

Marketing Innovation in the Retail Tech Titan Era

What Retailers are Doing to Survive and Thrive

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures

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30 April 2012



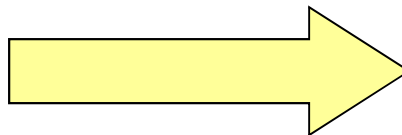
Agenda

1. Macro Factors Affecting Consumers and Marketing Innovation in Retail
2. Key Technology Themes to Watch in 2012
3. Tips and Examples from Five Top Companies
4. Takeaways and Conclusions

Macro

Retailers Move from Defense to Offense with Technology

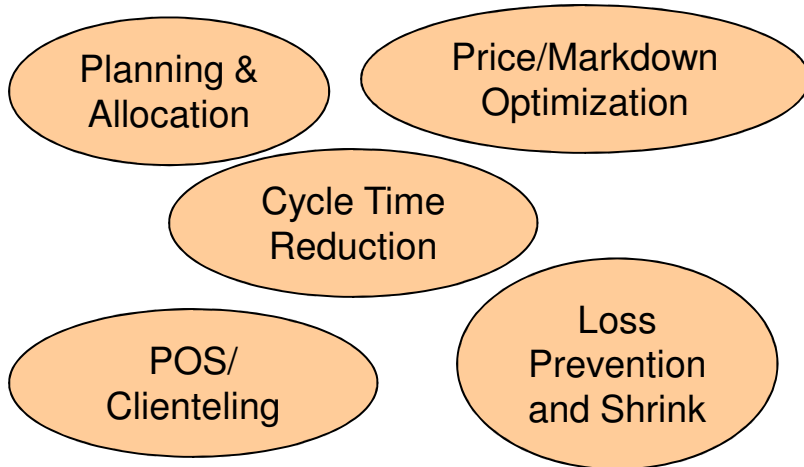
Recession



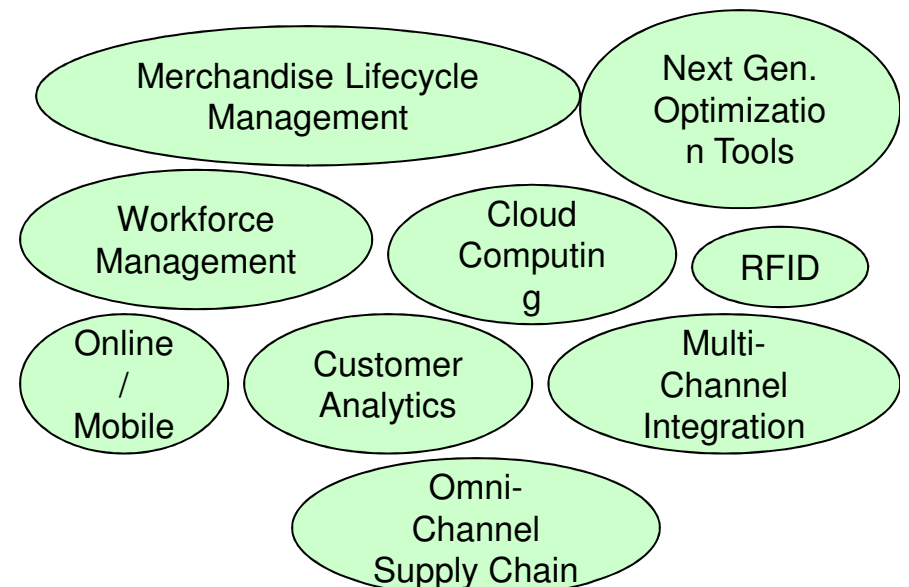
Recovery



- During the recession, retailers invested in technology to protect margins and lower costs.



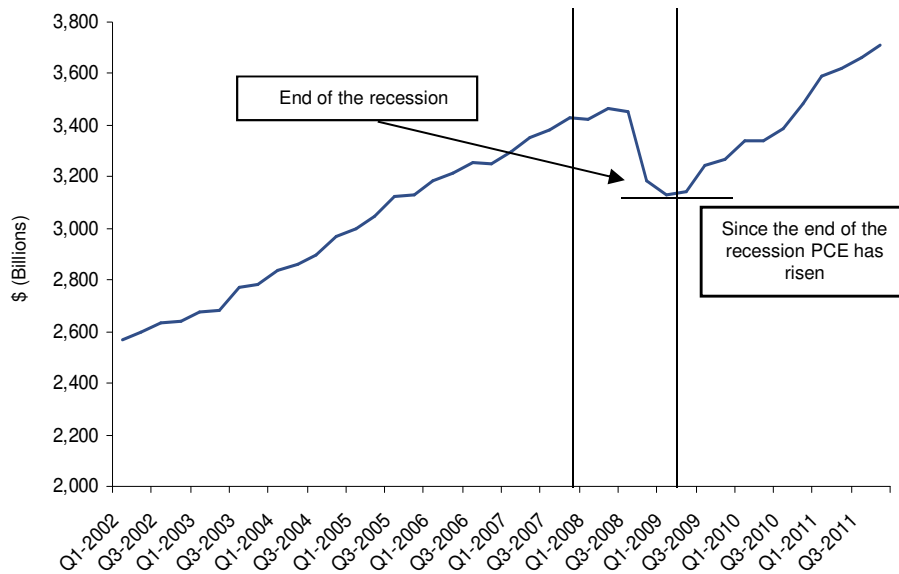
- As the recovery unfolds, we expect retailers to utilize technology to drive sales, improve buying and allocation decisions, enhance margins, and leverage stronger topline trends.



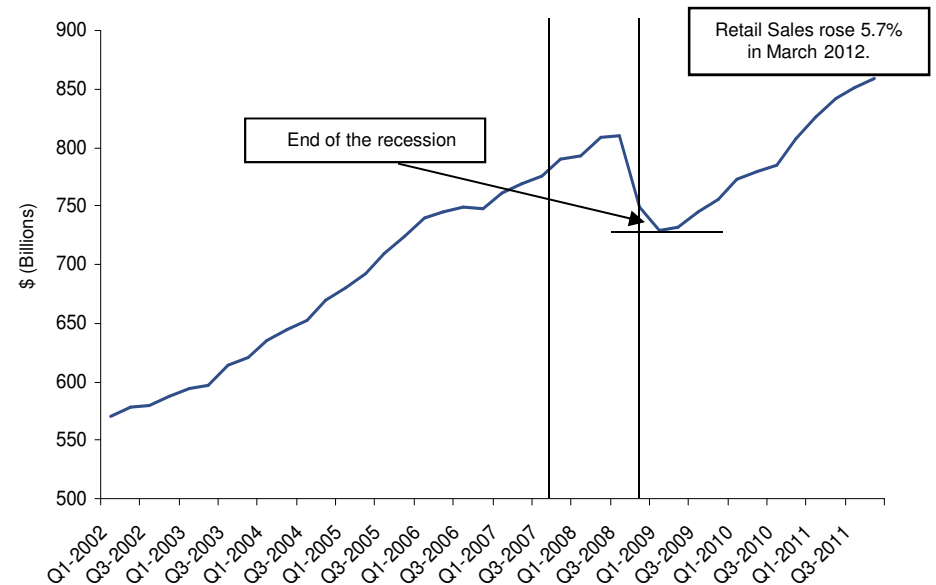
Consumer Spending and Retail Sales Have Recovered Nicely

- CIRA's Economics team expects GDP to increase +2.1% and PCE to increase +2.0% YOY in 2012.

PCE – Goods (\$B)



Retail Sales ex. Auto (\$B)

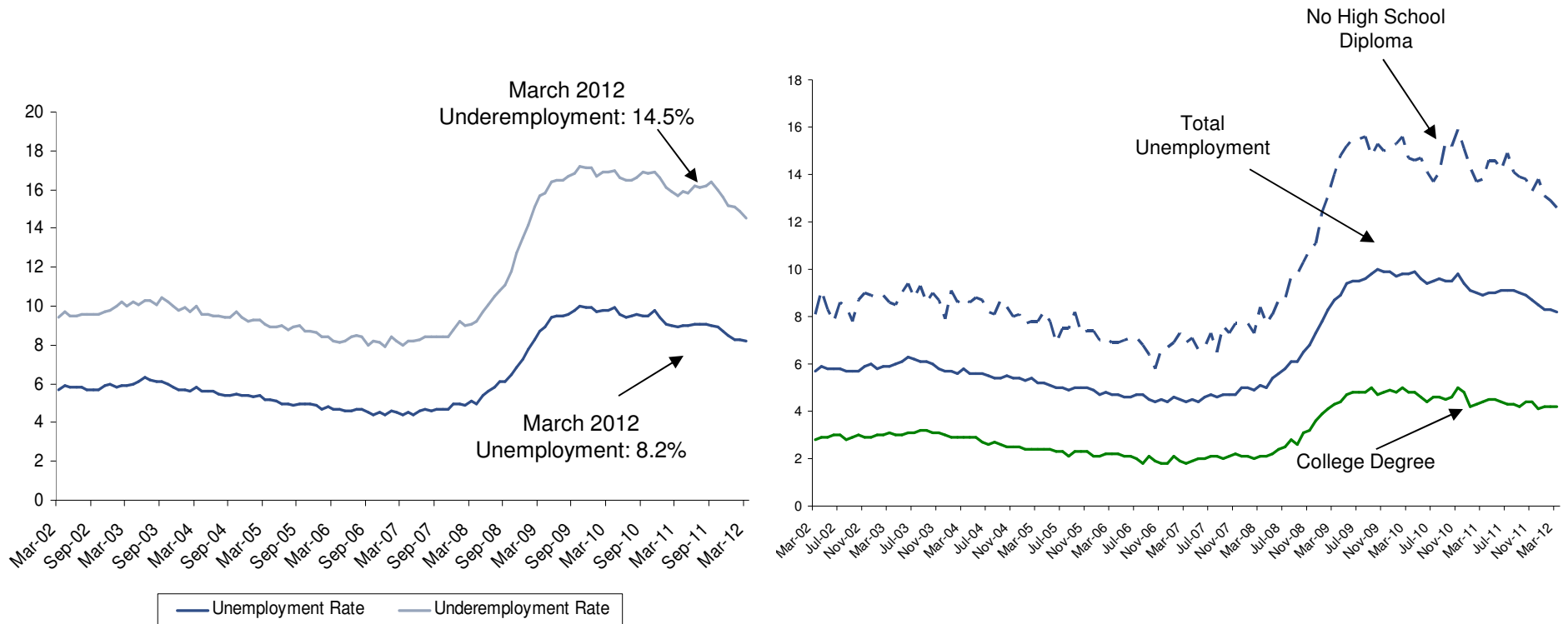


Consumer spending on goods was 7% above pre-recession peak as of 4Q11.

