
**Kroger Co. (The)**

**S&P Recommendation**: HOLD ★ ★ ★ ★ ★

**GICS Sector**: Consumer Staples

**Sub-Industry**: Food Retail

**Summary**: This supermarket operator, with about 2,500 stores in 31 states, also operates convenience stores, jewelry stores, supermarket fuel centers, and food processing plants.

**Key Stock Statistics**

<table>
<thead>
<tr>
<th>52-Wk Range</th>
<th>Trailing 12-Month P/E</th>
<th>$10K Invested 5 Yrs Ago</th>
<th>S&amp;P Oper. EPS 2011E</th>
<th>Market Capitalization(B)</th>
<th>Beta</th>
<th>S&amp;P 3-Yr. Proj. EPS CAGR(%)</th>
<th>S&amp;P Credit Rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>$24.14– 19.08</td>
<td>12.8</td>
<td>$12,309</td>
<td>1.77</td>
<td>$13,737</td>
<td>1.94</td>
<td>12</td>
<td>BBB</td>
</tr>
</tbody>
</table>

**Price Performance**

- 12-Mo. Target Price: $23.00
- 30-Week Mov. Avg.
- Relative Strength: Up

**Investment Rationale/Risk**

- We believe the company is well positioned to benefit from market share gains achieved during the recent recessionary environment and early economic recovery. Based on our expectation for an improved economic environment in FY 12, we believe the company will benefit as consumers begin to trade back up to higher-priced and wider-margin goods. Additionally, we see the company willing to pass along commodity cost increases to consumers in the form of higher product prices.

- Risks to our recommendation and target price include potential weakness in the economy that would cause consumers to become more price conscious, and increased price competition.

- Our 12-month target price of $23 is based on our P/E analysis and is supported by our EV/EBITDA valuation. Reflecting benefits we see from food inflation, we think the shares should trade at about 11.1X our FY 12 EPS estimate of $2.05, in line with its historical average discount to the P/E multiple of the S&P 500, leading to a projected value of $23. Our target price is supported by applying a 5.2X multiple, slightly below KR’s closest peers’ average of 5.3X, to our FY12 EBITDA estimate of $4.3 billion.

- Dividends have been paid since 2006. Source: Company reports.

Analysis prepared by Joseph Agnese on December 13, 2010.

**Highlights**

- We see sales of $86.3 billion in FY 12 (Jan., up 5.0% from our estimate of $82.2 billion in FY 11, reflecting 1.0% square footage growth, 3.0% identical-store sales gains (excluding fuel) and increased gas sales. We expect the company’s aggressive low pricing strategy to ease through FY 12 as food inflation accelerates.

- We believe EBITDA margins will widen in FY 12 as KR leverages increases we see it making in pricing in the face of low single digit food inflation, despite negative impacts from customers trading down to lower priced alternatives. We also see margin benefits from a more stable promotional spending environment, and expect additional cost-saving opportunities in areas such as administration, labor, shrinkage and transportation. In addition, we believe merchandising, such as increased private label sales, will help the company compete against lower-priced mass merchants.

- After benefits from fewer shares outstanding due to an active repurchase program, we expect FY 12 EPS to increase 16%, to $2.05, from our EPS estimate of $1.77 in FY 11.

Please read the Required Disclosures and Analyst Certification on the last page of this report.
CORPORATE OVERVIEW. Kroger is one of the largest U.S. supermarket chains, with 2,470 supermarkets as of September 2010. The company’s principal operating format is combination food and drug stores (combo stores). In addition to combo stores, Kroger also operates multi-department stores, marketplace stores, price-impact warehouses, convenience stores, fuel centers, jewelry stores, and food processing plants. Total food store square footage was approximately 148 million as of January 31, 2010.

Retail food stores are operated under three formats: combo stores, multi-department stores, and price-impact warehouse stores. Combo stores are considered neighborhood stores, and include many specialty departments, such as whole health sections, pharmacies, general merchandise, pet centers, and perishables, such as fresh seafood and organic produce. Combo banners include Kroger, Ralphs, King Soopers, City Market, Dillons, Smith’s, Fry’s, QFC, Hilander, Owen’s, Jay C, Baker’s, Pay Less and Gerbes.

Multi-department stores offer one-stop shopping, are significantly larger in size than combo stores, and sell a wider selection of general merchandise items, including apparel, home fashion and furnishings, electronics, automotive, toys, and fine jewelry. Multi-department formats include Fred Meyer, Fry’s Marketplace, Smith’s Marketplace and Kroger Marketplace. Many combination and multi-department stores include a fuel center.

