcy protection on Dec. 11, 2008, with plans to hold going-out-of-business sales at its stores.

Moore-Handley and the **Bostwick-Braun Company** announced that Moore-Handley received a letter of interest from Bostwick-Braun, indicating its preliminary interest in pursuing the purchase of certain of Moore-Handley's assets by a new company to be formed by Bostwick-Braun. Any deal would entail a bankruptcy court auction and approval by the court.

The **Fortunoff** and **Mayrock** families, who owned and operated **Fortunoff** for four generations, have bought back all the company's intellectual property, including the Fortunoff name. What the families plan to do with the reclaimed brand is unclear at this time.

(continued on page 4)

Did You Know...?

The index of leading economic indicators rose 0.7% in June, the Conference Board reported. The index was up 1.0% and 1.3% in April and May, respectively.

RETURN TO FIRST PAGE

Bankruptcy Blotter

(continued from page 3)

Unsecured creditors **Simon Property Group Inc.**, **Vera Bradley Designs Inc.** and others say they need more time and money to investigate debt racked up by **Crabtree & Evelyn Ltd.** in the months leading up to its bankruptcy filing. The unsecured creditors committee currently has a budget of $25,000 to probe the "pre-petition claims, liens, acts and conduct of the pre-petition lender," **KLK Overseas Investments Limited**. But the creditors want their deadline moved and funding increased so they can thoroughly explore several notes KLK issued to the seller of scented lotions and soaps in April.

The Global World of Sports and Footwear

Payless parent **Collective Brands** detailed strategic plans for its retail chain at a recent Oppenheimer & Co. conference. Payless, whose sales hit $2.6 billion in FY08, ended the year with 4,522 stores in 16 countries and territories. Women's (51%) led all product categories followed by children's (25%), men's (6%) and accessories (8%). The format is largely in strip centers (40%) followed by malls (26%), junior centers (13% and free-standing locations (11%). This FY, Payless will open 40 net new stores in Latin America with at least 25 of them situated in Colombia where the chain enjoys higher sales and ROIC than the average Payless location. In the U.S., meanwhile, Payless is increasing its focus on the Hispanic market this year with a 500 b.p. increase in marketing spending that targets the demographic.

Dick's Sporting Goods and **Gander Mountain** are at legal odds over the employment of Ken Sarber, DKS' senior buyer for fishing equipment and tackle since 2003, who recently took a similar position with Gander. DKS filed a breach of contract lawsuit against Sarber and his "new employers" on Jul. 22 in U.S. District Court in Pittsburgh. The suit alleges Sarber signed a 12-month non-compete document with Dick's that prevents him from working for any of the national chain's rivals, including Gander Mtn. and all of its affiliates, for a 12-month period.

Sport Supply Group released its preliminary annual results for the 12 months ended June 30, forecasting more than $250 million in sales and earnings of $0.84 to $0.87 per share versus $0.81 a share in FY08. RBI is also expected to show that it ended the fiscal year with more than $10 million in cash. Annual results will be officially released in late August. Meanwhile, Sport Supply, saying it's positioned to take advantage in the current challenging U.S. marketplace, initiates FY09 guidance for earnings of $0.89 to $0.97 per share.

Recreational Equipment Inc. will introduce an expanded own-brand product line in January 2010. The mix will include new and revised product and apparel offerings designed for backcountry, backpacking, active and urban lifestyles.

Dick's Sporting Goods will offer in-store web ordering, enabling sales associates to order items online for customers when they aren't available at the particular brick and mortar location. The process is currently in a pilot phase in 20 Dick's stores. Also, in 2010, according to *Internet Retailer*, Dick's intends to begin in-store merchandise pick-ups and returns from online orders. The retailer has already begun integrating its web site into all digital promotions and brick-and mortar strategies.

Schuylkill Valley Sports opens a new 5,000 sq. ft. store in Wilkes-Barre, PA. The new Wyoming Valley Mall store is Schuylkill's 18th.