Retail Sales (ex. auto) were 6% above pre-recession peak as of 4Q11.

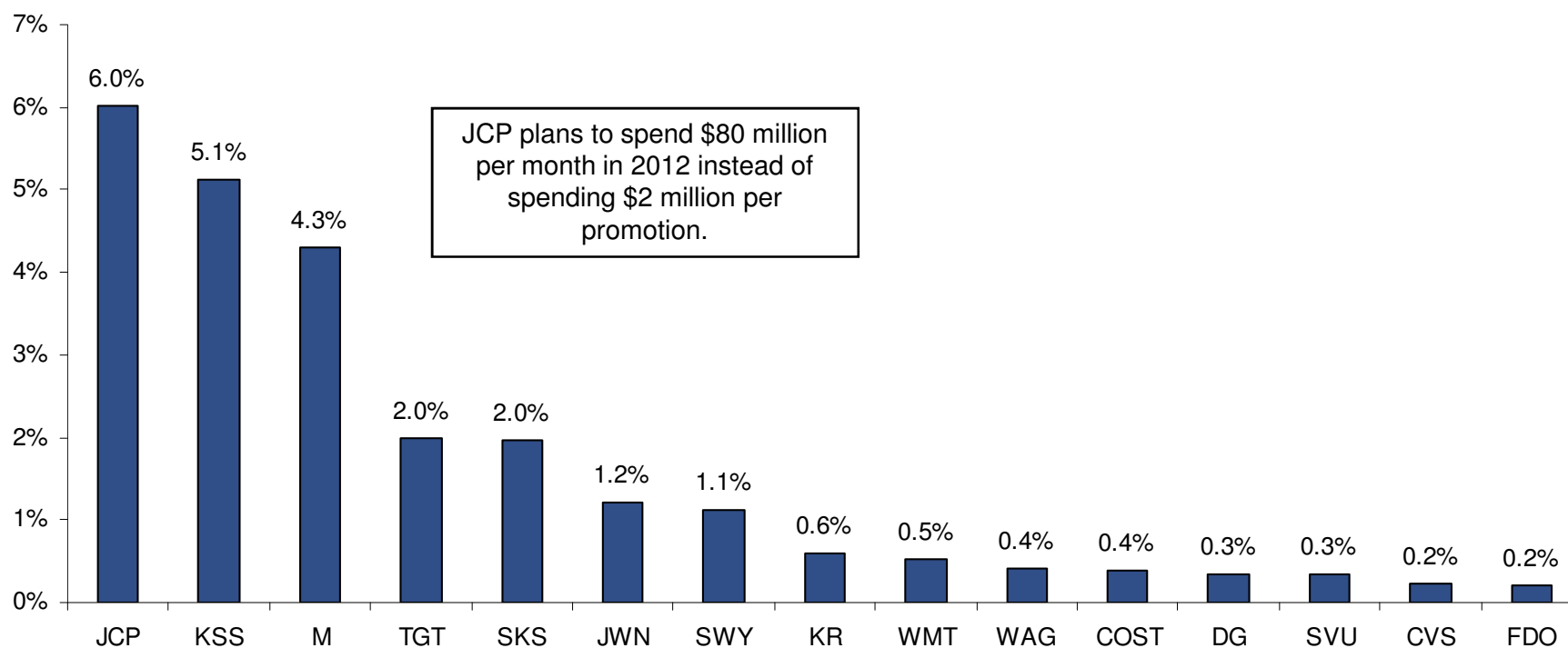
Unemployment Continues to Creep Lower

- The unemployment rate is down (-180) bps from peak; underemployment is down (-270) bps from peak.
- CIRA's Economics team expects the unemployment rate to fall to 7.8% by 4Q12.



Advertising as a Percent of Sales in 2011 at the Broadlines Retailers

- In 2011, the Broadlines and Food and Drug Retailers spent 1.6% of total sales (vs. 1.7% in 2010) on average on advertising expenses.
- Citi Investment Research's Media Analyst, Jason Bazinet, believes retail media ad spend is about 7% of total ad spend. Across all industries he estimates 19% of total ad spend is on digital media.



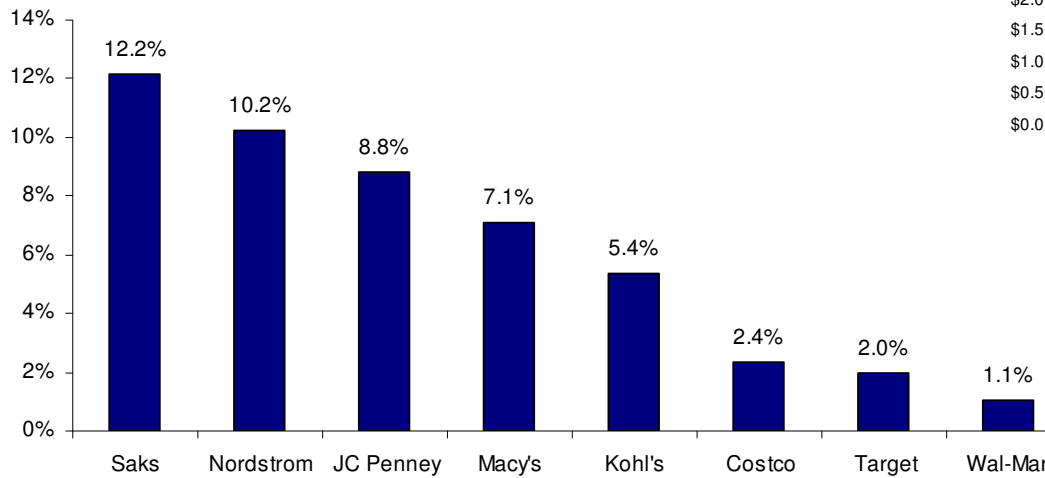
Source: Company Reports, CIRA

* COST does not disclose advertising expense. We assume 0.4% of sales.

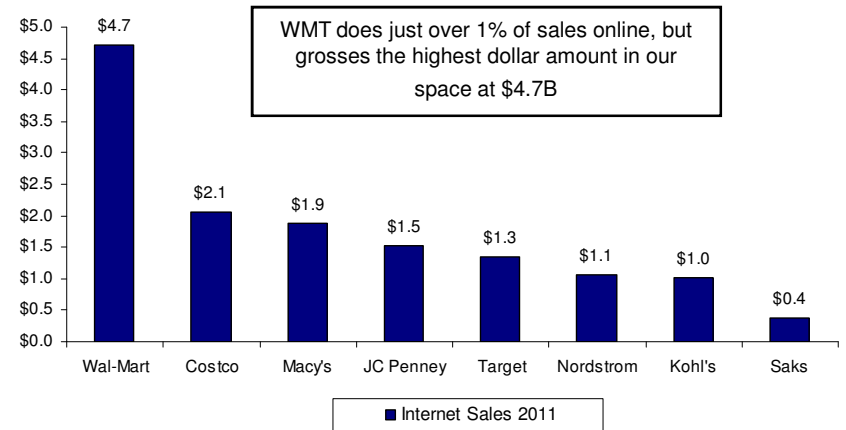


E-Commerce Grows in Importance at the Broadlines Retailers

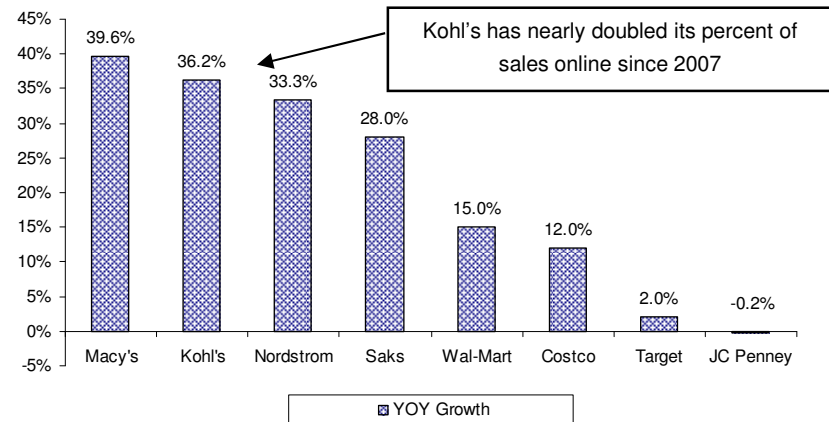
Percent of Sales Online (2011)



Gross \$ of Sales Online (2011)



2011 Online Sales Growth YOY



Source: Citi Investment Research and Analysis, Company Reports.

