**Second Quarter 2015**
**Investor Conference Call Prepared Remarks**
**September 11, 2015**

***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 second quarter press release and our prepared remarks from this conference call will be available on our website at ir.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 question, and one follow-up question, if necessary. Thank you.

Please save the date for our 2015 Investor Conference, which we will hold at the New York Stock Exchange on October 27. Details will be coming soon and we hope you can join us.

I will now turn the call over to Kroger's Chairman and Chief Executive Officer, Rodney McMullen.

***Comments by Rodney McMullen:***
Thank you, Cindy. Good morning everyone and thank you for joining us today. With me to review Kroger's second quarter 2015 results is Mike Schlotman, Executive Vice President and Chief Financial Officer. The next time you see Mike, please congratulate him on his well-deserved and well-earned promotion.

**Second Quarter Highlights**

We are pleased with our strong second quarter results. Our 5.3% identical supermarket sales growth without fuel allowed us to continue investing in our business and delivering on our aggressive growth plan. Strong fuel margins toward the end of the quarter allowed us to deliver results that exceeded our original expectations.

During the second quarter, we:

- Achieved our 47th consecutive quarter of positive identical supermarket sales growth;
- Exceeded our goal to slightly expand FIFO operating margin, without fuel, on a rolling four quarters basis;
- Kept costs down, which – together with identical supermarket sales growth – allowed Kroger to leverage operating expenses as a rate of sales; and we
- Continued to grow market share by improving our connection with customers, which fuels both our top and bottom lines and enables strategic Customer 1st investments.

These consistently remarkable financial results are possible, quarter after quarter, because our business is built on the belief that serving customers is serving shareholders. Based on the strength of our second quarter results, we are raising our net earnings per diluted share and identical supermarket sales growth guidance for the year.

**Economy and Customer Shopping Behavior**

While customers continued to feel optimistic about the economy throughout the second quarter, they also continued to tell us they want to spend less. More and more, they want retailers to help them save money with sales and coupons. We are well-positioned with our everyday low prices *and* our weekly sales and digital offers to solve this for our customers.

**Innovation and Investment in Technology, Food and People**

As you know, the food retail business is in a constant state of change. Part of what makes our Customer 1st Strategy so powerful is that it provides Kroger a firm foundation from which to approach new opportunities in the right way – to benefit our customers, associates and shareholders. While there are many examples where our business is rapidly evolving, I'd like to highlight three key areas of innovation and investment today – Technology, Food and People – and how the steps we are taking in each of these areas are broadening our competitive advantages for the future.

Investing in Technology

We are actively expanding our use of technology in ways we believe will make a difference for customers.

This summer we expanded our online ordering pilot in Cincinnati to three additional divisions. We are now offering our order online, pickup at the store solution in select Kroger stores in Louisville and Indianapolis, and Fred Meyer stores in the Portland area. This is, of course, in addition to Harris Teeter's successful *Express Lane* service.

When we think about digital opportunities, we do not limit our focus to ecommerce. Digital, for Kroger, includes a broad range of efforts to interact with customers in increasingly relevant and meaningful ways, whether online or through our mobile app. A key metric is our measure of digital household engagement, and during the second quarter we continued to gain household engagement at record numbers.

Our Kroger Technology team continues to earn recognition for leading-edge initiatives to establish the *Internet of Things* in our stores. Earlier this summer Kroger's electronic temperature monitoring project was named a winner of the *CIO 100 Award* by *CIO Magazine*.

And, as we shared with you in June, the talented team at 84.51° is helping us grow and evolve even faster due to their closer daily involvement in our business. 84.51°'s specialty – helping us make data-driven decisions that truly put the customer first – is a significant competitive advantage for Kroger.

<u>Food Innovation: Introducing HemisFares</u>

Our multi-tiered Corporate Brands portfolio has always been a powerful differentiator for Kroger. *Simple Truth* continues to see explosive growth. *Private Selection* remains a vibrant billion dollar brand that is growing in the double digits and developing unique offerings in many categories.

I'm pleased to share with you that later this month we will launch an entirely new brand called *HemisFares*. *HemisFares* brings only the best food finds from around the globe to our food-curious customers for an amazing and authentic eating experience. It's a guided tour of the best tastes on earth. Imagine landing in a country known for its incredible food and experiencing the finest examples of its region's most famous and delectable eats. Every *HemisFares* product is curated from the source and imported directly to our stores. The most exciting part is that no one else has a brand like this. *HemisFares* is a great example of what makes our Corporate Brands unique and we think it will appeal to millennials, foodies and – ultimately – *all* of our customers.

<u>An Opportunity Culture: Hiring Our Heroes</u>

Our reputation for consistent execution rests squarely on the shoulders of our 400,000 associates who make it all happen in our stores, distribution centers, manufacturing facilities and offices.