West Marine Inc. settled an SEC lawsuit which had alleged the retailers had filed false financial statements. The settlement neither admitted nor denyed the SEC's allegations.

Specialty Items

Aaron's, Inc. updated its guidance for 2009 and now expects third quarter revenues of approximately $420 million, with earnings in the range of $.39 to $.44 per share. For the full fiscal year, revenues are expected to be approximately $1.75 billion, revised down from prior guidance of $1.80 billion due primarily to lower non-retail sales. Earnings are expected to be $1.95 to $2.05 per share for the year, at the high end of previous guidance of $1.90 to $2.05.

United Rentals, Inc. acquired the operating assets of Ohio-based industrial equipment rental company Leasco Equipment Services, Inc. Terms were not disclosed.

RETURN TO FIRST PAGE

Management on the Move

Ulta Salon, Cosmetics & Fragrance, Inc. elected **Lorna E. Nagler** as an independent director on the company's board. Nagler is President and CEO of Christopher & Banks Corp.

Zale Corp. appointed **Richard A. Lennox** EVP and Chief Marketing Officer. Lennox comes from J. Walter Thompson-New York, where was EVP and Director of the De Beers Group's "A diamond is forever" marketing campaign.

Finish Line, Inc. elected **Norman H. Gurwitz** as a new director. He replaced company co-founder **David I. Klapper** who is retiring. Gurwitz is an advisor to broadcasting company Emmis Communications.

Pharmaca Integrative Pharmacy appointed Mark Panzer as its CEO. Panzer was a SVP at Rite Aid Corp. from 2005 to 2008.

Stater Bros. Holdings appointed **Dave Harris** VP of Finance. Harris was most recently with accounting firm Soren McAdam Christenson.

Coldwater Creek appointed **Jerome Jessup** EVP and Creative Director. Jessup has held senior positions with Ann Taylor and Gap Inc.

Hibbett Sports, Inc. named **Rebecca Jones** VP of Merchandising. Jones is currently VP and GMM - Crafts at Jo-Ann Fabric.

Shaw's Supermarkets named **Mike Witynski** President of its Osco and Star Market division, replacing Larry Wahlstrom who is retiring. Witynski was Group VP, Our Own Brands for Supervalu.

Belk Inc. promoted SVP Operations **Ron Shealy** to replace EVP of Operations, **Jim Harvey**, who is retiring.

Cardinal Health appointed **Patricia Morrison** Chief Information Officer. Morrison has served as CIO at Motorola, Inc. and CIO of Office Depot, Inc.

Schnuck Markets Inc. appointed CFO **Todd Schnuck** as Chief Operating Officer. Six other executives were also promoted

- **Dave Bell** replaces Schnuck as CFO.
- **Ryan Cuba** was named VP of Store Operations.
- **Lori Caster** is now VP of Merchandising Reporting.
- **Mary Moorkamp**, currently general counsel and secretary, now is in charge of real estate, facilities research, loss prevention and food safety.
- **Rick Frede** was appointed Chief Talent and Strategy Officer.
- **Steve Carroll** becomes VP of Logistics.

Mass Merchant Musings

Wal-mart is pushing vendors to give the retailer more of their advertising budgets (both trade and consumer) for co-branded ads, in-store TV and banner ads on Walmart.com, *Ad Age* reported. WMT is reportedly looking for a contribution in proportion to the share of the vendor's sales that it represents.

Wal-Mart unveiled its new privacy policy governing communications with customers, *Information Week* reported. The new policy covers physical stores and online operations, and invites customers to opt-in to new channels—such as text messages and mobile phones—which suggests that the company will be exploring those areas in the future.

As **Wal-Mart** lobbies for permission to build a Chicago store in the union-dominated city, the company will hold a farmers market on the proposed south-side site.

In Washington state, **Wal-Mart** has settled an eight year old class action suit over alleged missed breaks and unpaid hours of work. WMT will pay $35 million to up to 88,000 former employees.

