



Yale SCHOOL of MANAGEMENT

Food Retail Report *February 14, 2006*

Industry View:
Overweight

Grocery Stores

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Food Retail – US Grocery Stores

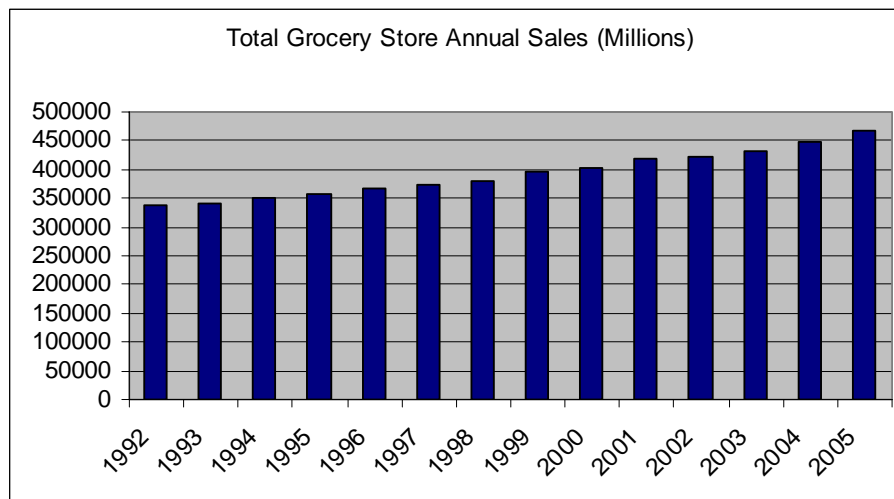
Current Price: \$50.28 billion

Price Target: \$75.16 billion

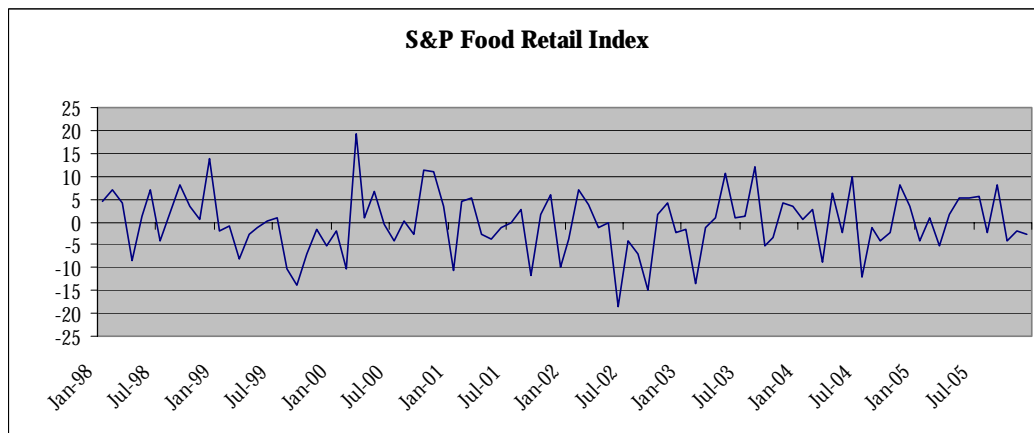
- We initiate coverage of the US Grocery Store industry with a rating of overweight.
- Though the weekly grocery shopping trip is threatened by alternative channels emerging in the market, we believe the strategy shift toward differentiation and technology upgrades will sustain the need for traditional grocery stores.
- Rising healthcare and general labor costs continue to put pressure on the already low operating margins in the industry.
- Applying a conservative sales forecast for the industry generates a combined market capitalization of \$75.16 billion compared with the market valuation of \$50.28 billion, justifying an overweight recommendation for the industry.
- Though the food industry is mature, the demand for food is inelastic and should grow in line with population and inflation.

Industry Overview

The food retail industry includes revenues generated by food sales through the following channels: supermarkets, discounters, wholesale clubs, convenience stores, independent grocers, and other retailers of food. Generally, these retailers sell food that is for preparation and consumption in the home. Many of the large supermarkets have food courts, full-service banks, postal services, flower shops, bakeries, and pharmacies. For the purpose of this report, we focused on the top ten U.S. grocery stores by market capitalization (as of February 2, 2005). In 2005, grocery stores generated \$467.2 billion in sales, a 4.3% increase from 2004 which is the largest year-over-year gain for the past thirteen years. In real terms, sales growth for 2005 was 1.78% which was almost double the 0.9% gain seen in 2004. While these numbers may seem low, they reflect the competitive and mature nature of the industry. However, supermarkets continue to be the primary source of income for the food retail market, maintaining about 55% share of the retail food market. Despite the low sales gains, the S&P Retail Food Index (KR, SWY, ABS, WIN) returned 14.5% for 2005, versus 3.8% gain in the S&P 1500. Contributing to the strong performance were to strategy shifts in the industry, consolidation, and stabilizing margins due to cost cutting efforts.



Source: US Census



Source: Bloomberg

How It Operates

Food retailing used to be a very personalized business with mom-and-pop shops where the owners lived in the neighborhood and got to know the customers, their names, how much they earned, and their preferences. As people began moving out of the cities and into suburbs, the merchants followed them and supermarket chains began to develop. Now retailers spend a great deal of money to gather information on their consumers that they previously knew firsthand. These new costs associated with researching and segmenting customers allows the retailers to market effectively and compete in the difficult environment. In addition they are able to purchase from a wide array of suppliers, bring products to their stores where customers can choose among them and purchase at cash registers. The main categories within food retailing include:

Supermarkets – generally have over 5000 square feet of selling space and more than \$2 million dollars in annual sales. This group contains traditional supermarkets, superstores (at least 40000 square feet of selling space and 25000 SKUs), combo stores (features of a superstore with a full-service drugstore), and supercenters (offer goods of a discount store and superstore in one location).

