First Quarter 2011
Investor Conference Call Prepared Remarks
June 16, 2011

Cindy Holmes, Director of Investor Relations:
Good morning and thank you for joining us. Before we begin, I want to remind you that today's discussion will include forward-looking statements. We want to caution you that such statements are predictions, and actual events or results can differ materially. A detailed discussion of the many factors that we believe may have a material effect on our business on an ongoing basis is contained in our SEC filings, but Kroger assumes no obligation to update that information.

Both our first quarter press release and our prepared remarks from this conference call will be available on our website at www.kroger.com.

After our prepared remarks, we look forward to taking your questions. In order to cover a broad range of topics from as many of you as we can, we ask that you please limit yourself to one topic with one question, and one follow-up question, if necessary. Thank you.

I will now turn the call over to David Dillon, Chairman and Chief Executive Officer of Kroger.

Comments by Dave Dillon:
Thank you, Cindy. Good morning everyone and thank you for joining us today. With me to review Kroger's first quarter 2011 results are Rodney McMullen, Kroger's President and Chief Operating Officer, and Mike Schlotman, Senior Vice President and Chief Financial Officer.

First Quarter Performance
We are very pleased with the exceptional overall results the Kroger team achieved in the first quarter. Our associates delivered on all facets of our Customer 1st strategy. We achieved strong sales, earnings and cash flow growth. Needless to say, Kroger continued to grow market share in the first quarter. In sum, we successfully managed our strategy throughout the quarter, which drove solid performance in all of the areas that are important to our business.

Identical supermarket sales increased 4.6%, without fuel, during the quarter. This continues Kroger's industry-leading trend of positive identical sales growth for 30 consecutive quarters. I want to thank all of our associates for their hard work to produce such outstanding results.

Our first quarter performance was broad-based. Each of our 18 retail divisions had positive identical sales, excluding fuel. We are particularly pleased with sales in our Deli/Bakery, Grocery, and Natural Foods departments.

These overall results have given us confidence to increase the original guidance we issued in March, which Mike will outline for you in a few minutes. Our guidance for the year reflects the balance we strive to achieve across our business – including strong identical sales growth and outstanding cost control, as well as increased earnings and earnings per share.

Our Customer 1st strategy is clearly connecting with customers. We have shown that our focus on people, products, prices and the shopping experience is meaningful to customers through both good and challenging times. Our strategy positioned us well to weather the recession and will continue to differentiate Kroger from our competitors, whatever the operating environment.

<u>Influencing Factors</u>

I'd like to touch on two themes that will have the most impact on our business over the course of the year. The first is our commitment to the Customer 1st strategy that we just discussed. We want to reduce the overall cost of running our business, and do it in a way that does not negatively impact our customers. We then reinvest those savings in our customers to drive higher sales which, in turn, will increase earnings.

The second theme is made up of several external factors that will influence Kroger's business this year. We discussed these five factors in March, and I'd like to briefly update you on what we are seeing in each of these areas.

- First, as you know, the weak economy continues to present significant challenges for most households. The promising signs of improvement we saw earlier this year seem to have stagnated. Unemployment remains high in most of our markets and food stamp and other government program use continues at high levels.

- As predicted, rising prices for food and fuel are affecting customer spending behavior. Rodney will have more to say about food inflation shortly.

- The overall retail environment is generally rational but strong competition for customers' limited dollars remains. Our price checks show that most competitors are passing higher costs on to consumers.

- We expect to face approximately $200 million of incremental expense from rising pension and health care costs for the year. Continued cost reduction in other areas is helping to offset these expenses so we can invest in areas that matter most to our customers.

- Finally, during the first quarter, our retail fuel operations generated the same earnings per share this year as last year. Because fuel is volatile we should expect variability over the next several quarters. Even so, fuel remains a meaningful offering for our customers.

Of these factors, only one had a negative effect on our business this quarter – the rising price of fuel. This is because a one-dollar-per-gallon increase takes a big chunk out of household budgets, perhaps as much as $100 per month, which forces families to make choices that change spending behavior. The other factors had a neutral to positive effect on our performance for the quarter.