And up north, **Wal-Mart** is planning to open two 185,000 sq. ft. supercenters in Saskatchewan, Canada next year.

A **Kmart** in Birmingham, Alabama is the site of the first Sears-branded major appliance shop-in-shop, *TWICE* reported. The store is focused on opening-price-points models. The concept will be rolled out to additional Kmart locations, according to Sears.

Target Corp. Grand Opened 23 new stores yesterday – 21 general merchandise stores, 17 of which have expanded food options and two full-grocery SuperTarget stores.

Did You Know...?

First-time state unemployment claims rose by 30,000 to 554,000 in the week ended July 18, the Labor Department reported. The four-week moving average of first time claims fell by 19,000 to 566,000 and continuing claims also fell by 88,000 to 6.22 million for the week ended July 11.

RETURN TO FIRST PAGE

Hi Tech Entertainment

Amazon.com, Inc. noted that its lower second quarter earnings (see the scorecard) suffered from foreign exchange rate effects of $30 million. Also, AMZN's $51 million expense for the settlement with Toysrus.com and $53 million non-cash gain from the sale of its European DVD rental assets both occurred during the second quarter. Looking ahead, Amazon expects third quarter sales of $4.75 to $5.25 billion, up 11% to 23% compared with Q3 2008. Operating income is expected to be $120 to $210 million, between a 22% decline and 36% growth from Q3 last year.

Also, **Amazon.com** will acquire **Zappos.com** for $807 million. Under terms of the deal, Amazon.com, Inc. will buy all outstanding shares, warrants and options of Zappos in exchange for approximately 10 million Amazon shares. AMZN is also reportedly kicking in $40 million in cash and restricted stock bonuses for Zappos staffers. In a letter to employees, Zappos CEO Tony Hsieh confirmed that the company will be run as a wholly owned subsidiary from its Las Vegas headquarters and will maintain its Kentucky distribution center.

Barnes & Noble launched it's eBookstore at www.bn.com/ebooks, which offers more than 700,000 titles. It also introduced an upgraded version of its eReader application, using technology acquired last year as part of Fictionwise. Also, BN has partnered with Plastic Logic, who makes a large format reader device that some have dubbed a possible "Kindle killer," referring to Amazon.com's e-book reader.

Office Depot Inc. saw Ohio and California's Attorneys General open fraud investigations related to pricing practices under its $700 million dollar "U.S. Communities" contract with states and local governments.

HHGregg, Inc. priced its previously announced secondary offering of its common stock at $16.50 per share. The company also increased the number shares offered to 3.5 million, with a 525,000 share overallotment.

Blockbuster Inc. has partnered with Archos, and will sell the company's Archos 10 netbooks in Blockbuster stores, *Pacific Business News* reported.

Best Buy's European joint venture partner The Carphone Warehouse Group PLC said Best Buy Europe revenues were up 6% in its fiscal first quarter to GBP773 million. On a constant currency basis revenues increased 0.7%. Same store sales increased 5.4%, or 0.2% constant currency.

Major appliance unit sales fell 29.2% in June to just 5.7 million compared to June 2008, according to Association of Home Appliance Manufacturers data reported in *TWICE*. Last month, sales were off 17.4% year-on-year.

FYI for the DIY

Huttig Building Products, Inc. will close its Anchorage, Alaska branch. The shutdown, scheduled to be completed by Q4 2009, will result in total charges of $0.5 and $0.7 million of which approximately $0.2 million will be cash payments.

Sherwin-Williams Co. expects third quarter sales will be down 10% to 13% from last year, with net income of $1.15 to $1.45 per share compared to $1.52 per share in Q3 2008. Full year sales are expected to be off 11% to 12.5% from 2008, and net income for the year is expected to be $3.30 to $3.80 per share down from $4.00 per share in 2008.

Carter Lumber has acquired Kempsville Building Materials in Chesapeake, Virginia, which was scheduled to be closed by owner Stock Building Supply. Carter Lumber is based in Ohio and operates 195 locations in 10 states.