Price-impact warehouse stores offer everyday low prices, plus promotions for a wide selection of grocery and health and beauty care items. Price-impact warehouse stores include Food 4 Less and Foods Co.

KR also operates convenience stores, jewelry stores, and food processing plants. The company’s 784 convenience stores offer a limited assortment of staple food items and general merchandise, and, in most cases, sell gasoline. Convenience store banners include Kwik Shop, Loaf ‘N Jug Mini Mart, Guik Stop markets, Tom Thumb Food Stores, and Turkey Hill Minit Markets. With 375 jewelry stores, the company is one of the largest U.S. jewelry retailers. Jewelry stores operate under banners such as Barclay Jewelers, Fred Meyer Jewelers, and Littman Jewelers. In addition, KR operates 40 manufacturing plants, consisting of 18 dairies, 10 deli or bakery plants, five grocery products plants, three beverage plants, two meat plants, and two cheese plants.

CORPORATE STRATEGY. Kroger aims to increase shareholder value through its dividend program and sustained earnings growth created by strong identical store sales, slight operating margin improvement, and continued share repurchases. The company strives to grow market share as this allows it to leverage fixed costs over a wider revenue base. According to Nielsen Homescan Data, the company’s estimated market share increased in total by about 60 basis points in 2009 across the 17 divisions in which it operates. Market share increased in 13 of the divisions, declined in three, and remained unchanged in one.

To generate identical store sales growth and market share gains, the company adheres to its Customer 1st strategy. This strategy focuses company efforts on improving employee communications and training; using customer research and loyalty data analysis to personalize stores on a market by market and store by store basis; improving customer loyalty by improving customers’ shopping experience (improved convenience and accessibility through multiple store formats, store cleanliness and security, reducing checkout wait times, etc.); and pricing within an acceptable range of discounters’ prices so that price becomes a neutral factor in customers’ shopping decisions.

As an important part of its merchandising strategy, KR offers about 11,000 private label items. Products are sold in three tiers. Private Selection is a premium quality brand, designed to meet or beat the gourmet or upscale national or regional brands. The banner brand (Kroger, Ralphs, King Soopers, etc.) represents the majority of KR’s private label items, and is designed to be equal to or better than the national brand. The Kroger Value brand is designed to deliver good quality at an affordable price. Kroger brands generated 35% of grocery unit sales and 27% of sales in the fourth quarter of FY 10 (Jan.). About 39% of corporate brand volume was manufactured in the company’s plants as of January 2010.

FINANCIAL TRENDS. In the five years through FY 10, the company experienced a compound annual growth rate (CAGR) for revenues of 6.3%, reflecting increased same-store sales and square footage expansion. The company reduced shares outstanding by 12.2% between its fiscal years ended in 2005 and 2010. As of January 2010, $337.1 million remained under a $1 billion stock repurchase program that directors approved in January 2008.
### S&P Fair Value Rank

Based on S&P's proprietary quantitative model, stocks are ranked from most overvalued (1) to most undervalued (5).

**Fair Value Calculation**

Analysis of the stock's current worth, based on S&P's proprietary quantitative model suggests that KR is slightly undervalued by $1.40 or 6.5%.

### Investability Quotient

KR scored higher than 98% of all companies for which an S&P Report is available.

### Volatility

Since December, 2010, the technical indicators for KR have been NEUTRAL.

### Insider Activity

Data for this section is as of the date of the report. Since then, there have been no insider transactions.

### Key Growth Rates and Averages

<table>
<thead>
<tr>
<th>Past Growth Rate (%)</th>
<th>1 Year</th>
<th>3 Years</th>
<th>5 Years</th>
<th>9 Years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>0.97</td>
<td>5.40</td>
<td>6.73</td>
<td>5.71</td>
</tr>
<tr>
<td>Net Income</td>
<td>-94.40</td>
<td>-56.17</td>
<td>NM</td>
<td>13.68</td>
</tr>
</tbody>
</table>

### Ratio Analysis (Annual Avg.)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Margin (%)</td>
<td>0.09</td>
<td>1.14</td>
<td>1.34</td>
<td>1.28</td>
</tr>
<tr>
<td>% LT Debt to Capitalization</td>
<td>57.68</td>
<td>57.03</td>
<td>55.86</td>
<td>56.01</td>
</tr>
<tr>
<td>Return on Equity (%)</td>
<td>1.39</td>
<td>16.72</td>
<td>19.61</td>
<td>18.73</td>
</tr>
</tbody>
</table>