We expect these factors will have a dynamic effect on the overall operating environment this year. We will continue to follow our business strategy and will make tactical adjustments as needed to weather these influences.

Rodney will now offer some insight into Kroger's strong business trends in the first quarter.

Comments by Rodney McMullen:
Thank you, Dave. Good morning everyone.

The Kroger team did a great job during the quarter to set the stage for the rest of the year. Our associates' efforts to control expenses enabled us to maintain a compelling price position relative to both discount and traditional grocery competitors, even as we continue to pass on cost increases. We are particularly pleased with our associates' dedication to connecting with our customers. This will truly differentiate Kroger from our competitors.

Loyal Household Growth
One measure of that connection is total household growth, which is up for the quarter. Our loyal household count grew at a faster rate than total household growth, indicating that our best customers are the primary beneficiaries of the investments we are making in the four key areas of our Customer 1st strategy. We continue to reward our best customers for their increased loyalty.

Customers visited our stores more frequently this quarter, and purchased more total units, compared to the same quarter last year.

Price per unit was higher in the first quarter compared to a year ago, reflecting the effect of price increases from our vendors. The combination of more households, more visits per household, more total units purchased and higher retail prices drove sequential improvement in identical sales.

When we dive deeper into Kroger's results for the quarter, we see that identical sales were positive for both total households and loyal households. Identical sales growth among loyal households was stronger than the overall result.

Tonnage Growth
Kroger continued to see positive tonnage growth throughout the quarter, which comes on top of strong unit movement last year. Our promotional and pricing strategies are

designed to deliver these sustainable results. The initiatives we implement focus on building long-term loyalty and expanding Kroger's competitive advantage.

Strong Corporate Brands

Kroger's first quarter results reflect the power of offering our customers a choice of both Corporate Brands and national brands. Millions of loyal households shop with us, and 99.9% of them bought at least one Corporate Brand item this quarter. This is particularly important today as many shoppers continue to watch their spending and look for quality items at good prices.

For the first quarter, Corporate Brands represented approximately 26% of Grocery department sales dollars and 33% of the Grocery department units sold. These figures compare with 26% and 34%, respectively, for the first quarter last year. Growth in national brand categories where Kroger does not have a presence was the primary driver of this decline. Corporate Brand share overall continues to be well in excess of pre-recession levels.

A highlight of the quarter was the launch of our new home essentials brand, Kroger Home Sense, with 200 reformulated or re-branded products. The collection of smart, simple solutions helps customers get great results everywhere in their home. You'll find our new brand in paper towels, facial tissue, paper house wares, and more. We also introduced new artisan-inspired Private Selection Hearth Baked Pizzas in the first quarter. These new offerings, and others like them, will help ensure our customers' continued loyalty through our exclusive preferred brands.

Food Costs

As Dave mentioned earlier, rising food costs are affecting consumer behavior. For the quarter, our estimated product cost inflation, excluding fuel, was approximately 3.5%.

We saw inflation in all categories, including Grocery, for which product cost inflation approached 2.1%, excluding milk.

Last quarter we mentioned that rising costs for many agricultural commodities were driving higher retail prices for packaged goods in our Grocery department. While that continues, inflation is disproportionately affecting our perishable departments – especially Seafood. We expect this trend to continue as well.

We are passing along product cost increases from suppliers and we plan to continue to do so. At the same time, we will continue to invest aggressively in our four keys – our pricing, people, products and customer shopping experience. Our customers continue to seek value in this economy. With inflation and rising gas prices, customers' budgets are stretched. The value we offer them through lower everyday prices, weekly features, and personalized rewards to loyal customers continue to resonate with them. We estimate we are currently saving our customers $2.1 billion per year. This demonstrates that while we are passing on inflation, we continue to provide significant value to our customers, including price.

Sustainability Efforts

We have done a lot of work over the last several years to integrate sustainable practices into our everyday business operations. Next week, we will publish our fifth sustainability report. As a preview, I'd like to highlight some of our most successful initiatives.