ProBuild Holdings acquired the leases of three lumberyards sites in Hampshire, Chicago and Elgin, Illinois from Stock Building Supply, *Building Products.com* reported. The Hampshire location will continue operating under Mark Seigle, whose family sold the yard to Stock in 2005.

Home improvement hardlines distributor **Orgill** will open its Mid-America Super Center on August 3. The 795,000 sq. ft. distribution center in Sikeston, Missouri is the company's largest.

RETURN TO FIRST PAGE

Heard in the Grocery Aisle

Did You Know...?

Existing home sales rose 3.6% in June to an annual rate of 4.89 million, up from a downwardly revised 4.72 million pace in May, the National Association of Realtors reported.

The state of New Jersey will invest $7 million in a new public-private partnership aimed at encouraging supermarket development in poor communities, the *Press of Atlantic City* reported. A similar program in neighboring Pennsylvania combined $30 million in state funding and $86 million in private investment to open 70 grocery stores there.

Weis Markets, Inc. completed the acquisition of Binghamton based Giant Markets, which operates 12 stores in Southern New York.

Winn-Dixie Stores, Inc. raised its fiscal 2009 full year guidance, and now expects sales of approximately $7.4 billion with identical stores sales up 1.2%. Adjusted EBITDA is now expected to be $164 million, above the high-end of previous guidance of $152 million. Looking ahead to fiscal 2010, WINN expects adjusted EBITDA of $170 to $180 million, assuming identical store sales of +1% to +2%.

Safeway Inc. saw its second quarter profit boosted to a year-on-year gain by $57.8 million tax benefit from the resolution of a tax matter. SWY lowered earnings guidance for the year 2009 to $1.70 to $1.90 per share assuming identical-store sales, excluding fuel, of –1.0% to –1.7%.

Great Atlantic & Pacific Tea Company, Inc. is selling $175 million of convertible preferred stock to existing shareholders in a private offering. The Yucaipa Companies, LLC will invest $115 million and Tengelmann Warenhandelsgesellschaft KG will invest $60 million. The preferred stock has a dividend of 8% of payable in cash, or 9.5% paid in additional preferred stock, and is convertible at $5.00 per share. Yucaipa will name two additional directors to GAP's board.

Also, **A&P** sales fell 4.5% to $2.790 billion for its first quarter ended June 20. Comp store sales decreased 3.3%. Net loss from continuing operations was $58.3 million compared to income of $2.8 million for last year's first quarter, which included a $48.6 million gain on fair value adjustments. Operating loss was $1.8 million, down from an operating profit of $2.1 million during the prior year period.

Loblaw Companies Ltd. will buy 17 store T&T Supermarket Inc., which focuses on the Asian market, for $225 million. The deal consists of $191 million in cash and the rest in newly issued preferred shares, the value of which will be tied to future performance.

Also, **Loblaw** expects sales and margins to be "significantly challenged" in Q3 and Q4 with declining market volumes, decreasing inflation, competition and the implementation of the company's renovation initiative.

Rating Changes & Outlooks

Company	S&P Credit Rating		S&P Credit Outlook		GCS Credit Rating
	Current	Prior	Current	Prior	Current
LANDRYS RESTAURANTS INC	B	B	NEGATIVE	STABLE	E+
BARNEYS NEW YORK INC	CCC	B-	NEGATIVE	NEGATIVE	E
DAVE & BUSTERS INC	B	B	STABLE	NM	D-
SUPERVALU INC	BB-	BB-	NEGATIVE	STABLE	D-
DEL MONTE CORP	BB-	BB-	POSITIVE	STABLE	NR
ADVANCE AUTO PARTS INC	BB+	BB+	STABLE	NEGATIVE	B
ADVANCE STORES COMPANY INC	BB+	BB+	STABLE	NEGATIVE	NR

RETURN TO FIRST PAGE

Retailer of the Week: Walgreen Co.