Our workforce is expanding rapidly to support our growth strategy. Last year, we created 25,000 new jobs. And right now we are hiring to fill an estimated 20,000 new and permanent positions in our stores. We are looking for people who want to be a part of a team, take pride in everything they do and want to grow with us.

One important and untapped resource for new associates is our country's military veterans. Since 2009, more than 29,000 veterans have joined our ranks – and hundreds of current associates continue to actively serve in the military. Over the past several years, Kroger has formalized our military hiring initiatives. We joined the "100,000 Job Mission", a coalition of companies with the common goal of hiring transitioning service members and military veterans, and we have increased our presence at military recruiting events. Next week, we are hosting our first-ever *Honoring our Heroes hiring* *event*, during which we will hold open interviews at every one of our supermarket locations on Tuesday, September 15, for all veterans and their family members.

The fact that nearly 70 percent of our store managers started as hourly associates, stocking shelves or bagging groceries, speaks to Kroger's *opportunity culture*, which we believe is a differentiator for us today and will continue to be in the future.

<u>Executive Changes</u>

Before I turn it over to Mike, I'd like to comment on our announcement yesterday of a new organizational structure for our senior leadership team. We take a team approach to leadership, and this new structure is designed to better align resources to our company's goals. It also streamlines decision-making and accelerates progress on our growth strategy. As I said in our announcement yesterday, Kroger is incredibly fortunate to have such an exceptionally strong group of leaders across our company, and our senior leadership team has unmatched depth and experience to continue delivering for our customers, associates and shareholders.

Now Mike Schlotman will offer more detail on Kroger's second quarter results, provide an update on labor relations, and update our guidance for 2015. Mike?

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

**Second Quarter Growth Metrics**

First, I'd like to spend a few minutes discussing our results for the quarter in each of the key performance target areas for our long-term growth plan.

<u>Identical Supermarket Sales</u>

Our first metric is identical supermarket sales without fuel. Our identical supermarket sales growth of 5.3% in the second quarter demonstrates the strength of our core business.

Our identical supermarket sales growth was driven by a combination of strong tonnage growth and an increase in the number of households shopping with us in the second quarter.  We also met our goal to grow the number of loyal households at an even faster rate than total household growth during the quarter.

All geographies and supermarket departments had positive identical supermarket sales, excluding fuel, during the quarter. We continue to see outstanding, double-digit identical sales growth in our Natural Foods department. Our Meat, Deli and Pharmacy departments also posted strong quarter results.

<u>FIFO Operating Margin</u>

Rolling four quarters FIFO operating margin – excluding fuel, the 2014 and 2013 adjustment items, and the contributions to the pension and foundation in the third and fourth quarters of 2014 – increased by 20 basis points. This exceeded our commitment to grow the rate slightly over time on a rolling four quarters basis.

Return on Invested Capital

Return on invested capital, on a rolling four quarters basis, was 14.24%. We are not presenting a comparative number this quarter because the last year's second quarter calculation does not include a full year of Harris Teeter assets and results. We continue to expect return on invested capital for fiscal 2015 to increase slightly from the fiscal 2014 result. This is an important metric as we continue to increase our capital investment to drive our future growth.

**Fuel Margins and Inflation/Deflation**

Before I share our second quarter results in more detail, I'd like to discuss how we are successfully managing through the current operating environment, which has more volatility than normal – specifically, fuel margins and inflation.

We benefited from higher fuel margins late in the second quarter. As Rodney said, our non-fuel results were right where we expected them to be. We expect fuel volatility to continue for the remainder of the year.

Another factor we are actively managing is product costs. While inflation continued at a lower rate during the second quarter – which we estimate was approximately 1.4% without fuel – some commodities had high inflation and others had deflation. Seafood and Milk were deflationary. Produce prices were less deflationary in the quarter. And we continue to see inflation in generic pharmaceuticals.

It bears repeating that if you look back over the past several years, we've had periods of high and low inflation and we've shown that regardless of the environment, we will deliver greater value and convenience for our customers.

**Second Quarter 2015 Results**

Now, I'll share our second quarter 2015 results in more detail.

Second Quarter Total Sales

As you know, we don't provide guidance for total sales because of the unpredictable impact that fuel has on our overall results. Total sales in the second quarter were impacted by the low retail price of fuel, much like in the first quarter. The average price of retail fuel during our second quarter was $2.67 compared to $3.54 last year.

Total sales in the second quarter increased 0.9% to $25.5 billion, compared to $25.3 billion in the same period last year. Excluding fuel, total sales increased to 5.7% for the second quarter compared to the same period last year.