*Nordstrom Direct which includes internet, flash sale site HauteLook, and catalog

Fashion Trends for Spring 2012

- We believe that consumers continue to respond to fashion newness. From a category perspective, accessories and footwear have been driving comps recently, while apparel has experienced lackluster sales, particularly in the women's category.
- Additionally, unseasonably warm weather has led to soft sales in outerwear and other cold weather merchandise. However, early reads on new Spring receipts have been encouraging.
- The top five looks of the season are:

#1: Color-Driven with an Emphasis on Fit



#2: Color Blocking



#3: Stripes



#4: "Day Shine" metallic glazers, glitter, and sequins



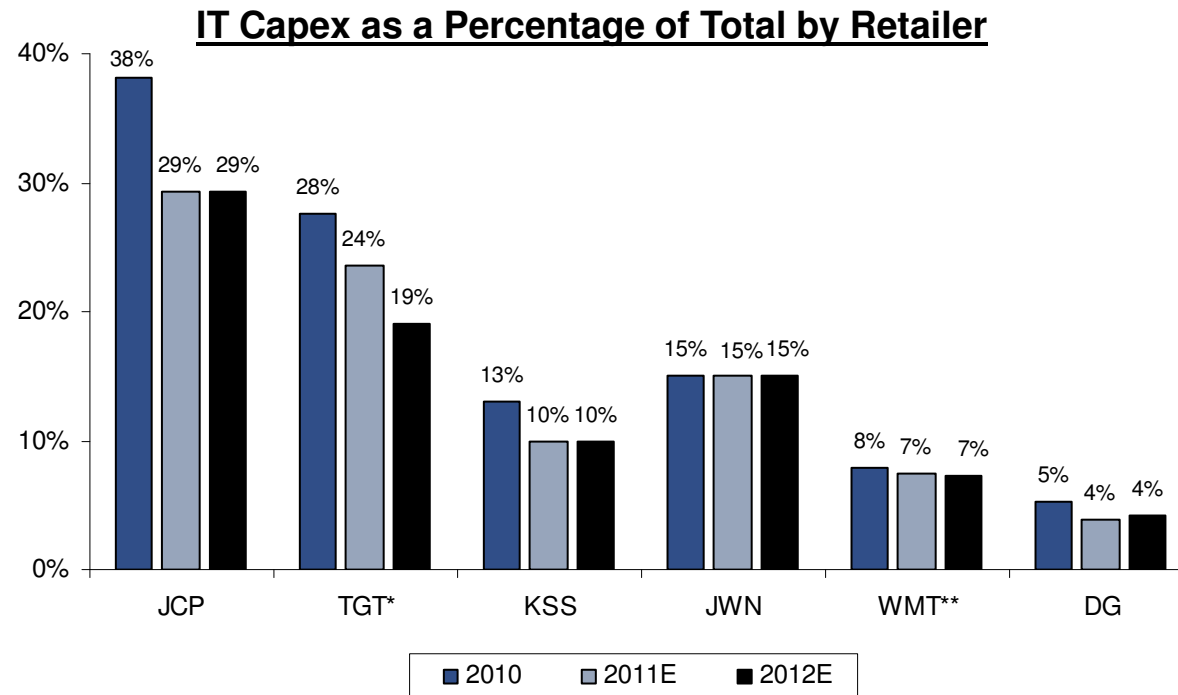
#5: Lace/Open Work



Colors: Bright Green, Mint Green, Yellow, and Orange

Retail IT Spending on the Rise for the Broadlines Retailers

- Technology capex is expected to comprise 10.9% of the total capex budget in 2012, down from 11.1% in 2011.
- Overall, capital spending on technology is expected to increase +3.5% in 2012 for the Broadlines retailers, vs. a +4.9% increase in total capex, as retailers embrace pay-as-you-go software (software as a service), which is expensed and not capitalized. This allows retailers to test the technology, and avoid the upfront costs associated with capitalized projects



*TGT classifies IT capex under Information Technology, Distribution, and Other.

**For WMT, we assume IT capex is equal to corporate capex, as the majority of corporate capex is invested in technology to support WMT's three operating segments.



Showrooming and How Retailers Are Fighting Back

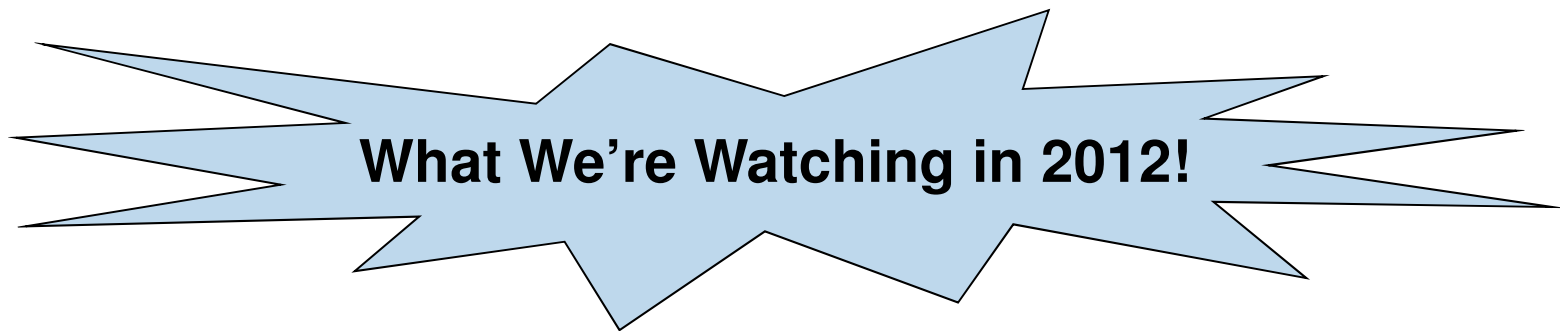
- Showrooming is when consumers preview/view products in-store, but buy the product on their mobile device.
- A 'showrooming' study by ClickIQ showed that 46% of respondents who shopped online within the past six months first checked out the product at their local retail stores and then made the purchase online, often from a different source. 48% made their final purchase at Amazon, regardless of retail store they used to comparison shop.
- Target is actively trying to ensure that its stores are not used as showrooms by proactively reaching out to the vendor community. Other retailers have taken a much more defensive approach (i.e. Best Buy).
- Target recently wrote a letter to challenge its vendor partners to work with them to develop an assortment and pricing strategy that will allow Target to be competitive and profitable across all channels.
- One strategy outlined in the letter suggested developing membership or subscription-based pricing online to compete with online pricing models in the market. We believe that the online pricing models referred to programs like AMZN's Subscribe and Save, which launched in 2007 and offers regular shipments of frequently-purchased items at a discount.



Technology Themes

Key Technology Themes to Watch in 2012

- 1) Retailers Engage Customers through Mobile Devices
- 2) Mobile & Social Analytics Shape Retailers' Views of the Customer
- 3) Maximize Returns with Optimization Technologies
- 4) Moving to One View of the Customer: Customer Analytics
- 5) Marketing & IT Converge

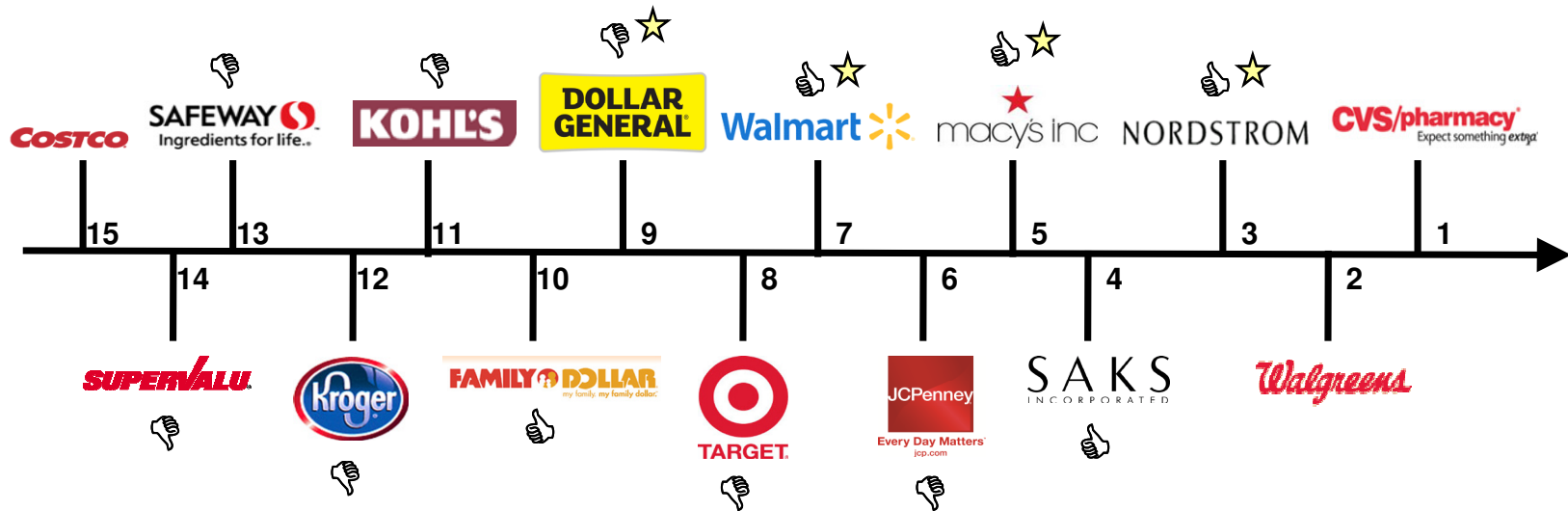


What are Bricks and Mortar Retailers Doing to Survive and Thrive?

Where Do Retailers Stand on the Technology Continuum?