### Company Financials

**Fiscal Year Ended Jan. 31**

### Balance Sheet & Other Financial Data (Million $)

<table>
<thead>
<tr>
<th>Cash</th>
<th>424</th>
<th>263</th>
<th>918</th>
<th>803</th>
<th>210</th>
<th>144</th>
<th>159</th>
<th>171</th>
<th>161</th>
<th>161</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Assets</td>
<td>7,450</td>
<td>7,206</td>
<td>7,114</td>
<td>6,755</td>
<td>6,466</td>
<td>6,406</td>
<td>5,619</td>
<td>5,566</td>
<td>5,512</td>
<td>5,416</td>
</tr>
<tr>
<td>Total Assets</td>
<td>23,093</td>
<td>23,211</td>
<td>22,299</td>
<td>21,215</td>
<td>20,482</td>
<td>20,491</td>
<td>20,194</td>
<td>20,102</td>
<td>19,057</td>
<td>18,190</td>
</tr>
<tr>
<td>Current Liabilities</td>
<td>7,714</td>
<td>7,629</td>
<td>6,889</td>
<td>7,581</td>
<td>6,719</td>
<td>6,316</td>
<td>5,586</td>
<td>5,608</td>
<td>5,485</td>
<td>5,591</td>
</tr>
<tr>
<td>Long Term Debt</td>
<td>7,477</td>
<td>7,505</td>
<td>6,529</td>
<td>6,154</td>
<td>6,678</td>
<td>7,900</td>
<td>8,116</td>
<td>8,222</td>
<td>8,412</td>
<td>8,210</td>
</tr>
<tr>
<td>Common Equity</td>
<td>4,906</td>
<td>5,176</td>
<td>4,914</td>
<td>4,923</td>
<td>4,390</td>
<td>3,540</td>
<td>4,011</td>
<td>3,850</td>
<td>3,502</td>
<td>3,089</td>
</tr>
<tr>
<td>Total Capital</td>
<td>12,963</td>
<td>12,913</td>
<td>11,810</td>
<td>11,799</td>
<td>11,911</td>
<td>12,379</td>
<td>13,117</td>
<td>12,072</td>
<td>11,914</td>
<td>11,299</td>
</tr>
<tr>
<td>Capital Expenditures</td>
<td>2,297</td>
<td>2,149</td>
<td>2,128</td>
<td>1,683</td>
<td>1,306</td>
<td>1,634</td>
<td>2,000</td>
<td>1,891</td>
<td>2,139</td>
<td>1,623</td>
</tr>
<tr>
<td>Cash Flow</td>
<td>1,595</td>
<td>2,691</td>
<td>2,537</td>
<td>2,387</td>
<td>2,223</td>
<td>1,156</td>
<td>1,524</td>
<td>2,320</td>
<td>2,016</td>
<td>1,787</td>
</tr>
<tr>
<td>Current Ratio</td>
<td>1.0</td>
<td>1.0</td>
<td>0.8</td>
<td>0.9</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
</tr>
<tr>
<td>% Long Term Debt of Capitalization</td>
<td>57.7</td>
<td>58.1</td>
<td>55.3</td>
<td>55.6</td>
<td>56.1</td>
<td>63.8</td>
<td>61.9</td>
<td>68.1</td>
<td>70.6</td>
<td>72.7</td>
</tr>
<tr>
<td>% Net Income of Revenue</td>
<td>0.1</td>
<td>1.6</td>
<td>1.7</td>
<td>1.7</td>
<td>1.6</td>
<td>NM</td>
<td>0.6</td>
<td>2.4</td>
<td>2.1</td>
<td>1.8</td>
</tr>
<tr>
<td>% Return on Assets</td>
<td>0.3</td>
<td>5.5</td>
<td>5.4</td>
<td>5.4</td>
<td>4.7</td>
<td>NM</td>
<td>1.6</td>
<td>6.3</td>
<td>5.8</td>
<td>4.9</td>
</tr>
<tr>
<td>% Return on Equity</td>
<td>1.4</td>
<td>24.8</td>
<td>24.0</td>
<td>24.0</td>
<td>23.9</td>
<td>NM</td>
<td>8.0</td>
<td>33.5</td>
<td>31.6</td>
<td>30.5</td>
</tr>
</tbody>
</table>

Our fundamental outlook for the food retail sub-industry for the next 12 months is neutral. While we believe an unfavorable operating environment led to intense pricing competition in the first nine months of 2010, we believe a more stable economic environment and rising food inflation will support margin expansion through in 2011. Through the first nine months of 2010, food retailers were more price competitive in an effort to protect market share as consumers became more price conscious in an adverse economic environment. As a result, margins were negatively impacted as retailers chose to pass along any food cost decreases quickly in an effort to maintain store traffic. Based on deflationary food pricing pressures in the first half of 2010, we look for traditional grocery chains on average to experience sluggish comparable-store sales growth for all of 2010.