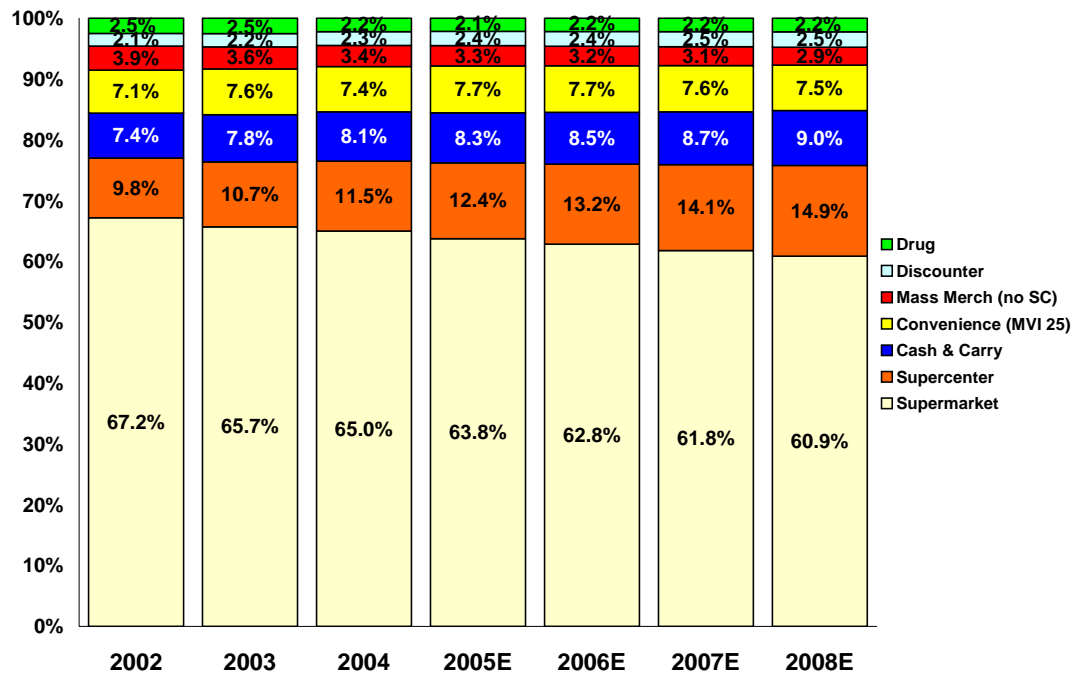
Wholesale Clubs – membership based retail in warehouse type setting that sells limited items in bulk or large sizes.

Convenience Stores – sell some groceries, prepared foods, and sometimes gasoline.

Issues

There are a number of issues affecting the food retail industry. Containing costs is an ongoing concern in this low margin business. As costs associated with retail operations have risen, there have been many consolidations in the industry in hopes of building power over suppliers and drive down prices. Also relevant are labor costs, which often represent supermarkets' greatest expense. Tied to the excessive labor costs are increasing health care costs. Like many other industries, rising health care costs are significantly affecting US grocery retailers and are cutting into margins. In an effort to curtail these costs, many of the large retailers have worked to renegotiate union contracts to increase employee contributions to health care and retirement costs. Other concerns include increasing regulatory costs and high energy prices. Regulatory costs are impacting the industry as new labeling and record keeping requirements are proving a significant expense. This will probably result in higher food prices as the retailers seek to pass the cost on to consumers. High energy costs also impact the industry in terms of reduced customer income and visits as well as high packaging and transportation costs the retailers now face. Low unemployment rates also hurts this labor intensive industry, as reliable employees are difficult to attract and retain. Wal-Mart and "supercenters" are also an issue for food retailers as they continue to operate with their Everyday Low Price strategy, engage in store expansion, and pay lower labor costs than supermarkets (since they do not employ union workers). As Wal-Mart plans to add 60 million square feet of retail space through 2007, some estimates have them taking on a 20% market share of the US grocery market in the coming years. The supercenter format has stolen significant share of total food and related product sales from traditional supermarket operators in recent years. The share

shift is predominantly driven by Wal-Mart's aggressive rollout of its supercenter format through new stores and retrofits of existing discount stores into the larger supercenter format. Research from Management Ventures Inc. measures this share shift to decrease traditional supermarkets total share of food sales by 6.1% between 2002 and 2008.



Source; MVI Research, NACDS & Census

Trends

With increased competition from new players and technologies, supermarkets are changing the way they do business...a big move for the mature industry. In recent years, some stores have moved away from the weekly special model and toward the every day low prices to compete with the discount stores. Going forward, instead of competing on price, grocery stores are trying to compete by offering distinct products and services. Creating a brand (generating loyalty), upgrading to more upscale products, downgrading to cheaper products, and providing differentiated products and services are how these firms will seek out growth and market share. This strategy shift is not only a response to the Wal-Marts of the world, but also online grocers, organic retailers and other alternatives and could be a valuable boost for the industry.

Traditional food retailers are now targeting customers that value service and saving time over saving money. Providing more convenience, cleaner stores, and better options will be the focus to differentiate from each other, especially the superstores, which will better poise the grocery stores to serve consumers and generate sales. The strategy to highlight upscale products will complement the recent trend for natural and organic foods. With the success of

many specialty retailers like Trader Joe's and Whole Foods, consumer interest in this segment is sustainable at least for the medium term. In addition to gourmet and organic foods, stores like Safeway are looking to add wine and roses to their aisles as well as classes on flower arranging to define them as an upscale provider. While some stores are focusing on capturing the upper part of consumers, other stores such as Albertson's Super Saver banner, are focusing on the lower end offering limited-assortment stores with lower prices. This strategy to leave the middle market to the supercenters and focus on the outer markets should work to the benefit of these companies.

Store-branded products continue to become more prevalent in today's markets. According to ACNielsen, sales of private-label goods have grown at more than twice the rate of branded goods. These products continue to gain acceptance by consumers and now account for 15% of supermarkets' packaged-goods revenue. This growth benefits the grocers since these products have wider profit margins.

Some steps taken to increase efficiency include the addition of self-checkout centers. While customer acceptance of these are still to be seen, they speed up checkout, give a modern appearance, and allow the consumer a more personal shopping experience. Also being implemented are checkout centers that give shoppers ids and the ability to checkout using their finger. This technology allows customers to register for the program by scanning their finger and registering a credit/debit card. They are then issued an identification number and can then proceed to checkout and pay by scanning their finger. Other technological advancements include checkouts that can scan the entire cart without the usual transfer to a conveyor belt (this could also reduce labor costs by eliminating cashiers). While in the short run these unique elements will improve convenience for grocery shoppers, if successful, supercenters or other competitors could adopt the same technology and the differentiation benefit would dissolve.