- We consider CVS and Walgreens to be the most advanced from a technology perspective, as the drug retail business model requires these companies to have advanced inventory management and pharmacy workflow optimization systems.
- Costco has fewer technology and inventory management needs as a result of its unique business model.
- Family Dollar was one of the most improved retailers in 2011, as the company invested in a number of innovative technologies to drive change and boost sales/margins.

Broadlines 2011 Technology Continuum



- 👍 = Moved up the continuum in 2011
- 👎 = Moved down the continuum in 2011
- ★ = Top Picks



What are Retailers Doing to Thrive in the Era of the Titans?

5 companies that exemplify 5 tech themes in today's retail environment.

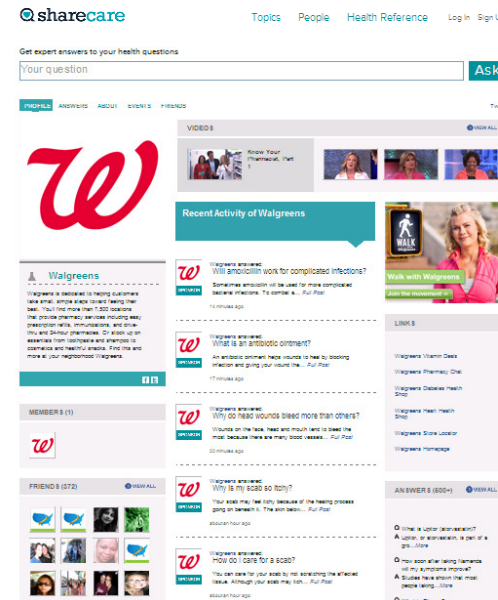
- **Walgreens**
 - **Theme #1 : Retailers Engage Customers through Mobile Devices**
 - The Epitome of SOLOMO
- **Nordstrom**
 - **Theme #2 : Mobile and Social Analytics Shape Retailers' Views of the Customer**
 - Paving the Way for Omnichannel in Department Store Retailing
- **Family Dollar**
 - **Theme #3 : Maximize Returns with Optimization Technologies**
 - Investing in the Right Place
- **Kroger**
 - **Theme #4 : Moving to One View of the Customer: Customer Analytics**
 - Catering to the Customer
- **Costco**
 - **Theme #5 : Marketing and IT Converge**
 - Exploring E and M-Commerce

Theme #1: Retailers Engage Customers through Mobile Devices

Walgreens – The Epitome of SOLOMO



- Tapping into the power of SOLOMO
 - **SO:** Walgreens is taking advantage of all of the major social media websites to drive traffic and generate buzz about its brand, their latest services, and events such as online healthcare seminars. Walgreens believes social media is especially effective in educating and connecting with patients about medical questions.
 - People love to share photos and the photo center enables customers to share via social media outlets and print physical copies.
 - “When someone is pinning, you’re probably winning in retail” – Pinterest
 - Walgreens Social Care is the service that responds to customer concerns expressed on Twitter and other outlets.
 - Walgreens Share Care is a social media partner that serves as a forum to provide answers to medical questions featuring Dr. Oz.

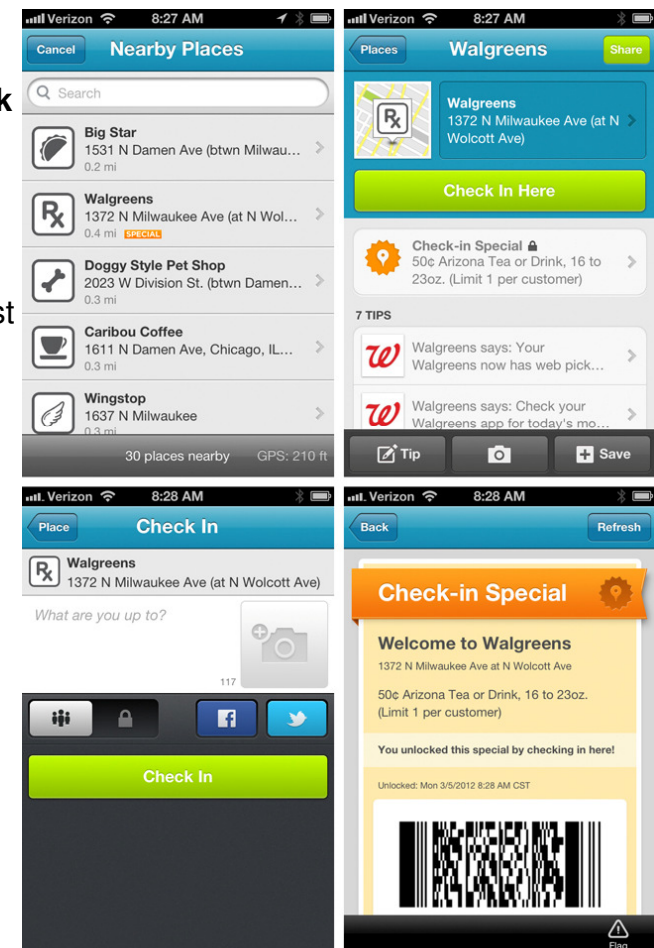
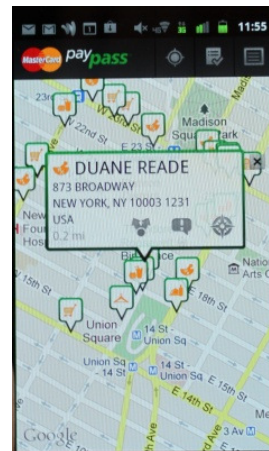


Theme #1: Retailers Engage Customers through Mobile Devices

Walgreens – The Epitome of SOLOMO



- Tapping into the power of SOLOMO
 - **LO: The couponing partnership with the social location-based check in startup FourSquare is the first of its kind.**
 - Customers that check in at any Walgreens through FourSquare will instantly receive a unique scannable coupon via smartphone that can be redeemed in store (March 2012).
 - Walgreens' Duane Reade NYC chain of drugstores was one of the first retailers to pilot the Google Wallet, which utilizes near field communication (NFC) technology to transmit payments, store loyalty card information, and alert customers of offers from participating merchants.

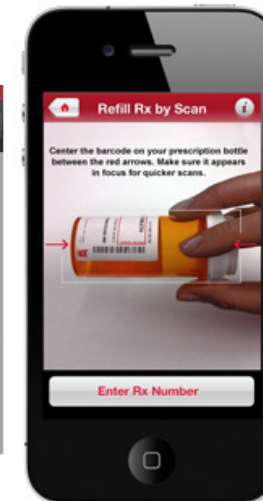
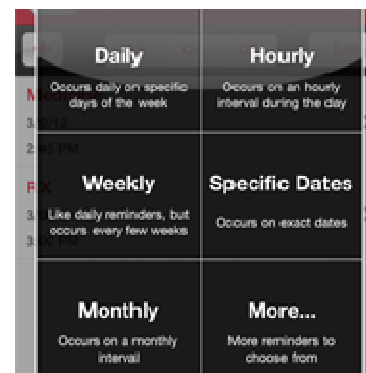
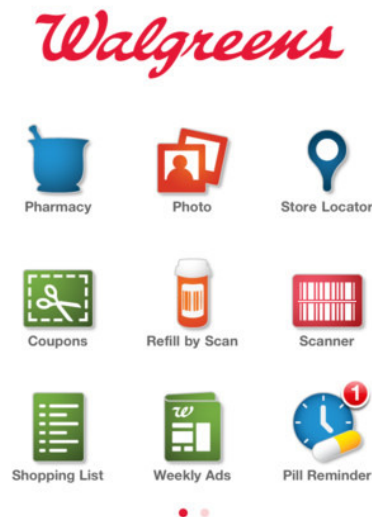


Theme #1: Retailers Engage Customers through Mobile Devices

Walgreens – The Epitome of SOLOMO



- Tapping into the power of SOLOMO
 - **MO: The main idea behind Walgreens' mobile strategy is making the store available in your pocket.**
 - Walgreens was the first retailer on Black Friday to issue coupons that could be scanned from a mobile phone at the register and has since deployed several other mobile features for its customers.
 - The company has also been working on digital engagement in stores with QR codes to make stores more accessible.
 - Walgreens has created several pharmacy and healthy living applications for mobile phones.
 - Pill Reminder was recently released and allows patients to refill their prescriptions by scanning the barcode with a phone. Refills by scan accounts for over 40% of online prescription refills. Pill Reminder also reminds patients that opt-in of when they need to take their pills and has been proven to help patients adhere to prescribed regimens.
 - Transfer by Scan is also a feature within the new Walgreens mobile app.
 - Walgreens Text Alerts are sent to customers via SMS with in-store promotion information and links to coupons. There are over 3 million subscribers thus far.



Theme #1: Retailers Engage Customers through Mobile Devices

Walgreens – The Epitome of SOLOMO

Walgreens

- **Recognizing the value of the multichannel customer**
 - According to research conducted by Walgreens, the multichannel customer is 3x more valuable than the mono-channel consumer.
 - Though online sales penetration is relatively low, Walgreens.com has experienced significant double digit growth for the past few years. Web pick-up (a feature that allows customers to order online and pick-up in stores) has driven traffic and enhanced the customer experience through incremental convenience.
- **Reassuring customers that their privacy is a top priority**
 - Two of the biggest concerns about SOLOMO in the retail pharmacy sector are privacy and security. Walgreens has placed several safeguards to protect consumers from sharing details about their medications on social media.
- **Preserving the community pharmacy through personalization features**
 - A new tool released in late April 2012 called “Find Your Pharmacist” allows customers to search more than 20,000 pharmacist profiles, ask pharmacists questions 24/7 via one-on-one live online chats, and match their health care needs with the areas of expertise, specialties, languages, and clinical backgrounds of Walgreens pharmacists.
 - Though location is usually the leading factor in pharmacy selection, recent studies showed nearly 70% of consumers would consider a different location if the pharmacist was trained in a specific area.
 - The tool is expected to advance community pharmacies and help customers connect more meaningfully with their pharmacists, ultimately driving loyalty.