We think competitive pressures were intense in the first nine months of 2010 despite major U.S. chains focusing on increasing the number of remodels, rather than new store openings. However, we expect food price inflation in the low single digits in 2011 will help provide support for comparable store sales gains in the low single digits in 2011. In addition to an improved inflationary environment, we expect a more stable economic environment in the rest of this year and in 2011 to result in improved transaction sizes and lead to reduced pricing competition. We believe that consolidation may help ease competitive pricing pressures in some markets, as well as improve operating profitability over the intermediate term for active participants, by further leveraging overhead expenses over a greater number of stores. However, large scale consolidation is unlikely, in our view, as we believe retailers will be hesitant to risk balance sheet strength in an adverse economic environment. We see food retailers benefiting from increased traffic, as consumers who are looking to save money trade down from food service providers. Within stores, retailers should benefit from an improved product mix as consumers trade down to lower priced but wider margin private label brands.

Year to date through December 10, the S&P Food Retail Index increased 10.5%, compared to a 12.7% rise for the S&P 1500. We believe underperformance thus far in 2010 reflects investor concerns over food retailers’ ability to achieve margin expansion in a slowly growing economic environment. In 2009, the S&P Food Retail Index decreased 6.5%, compared to a 24.3% rise for the S&P 1500. We believe last year’s significant underperformance reflected investors’ increased appetite for risk during 2009.

--Joseph Agnese

### Sub-Industry : Food Retail Peer Group*: Food Chain Cos. - Large

<table>
<thead>
<tr>
<th>Peer Group</th>
<th>Stock Symbol</th>
<th>Stk. Mkt. Cap. (Mil. $)</th>
<th>Recent Stock Price($ High/Low($)</th>
<th>52 Week Beta</th>
<th>Yield (%)</th>
<th>P/E Ratio</th>
<th>Fair Value Calc.($$)</th>
<th>S&amp;P IQ %ile</th>
<th>Return on Revenue (%)</th>
<th>LTD to Cap (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kroger Co</td>
<td>KR</td>
<td>13,737</td>
<td>21.60</td>
<td>24.14/19.08</td>
<td>0.25</td>
<td>1.9</td>
<td>13</td>
<td>23.00</td>
<td>B</td>
<td>98</td>
</tr>
<tr>
<td>Ahold Ltd ADR</td>
<td>AHONY</td>
<td>14,934</td>
<td>12.71</td>
<td>14.31/11.76</td>
<td>0.57</td>
<td>2.0</td>
<td>11</td>
<td>12.60</td>
<td>NR</td>
<td>80</td>
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<tr>
<td>Etablissements Delhaize ADR</td>
<td>DEG</td>
<td>7,215</td>
<td>71.80</td>
<td>85.43/65.69</td>
<td>0.70</td>
<td>2.0</td>
<td>10</td>
<td>76.90</td>
<td>NR</td>
<td>55</td>
</tr>
<tr>
<td>Great Atl &amp; Pac Tea</td>
<td>GAPTQ</td>
<td>11</td>
<td>0.20</td>
<td>12.00/0.12</td>
<td>2.19</td>
<td>Nil</td>
<td>Nil</td>
<td>NM</td>
<td>NA</td>
<td>16</td>
</tr>
<tr>
<td>Publix Super Mkt</td>
<td>PUSH</td>
<td>NA</td>
<td>0.00</td>
<td>25.00/15.00</td>
<td>0.06</td>
<td>Nil</td>
<td>Nil</td>
<td>NM</td>
<td>NA</td>
<td>NA</td>
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<tr>
<td>Safeway Inc</td>
<td>SWY</td>
<td>7,877</td>
<td>21.13</td>
<td>27.04/18.73</td>
<td>0.66</td>
<td>2.3</td>
<td>N/A</td>
<td>18.30</td>
<td>B</td>
<td>90</td>
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<tr>
<td>Supervalu Inc</td>
<td>SVU</td>
<td>1,837</td>
<td>8.66</td>
<td>17.89/8.20</td>
<td>1.07</td>
<td>4.0</td>
<td>NM</td>
<td>18.40</td>
<td>B+</td>
<td>54</td>
</tr>
</tbody>
</table>

*For Peer Groups with more than 15 companies or stocks, selection of issues is based on market capitalization.
S&P Analyst Research Notes and other Company News

December 16, 2010
The Kroger Co. announced that Sukanya R. Madlinger has been named President of Kroger’s Cincinnati/Dayton Division, replacing Geoff Covert who has been named Senior Vice President, Retail Operations for the company. Mrs. Madlinger, 47, began her career with Kroger in 1986 in the company’s store management training program. She has held several leadership roles in the division and was the company’s vice president of drug/general merchandise/pharmacy merchandising. She has been the Vice President of Merchandising for the Cincinnati/Dayton Division since 2006.