Five of our manufacturing plants have achieved the impressive goal of sending zero waste to landfills. That means that every ounce of raw material that arrives in a plant is either used for product, turned into energy, or recycled by our associates. We're on our way to achieving zero waste in our other manufacturing facilities as well. Since 2009, our Manufacturing Division has reduced our monthly waste to landfills by more than 50%.

Improved bagging techniques and increased use of reusable bags translated into saving an additional 159 million plastic bags in 2010. This puts us more than 35% of the way towards reaching our goal of saving a billion plastic bags by 2014.

I am proud to announce that our stores have now reduced their overall energy consumption by 30% since 2000. That's enough electricity to power every single-family home in Fort Worth, Texas for one year. I'd like to thank our associates for helping reduce Kroger's energy consumption through their individual actions every day. These efforts by our associates are helping make the world a better place to live.

Labor

Turning now to labor relations, we completed successful contract negotiations for our associates in Fort Wayne, Indiana, and negotiations continue in Southern California and with the Teamsters, who represent some of our associates in distribution and manufacturing operations in the Midwest. We will soon begin contract discussions in West Virginia as well as the Memphis area.

Our objective in every negotiation is to find a fair and reasonable balance between competitive costs and compensation packages that provide good wages, high-quality, affordable health care and retirement benefits for our associates.

It is worth noting that pension and health care costs attributable to our labor contracts in Southern California are extraordinarily high, making those negotiations particularly challenging. The labor and benefits costs in this market have had an impact on results, and we have not been enjoying the same level of success there as we have in the rest of the Company. We are hopeful that both sides will continue their hard work to find mutually acceptable solutions.

Now, Mike will offer more detail on the first quarter and Kroger's financial strategy. Mike?

Comments by Mike Schlotman:
Thanks, Rodney. Good morning everyone.

<u>First Quarter 2011 Results</u>

<u>First Quarter Net Earnings</u>

As Dave mentioned earlier, our identical supermarket sales, without fuel, increased 4.6% in the first quarter. Those sales drove the strong first quarter net earnings we reported earlier today, totaling $432.3 million, or $0.70 per diluted share. Net earnings in the same period last year were $373.7 million, or $0.58 per diluted share.

<u>First Quarter FIFO Gross Margin</u>

Excluding retail fuel operations, FIFO gross margin decreased 4 basis points. While this was helped by favorable shrink results, it was partially offset by higher diesel fuel costs.

<u>First Quarter OG&A Expenses</u>

Kroger's first quarter OG&A rate, excluding fuel, was 36 basis points lower than the same period last year. The benefits of leverage from strong sales, productivity improvements, and outstanding cost control more than offset rising credit card fees, health care and pension costs. Our objective is to invest in all four keys of our Customer 1st strategy. Identifying and delivering sustainable operating cost reductions allows us to make those investments consistently over time.

<u>Rent and Depreciation Expenses</u>

Our strong non-fuel sales allowed us to leverage rent and depreciation to provide a slight boost of about 7 basis points to the non-fuel operating margin.

<u>First Quarter Operating Margin</u>

While we saw a strong increase in the first quarter operating margin excluding fuel, we believe it is most beneficial to view operating margin over an annualized timeframe. On a rolling four quarters basis, our operating margin, excluding fuel, increased by 12 basis points. With our expectation of earnings per share near the top end of our guidance, we would expect fiscal year 2011 non-fuel operating margin to be slightly lower than this. It plays hand in hand with our strategy to continue to invest in gross margin as we are able to realize reductions on the OG&A line. We do expect to continue investments in our Customer 1st strategy during the year.

<u>Retail Fuel Operations</u>

Turning now to Kroger's retail fuel operations. In the first quarter, our supermarket fuel centers and convenience stores produced solid identical gallon growth. These outlets earned approximately 12.4¢ per gallon compared to 11.7¢ in the same quarter last year. As Dave noted earlier, strong fuel margins did not enhance Kroger's first quarter earnings per share on a year-over-year basis. This was primarily due to higher credit card fees, which increase as retail fuel prices rise. We need the higher margins to cover this expense.

We continue to expect margins of approximately 11.5 cents per gallon for fiscal 2011.