As mentioned above online grocers present a different type of competition for the grocery stores. There are two types of e-grocers:

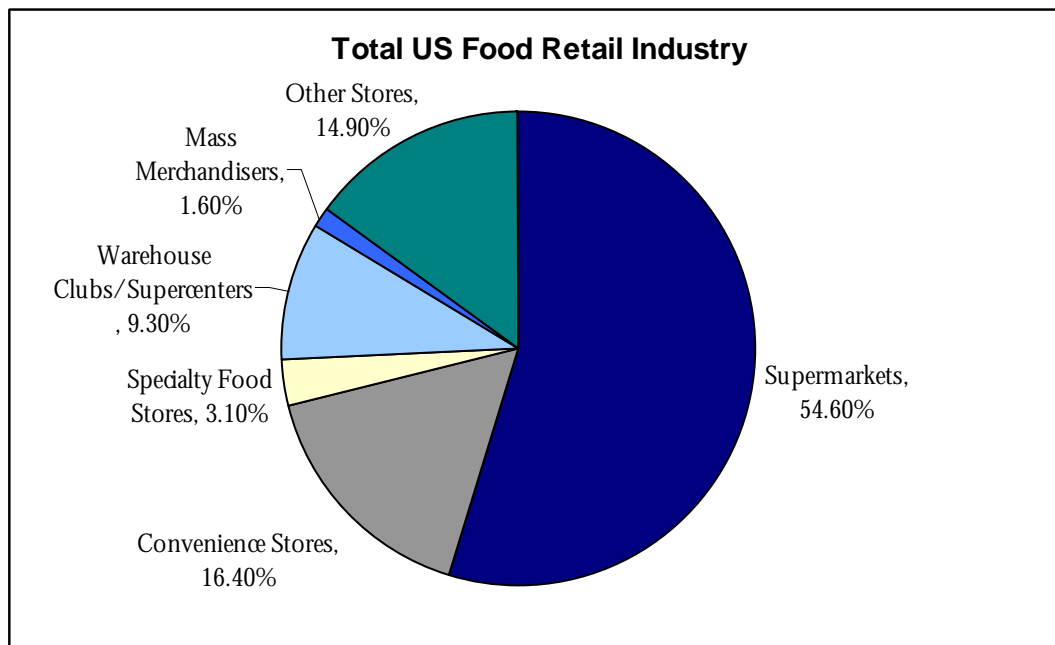
Bricks & Clicks – traditional grocers that also offer online shopping
Pure Plays – organizations that solely sell online

Though stand-alone efforts such as Webvan have failed, the field has significantly improved since 2003 as they pursue growth one city at a time, a more controlled expansion than those developed during the dot.com phase. While this seems to still be a niche market Forrester research projects growth to be 46% this year, to \$3.5 billion.

Consolidation has been a trend in this industry for a long time with the most recent deal involving the sale of Albertsons to SUPERVALU, CVS, and other investors. This deal, and others like it, significantly and quickly increase number of stores and market share for the buyers. These consolidations can reduce competitive pricing pressures and improve operating profitability, as the companies are able to leverage overhead expenses over more stores. Also in line with this additional source of growth, some companies are seeking to unlock real estate value. This is a trend across the retail industry that may not be sustainable if real estate values decline as predicted.

Top Ten US Food Retail (by market cap) \$mm	
Publix Super Markets	14966.4
Kroger Co.	13269.1
Safeway Inc.	10576.5
Whole Foods Market Inc.	10106.8
Albertson's Inc.	9287
SUPERVALU Inc.	4321.3
The Great Atlantic & Pacific Tea Co.	1290.1
Casey's General Stores Inc.	1258.7
Weis Markets Inc.	1160.2
Ruddick Corp	1104.1
Industry Overall - Food Retail	211703.4

Source: CapitalIQ as of February 2, 2006)



Competitive Analysis

Rivalry Among Existing Firms – High

Threat of New Entrants – Medium

Threat of Substitutes – High

Bargaining Power of Buyers – Low

Bargaining Power of Suppliers - Low

Rivalry among existing firms is high in this industry. The slow growth, low margin industry means that companies are always fighting for market share. Companies are not only competing on price, but also differentiated products and services. Operating margins in the industry have decreased from a 4% range through 2002 to 3% in 2004. While labor and product cost-cutting efforts could improve margins and consolidation should have some

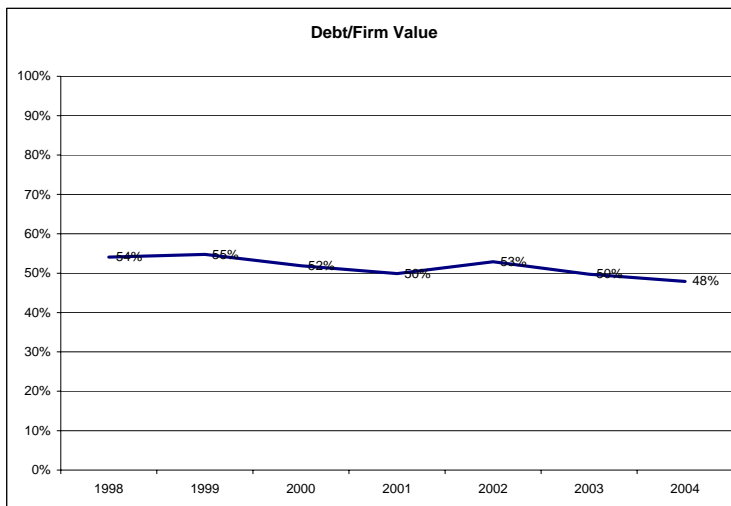
impact on pricing pressures and margins, it is not yet clear how the new marketing/operating strategies will actually affect growth.

There is a medium threat of new entrants. There is significantly high start-up costs associated with entering this industry. In addition, it is difficult to establish favorable supply contracts or leases and compete with large retailers that benefit from centralized buying. Especially as supermarkets begin to distinguish themselves and work on branding, it may be more difficult to capture customers. Though the new operation strategy may actually push up prices as the stores seek to establish a reputation of high quality. This effect may drive some customers to discount stores or supercenters. Also a consideration is the benefit a regional operator might have; knowing your constituency is a significant factor for this type of business and the large, chain retailers may find it difficult to develop nationwide strategies that are successful across various regions.

The threat of substitutes is high, though we might not think of giving up the weekly trip to the supermarket. These substitutes come in many forms including Wal-Mart as mentioned above. Supercenters have been gaining market share significantly over the past few years and will continue to do so as they increase sale space. In addition, warehouse clubs are beginning to expand their product offerings particularly in the fresh food category overlapping even more with the traditional supermarkets. Specialty stores are also a significant threat to grocery stores as the trend for natural and organic foods continues to boost sales at stores like Trader Joes and Wild Oats. E-grocers are an advancement that could change the way customers shop for groceries. However, if the grocery stores are able to successfully reposition themselves and provide unique products and services, these other store types will be more compliments than substitutes.