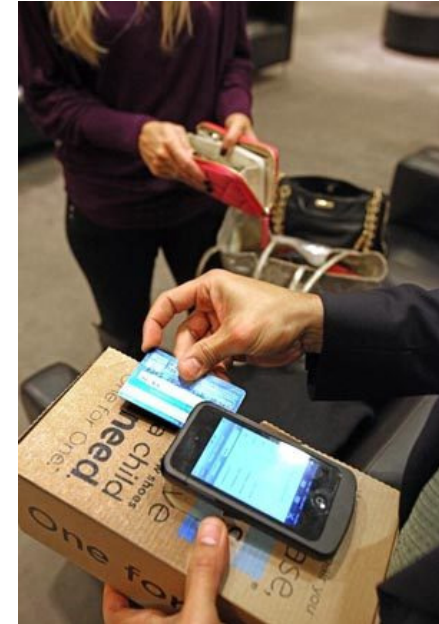


Theme #2: Mobile & Social Analytics Shape Retailers' View of the Customer

Nordstrom – Paving the way for Omnichannel in Department Store Retailing

- **The definition of service is evolving and continually enhancing the customer experience is an imperative**
 - Nordstrom values its customer service reputation and is experimenting with technology to translate superior service online. Specifically, the company has invested in personalization technology that recognizes a customer's unique preferences and style to foster improved relationships with online customers.
 - The consumer's path to purchase has evolved... and Nordstrom is evolving with them.
 - The company listens to customers and responds by expanding the merchandise assortment and creating innovative purchasing platforms. For example, Nordstrom is bringing Bonobos, a pure-play online menswear company, into its stores. The partnership is expected to be "symbiotic" and allow Nordstrom to learn from Bonobos' e-commerce successes and digital marketing strategy.
- **Bring Checkout to the Customer with Mobile POS Devices**
 - To make more space in the stores (on average 300 to 400 sq feet), Nordstrom has removed some cash wraps in full-line stores and deployed mobile POS (point-of-sale) devices that allow customers to speedily checkout anywhere in the store through a modified handheld.
 - These mobile checkouts have been more impactful at the Nordstrom Rack division because it reduces wait time and the number of registers.
 - A total of 6,000 mobile POS units were adopted at the full line department stores by the end of the third quarter in 2011.
 - Nordstrom rolled out the technology very quickly. It only took 9 months to go from idea to engineering and coding to implementation.
 - Mobile POS has some limitations but Nordstrom is innovating to get the functionality on par with traditional POS by the end of 2012.

NORDSTROM



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Theme #2: Mobile & Social Analytics Shape Retailers' View of the Customer

Nordstrom – Paving the way for Omnichannel in Department Store Retailing

NORDSTROM

- **Hiring top talent to secure an innovative future**
 - Nordstrom has hired approximately 400 new employees to help grow its digital business.
 - Expertise in mobile and social commerce is limited because it is an emerging channel. Nordstrom is tapping external talent to implement its omnichannel initiatives and invest in personnel that can utilize cutting edge analytics to better predict customer behavior and sales trends.
 - The company has also invested in a larger IT team to create, develop, and test new platforms and ideas.
- **In the early innings of utilizing social media to drive sales**
 - The majority of marketing spend at Nordstrom has shifted to online media (email and search) and many companies are still trying to figure out how to use social media as a sales driver.
 - Social media is presently used as a traffic driver to communicate events, company initiatives, and service enhancements.
- **Offer Free Shipping and Returns**
 - The company began offering everyday free shipping and free returns with no minimum purchase threshold in August 2011. As a result, conversion is up and average order size has held up surprisingly well.
 - Free shipping is now one of the drivers of the online business.
 - Nordstrom is also piloting same-day delivery services. These delivery services have the potential to drive incremental sales and improve sales productivity.

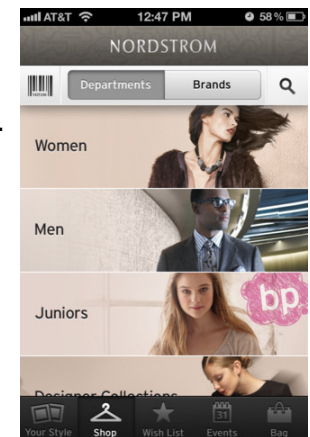
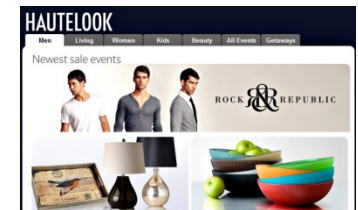


Theme #2: Mobile & Social Analytics Shape Retailers' View of the Customer

Nordstrom – Paving the way for Omnichannel in Department Store Retailing

NORDSTROM

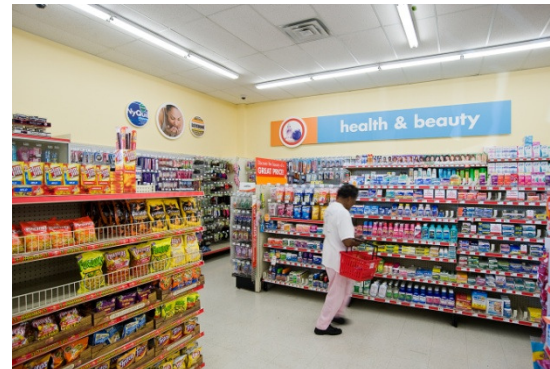
- **Thinking Outside of the Box**
 - Nordstrom recognized that speed is key for e-commerce and m-commerce.
 - “It’s about how fast you can move in that space.”
 - Nordstrom acquired HauteLook in 2011 to enter the fast-growing flash sales business.
 - It took 100+ years to get 10 million customers at Nordstrom and within a few years and little advertising HauteLook had 4 million customers.
 - By the end of 2011, HauteLook had over 7 million customers and the company expects it will break even early 2013.
 - Nordstrom is experimenting with new ways to acquire and engage customers.
 - Nordstrom now uses Pandora (internet radio and subscription service) to collect email addresses.
 - According to Nordstrom, the younger consumer is saying to retailers: “I know you have tons of data about me and you need to use it!”
 - Nordstrom updates their website often.
 - In the past, Nordstrom’s site upgrade cadence was once or twice a year.
 - For the past six months, they have been updating monthly.
 - The key to personalization is to marry the technology and the sales person.
 - Nordstrom started to give commissions to sales people that referred customers to purchase merchandise online.
 - **One Strategy.**
 - The company does not separate its e-commerce and store strategy.
 - Nordstrom has one merchandising strategy and one customer strategy.



Theme #3: Maximize Returns with Optimization Technologies

Family Dollar – Investing in the Right Place

- **Driving Traffic through an Improved Customer Offering**
 - Family Dollar is starting to attract new customers through expanding their assortment and investing in new categories.
 - In F3Q12, approximately 1,000 new SKUs will be rolled out to food and health and beauty aids. The company added Pepsi products this quarter.
 - Family Dollar will be adding tobacco products to reach a totally different customer. The next frontier is beer. These additions will result in incremental items in the basket and it should capture an additional trip from its most loyal customers.
 - These assortment changes will help Family Dollar capture a greater share of its customer's grocery budget and drive improved sales productivity.
- **Truly Localizing the Assortment with Advanced Optimization Technologies**
 - Local is the cornerstone of the merchandising and inventory strategy.
 - Leverages granular statistical and economic modeling to constantly analyze inventory and replenishment levels to maximize promotional effectiveness and gross margins. The technology has reduced markdown risk and configures store clusters using efficient frontier modeling.
 - Family Dollar has combined the power of Big Data analytics and the cost efficiency of the cloud to deliver the right inventory in the right stores to optimize sales performance. In addition, the company does zone pricing that Dollar General does not.



Theme #3: Maximize Returns with Optimization Technologies

Family Dollar – Investing in the Right Place **FAMILY DOLLAR**

- **Redesigning Store Interiors to Make Spaces More Inviting**

- Real Estate in retail has been fundamentally changed by the digital revolution, but dollar stores continue to grow at breakneck speed.
- Family Dollar is building new stores and renovating older locations with more intuitive merchandising adjacencies, improved signage, high capacity fixtures, and expanded consumable sections, and additional refrigeration and coolers.
- These stores have experienced a 10% sales lift between the redesign and expanded assortment.

- **E-Commerce is Still an Opportunity**

- Family Dollar does not have an e-commerce presence now.
- There is an opportunity for incremental growth and upside should the company establish an e-commerce storefront.

FDO's Standard Store (Before)



FDO's Revitalized Store (After)

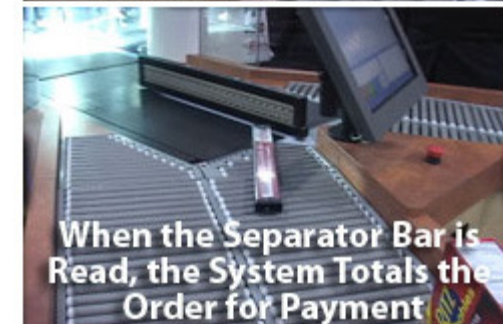


Theme #4: Moving to One View of the Customer: Customer Analytics

Kroger – Catering to the Customer



- **Helping Resourceful Customers Save Money In-Store**
 - Electronic Coupons: To drive traffic to their website, Kroger has made Kroger.com the portal that aggregates 5 different coupon sites seamlessly integrated on one.
 - Customers can download the coupons from Kroger.com or to the loyalty card.
 - Kroger’s Fuel Rewards is a “cents-off” card that offers pharmacy, grocery, and gift card customers \$0.10 cents off per gallon of fuel with qualifying purchases.
- **Honor the Customer’s Busy Schedule**
 - To improve the customer experience and wait times in-stores, Kroger has invested in front-end and “line busting” technologies to lower the average time spent in line to 40 seconds vs. 6 minutes five years ago.
 - Scan Tunnel removes barcode scanning from the grocery checkout equation by utilizing auditing technology that detects the shape, weight, and other characteristics of each item.