December 13, 2010
The Kroger Co. announced that Geoffrey J. Covert has been named Senior Vice President of Retail Operations, effective January 1, 2011. Mr. Covert will be responsible for leading the Company’s programs and processes focused on operating efficiency, store productivity, and associate and customer safety. Mr. Covert joined Kroger in 1996. He has served as President of the company’s Cincinnati/Dayton Division for the past six years.

December 2, 2010
DOWN 2.08 to 21.78... KR posts $0.32 Q3 EPS vs. $1.35 loss (incl. charges) on 2.4% same-store sales rise (excl. fuel), 3.1% total sales rise (excl. fuel). Narrows 2.0%-3.0% FY 11 same-store sales growth guidance to 2.5%-3.0%, narrows $1.60-$1.80 FY 11 EPS guidance to $1.65-$1.78. Street was at $1.78.

December 2, 2010
02:43 pm ET ... THE KROGER CO. (KR 21.7) DOWN 2.16, KROGER (KR) POSTS Q3. NARROWS OUTLOOK. JANNEY LOWERS ESTIMATES, MAINTAINS BUY... Analyst Jonathan Feeney tells salesforce $0.32 Q3 EPS match his in-line estimate. Says while KR’s strong competitive position, enforced by a growing loyal household base, allows it to continue to take share, EPS growth appears more dependent on cost savings than structural growth. Notes with the top line seemingly picking up and inflation apparently starting to take hold, this outlook could change, but today’s announcement is a reminder of just how slowly, if at all, the profit pool is expanding. Cuts $1.60 FY 11 EPS est. to $1.75, $1.99 FY 12 to $2.53. B.Brodie

December 2, 2010
12:16 pm ET ... S&P REITERATES HOLD RECOMMENDATION ON SHARES OF KROGER CO (KR 21.7****): KR reports Oct-Q EPS of $0.32, vs. operating EPS of $0.27, and in line with our view. Results benefited from identical store sales growth of 2.4% (excluding fuel), below our 3.2% estimate, and productivity improvements, despite rising employee costs and credit card fees. Given near-term pricing pressure we forecast, we are reducing our FY 11 (Jan.) EPS estimate $0.03 to $1.77. However, we keep FY 12’s EPS of $2.05, as we believe a more inflationary environment will alleviate margin pressures. We also keep our 12-month target price of $23, based on comparative analysis. /J.Agnese

November 29, 2010
The Kroger Co. announced that Paul Scutt, Senior Vice President, Retail Operations, will retire in late February 2011 after a distinguished 45-year career with the company.

October 26, 2010
The Kroger Co. announced that Jeffrey D. Burt has been promoted to Group Vice President of Perishables Merchandising and Procurement. Mr. Burt, 48, previously served as Vice President of Deli/Bakery Merchandising and Procurement for the Company, a position he has held since 2004. Prior to that, Mr. Burt held leadership roles at UFC.

September 14, 2010
12:24 pm ET ... S&P LOWERS OPINION ON SHARES OF KROGER CO TO HOLD FROM BUY (KR 21.61***): Our downgrade is based on valuation as the shares are trading near our 12-month target price of $23, based on our comparative and P/E analyses. KR reports Jul-Q EPS of $0.41, vs. $0.39, $0.04 above our estimate. Results benefited from 2.7% identical store sales growth (excluding fuel), compared to our 2.0% estimate, a lower effective tax rate and fewer shares outstanding. However, margins narrowed more than we expected on increased competition. With food inflation rising slower than we anticipated, we are reducing our FY 11 EPS estimate by $0.02 to $1.80. /J.Agnese

June 18, 2010
DOWN 0.74 to 20.01... BOA/Merrill downgrades KR, SWY to underperform. Yesterday KR posted $0.56 vs. $0.66 Q1 EPS.

June 17, 2010
UP 0.96 to 21.04... KR posts $0.58 vs. $0.66 Q1 EPS despite 3.1% sales rise (excl. fuel). The Street was looking for $0.54 EPS. Says it continues to expect identical supermarket sales growth, excl. fuel, of 2%-3% for FY 11, EPS in the range of $1.60-$1.80.