Bargaining power of buyers is low in this industry. It is generally not the case that you can negotiate the price of milk at the store. While coupons or buying items on special allows the customer to pay reduced prices, there is little the customer can do to alter the selling patterns of the grocery store. However, the consumer base as a whole drives trends and demands high quality products at reasonable prices, which does influence the stores.

Bargaining power of suppliers is low in this industry. The consolidations give the large retailers more influence in terms of negotiating contracts. Since large retailers are able to leverage their size in negotiations, the suppliers do not have much bargaining power. Especially for smaller supply companies, large contracts can make or break their business and they try to remain as accommodating as possible to retain the relationships. Not having placement in one of the three largest grocery channels is simply not an option for many traditional food manufacturers. The introduction of RFID (Radio Frequency Identification) into the industry will also lead to reduced costs and the stores being able to get specific products and certain amounts on demand as they can locate any good along the supply chain. Also relevant are slotting fees. Grocers are now moving away from the old practice of charging product makers for shelf space and other promotions. This practice not only reduces costs (paid to suppliers and internal accountants and staff dealing with the transactions), but also gives the grocers more control over which products to purchase, how much of it, and how it should be displayed. Though these fees are far from being entirely eliminated, the move in this direction works well in conjunction with the plan to be more deliberate in selecting products and consumers to target.

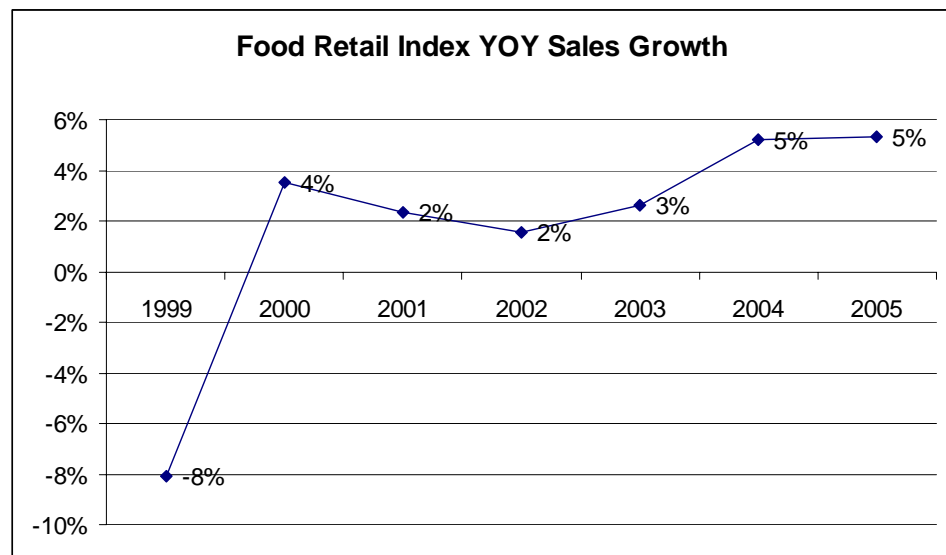


Valuation

WACC or APV? We calculated the debt to value for the companies in our index for the last seven years and found the ratio to be relatively constant between 48% to 55% over time. For this reason we chose to use the discounted cash flow method to arrive at a valuation for the industry.

Sales Forecast

There are various and often conflicting opinions of the growth of the food retail sector. Holding all other factors constant one would not expect there to be drastic fluctuations in aggregate food sales given food is a necessity in every day life. General estimates for the growth in overall food retail range from 2%-4% over the next 5-10 years. The question for the traditional US grocery stores included in our industry index is what will be there share of future growth in food sales and how will the increasing acceptance of alternative channels of food

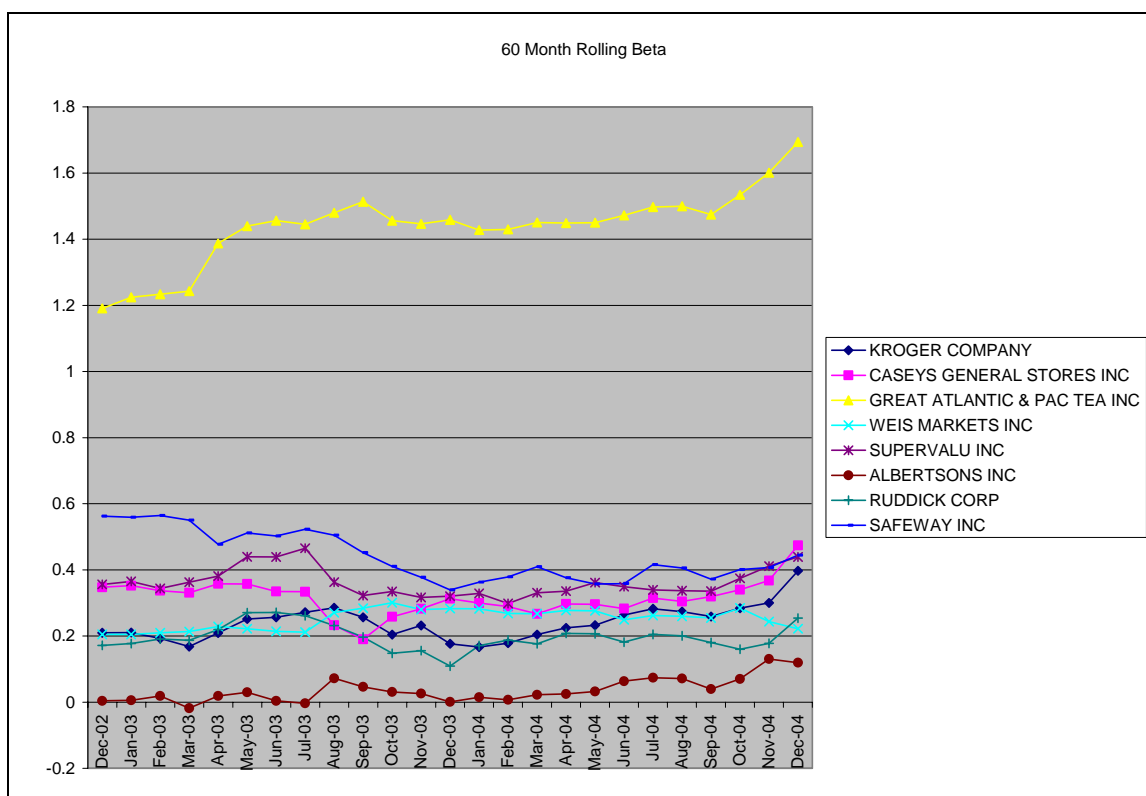


retail including supercenters impact total sales growth moving forward. Sales trended downward through 2002 and recently saw a slight increase in 2003 and 2004 as many of the traditional grocers responded to increased competition with operational improvements. Given the fact that the majority of the grocers included in our index are traditional operators with mature store growth and expansion opportunities it is not likely that they will be able to sustain growth rates in the 5% range moving forward. Because Whole Foods is included in our index and we expect their expansion to drive sales in the near future we predict sales growth for the index in the 3%-4% range for the near future and then dropping off to 2% as a

terminal growth rate. Our terminal year was chosen as 2012 as this was the year the industry was projected to begin earning zero economic profits.