Source: SCDigest

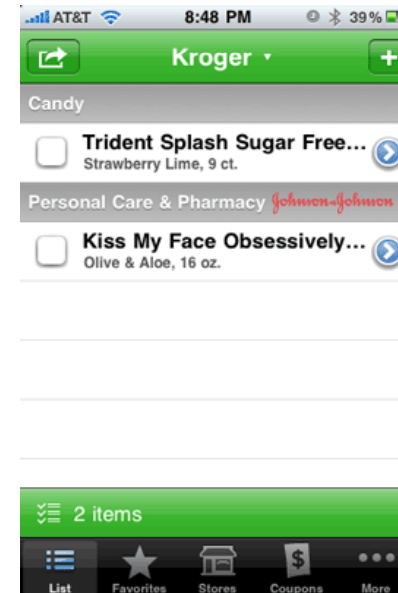


Theme #4: Moving to One View of the Customer: Customer Analytics

Kroger – Catering to the Customer



- **Respond to the Customer's Desire for Customization and Convenience**
 - Kroger also released a cloud based shopping list that can be updated on a mobile device and modified on the website.
 - The big focus is on customization, localization, and personalization.
 - The company has a joint venture with dunnhumby USA that performs data mining services for the loyalty program and targets promotions for specific customers and segments.
- **Investing in the Future**
 - Kroger Labs is the hub of the company's intellectual property portfolio.
 - Constantly researching and developing patented technologies to implement or license to other companies.



Theme #5: Marketing and IT Converge

Costco – Exploring E and M-Commerce



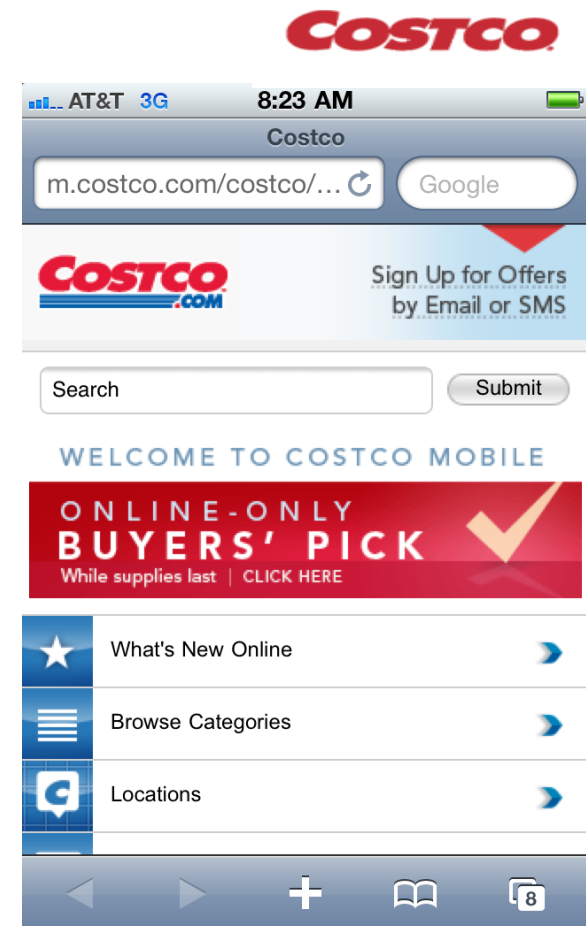
- **Knowing your strengths**
 - Costco admits it prefers to stick with what it does best, Warehouse retailing and member satisfaction. As a result, the company has been slower to implement cutting-edge SOLOMO technologies.
 - Instead, they have focused on other priorities such as getting their Asian and Australian businesses up and running.
- **Investing in e-commerce optimization tools**
 - Costco does very little marketing of its online business and Costco.com items do not currently appear in Google searches.
 - Costco has solved this problem by investing in search engine optimization tools and re-platforming the website, which will be operational by summer 2012 (F2Q12). This initiative inspired marketing and IT to collaborate.
 - Costco has recently begun testing QR (quick response) codes to gauge customer interest in using mobile technology to research Costco products and offers.
 - To advertise online promotions, Costco has collected 12 million email addresses and experiments with email marketing 3x per week.
 - Translating the e-commerce website, logistics, and customer experience across geographies is a challenge in retail. Costco will be introducing its e-commerce business to the UK market in September. In the future, the company plans to open in Japan and South Korea.



Theme #5: Marketing and IT Converge

Costco – Exploring E and M-Commerce

- **The Warehouse in your pocket**
 - Within the next few months, Costco will launch an iPhone and Android app.
 - The app will feature a full suite of features such as:
 - Speak or type to search
 - Coupon storage and shopping lists
 - Refill prescriptions
 - Small business supply replenishment and pick-up orders
 - Warehouse Locator and Membership Renewal
- **Low tech can still enhance the customer experience**
 - Costco has improved the customer experience by investing in front-end technologies that speed up the checkout process.
 - Amex cardmembers do not have to sign receipts for transactions less than \$100.
 - All of the receipt printers were upgraded to produce customer receipts more efficiently.



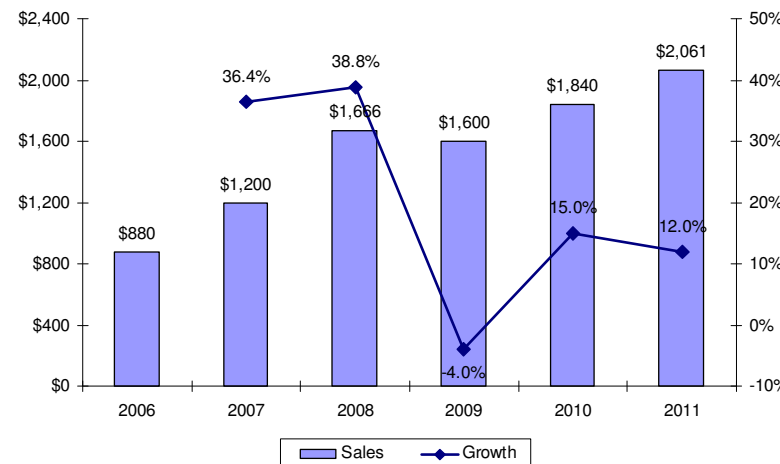
Theme #5: Marketing and IT Converge

Costco – Exploring E and M-Commerce



- **The benefits Costco experienced when marketing and IT collaborated**
 - Positive SSS YTD.
 - Average ticket online is \$350 vs. \$140 in clubs.
 - SKU overlap is only 20% (to complement in-club jewelry offering and other select categories).
 - Costco.com maintains a relatively low SKU count online (3,700 to 3,800).
 - Big ticket items compose the majority of sales (furniture, appliances, pool tables, hot tubs, exercise equipment).
- **What's next for Costco in e and m-commerce?**
 - Plans to double or triple the e-commerce business in 7 to 8 years.
 - Opportunity to continuously improve both web and mobile storefronts and experiment with social media advertising campaigns.
 - There is a substantial plan in place to roll out e-commerce to all countries where Costco has a presence.

Costco Historic Sales and Growth



Costco's fiscal year runs through August 2009. Also, Costco's online business is mostly big ticket, which got hit during the recession.



Takeaways and Conclusions

The Challenge for Marketing

- **SOLOMO as a business imperative**
 - As Social and Mobile become more important in terms of marketing dollars spent, we are beginning to see marketing and IT converge. Mobile ad spend worldwide was predicted at \$3.3 billion in 2011 and projected to grow to \$20.6 billion in 2015 (source:mobiThinking).
- **Need for Collaboration**
 - Marketing and IT have come together to integrate web intelligence, allowing retailers to view consumer browsing behavior. Historically, the biggest barrier to effective collaboration has been the lack of process integration and defined success criteria.....that is beginning to change!
- **Big Data**
 - With such aggressive growth expected for the volume of data in 2012, the IT world scrambled during 2010 and 2011 to advance Big Data to be able to extract useful insights from increasingly large sets of information and, specifically, the unstructured data that social media and sensors provide.
- **Better Insights**
 - The possession of better insights on customers from data sets will enable retailers to further experiment with digital marketing initiatives and develop more relevant campaigns.
- **Social Data**
 - With respect to social data, marketing and IT will unite when social CRM becomes a critical component in “operationalizing” the large amounts of social data to enhance business operations.
- **The Titans are Coming to Store Near You**
 - Online retailers are beginning to open physical stores and the need for differentiation beyond price will increase.



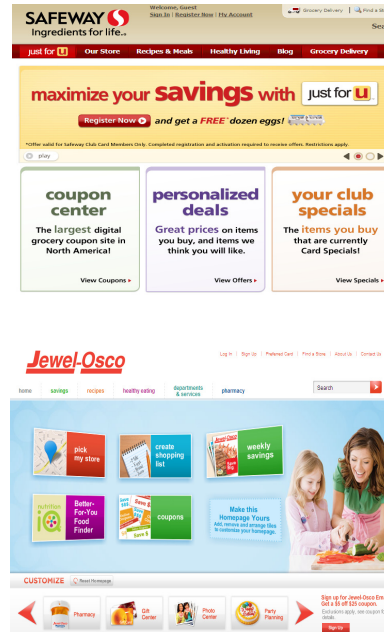
Driving Loyalty through Analytics and Technology

- Customer analytics allows retailers to build predictive capabilities, improve customer retention, and better plan for the future. Using customer analytics, retailers can create a sense of brand loyalty and help drive sales.
- According to dunnhumby, sales from one loyal customer equals 12 non-loyal customers. Retailers continue to try to unlock this value by targeting loyal customers and offering deals and discounts that fit their spending habits.
- Many of our retailers have increased their focus on loyal customers. KR and M continue to use loyalty programs to analyze their customers' spending behavior, SVU and SWY have improved their websites to offer targeted promotions, and TGT has instituted a 5% rewards program for customers that use its credit cards.