(continued from page 1)

files from 11 Drug Fair pharmacies, along with 32 other Drug Fair stores out of bankruptcy. This move boosted Walgreen's New Jersey presence and narrows the gap between itself and CVS.

OPERATING PERFORMANCE: 9 MONTHS ENDED MAY 31, 2009

$ in millions, 9 months ended	May 31, 2009	YOY Var.	May 31, 2008
Total Revenue	$47,632	7.2%	$44,437
Comparable Store Sales	1.9%		4.5%
Adjusted Operating Profit	$2,719	(-0.4%)	$2,730
Net Income	$1,570	(-8.4%)	$1,714
Gross Margin	27.85%	(48 bps)	28.37%
SG&A Burden	22.51%	28 bps	22.23%
Adjusted Operating Margin	5.71%	(43 bps)	6.14%
Return on Sales	3.30%	(56 bps)	3.86%
EBITDAR / (Interest Expense + Rent) *	3.17x	(31 bps)	3.48x

*- based upon EBITDA of $3.286 billion and $3.337 billion in fiscal 2009YTD and fiscal 2008YTD, respectively; annualized rent expense of $1.787 billion during fiscal 2008. We have estimated fiscal 2009 rent expense to approximate $1.9 billion.

For the nine months ended May 31, 2009, Walgreen watched its top-line improve 7.2% to $47.6 billion. During that period, the retailer's comparable store sales registered a 1.9% increase, spurred on by third quarter comps growth of 2.8%, which marked Walgreen's best figure in twelve months. Pharmacy comps, which account for nearly 65% of Walgreen's revenue base, rose 3.1% on a year-to-date basis and increased 3.8% during Q3 2009. Front-end comps have suffered a 0.2% decline on a year-to-date basis but did achieve positive growth of 0.9% in Q3 2009 (see Comparable Store Sales).

The retailer is aggressively looking to upgrade its shopping experience through its Customer Centric Retailing (CCR) project. Beyond simply rationalizing its SKUs, the druggist is looking to prioritize certain categories and within these categories, emphasize particular items in accordance with its customers' preferences. Thus far, 4,500 SKUs, or 18% of Walgreen's total SKU base, have been eliminated. These optimized assortments, to occur in a select group of pilot stores, will be accompanied with a new format marked by lower store profiles and new layouts. With respect to cost savings initiatives, Walgreen hopes that recent and future restructuring moves will contribute $500 million in cost savings in fiscal 2010 and $1 billion in cost savings in fiscal 2011. Private label business, which comprises about 20% of the chain's front-end sales, is growing at rates much faster than its drugstore peers and other retail competitors.

Total restructuring initiatives ran the company $174 million during the first nine months of fiscal 2009; severance benefits tallied $65 million, inventory writedowns totaled $44 million, consulting fees amounted to $57 million, and project cancellation settlements cost $8 million. Approximately 75% of these pre-tax charges were embedded in the firm's SG&A line, with the remainder being found in the cost of goods sold line. Excluding the impact of these one-time items, Walgreen's adjusted operating income was down only 0.4% to $2.7 billion. The firm's adjusted operating margin of 5.7%, though less than it's been in previous years, is still a more than respectable figure.

LIQUIDITY AND FINANCIAL STRUCTURE

As of May 31, 2009, Walgreen's asset-side liquidity was anchored by $2.3 billion of cash and equivalents residing on its balance sheet. The company had neither direct borrowings nor commercial paper against its two $600 million bank lines which mature in August 2009 and August 2012, respectively. Therefore, full availability existed on these bank agreements as of May's end (see Bank Reference).

(continued on page 9)

RETURN TO FIRST PAGE

Retailer of the Week: Walgreen Co.