Beta Estimation

We applied several methods to estimate an equity beta for the industry. Our first method was to take monthly returns for all but two of the retailers in our index, Whole Foods and Publix, because data was not available in the WRDS database. We then regressed the excess monthly returns from 1998 through 2004 with the excess returns of the market over the same period for each retailer. To check for consistency we also ran 60 month rolling betas for the eight retailers over the same period.



The resulting beta's varied widely amongst the retailers and to arrive at an industry equity beta estimate we took a market capitalization weighted average of the eight grocers in our sample arriving at a final value of .40. For further accuracy, we un-levered each individual grocer's equity beta using the equation $\beta_A = \beta_E [E + D/E]$ and took a market capitalization based weighted average of the resulting asset betas. We assumed a β_d of zero due to the fact that debt betas are typically very low reflecting the first priority of debt

Company	β_E	β_A
KROGER COMPANY	0.34	0.11
SAFEWAY INC	0.56	0.23
ALBERTSONS INC	0.13	0.06
SUPERVALU INC	0.51	0.43
GREAT ATLANTIC & PAC TEA INC	1.42	0.38
CASEYS GENERAL STORES INC	0.46	0.38
WEIS MARKETS INC	0.26	0.26
RUDDICK CORP	0.33	0.27

claimants.¹ The resulting industry asset beta was then re-levered using the formula $\beta_E = \beta_A[1 + D/E]$ using the industry's average debt to equity ratio to arrive at an equity beta estimate of .36.

WRDS DATA DRIVEN	
Capital Asset Pricing Model	
Industry Weighted Average Equity Beta	0.400
Industry Weighted Average Asset Beta	0.187
Re-levered Industry β_E	0.360
R_f	0.035
Risk Premium	0.060
R_E	0.057
WACC	
RE	0.057
Tax Rate	0.4
D	20,807,792
E	22,613,434
D+E	43,421,226
R_d	0.080
WACC	0.053

Our next step was to calculate the index's required return on equity by using the Capital Asset Pricing model: $R_E = R_F + \beta_E(R_m - R_f)$ imputing the following assumptions:

- A risk-free rate of .035 subtracting 1% from the 10-year treasury rate of 4.54%.
- A historic market risk premium of 6%

The resulting return on equity for the industry was 5.7%.

To check the accuracy of our beta calculations we performed two different checks. The first was to take the returns on the S&P Food Retail Index (Kroger, Albertson's, Safeway, and Winn Dixie) and calculate Beta using the same technique as before. This resulted in a beta of .30, which was inline with the individual numbers calculated for Kroger, Albertson's and Safeway in our previous index.

The second check we performed was to pull the current beta's listed for the retailers by Bloomberg. The current Bloomberg Betas were much higher than those calculated using historic returns through 2004 resulting in a weighted average of 1.04 for the industry. Without more detailed information about possible calculation differences in the current Bloomberg estimate and our own calculated Beta we assumed that a partial explanation is that the returns of the food retailers

have become more volatile in recent years and are now closer to the returns on the market resulting in a beta of 1. In order to control for the difference between the two estimates we chose to use the smoothing technique to improve our original beta estimate using the equation: Adjusted Beta = (.33) + (.67) Raw Beta². The smoothing formula helps to adjust

Smoothed Beta	
Capital Asset Pricing Model	
Industry Weighted Average Equity Beta	0.365
Industry Weighted Average Asset Beta	0.175
Re-levered Industry β_E w/smoothing	0.555
R_f	0.035
Risk Premium	0.060
R_E	0.069
WACC	
RE	0.069
Tax Rate	0.4
D	20,807,792
E	22,613,434
D+E	43,421,226
R_d	0.080
WACC	0.058796

¹ Valuation. *Measuring and Managing the Value of Companies*. Tim Koller, Marc Goedhart, and David Wesels. McKinsey&Company, 1990. p. 312-313

² Koller, Goedhart, Wessels p. 314

our betas towards 1 and eliminates some of the discrepancy of using older returns in our data sample. Using this technique arrives at a smoothed Beta of .56 and a corresponding return of equity of 7%.

WACC

Using the return on equity generated from the CAPM, we used the average tax rate and debt level of the industry to calculate the weighted average cost of capital of 5.9% in our smoothed Beta model. To calculate the cost of debt we first looked at the corporate ratings for the retailers in the index and found that many were unrated or unavailable. The major players, Kroger, Safeway and Supervalu, were all rated above investment grade eliminating any concern about interest rates overstating the true cost of debt. In light of an average index debt rating, we divided the total industry interest payments by the debt outstanding and arrived at a cost of debt of 8% for the industry.