KR and M use dunnhumby to develop a better understanding of their customer and offer targeted promotions to drive SSS



SVU and SWY have updated their websites to offer loyal customers promotions that fit their shopping habits. SWY is rolling out a program called "Just for U" that personalizes offers based on history and loyalty card data.



TGT's 5% Rewards program offers a 5% discount to all customers who use the company's store credit cards.



What will level the playing field?

- To compete with the titans retailers need to bring “online inside”:
 - **Same Day Shipping**
 - Nordstrom is piloting same-day delivery service.
 - **In-Store Pick-Up**
 - Walmart already has a strong Home Free program to pick up items for free in stores or at FedEx Kinkos locations.
 - Consumers can check the e-commerce site to see which store has inventory.
 - **Exclusive and Private Label Product**
 - Food retailers like Kroger have mastered this idea.
 - JCP’s new merchandising strategy will be anchored by exclusives like L’amour Nanette Lepore.
 - **In-Store Events and Trunk Shows**
 - Saks and Macy’s host events with designers in stores.
 - **Out of the Box Thinking**
 - Saks and Macy’s have also partnered with the reality TV show “Fashion Star.”

What will level the playing field?

- To compete with the titans retailers need to bring “online inside”:
 - **Loyalty Programs and Incentives**
 - Target started its 5% rewards program in which Target credit and debit card customers can save 5% on all purchases and get free shipping for all online orders.
 - Costco experiences an 89.4% renewal rate with its members in the U.S. and Canada.
 - Nordstrom is constantly learning from its trials and adjusted its Fashion Rewards program in 2012 to attract more customers by adding additional benefits, such as triple point days and free alterations.
 - Walgreens is using technology and access to its pharmacists to make the customer experience more convenient.
 - Family Dollar is driving additional trips by adding different merchandise categories consumables, tobacco.
 - Kroger has a best-in-class loyalty program through data mining.
 - **Online and In-Store Pricing Parity and Price Guarantees**
 - Currently, Target and Walmart prices are slightly cheaper (~1% to 2% less) online than in store.
 - Walmart had the Christmas Price Guarantee during Holiday 2011.
 - **More Ways to Pay**
 - Walmart started offering cash payment options for “underbanked” customers on its e-commerce store in April 2012.
 - **Unilateral Pricing Policy, also known as UPP**
 - This is especially relevant for electronics. (i.e. Apple iPads start at \$499 at most retailers).
 - Target also reached out in a letter to vendors to partner on pricing to combat the impact of showrooming.

How to Thrive in the Era of the Titans

- **Now that we know *WHAT* retailers need to do, *HOW* are they doing it?**
 - **Inventory Visibility**
 - Enabled by RFID (radio frequency identification) tags.
 - Visibility improves shipping and logistics to fulfill orders as quickly as possible.
 - **Smaller Store Footprints**
 - Walmart and Kohl's are building smaller stores that stock higher value products.
 - **Reconfigure and constantly refresh the interiors of stores**
 - Family Dollar is one example of stores that have been redesigned to arrange merchandise more intuitively and efficiently to maximize profitability.
 - **Customer Service**
 - Retailers can provide a level of customer service that cannot be duplicated online.
 - Equip associates with a deep knowledge of products, mobile devices and tablets that facilitate ordering online in store, and offer additional services

What's Next?

- **The 3 pain points that retailers need to address:**
 - Big Data needs to address the lack of data and the quality of data.
 - Lack of integration of marketing, IT, and merchandising.
 - Updating outdated systems and infrastructure (pent up demand for software).
- **Utilizing social media as a CRM tool (client relationship management)**
 - These are the largest self-maintaining database of individual consumer demographic, psychographic, and preference information that retailers can harness to engage customers and remain relevant.
 - Social media supports microsegmentation that retailers can use refine and identify the most valuable customers. It also facilitates customization and personalization of targeted promotions.
- **Rise of the Chief Mobility Officer?**
 - According to Forrester, there will be over a billion smartphones and tablets in circulation by 2016 and companies need a centralized department and executives to improve the coordination of mobile initiatives.
 - Spending on mobile apps will grow by 100% by 2015 and spending to develop apps is projected to be \$55 billion in 2016.
 - Investment in tablets will increase substantially YOY and enterprise mobility management will become a larger department within IT.
 - “If you’re not doing mobile, you’re not doing anything.”
- **Innovation is rampant in retail right now. Where are you on the innovation curve?**
 - The Apple-ization of retail
 - In-store Wi-Fi Networks which will allow customers to use mobile phones as a shopping tool (and not a curse).
 - QR codes are the simplest way to take a customer to an application and support promotions in a meaningful way.
- **Cloud and the pay-as-you-go software model could free up budgets to invest in other projects.**
 - The cloud minimizes investment in hardware and retailers can use funds to develop a better customer experience.
- **Real-time data and insights have high potential.**
 - One of the fundamental problems in retail is operating off old information.
 - Real-time insights have been proven to raise overall profitability and marketing effectiveness.

Questions?

Valuation

DEPARTMENT STORES

Rating	Company	TKR	Price Target	2012 P/E Mult.	2012 Tgt. EV/EBITDA	Price 4/25/2012	Return to Target	Sales 2011 (MM)	Shares Out (MM)	Mkt. Cap. MM	52 Wk Range		EPS			CAGR 08-11	P/E			Relative P/E		PE/G	Div 5-Yr Yld %	P/S	EV/EBITDA 2012	FCF Yield 2012	Performance		
											High	Low	2010	2011	2012E		2010	2011	2012E	2011	2012E						2011	2012E	1-Week
NR	Dillard's	DDS	N/A	N/A	N/A	\$63.88	N/A	\$6,569	46.2	\$2,952.4	\$64.84	\$38.99	\$2.55	\$4.34	\$5.13	NM	NM	NM	NM	NM	NM	NM	0.3	0.4	5.8x	NR	-0.6%	39.1%	42.3%
Buy	JC Penney	JCP	\$50	N/A	8.0x	35.66	40.2%	17,260	213.5	7,615.2	43.18	23.44	1.59	1.25	1.75	-21.1%	22.4x	28.5x	20.4x	201%	148%	-17.5x	2.4	0.4	6.4x	3.5x	3.3%	-4.6%	1.5%
Buy	Nordstrom	JWN	\$63	17.0x	N/A	55.18	14.2%	10,497	207.6	11,455.4	56.75	37.28	2.75	3.14	3.63	19.7%	20.1x	17.6x	15.2x	124%	110%	0.9x	2.0	1.1	7.5x	7.0%	-1.4%	16.6%	11.0%
Buy	Kohl's	KSS	\$57	12.0x	N/A	49.76	14.5%	18,804	253.4	12,610.7	57.39	42.14	3.66	4.30	4.78	15.5%	13.6x	11.6x	10.4x	81%	76%	-0.4x	1.9	0.7	5.2x	11.3%	-2.7%	-4.4%	0.8%
Buy	Macy's	M	\$49	14.0x	N/A	39.94	22.7%	26,405	414.2	16,543.1	41.27	22.66	2.11	2.88	3.50	30.6%	18.9x	13.9x	11.4x	98%	83%	-0.4x	2.1	0.6	5.7x	11.7%	-0.6%	65.3%	24.1%
NR	Sears Holdings	SHLD	N/A	N/A	N/A	52.25	N/A	39,658	106.3	5,554.2	87.12	28.89	1.34	-4.69	-4.65	NM	39.0x	NM	NM	NM	NM	NM	0.0	0.1	21.0x	NR	-8.9%	-36.5%	64.4%
Buy	Saks	SKS	\$14	N/A	8.0x	10.78	29.9%	3,014	159.9	1,723.5	12.14	7.67	0.19	0.44	0.53	NM	56.7x	24.5x	20.3x	172%	143%	-0.7x	0.0	0.6	5.7x	5.4%	-3.3%	-6.3%	10.6%

DISCOUNT STORES

Rating	Company	TKR	Price Target	2012 P/E Mult.	2012 Tgt. EV/EBITDA	Price 4/25/2012	Return to Target	Sales 2011 (MM)	Shares Out (MM)	Mkt. Cap. MM	52 Wk Range		EPS			CAGR 08-11	P/E			Relative P/E		PE/G	Div 5-Yr Yld %	P/S	EV/EBITDA 2012	FCF Yield 2012	Performance		
											High	Low	2010	2011	2012E		2010	2011	2012E	2011	2012E						2011	2012E	1-Week
Buy	Target	TGT	\$67	14.0x	N/A	\$56.83	17.9%	\$68,466	669.3	\$38,036.3	\$58.95	\$45.28	\$3.86	\$4.26	\$4.30	13.8%	14.7x	13.3x	13.2x	94%	96%	-0.5x	2.1	0.6	6.6x	23.1%	-1.3%	13.9%	11.0%
Buy	Wal-Mart	WMT	\$71	14.0x	N/A	57.36	23.8%	443,854	3,424.7	196,440.6	62.63	48.31	4.07	4.49	4.92	9.5%	14.1x	12.8x	11.7x	90%	85%	-0.5x	2.8	0.4	6.4x	8.2%	-7.3%	7.1%	-4.0%