June 17, 2010
02:07 pm ET ... S&P REITERATES BUY RECOMMENDATION ON SHARES OF KROGER CO. (KR 20.8****): KR reports May-Q EPS of $0.58 vs. $0.66, $0.06 above our expectations. Results benefited from a 2.4% increase in identical store sales, above our 2.0% estimate, improved sales leverage and productivity improvements, despite higher healthcare and pension costs. We believe results for the remainder of FY 11 (Jan.) will benefit as rising food inflation boosts identical store sales and from easier margin comparisons. As a result, we are raising our FY 11 EPS estimate $0.03 to $1.82. Our 12-month target price remains $23, based on our updated comparative and P/E analyses. /J.Agnese

June 11, 2010
09:50 am ET ... S&P UPGRADES RECOMMENDATION ON SHARES OF KROGER CO TO BUY FROM HOLD (KR 19.82****): Our upgrade is based on valuation as the shares are trading below our 12-month target price of $23, based on our comparative and P/E analyses. We expect KR to report May-Q EPS of $0.52 vs. $0.66 before the market opens on Thursday, June 17th. We are projecting same store sales will grow 2.0%, excluding fuel, as deflationary food pressures begin to subside, although industry pricing competition remains intense. We expect margins to narrow reflecting the company’s strategy of using lower pricing to grow market share, despite benefits we expect from increased labor productivity. /J.Agnese

April 19, 2010
The Kroger Co. has named Michael J. Stoll as Chief Executive Officer of The Little Clinic, Kroger’s wholly-owned in-store health clinic subsidiary. Theresa Monti has been promoted to Vice President of Corporate Benefits, succeeding Stoll. Prior to her promotion, Monti served as Director of Corporate Health & Welfare Benefit Programs for Kroger. In her new role, Monti will lead the development, implementation and administration of policies and strategies for the Company-sponsored health, welfare and retirement benefit plans. Prior to joining Kroger in 1999, Monti held national account management positions with both Kaiser Permanente and Prudential Health Care.

April 19, 2010
Kroger Co. announced Bryan Kaltenbach has been promoted to President of Kroger’s Food 4 Less Division, effective immediately. Mr. Kaltenbach has held several leadership positions in the company, including his most recent role as Senior Vice President of Sales and Marketing for Food 4 Less. Bryan brings extensive retail experience to his new position and his leadership will be a tremendous asset to team members and Food 4 Less customers. Mr. Kaltenbach began his career in 1973 at Alpha Beta Markets in California. He held a variety of roles at Alpha Beta, which merged with Food 4 Less in 1991.
Of the total 23 companies following KR, 23 analysts currently publish recommendations.

<table>
<thead>
<tr>
<th>No. of Ratings</th>
<th>% of Total</th>
<th>1 Mo. Prior</th>
<th>3 Mos. Prior</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buy</td>
<td>6</td>
<td>26</td>
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</tr>
<tr>
<td>Buy/Hold</td>
<td>8</td>
<td>35</td>
<td>8</td>
</tr>
<tr>
<td>Hold</td>
<td>5</td>
<td>22</td>
<td>5</td>
</tr>
<tr>
<td>Weak Hold</td>
<td>3</td>
<td>13</td>
<td>3</td>
</tr>
<tr>
<td>Sell</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>No Opinion</td>
<td>1</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Total</td>
<td>23</td>
<td>100</td>
<td>23</td>
</tr>
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</table>

**Wall Street Consensus Estimates**

<table>
<thead>
<tr>
<th>Fiscal Years</th>
<th>Avg Est.</th>
<th>High Est.</th>
<th>Low Est.</th>
<th># of Est.</th>
<th>Est. P/E</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>1.92</td>
<td>2.05</td>
<td>1.77</td>
<td>22</td>
<td>11.3</td>
</tr>
<tr>
<td>2011</td>
<td>1.75</td>
<td>1.78</td>
<td>1.70</td>
<td>21</td>
<td>12.3</td>
</tr>
<tr>
<td>2012 vs. 2011</td>
<td>▲10%</td>
<td>▲15%</td>
<td>▲4%</td>
<td>▲5%</td>
<td>▼8%</td>
</tr>
<tr>
<td>Q4'12</td>
<td>0.50</td>
<td>0.45</td>
<td>0.29</td>
<td>7</td>
<td>43.2</td>
</tr>
<tr>
<td>Q4'11</td>
<td>0.44</td>
<td>0.47</td>
<td>0.38</td>
<td>18</td>
<td>49.1</td>
</tr>
<tr>
<td>Q4’12 vs. Q4’11</td>
<td>▲14%</td>
<td>▼-4%</td>
<td>▼-24%</td>
<td>▼-61%</td>
<td>▼-12%</td>
</tr>
</tbody>
</table>