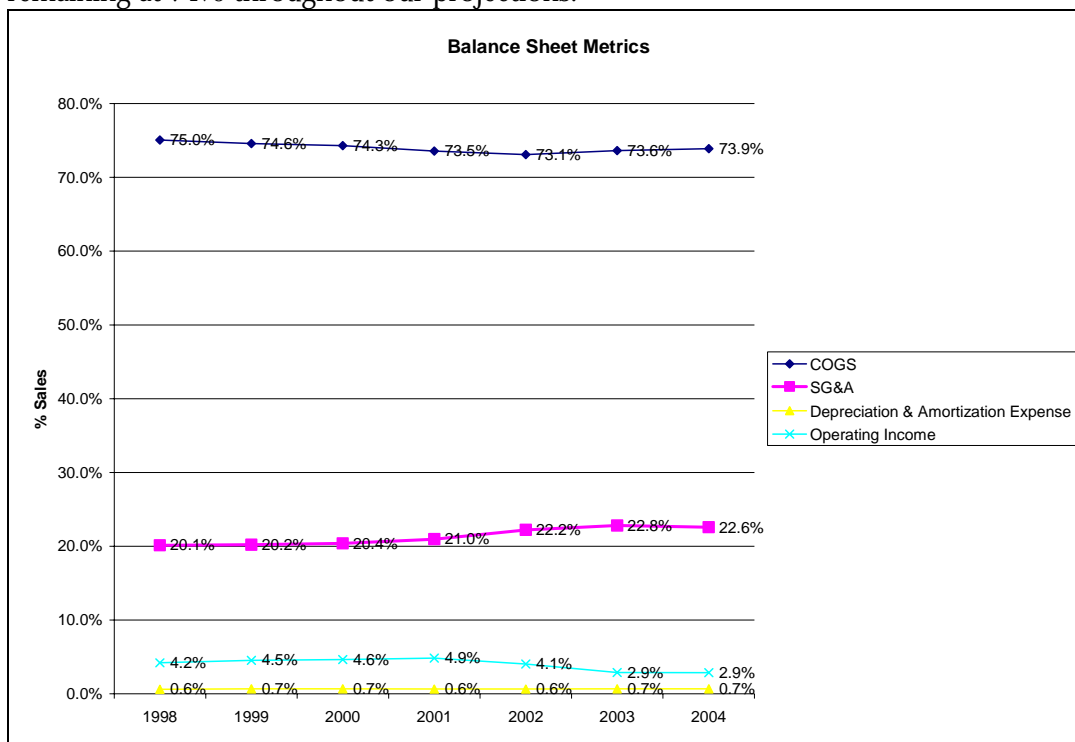
Discounted Cash Flows

To calculate a final valuation of the industry we used the aggregate balance sheet and income statements for the ten retailers in our index. Looking at the various balance sheet items as a percentage of sales over time revealed consistent results particularly in the past two to three years. Given the mature nature of the industry we projected the balance sheet line items at a constant percentage of sales as the 2004 numbers.

	A	B	C	D	E	F	G	H	I
3									(% of Sales)
4	year of fiscal y/end	1999	2000	2001	2002	2003	2004	2005	Assumptions
5									apply to 2005 on
6	Balance Sheet (000's)								
7	Cash + M/S	1,050,384	743,625	368,545	588,215	1,564,647	2,056,748	2,663,469	1.4%
8	% of Sales	0.8%	0.5%	0.3%	0.4%	1.0%	1.3%	1.6%	
9	Accounts Receivable	2,201,746	2,320,382	2,263,171	2,324,986	2,262,941	2,297,666	2,376,010	1.4%
10	% of Sales	1.6%	1.6%	1.5%	1.6%	1.5%	1.4%	1.4%	
11	Inventories	11,820,729	11,796,283	11,255,771	11,430,652	11,436,121	11,796,546	11,843,827	6.8%
12	% of Sales	8.6%	8.2%	7.7%	7.7%	7.5%	7.3%	7.0%	
13	Other Current Assets	1,367,570	1,280,997	4,032,432	1,452,307	1,631,701	1,474,473	1,236,940	0.90%
14	% of Sales	1.0%	0.9%	2.8%	1.0%	1.1%	0.9%	0.7%	
15	Current Assets	16,440,429	16,141,287	17,959,919	15,802,160	16,908,410	17,642,433	18,120,246	
16	Net PP&E	27,142,841	29,355,610	30,075,252	31,938,477	32,520,045	34,712,987	34,433,098	Plug
17	% of Sales	19.6%	20.5%	20.5%	21.5%	21.3%	21.6%	20.4%	
18	Intangibles & Goodwill	11,952,380	11,763,192	10,497,325	9,992,225	8,861,839	9,650,533	9,735,619	5%
19	% of Sales	8.7%	8.2%	7.2%	6.7%	5.8%	6.0%	5.8%	
20	Other Long Term Assets	2,194,801	2,189,512	2,278,230	2,222,430	1,826,515	1,833,269	1,748,098	1.8%
21	% of Sales	1.6%	1.5%	1.6%	1.5%	1.2%	1.1%	1.0%	
22	Total Assets	57,730,451	59,449,601	60,810,726	59,955,292	60,116,809	63,839,222	64,037,061	
23	Accounts Payable	8,529,378	8,745,714	8,053,474	8,307,698	7,379,141	8,671,330	9,302,635	5.4%
24	% of Sales	6.2%	6.1%	5.5%	5.6%	4.8%	5.4%	5.5%	
25	Debt in Current Liabilities	1,975,451	1,090,296	1,237,918	1,291,683	1,350,229	1,208,405	1,393,960	
26	Other Current Liabilities	5,797,284	5,514,752	6,111,082	5,359,922	6,698,999	6,685,199	6,535,943	4.0%
27	% of Sales	4.2%	3.9%	4.2%	3.6%	4.4%	4.2%	3.9%	
28	Current Liabilities	16,302,113	15,350,762	15,402,474	14,959,303	15,428,369	16,564,934	17,232,538	excl. curr. debt
29	Long Term Debt	21,508,095	21,862,840	21,879,146	22,137,222	20,470,937	20,619,434	18,584,569	
30	Other Long Term Liabilities	3,954,858	4,531,055	4,917,133	6,567,826	7,115,982	8,797,534	7,999,345	4.6%
31	% of Sales	2.9%	3.2%	3.4%	4.4%	4.7%	5.5%	4.7%	
32	Total Liabilities	41,765,066	41,746,800	42,198,753	43,664,351	43,015,288	45,981,902	43,816,452	
33	Book Value of Common Stock	15,965,385	17,702,801	18,611,973	16,290,941	17,101,521	17,857,320	20,220,609	
34	Current Debt + LT Debt + Common Equity	39,448,931	40,655,937	41,729,037	39,719,846	38,922,687	39,685,159	40,199,138	plug

On the income statement, the major decision to be made was how to forecast Selling, General, and Administrative expense over time. In recent years, the grocers have faced significant upward pressure on SG&A primarily driven by increasing labor costs. Since 2001 SG&A as a % of sales increased from 21% of sales to 22.6% of sales in 2004. Moving forward we predict that the pressures on labor will increase in addition to the rising cost of health insurance. Moving forward, we forecast SG&A to represent 22.9% of the grocer's sales. In terms of Cost of Goods sold, this metric has been fairly constant at around 74% percent of sales over

the past six years and we do not predict a significant deviation in this metric moving forward remaining at 74% throughout our projections.



We discounted the future cash flows from 2006 through 2009 applying our balance sheet and income statement projections to arrive at an industry valuation of 86 billion using our smoothed beta. As of February 2006, the combined market capitalization for the retailers in our index was 67.3 billion leading us to a recommendation of overweight for the index. We believe that the implied discount factor of the current market valuation of 6.6% is too high and does not properly reflect the stability of the industry as a necessary component of American's retail expenditures.