Financial Strategy

Capital Investment

I'll now update you on our long-term Financial Strategy. We are very focused on allocating the substantial cash flow of Kroger's business to reward our shareholders – both today and in the future. During 2011, Kroger plans to use cash flow from operations and cash on hand to fund capital expenditures, repurchase shares, pay dividends to shareholders, and maintain our current debt rating.

Capital investment, excluding acquisitions and purchases of leased facilities, totaled $573.1 million for the first quarter, compared with $532.2 million for the same period last year. We expect capital investment for the year to be consistent with our original guidance of $1.7 to $1.9 billion.

Kroger saw nice improvement in working capital during the quarter. One item that helped was higher fuel costs. We sell fuel before we have to pay for it so it lowers working capital. Additionally, we have implemented systemic improvements that will advance our progress in this area.

Share Repurchase and Dividend

During the first quarter, we invested $544.3 million to repurchase 23.1 million shares of stock at an average price of $23.55 per share. At the end of the first quarter, approximately $602.7 million remained under the $1 billion stock repurchase program authorized in March. We expect to use the full billion dollars during Fiscal Year 2011.

Debt Reduction

Net total debt was $7.1 billion, an increase of $47.3 million from a year ago. On a rolling four quarters basis, Kroger's net total debt to EBITDA ratio, adjusted for impairment charges in 2010 and 2009, was 1.79 compared with 1.91 during the same period last year.

Updated Guidance for Fiscal 2011

Just as the first quarter results position us well to continue investing in our Customer 1st strategy this year, they also position us for a better year than we originally thought. Therefore, we are increasing our identical supermarket sales and earnings guidance for fiscal 2011. We now expect identical supermarket sales growth, excluding fuel, of 3.5% to 4.5% for the year. The previous guidance range was 3% to 4%.

Kroger increased its earnings guidance for the year to $1.85 to $1.95 per diluted share. Based on the current operating environment, the Company expects to achieve results near the top end of this range. The increase reflects the strength of our first quarter results and the higher estimated LIFO charge of $150 million. The original guidance was $1.80 to $1.92 per share.

Additionally, we now expect product cost inflation to be in the range of 3% to 4%. The previous range was 1% to 2%.

Keep in mind the factors Dave mentioned that will continue to influence Kroger's sales and earnings performance throughout the year:

- The pace of the economic recovery;
- The impact of rising gasoline and food prices on customer spending;
- The competitive environment;
- Higher pension and healthcare costs; and
- Retail fuel margins.

As Dave said, most of these were favorable in the first quarter and it is too early in the year to know if that will continue.

Earnings per share growth rates in the second and third quarters will be near the low end of our full-year earnings per share growth expectations. This is primarily the result of the 2 cents per share tax benefit recorded in each of these quarters last year. This is consistent with the annual guidance we provided in March.

Our long term growth model is to generate 6% to 8% annual earnings per share growth over a rolling three-to-five-year time horizon. Including dividends, the total shareholder return rate is 8% to 10%. We aim to produce this with less volatility than the S&P 500 over that same timeframe. We are not opposed to a year occasionally exceeding this range, which is what we now expect to deliver in 2011.

Now, I will turn it back to Dave.

Comments by Dave Dillon:

This was a very strong quarter for Kroger. As a result of associates' hard work, we strengthened our connection with our customers, who, in turn, are spending more with us. Our Customer 1st strategy is producing positive results and will drive increased sales and earnings growth well into the future.

Now, we look forward to your questions.

Comments by Dave Dillon:
Before we end the call, I want to share some additional thoughts with our associates. First, thank you for your contributions to a solid start to the new fiscal year. You continued to delight and connect with our customers, and you achieved outstanding cost control in the first quarter. Your actions every day make a real difference.

I'd also like to recognize associates in several retail divisions for their heroic efforts during the recent severe storms.

- In Paducah, Kentucky, a team of nearly 100 associates and customers built a levee around Kroger store #414 to keep rising water from flooding the store.

- When tornadoes hit Huntsville, Alabama, associates kept our stores open and stocked – even without power and hot water – for customers needing food and supplies.