Second Quarter Net Earnings
In the second quarter, our net earnings totaled $433 million, or $0.44 per diluted share. Net earnings in the same period last year were $347 million, or $0.35 per diluted share.

Second Quarter LIFO
Kroger recorded a $21 million LIFO charge during the second quarter compared to a $26 million LIFO charge in the same quarter last year.

Second Quarter FIFO Gross Margin
FIFO gross margin, excluding retail fuel operations, decreased 7 basis points from the same period last year.

Second Quarter Total Operating Expenses
Strong identical supermarket sales growth and cost controls allowed Kroger to leverage operating expenses as a rate of sales in the second quarter.

Total operating expenses – excluding retail fuel operations – decreased 35 basis points as a percent of sales compared to the prior year.

Second Quarter FIFO Operating Margin
Second quarter FIFO operating profit, excluding fuel, increased approximately $93 million over the prior year.

Retail Fuel Operations
Now for retail fuel operations. In the second quarter, our cents per gallon fuel margin was approximately 19.0¢ compared to 18.3¢ in the same quarter last year. We continue to expect fuel margins to be volatile during the back half of the year.

Corporate Brands
Corporate Brands' performance during the second quarter was solid, representing approximately 26.4% of total units sold, and 25.1% of sales dollars, excluding fuel and pharmacy.

**Labor Update**

I will provide a brief update on labor relations.

We recently agreed to new contracts in Columbus and Memphis, and have ratified all the local agreements associated with a master agreement with the Teamsters covering several distribution and manufacturing facilities.

We are currently negotiating contracts with the UFCW for store associates in Denver and Portland, and with the Teamsters covering our Southern California distribution centers.

Our objective in every negotiation is to find a fair and reasonable balance between competitive costs and compensation packages that provide solid wages, good quality, affordable health care, and retirement benefits for our associates. Kroger's financial results continue to be pressured by rising health care and pension costs, which some of our competitors do not face. Kroger and the local unions, which represent many of our associates, should have a shared objective – growing Kroger's business and profitability, which will help us create more jobs and career opportunities, and enhance job security, for our associates.

**Financial Strategy**

Our long term financial strategy continues to be to:

1. Repurchase shares,
2. Have an increasing dividend,
3. Fund increasing capital investments, and
4. Maintain our current investment grade debt rating.

Share Repurchases

Our strong financial position has allowed us to return $1.0 billion to shareholders through share buybacks and dividends over the last four quarters.

During the second quarter, Kroger repurchased 1.1 million common shares for a total investment of $43 million.

Capital investments

Capital investments, excluding mergers, acquisitions and purchases of leased facilities, totaled $812 million for the second quarter, compared to $672 million for the same period last year.

We expect capital investments excluding mergers, acquisitions and purchases of leased facilities, to be at the high end of the $3.0 to $3.3 billion range for the year.

We are trending towards the high end because we see a strong pipeline of high quality projects, and we continue to be encouraged by the results from our new stores.

In order to have a steady flow of projects, and increase the total number of store projects, we are spending on stores scheduled to open in 2016 to make sure they are ready to meet our target dates. Additionally, we continue to reduce the amount of time it takes to complete projects.

Maintain Current Investment Grade Debt Rating

The company's net total debt to adjusted EBITDA ratio decreased to 2.02, compared to 2.32 during the same period last year.

Kroger's net total debt is $11.3 billion, compared to $11.1 billion during the same period last year.

As I mentioned last quarter, we have essentially maintained our absolute debt level while returning $1.0 billion to shareholders through share buybacks and dividends over the last four quarters, investing $3.1 billion in capital on a rolling four quarters basis, plus an additional $426 million on mergers, acquisitions and purchases of leased facilities. In other words, we are keeping our commitments to our bondholders and shareholders, and opportunities for our associates.

**Updated 2015 Guidance**

Now I'd like to update our growth objectives for 2015.

Based on our strong year-to-date performance, we raised our identical supermarket sales growth guidance, excluding fuel, to a range of 4.0% to 5.0% for 2015. The prior guidance was 3.5% to 4.5%.

We also raised our net earnings per diluted share guidance to a range of $1.92 to $1.98 for fiscal 2015. The previous guidance was $1.90 to $1.95 per diluted share. This range exceeds the company's long-term net earnings per diluted share growth rate guidance of 8 – 11%. Shareholder return will be further enhanced by a dividend expected to increase over time.

We continue to expect the third quarter to be at the high end of our long-term growth range, and the fourth quarter to be below the range.

Our second quarter results demonstrate that our base business is performing very well. The volatility of fuel in the back half of the year will determine where we end up in the range.

Now, I will turn it back to Rodney.