Market Cap 5/06 (000s)	
KR	13680000
SWY	10690000
ABS	9260000
SVU	4300000
WMK	1170000
RDK	1130000
Whole Foods	10050000
Total Index Market Capitalization	50,280,000
Valuation w/ Smoothed Beta	75,162,852

Sensitivity analyses were used to confirm our recommendation. First, WACC was calculated at various levels of return on equity and Beta estimates. The results show that even a beta in the range of .7, compared with our smoothed beta of .57, results in a return on equity of 7.7%

and a market valuation of 74 billion dollars, still significantly higher than the current market value of 67 billion.

Sensitivity Anlaysis		Sensitivity Anlaysis	
Beta	R _E	R _E	WACC
0.50	6.5%	6.5%	5.7%
0.60	7.1%	7.1%	6.0%
0.70	7.7%	7.7%	6.3%
0.80	8.3%	8.3%	6.6%
0.90	8.9%	8.9%	7.0%
1.00	9.5%	9.5%	7.3%
1.10	10.1%	10.1%	7.6%

Sensitivity Analysis	
WACC	Market Value D+E
5.7%	93,447,684
6.0%	83,143,768
6.3%	74,374,918
6.6%	66,829,604
7.0%	60,274,917
7.3%	54,533,258
7.6%	49,466,844

Smoothed Beta Discounted Cash Flow Valuation

month of fiscal y/end year of fiscal y/end sales growth	projections							
	2006 4%	2007 3%	2008 3%	2009 3%	2010 2%	2011 2%	2012 2%	
Free cash flow projections								
NOPAT (after-tax EBIT), assuming a 40% tax rate	\$ 4,470,003	\$ 4,604,103	\$ 4,742,226	\$ 4,884,493	\$ 4,982,182	\$ 5,081,826	\$ 5,183,463	
+ depreciation and amortization	\$ 4,078,983	\$ 4,201,352	\$ 4,327,393	\$ 4,457,215	\$ 4,546,359	\$ 4,637,286	\$ 4,730,032	
-changes in current assets	\$ (341,012)	\$ (553,838)	\$ (570,453)	\$ (587,566)	\$ (403,462)	\$ (411,532)	\$ (419,762)	
+changes in current liab (other than current debt)	\$ 337,001	\$ 485,267	\$ 499,825	\$ 514,820	\$ 353,510	\$ 360,580	\$ 367,792	
- Capex	\$ (3,692,252)	\$ (3,803,019)	\$ (3,917,110)	\$ (4,034,623)	\$ (4,115,316)	\$ (4,197,622)	\$ (4,281,574)	
-changes in other LT assets	\$ (1,416,689)	\$ (94,944)	\$ (97,792)	\$ (100,726)	\$ (69,165)	\$ (70,548)	\$ (71,959)	
-change in intangibles	\$ 944,544	\$ (263,732)	\$ (271,644)	\$ (279,794)	\$ (192,125)	\$ (195,967)	\$ (199,887)	
+ changes in LT liabilities (other than debt)	\$ 88,444	\$ 242,634	\$ 249,913	\$ 257,410	\$ 176,755	\$ 180,290	\$ 183,896	
=fcf to D+E	\$ 4,469,021	\$ 4,817,823	\$ 4,962,358	\$ 5,111,229	\$ 5,278,739	\$ 5,384,313	\$ 5,491,999.54	
fcf check (= NOPAT- change in BV of D+E)	4,469,021	4,817,823	4,962,358	5,111,229	5,278,739	5,384,313	5,492,000	
YoY growth		8%	3%	3%	3%	2%	2%	
WACC	5.88%	5.88%	5.88%	5.88%	5.88%	5.88%	5.88%	
PV of fcf 2004	4220853	4297605	4180725	4067023	3967065	3821707	3681674	
terminal growth	2%							
2011 fcf	4067023							
terminal value at 1/2012:	104,831,848							
PV of terminal value as of 2005	74,408,109							
PV of remaining fcf	20,733,272							
unadjusted PV of D+E as of 2005	95,141,381							
subtract debt in 2005	(19,978,529)							
PV of E as of 1/2005	75,162,852 (000s)							
Net Income	3,694,229.8	3,511,033.2	3,645,133.3	3,783,256.3	3,925,523.1	4,023,213.0	4,122,856.6	4,224,493.1
Equity	20,221,590	20,007,870	19,787,737	19,561,001	19,264,445	18,961,958	18,653,421	18,253,081
EVA	2,505,288	2,334,657	2,481,700	2,633,154	2,792,857	2,908,332	3,026,116	4,224,493
	2,131,446.83	1,912,750.86	2,046,850.94	2,184,974.02	2,327,240.79	2,424,930.64	2,524,574.29	2,626,210.81

Income Statement- Actuals

	A	B	C	D	E	F	G	H
2	year of fiscal y/end	1999	2000	2001	2002	2003	2004	2005
3								
4	Income Statement (000's)				7,318,019.00			
5	Sales	\$ 138,151,219	\$ 143,054,581	\$ 146,395,708	\$ 148,647,537	\$ 152,576,210	\$ 160,528,399	\$ 169,059,141
6	YoY growth		4%	2%	2%	3%	5.2%	5.3%
7	COGS	\$ 103,319,268	\$ 106,504,156	\$ 107,756,608	\$ 108,692,571	\$ 112,610,867	\$ 118,867,194	\$ 125,670,363
8	% of Sales	74.8%	74.5%	73.6%	73.1%	73.8%	74.0%	74.3%
9	SG&A	\$ 27,190,270	\$ 28,364,636	\$ 29,960,276	\$ 32,636,947	\$ 34,515,184	\$ 36,129,152	\$ 36,791,911
10	% of Sales	19.7%	19.8%	20.5%	22.0%	22.6%	22.5%	21.8%
11	Non-Operating Income	\$ (667,684)	\$ (318,231)	\$ (694,323)	\$ 24,955	\$ 7,806	\$ 164,218	\$ 64,842
12		-0.5%	-0.2%	-0.5%	0.0%	0.0%	0.1%	0.0%
13	Operating Income	\$ 6,973,997	\$ 7,867,558	\$ 7,984,501	\$ 7,342,974	\$ 5,457,965	\$ 5,696,271	\$ 6,661,709
14	% of Sales	5.0%	5.5%	5.5%	4.9%	3.6%	3.5%	3.9%
15	Interest Expense	1,529,616	1,660,078	1,652,685	1,620,578	1,623,876	1,622,887	1,562,783
16	Cost of Debt	6.7%	7.2%	7.1%	7.4%	7.4%	8.1%	7.8%
17	Pretax Income	\$ 5,444,381	\$ 6,207,480	\$ 6,331,816	\$ 5,722,396	\$ 3,834,089	\$ 4,073,384	\$ 5,098,926
18	% of Sales	4%	4%	4%	4%	3%	3%	3%
19	Tax Expense	\$ 1,959,168	\$ 2,091,384	\$ 2,110,882	\$ 2,212,873	\$ 1,425,606	\$ 1,245,999	\$ 1,404,696
20	% of Pretax Income	36%	34%	33%	39%	37%	31%	28%
37								