(continued from page 8)

The druggist's previous commercial paper borrowings were eliminated thanks to the proceeds from the January 2009 issuance of $1 billion worth of 5.25% 10-year notes. Both these notes and the $1.3 billion of 4.875% five-year notes issued in July 2008 represent unsecured capital. Despite debt being up on a year-over-year basis at the drugstore chain, borrowings have become more long-term in nature since the spring of 2008. The firm's debt-to-capitalization of 14% is up from 8% one year ago but remains reasonable from our perspective. After seeing debt-to-capitalizations of 129% and 24% at Rite Aid and CVS Caremark, respectively, it's easy to understand that Walgreen's leverage picture compares favorably to its peers. Tangible net worth has risen 14% over the past twelve months to $12.7 billion.

Newly issued longer-term debt capital provided proceeds to noticeably reduce C/P borrowings and boost cash balances, helping to explain the significant 97% rise the firm's GAAP working capital to $5.3 billion. During the first nine months of fiscal 2009, cash flow from operations of nearly $3.3 billion successfully funded capital spending of $1.5 billion. While cash flow from operations was 31% higher than levels seen during the first nine months of the prior fiscal year, inventory management was a major contributor to this growth. Capital spending is expected to approximate $1.8 billion during fiscal 2009, as Walgreen looks to open 540 new drugstores (or a net increase of 475 stores after considering relocations and store closings). In addition to the 414 net store additions booked to date, Walgreen also opened a new distribution center in Windsor, Connecticut during Q2 2009. Moving forward, organic store growth will moderate by 2011 to approximately 3% to invest in the shopping experience in a prudent manner.

Looking at the cash flow statement and specifically the drugstore's ability to generate free cash flow, we remain unfazed by the level of stock repurchase activity ($140 million through nine months) and shareholder dividends ($334 million through nine months).

Off the Rack

Cache, Inc. introduced third quarter guidance for sales of $48 to $50 million, down from $58.1 million in Q3 2008, with comp store sales down mid-to-high teens vs. -4% in Q3 2008. Net loss is expected to be $0.22 to $0.17 per share from a Q3 2008 loss of $0.12 per share including charges of $0.02 per share for store closures.

Limited Brands, Inc. launched a cash tender offer for its $294.6 million in 6-1/8% Notes due 2012. The offer expires August 14. LTD is financing the purchase with proceeds from its recent offering of 8-1/2% Senior Notes due 2019.

TJX Companies, Inc. is offering $400 million of 4.20% notes due 2015. Proceeds will be used to pay its $200 million of 7.45% notes due December 15, 2009 at maturity, and to refinance the C$235 million term credit facility of its Canadian subsidiary, which is due January 11, 2010.

Nordstrom, Inc. will open its first Nordstrom Rack in Manhattan in spring 2010 – a 32,136 sq. ft. store at One Union Square South.

Pacific Sunwear warned that comp store sales fell 24% in the second quarter ended June 30 versus an expectation of a 17-20% decline. That trend combined with higher quarterly store asset impairment charges of $5.5 million has forced Pacific Sunwear to increase its Q2 loss range to $0.22 to $0.24 versus prior guidance of a $0.11 to $0.17 loss. Pacific Sunwear is slated to report Q2 results on August 20.

Charlotte Russe Holding, Inc. sales increased 4.9% to $202.7 million for the third fiscal quarter ended June 27. Comp store sales fell 3.6%. Net income was off 4.5% to $6.3 million; income would have increased but for one-time charges of $1.3 million. Looking forward to the fourth fiscal quarter, CHIC expects comp store sales in the negative low- to mid-single digits, with earnings of $0.18 to $0.26 excluding charges.

Shareholders have filed a class-action lawsuit challenging **Dress Barn**'s acquisition of **Tween Brands** arguing the price is too low. The stock swap values Tween Brands at approximately $6.22 per share, below book value and below the price TWB shares traded for last fall.