A company’s earnings outlook plays a major part in any investment decision. Standard & Poor’s organizes the earnings estimates of over 2,300 Wall Street analysts, and provides their consensus of earnings over the next two years. This graph shows the trend in analyst estimates over the past 15 months.
a model, such as risks and opportunities, management analysts assess many factors that cannot be reflected in each. For instance, when designating STARS, S&P evaluations may at times contradict an analyst’s

In contrast to our qualitative STARS recommendations, Quantitative Evaluations should be reflective of risk factors related to a is a relative ranking to the S&P U.S. STARS universe, and as an ongoing concern. The Qualitative Risk Assessment was designed to meet the needs of investors looking to put their investment decisions in perspective.

STARS Average Annual Performance

S&P 12-Month Target Price
The S&P equity analyst’s projection of the market price a given security will command 12 months hence, based on a combination of intrinsic, relative, and private market valuation metrics.

Investment Style Classification
Characterizes the stock as Growth or Value, and indicates its capitalization level. Growth is evaluated along three dimensions (earnings, sales and internal growth), while Value is evaluated along four dimensions (book-to-price, cash flow-to-price, dividend yield and sale-to-price). Growth stocks score higher than the market average on growth dimensions and lower on value dimensions. The reverse is true for Value stocks. Certain stocks are classified as Blend, indicating a mixture of growth and value characteristics and cannot be classified as purely growth or value.

Qualitative Risk Assessment
The S&P equity analyst’s view of a given company’s operational risk, or the risk of a firm’s ability to continue as an ongoing concern. The Qualitative Risk Assessment is a relative ranking to the S&P U.S. STARS universe, and should be reflective of risk factors related to a company’s operations, as opposed to risk and volatility measures associated with share prices.

Quantitative Evaluations
In contrast to our qualitative STARS recommendations, which are assigned by S&P analysts, the quantitative evaluations described below are derived from proprietary arithmetic models. These computer-driven evaluations may at times contradict an analyst’s qualitative assessment of a stock. One primary reason for this is that different measures are used to determine each. For instance, when designating STARS, S&P analysts assess factors that cannot be reflected in a model, such as risks and opportunities, management changes, recent competitive shifts, patent expiration, litigation risk, etc.

S&P Quality Ranking
Growth and stability of earnings and dividends are deemed key elements in establishing S&P’s Quality Rankings for common stocks, which are designed to capitalize the nature of this record in a single symbol. It should be noted, however, that the process also takes into consideration certain adjustments and modifications deemed desirable in establishing such rankings. The final score for each stock is measured against a scoring matrix determined by analysis of the scores of a large and representative sample of stocks. The range of scores in the array of this sample has been aligned with the following ladder of rankings:

- A+ Highest
- A High
- A- Above Average
- B+ Average
- B Below Average
- C Lowest
- NR Not Ranked

S&P Fair Value Rank
Using S&P’s exclusive proprietary quantitative model, stocks are ranked in one of five groups, ranging from Group 1, the most undervalued issues, Group 5 stocks are expected to generally outperform all others. A positive (+) or negative (-) Timing Index is placed next to the Fair Value ranking to further aid the selection process. A stock with a (+) added to the Fair Value Rank simply means that this stock has a somewhat better chance to outperform other stocks with the same Fair Value Rank. A stock with a (-) has a somewhat lesser chance to outperform other stocks with the same Fair Value Rank. The Fair Value rankings imply the following: 5-Stock is significantly undervalued; 4-Stock is moderately undervalued; 3-Stock is fairly valued; 2-Stock is modestly overvalued; 1-Stock is significantly overvalued.

S&P Fair Value Calculation
The price at which a stock should trade up, according to S&P’s proprietary quantitative model that incorporates both actual and estimated variables (as opposed to only actual variables in the case of S&P Quality Ranking), Relying heavily on a company’s actual return on equity, the S&P Fair Value model places a value on a security based on placing a formula-derived price-to-book multiple on a company’s consensus earnings per share estimate.

Insider Activity
Gives an insight as to insider sentiment by showing whether directors, officers and key employees who have proprietary information not available to the general public, are buying or selling the company’s stock during the most recent six months. Funds From Operations (FFO) is Funds from Operations and equal to a REIT’s net income, excluding gains or losses from sales of property, plus real estate depreciation.