***Comments by Rodney McMullen:***
Thanks, Mike.

Kroger's business is strong. Our team of associates continues to drive our Customer 1st strategy by taking care of our customers in big and small ways, offering fresh foods and keeping costs down so that we can reinvest those savings in our associates, store experience, products and prices. As a result we continue to earn customer loyalty and gain market share.

We are investing to grow our business for the future while delivering on our promises today. Our stores are hiring to fill 20,000 new, permanent jobs. We are expanding our digital and ecommerce offerings. Our confidence in Kroger has never been stronger.

Now, we look forward to your questions.

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***Comments by Rodney McMullen:***

Before we end today's call, I'd like to take a moment to acknowledge that this morning is the 14th anniversary of the attacks of September 11. I know that many on the call today were personally affected by those events. We continue to mourn those we lost on that horrific day, and to honor their memory through our support for police, firefighters and other first-responders, as well as the military and their families.

Finally, I'd like to share some additional thoughts with our associates listening in today.

One of the most exciting things about working for a growing and expanding company is the additional opportunities it creates for associates. Many of you would agree that Kroger is a place where you can come for a job and stay for a career. When I ask associates and managers why they stayed, most tell me they fell in love with working with people – our customers and our associates – or they found a deep passion for food. Often, it's both! As I mentioned earlier, nearly 70 percent of our store managers started as hourly associates. I believe there are many young people working for us today who will become our future leaders.

Our Associates are people who care, who want to connect with something bigger and make a difference in our communities every day. We ask candidates to imagine 'YOU@Kroger' – because whether you're looking for a flexible part-time job or for a lasting and rewarding career, you can find it here. And we're looking for friendly, bright people who want opportunities to learn and grow. This is such an exciting time to be at Kroger. Together, we make a difference!

That completes our call today. Thanks for joining.

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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 "expect," "objective," "will," "guidance," "continue," "believe," and "plan." Various uncertainties and other factors could cause actual results to differ materially from those contained in the forward-looking statements. These include the specific risk factors identified in "Risk Factors" and "Outlook" in our annual report on Form 10-K for our last fiscal year and any subsequent filings, as well as the following:

- The extent to which our sources of liquidity are sufficient to meet our requirements may be affected by the state of the financial markets and the effect that such condition has on our ability to issue commercial paper at acceptable rates. Our ability to borrow under our committed lines of credit, including our bank credit facilities, could be impaired if one or more of our lenders under those lines is unwilling or unable to honor its contractual obligation to lend to us, or in the event that natural disasters or weather conditions interfere with the ability of our lenders to lend to us. Our ability to refinance maturing debt may be affected by the state of the financial markets.

- Our ability to use cash flow to continue to repurchase shares, fund dividends, increase capital investments and maintain our investment grade debt rating, could be affected by unanticipated increases in net total debt, our inability to generate cash flow at the levels anticipated, and our failure to generate expected earnings.

- Our ability to achieve sales, earnings and cash flow goals may be affected by: labor negotiations or disputes; changes in the types and numbers of businesses that compete with us; pricing and promotional activities of existing and new competitors, including non-traditional competitors, and the aggressiveness of that competition; our response to these actions; the state of the economy, including interest rates, the inflationary and deflationary trends in certain commodities, and the unemployment rate; the effect that fuel costs have on consumer spending; volatility of fuel margins; changes in government-funded benefit programs; manufacturing commodity costs; diesel fuel costs related to our logistics operations; trends in consumer spending; the extent to which our customers exercise caution in their purchasing in response to economic conditions; the inconsistent pace of the economic recovery; changes in inflation or deflation in product and operating costs; stock repurchases; our ability to retain pharmacy sales from third party payors; consolidation in the healthcare industry, including pharmacy benefit managers; our ability to negotiate modifications to multi-employer pension plans; natural disasters or adverse weather conditions; the potential costs and risks associated with potential cyber-attacks or data security breaches; the success of our future growth plans; and the successful integration of Harris Teeter. Our ability to achieve sales and earnings goals may also be affected by our ability to manage the factors identified above.

- During the first three quarters of each fiscal year, our LIFO charge and the recognition of LIFO expense is affected primarily by estimated year-end changes in product costs. Our fiscal year LIFO charge is affected primarily by changes in product costs at year-end.

- If actual results differ significantly from anticipated future results for certain reporting units including variable interest entities, an impairment loss for any excess of the carrying value of the reporting units' goodwill over the implied fair value would have to be recognized.

- Our effective tax rate may differ from the expected rate due to changes in laws, the status of pending items with various taxing authorities, and the deductibility of certain expenses.

- Changes in our product mix may negatively affect certain financial indicators. For example, we continue to add supermarket fuel centers to our store base. Since gasoline generates low profit margins, we expect to see our FIFO gross margins decline as gasoline sales increase.

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