- Our team at Dillons store #105 in Joplin, Mo., also deserves special recognition. Led by Co-Manager John Gollihugh, 35 associates and customers took shelter in the produce cooler when a tornado swept through the community. Remarkably, that produce cooler was the only part of the store still standing after the storm passed. John and his team had just a few minutes to react. Because they implemented the emergency procedures they were trained for, every person in the store survived.

We want to express our deepest appreciation to all of our associates who helped respond to these storms and serve our customers through this difficult time. You truly are great people.

That completes our call today. Thank you for joining us.

The remarks contain certain forward-looking statements about the future performance of the Company. These statements are based on management's assumptions and beliefs in light of the information currently available to it. Such statements are indicated by words or phrases such as "will," "guidance," "expect," "objective" and "plan." These forward-looking statements are subject to uncertainties and other factors that could cause actual results to differ materially. Our ability to achieve identical supermarket sales and earnings growth and earnings per share goals, the timing that those earnings occur within the year, our ability to achieve results near the upper end of our earnings guidance range, our ability to continue to invest in the four key components of our Customer 1st strategy, our ability to strike more of a balance between delivering solid near-term financial results and investing for the future growth of our business, and our ability to deliver operating margins at projected levels, may be affected by: labor disputes, particularly as the Company seeks to manage health care and pension costs; industry consolidation; pricing and promotional activities of existing and new competitors, including non-traditional competitors, and the aggressiveness of that competition; our response to these actions; unexpected changes in product costs; the state of the economy, including interest rates and the inflationary and deflationary trends in certain commodities; the extent to which our customers exercise caution in their purchasing behavior in response to economic conditions; the number of shares outstanding; the success of our future growth plans; goodwill impairment; volatility in our fuel margins; and our ability to generate sales at desirable margins, as well as the success of our programs designed to increase our identical sales without fuel. In addition, any delays in opening new stores, or changes in the economic climate could cause us to fall short of our sales and earnings targets. Our ability to increase identical supermarket sales also could be adversely affected by increased competition and sales shifts to other stores that we operate, as well as increases in sales of our corporate brand products. Earnings and sales also may be affected by adverse weather conditions, particularly to the extent that hurricanes, tornadoes, floods, and other conditions disrupt our operations or those of our suppliers; create shortages in the availability or increases in the cost of products that we sell in our stores or materials and ingredients we use in our manufacturing facilities; or raise the cost of supplying energy to our various operations, including the cost of transportation. Our results also will be affected by rising commodity costs, the inconsistent pace of the economic recovery, changes in government-funded benefit programs, consumer confidence, and changes in inflation or deflation in product and operating costs. Our capital expenditures could vary from our expectations if we are unsuccessful in acquiring suitable sites for new stores; development costs vary from those budgeted; our logistics and technology or store projects are not completed on budget or within the time frame projected; or if current operating conditions fail to improve or worsen. Our ability to use cash flow from operations and cash on hand to maintain our current debt rating, fund capital expenditures, repurchase shares, and pay dividends, could be affected by unanticipated increases in net total debt, our inability to generate free cash flow at the levels anticipated, and our failure to generate expected earnings. We could fail to achieve fuel margins of 11.5¢ per gallon if the pattern of rapid changes in fuel costs continues. Our estimate of product cost changes could be affected by general economic conditions, weather, availability of raw materials and ingredients in the products that we sell and their packaging, and other factors beyond our control. Our ability to pass along product cost increases will depend primarily upon the reactions of our customers and our competitors to those increases. The accuracy of our product cost inflation estimate will depend primarily on weather conditions, supply constraints, unrest in areas of the country in which products are grown or are produced, natural disasters, and the general economic climate. Our ability to use all of the billion dollar authority under our stock repurchase program during 2011 will depend primarily on the price at which our shares trade and our ability to generate cash flow sufficient to make those purchases. Our incremental expense from rising pension and health care costs could exceed our expectations if health care costs continue to rise faster than projected, if unforeseen medical expenses are incurred under our self-insured health benefit plans, or if the assumptions used to estimate pension expenses differ from actual experience. Please refer to Kroger's reports and filings with the Securities and Exchange Commission for a further discussion of these risks and uncertainties.

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