Investability Quotient (IQ)
The IQ is a measure of investment desirability. It serves as an indicator of potential medium-to-long term return and as a caution against downside risk. The measure takes into account variables such as technical indicators, earnings estimates, liquidity, financial ratios and selected S&P proprietary measures.

S&P’s IQ Rationale:
Kroger Co

<table>
<thead>
<tr>
<th>Score</th>
<th>Max Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proprietary S&amp;P Measures</td>
<td>54</td>
</tr>
<tr>
<td>Technical Indicators</td>
<td>31</td>
</tr>
<tr>
<td>Liquidity/Valuation Measures</td>
<td>16</td>
</tr>
<tr>
<td>Quantitative Measures</td>
<td>64</td>
</tr>
<tr>
<td>IQ Total</td>
<td>165</td>
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</tbody>
</table>

Volatility
Rates the volatility of the stock’s price over the past year.

Technical Evaluation
In researching the past market history of prices and trading volume for each company, S&P’s computer models apply special technical methods and formulas to identify and project price trends for the stock.

Relative Strength Rank
Shows, on a scale of 1 to 99, how the stock has performed versus all other companies in S&P’s universe on a rolling 13-week basis.

Global Industry Classification Standard (GICS)
An industry classification standard, developed by Standard & Poor’s in collaboration with Morgan Stanley Capital International (MSCI). GICS is currently comprised of 10 Sectors, 24 Industry Groups, 68 Industries, and 154 Sub-Industries.

S&P Issuer Credit Rating
A Standard & Poor’s Issuer Credit Rating is a current opinion of an obligor’s overall financial capacity (its creditworthiness) to pay its financial obligations. This opinion focuses on the obligor’s capacity and willingness to meet its financial commitments as they come due. It does not apply to any specific financial obligation, as it does not take into account the nature of and provisions of the obligation, its standing in bankruptcy or liquidation, statutory preferences, or the legality and enforceability of the obligation. In addition, it does not take into account the creditworthiness of the guarantors, insurers, or other forms of credit enhancement on the obligation. The Issuer Credit Rating is not a recommendation to purchase, sell, or hold a financial obligation issued by an obligor, as it does not comment on market price or suitability for a particular investor. Issuer Credit Ratings are based on current information furnished by obligors or obtained by Standard & Poor’s from other sources it considers reliable. Standard & Poor’s does not perform an audit in connection with any Issuer Credit Rating and may, on occasion, rely on unsatisfactory financial information. Issuer Credit Ratings may be changed, suspended, or withdrawn as a result of changes in, or unavailability of, such information, or based on other circumstances.

Exchange Type

S&P Equity Research Services
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Abbreviations Used in S&P Equity Research Reports
CAGR - Compound Annual Growth Rate; CAPEX - Capital Expenditures; CY - Calendar Year; BCF - Discounted Cash Flow; EBIT - Earnings Before Interest and Taxes; EBITDA - Earnings Before Interest, Taxes, Depreciation and Amortization; EPS - Earnings Per Share; EV - Enterprise Value; FCF - Free Cash Flow; FFO - Funds From Operations; FY - Fiscal Year; P/E - Price/Earnings; PEG Ratio - P/E-to-Growth Ratio; PV - Present Value; R&D - Research & Development; ROE - Return on Equity; ROIC - Return on Invested Capital; ROA - Return on Assets; SG&A - Selling, General & Administrative Expenses; WACC - Weighted Average Cost of Capital

Dividends on American Depositary Receipts (ADRs) and American Depositary Shares (ADSs) are net of taxes (paid in the country of origin).

Kroger Co. (The)

S&P Global STARS Distribution

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★★★★★ 5-STARS (Strong Buy): Total return is expected to outperform the total return of a relevant benchmark, by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.

★★★★ 4-STARS (Buy): Total return is expected to outperform the total return of a relevant benchmark over the coming 12 months, with shares rising in price on an absolute basis.

★★★★ 3-STARS (Hold): Total return is expected to closely approximate the total return of a relevant benchmark over the coming 12 months, with shares generally rising in price on an absolute basis.

★★★ 2-STARS (Sell): Total return is expected to underperform the total return of a relevant benchmark over the coming 12 months, and the share price not anticipated to show a gain.

★★★ 1-STARS (Strong Sell): Total return is expected to underperform the total return of a relevant benchmark by a wide margin over the coming 12 months, with shares falling in price on an absolute basis.

Relevant benchmarks: In North America the relevant benchmark is the S&P 500 Index, in Europe and in Asia, the relevant benchmarks are generally the S&P Europe 350 Index and the S&P Asia 50 Index.

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