Income Statement - Forecast

	A	I	J	K	L	M	N	O	P
2	year of fiscal y/end	2006	2007	2008	2009	2010	2011	2012	2013
3									
4	Income Statement (000's)								
5	Sales	175,821,507	181,096,152	186,529,036	192,124,907	195,967,406	199,886,754	203,884,489	207,962,179
6	YoY growth	4%	3%	3%	3%	2%	2%	2%	2%
7	COGS	135,382,560	139,444,037	143,627,358	147,936,179	150,894,902	153,912,800	156,991,056	160,130,878
8	% of Sales	77.0%	77.0%	77.0%	77.0%	77.0%	77.0%	77.0%	77.0%
9	SG&A	38,263,587	39,411,495	40,593,840	41,811,655	42,647,888	43,500,846	44,370,863	45,258,280
10	% of Sales	21.8%	21.8%	21.8%	21.8%	21.8%	21.8%	21.8%	21.8%
11	Non-Operating Income	\$ 5,274,645	\$ 5,432,885	\$ 5,595,871	\$ 5,763,747	\$ 5,879,022	\$ 5,996,603	\$ 6,116,535	\$ 6,238,865
12		3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
13	Operating Income	\$ 7,450,004	\$ 7,673,504	\$ 7,903,710	\$ 8,140,821	\$ 8,303,637	\$ 8,469,710	\$ 8,639,104	\$ 8,811,886
14	% of Sales	4.2%	4.2%	4.2%	4.2%	4.2%	4.2%	4.2%	4.2%
15	Interest Expense	1,598,282	1,598,282	1,598,282	1,598,282	1,598,282	1,598,282	1,598,282	1,598,282
16	Cost of Debt	8%	8%	8%	8%	8%	8%	8%	8%
17	Pretax Income	5,851,722	6,075,222	6,305,427	6,542,539	6,705,355	6,871,428	7,040,822	7,213,604
18	% of Sales	3%	3%	3%	3%	3%	3%	3%	3%
19	Tax Expense	\$ 2,340,689	\$ 2,430,089	\$ 2,522,171	\$ 2,617,015	\$ 2,682,142	\$ 2,748,571	\$ 2,816,329	\$ 2,885,442
20	% of Pretax Income	effective tax rate assumed for projections is 40%							

Balance Sheet Projections

	A	K	L	M	N	O	P	Q
4	year of fiscal y/end	2006	2007	2008	2009	2010	2011	2012
5		813,158						
6	Balance Sheet (000's)	30,417,121						
7	Cash + M/S	2,461,501	2,535,346	2,611,407	2,689,749	2,743,544	2,798,415	2,854,383
8	% of Sales	1.4%	1.4%	1.4%	1.4%	1.4%	1.4%	1.4%
9	Accounts Receivable	2,461,501	2,535,346	2,611,407	2,689,749	2,743,544	2,798,415	2,854,383
10	% of Sales	1.4%	1.4%	1.4%	1.4%	1.4%	1.4%	1.4%
11	Inventories	11,955,862	12,314,538	12,683,974	13,064,494	13,325,784	13,592,299	13,864,145
12	% of Sales	6.8%	6.8%	6.8%	6.8%	6.8%	6.8%	6.8%
13	Other Current Assets	1,582,394	1,629,865	1,678,761	1,729,124	1,763,707	1,798,981	1,834,960
14	% of Sales	0.9%	0.9%	0.9%	0.9%	0.9%	0.9%	0.9%
15	Current Assets	18,461,258	19,015,096	19,585,549	20,173,115	20,576,578	20,988,109	21,407,871
16	Net PP&E	34,046,367	33,648,033	33,237,750	32,815,158	32,384,115	31,944,450	31,495,993
17	% of Sales	19.4%	20.8%	20.8%	20.8%	20.8%	20.8%	20.8%
18	Intangibles & Goodwill	8,791,075	9,054,808	9,326,452	9,606,245	9,798,370	9,994,338	10,194,224
19	% of Sales	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
20	Other Long Term Assets	3,164,787	3,259,731	3,357,523	3,458,248	3,527,413	3,597,962	3,669,921
21	% of Sales	1.8%	1.8%	1.8%	1.8%	1.8%	1.8%	1.8%
22	Total Assets	64,463,487	64,977,668	65,507,273	66,052,767	66,286,476	66,524,859	66,768,009
23	Accounts Payable	9,142,718	9,417,000	9,699,510	9,990,495	10,190,305	10,394,111	10,601,993
24	% of Sales	5.2%	5.2%	5.2%	5.2%	5.2%	5.2%	5.2%
25	Debt in Current Liabilities	1,393,960	1,393,960	1,393,960	1,393,960	1,393,960	1,393,960	1,393,960
26	Other Current Liabilities	7,032,860	7,243,846	7,461,161	7,684,996	7,838,696	7,995,470	8,155,380
27	% of Sales	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
28	Current Liabilities	17,569,539	18,054,806	18,554,631	19,069,451	19,422,961	19,783,541	20,151,333
29	Long Term Debt	18,584,569	18,584,569	18,584,569	18,584,569	18,584,569	18,584,569	18,584,569
30	Other Long Term Liabilities	8,087,789	8,330,423	8,580,336	8,837,746	9,014,501	9,194,791	9,378,686
31	% of Sales	4.6%	4.6%	4.6%	4.6%	4.6%	4.6%	4.6%
32	Total Liabilities	44,241,897	44,969,798	45,719,536	46,491,766	47,022,031	47,562,901	48,114,588
33	Book Value of Common Stock	20,221,590	20,007,870	19,787,737	19,561,001	19,264,445	18,961,958	18,653,421
34	Current Debt + LT Debt + Common Equity	40,200,119	39,986,399	39,766,266	39,539,530	39,242,974	38,940,487	38,631,950

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