RETURN TO FIRST PAGE

Second Quarter Scorecard

$ in Millions. Quarter ended closest to 7/31/09	Sales				Net Income		
	2009	2008	Change	Comps	2009	2008	Change
Apparel							
Cache, Inc.	$56.9	$74.0	-23.1%	-23.0%	$0.8	$2.1	-59.9%
Drug							
Abbott	$7,495.0	$7,314.0	2.5%	NA	$1,288.0	$1,322.0	-2.6%
Shoppers Drug Mart (C$)	$2,288.8	$2,109.3	8.5%	5.7%	$136.1	$126.6	7.5%
Food							
Loblaw Companies Ltd (C$)	$7,233.0	$7,037.0	2.8%	2.5%	$193.0	$140.0	37.9%
Safeway, Inc.	$9,462.1	$10,120.0	-6.5%	-1.5%	$238.6	$234.3	1.8%
Weis Markets, Inc.	$615.4	$603.4	2.0%	2.4%	$15.2	$12.8	18.5%
High-Tech & Electronics							
Amazon.com, Inc.	$4,651.0	$4,063.0	14.5%	NA	$142.0	$158.0	-10.1%
Home Centers							
Builders FirstSource, Inc.	$175.5	$282.3	-37.8%	NA	($22.6)	($45.9)	50.8%
Griffin Land & Nurseries	$19.7	$21.1	-6.6%	NA	($1.0)	($0.4)	-158.1%
Sherwin-Williams Company	$1,947.8	$2,229.5	-12.6%	-13.5%	$158.0	$171.7	-8.0%
Tractor Supply Company	$946.5	$898.3	5.4%	-2.7%	$54.8	$43.4	26.3%
W.W. Grainger	$1,533.3	$1,756.9	-12.7%	tba	$92.5	$113.2	-18.3%
Wesco International	$1,159.2	$1,587.8	-27.0%	NA	$26.4	$58.0	-54.5%
Mass Merchants							
Overstock.com	$176.1	$188.8	-6.7%	NA	$0.4	($7.4)	105.4%
Specialty							
Aarons, Inc.	$417.3	$387.0	7.8%	8.4%	$27.8	$23.3	19.3%
Sports & Footwear							
West Marine, Inc.	$215.4	$226.7	-5.0%	-1.0%	tba	$6.1	tba
WinMark Corporation	$8.8	$8.7	1.4%	NA	$1.2	$0.9	28.5%

Numbers in italics are implied or company estimates.

Upcoming Reporting Dates

Company	Event	Date
Bebe Stores	Financial Results	Aug 27, 2009
Big 5 Sporting Goods	Financial Results	Aug 4, 2009
Blue Nile	Financial Results	Aug 6, 2009
Borders Group	Financial Results	Aug 25, 2009
Cabela's	Financial Results	Jul 30, 2009
CVS Caremark	Financial Results	Aug 5, 2009
Destination Maternity	Financial Results	Jul 29, 2009
Express Scripts	Financial Results	Jul 30, 2009
Golfsmith	Financial Results	Jul 30, 2009
GSI Commerce	Financial Results	Jul 29, 2009
Hibbett Sports	Financial Results	Aug 20, 2009
IAC Interactive	Financial Results	Jul 29, 2009
Ingram Micro	Financial Results	Jul 30, 2009
Interline Brands, Inc.	Financial Results	Jul 31, 2009
McKesson	Financial Results	Jul 28, 2009
Metro Inc.	Financial Results	Aug 6, 2009
Nash Finch	Financial Results	Jul 28, 2009
Nordstrom	Financial Results	Aug 13, 2009
Office Depot	Financial Results	Jul 28, 2009
OfficeMax	Financial Results	Jul 30, 2009
Pacific Sunwear	Financial Results	Aug 20, 2009
PC Connection	Financial Results	Jul 30, 2009
PC Mall	Financial Results	Aug 5, 2009
Rent-A-Center	Financial Results	Jul 28, 2009
Ross Stores	Financial Results	Aug 20, 2009
Spartan Stores	Financial Results	Jul 28, 2009
Supervalu	Financial Results	Jul 28, 2009
United Rentals	Financial Results	Jul 30, 2009
Whole Foods Market	Financial Results	Aug 4, 2009

RETURN TO FIRST PAGE