WHOLESALE CLUBS

Rating	Company	TKR	Price Target	2012 P/E Mult.	2012 Tgt. EV/EBITDA	Price 4/25/2012	Return to Target	Sales 2011 (MM)	Shares Out (MM)	Mkt. Cap. MM	52 Wk Range		EPS			CAGR 08-11	P/E			Relative P/E		PE/G	Div 5-Yr Yld %	P/S	EV/EBITDA 2012	FCF Yield 2012	Performance		
											High	Low	2010	2011	2012E		2010	2011	2012E	2011	2012E						2011	2012E	1-Week
Neutral	Costco (1)	COST	\$85	20.0x	N/A	87.28	-2.6%	87,048	434.9	37,960.6	92.10	70.22	3.13	3.50	4.12	4.3%	27.9x	24.9x	21.2x	175%	154%	2.2x	1.1	0.4	9.4x	4.2%	-0.4%	10.7%	4.8%

DOLLAR STORES

Rating	Company	TKR	Price Target	2012 P/E Mult.	2012 Tgt. EV/EBITDA	Price 4/25/2012	Return to Target	Sales 2011 (MM)	Shares Out (MM)	Mkt. Cap. MM	52 Wk Range		EPS			CAGR 08-11	P/E			Relative P/E		PE/G	Div 5-Yr Yld %	P/S	EV/EBITDA 2012	FCF Yield 2012	Performance		
											High	Low	2010	2011	2012E		2010	2011	2012E	2011	2012E						2011	2012E	1-Week
NR	Big Lots	BIG	N/A	N/A	N/A	87.28	N/A	\$6,093	65.6	\$5,725.8	\$92.10	\$70.22	\$2.93	\$3.30	\$3.86	13.0%	N/A	N/A	N/A	N/A	N/A	N/A	1.1	1.1	4.7x	NR	-4.5%	4.8%	-1.8%
Buy	Dollar General	DG	\$54	19.0x	N/A	46.30	16.6%	14,807	337.3	15,619.2	47.59	29.84	1.86	2.37	2.80	73.4%	24.9x	19.5x	16.5x	137%	120%	-0.8x	0.0	1.1	8.9x	4.1%	-0.5%	48.5%	12.5%
NR	Dollar Tree	DLTR	N/A	N/A	N/A	98.84	N/A	7,398	119.0	11,764.4	99.68	56.83	3.24	4.03	4.92	17.7%	30.5x	24.5x	20.1x	172%	146%	1.3x	0.0	1.6	8.7x	NR	0.6%	72.9%	16.9%
Buy	Family Dollar (1)	FDO	\$69	18.0x	N/A	66.90	3.1%	8,548	117.8	7,878.5	68.46	44.42	2.68	3.24	3.82	23.4%	25.0x	20.6x	17.5x	145%	127%	1.4x	1.3	0.9	8.7x	-0.5%	3.4%	28.2%	16.0%
NR	Fred's	FRED	N/A	N/A	N/A	14.32	N/A	1,879	37.0	530.3	15.27	10.27	0.75	0.86	0.99	14.7%	N/A	N/A	N/A	N/A	N/A	N/A	1.7	0.3	4.9x	NR	-4.5%	4.8%	-1.8%

DRUG RETAILERS

Rating	Company	TKR	Price Target	2012 P/E Mult.	2012 Tgt. EV/EBITDA	Price 4/25/2012	Return to Target	Sales 2011 (MM)	Shares Out (MM)	Mkt. Cap. MM	52 Wk Range		EPS			CAGR 08-11	P/E			Relative P/E		PE/G	Div 5-Yr Yld %	P/S	EV/EBITDA 2012	FCF Yield 2012	Performance		
											High	Low	2010	2011	2012E		2010	2011	2012E	2011	2012E						2011	2012E	1-Week
Buy	CVS	CVS	\$51	15.0x	N/A	\$43.80	16.4%	\$107,100	1,302.4	\$57,044.2	\$45.88	\$31.30	\$2.67	\$2.80	\$3.40	4.7%	16.4x	15.6x	12.9x	110%	94%	1.1x	1.5	0.5	4.9x	6.1%	-0.3%	21.0%	7.4%
NR	Rite Aid (2)	RAD	N/A	N/A	N/A	1.43	N/A	25,973	898.5	1,284.8	2.12	0.85	-0.64	-0.43	-0.22	NM	NM	NM	NM	NM	NM	0.0	0.0	7.1x	NR	-7.7%	38.8%	13.5%	
Sell	Walgreen (1)	WAG	\$29	11.0x	N/A	35.30	-17.8%	72,184	873.5	30,834.6	45.34	30.34	2.42	2.63	2.64	7.6%	14.6x	13.4x	13.4x	94%	97%	-0.7x	2.6	0.4	10.9x	6.5%	0.7%	-17.3%	6.8%

FOOD RETAILERS

Rating	Company	TKR	Price Target	2012 P/E Mult.	2012 Tgt. EV/EBITDA	Price 4/25/2012	Return to Target	Sales 2011 (MM)	Shares Out (MM)	Mkt. Cap. MM	52 Wk Range		EPS			CAGR 08-11	P/E			Relative P/E		PE/G	Div 5-Yr Yld %	P/S	EV/EBITDA 2012	FCF Yield 2012	Performance		
											High	Low	2010	2011	2012E		2010	2011	2012E	2011	2012E						2011	2012E	1-Week
Buy	Kroger	KR	\$28	12.0x	N/A	\$23.19	20.7%	\$90,374	574.8	\$13,328.9	\$25.85	\$21.14	\$1.76	\$2.00	\$2.32	1.3%	13.2x	11.6x	10.0x	82%	73%	-0.4x	2.0	0.1	4.6x	13.9%	-2.1%	-5.4%	-4.3%
Neutral	Safeway	SWY	\$22	11.0x	N/A	21.60	1.9%	43,630	268.0	5,788.8	25.43	15.93	1.55	1.73	1.95	-7.8%	13.9x	12.5x	11.1x	88%	80%	1.1x	2.0	0.1	5.0x	16.8%	-1.5%	-12.3%	2.7%
Neutral (H)	Supervalu	SVU	\$7	N/A	4.5x	6.15	13.8%	36,100	212.3	1,305.4	11.77	5.07	1.39	1.25	1.36	-24.4%	4.4x	4.9x	4.5x	35%	33%	1.0x	5.7	0.0	3.5x	17.6%	-4.5%	-43.9%	-24.3%
*	Whole Foods	WFM	*	N/A	N/A	83.04	N/A	11,612	182.4	15,143.8	86.35	53.32	1.44	1.93	2.30	28.5%	57.7x	43.0x	36.1x	303%	262%	2.2x	0.7	1.3	11.8x	NR	-3.1%	25.2%	19.3%

TOTAL GROUP

Market Cap Weighted Avg.		257.5	\$11,367.1	\$52.72	\$30.80	\$2.39	\$2.31	\$2.79	15.9%	20.5x	16.5x	13.5x	116%	98%	1.7	7.5x	-1.6%	18.5%	17.9%
Department Stores		257.5	\$11,367.1	\$52.72	\$30.80	\$2.39	\$2.31	\$2.79	15.9%	20.5x	16.5x	13.5x	116%	98%	1.7	7.5x	-1.6%	18.5%	17.9%
Discount Stores		2,977.7	170,744.6	62.03	47.82	4.04	4.45	4.82	10.2%	14.2x	12.9x	11.9x	90%	87%	2.6	6.5x	-6.3%	8.2%	-1.6%
Wholesale Clubs		434.9	37,960.6	92.10	70.22	3.13	3.50	4.12	4.3%	27.9x	24.9x	21.2x	175%	154%	1.1	9.4x	-0.4%	10.7%	4.8%
Dollar Stores		212.8	11,500.9	72.04	45.57	2.54	3.11	3.72	39.0%	26.8x	21.4x	17.9x	151%	130%	0.4	8.3x	0.7%	51.4%	15.2%
Drug Retailers (2)		1,151.9	47,847.9	45.69	30.96	2.58	2.74	3.13	5.7%	15.8x	14.9x	13.1x	105%	95%	1.9	7.0x	0.0%	7.5%	7.2%
Food Retailers		344.5	12,433.2	51.02	33.40	1.58	1.90	2.22	10.4%	31.9x	24.9x	21.1x	175%	153%	1.7	7.7x	-2.5%	5.1%	6.2%
Total		896.6	\$23,400.7	\$59.87	\$42.89	\$3.21	\$3.52	\$3.94	9.9%	18.5x	16.1x	14.1x	113%	103%	2.0	7.2x	-3.4%	14.1%	3.4%
Coverage Universe			\$30,279.0	\$57.80	\$42.54	\$3.31	\$3.68	\$4.09	11.2%	16.6x	15.0x	13.3x	105%	96%	2.2	6.8x	-3.4%	10.9%	2.8%

RELATIVE INDICES

Index	SPX	\$1,390.69	\$1,422.38	\$1,074.77	\$85.49	\$97.80	\$101.00	16.5%	16.3x	14.2x	13.8x	6.7x	0.0%	4.0%	10.6%
S&P 500	SPX	\$1,390.69	\$1,422.38	\$1,074.77	\$85.49	\$97.80	\$101.00	16.5%	16.3x	14.2x	13.8x	6.7x	0.0%	4.0%	10.6%
S&P RETAIL	SP421	622.23	628.35	465.36									-0.1%	16.3%	18.9%
S&P FOOD & STAPLES	SP481	21													

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Appendix A-1

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12 Month Rating			Relative Rating		
Buy	Hold	Sell	Buy	Hold	Sell
59%	34%	7%	10%	79%	10%
45%	42%	37%	50%	43%	46%

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