Capital Markets Research

Credit Focus

Retail/Consumer: Is the worst behind us?

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Q209 Review - Executive Summary

- Q209 has shown some early signs of improving market sentiment, with key indicators picking up after record low levels in Q109:
    - Consumer confidence indicator kept on falling, but at a slower pace in the largest European retail markets (UK, France, Germany, Italy and Spain), each month being more optimistic than the previous. It is worth noting that the rebound came earlier in the UK than in Continental Europe.
    - Retail sales rebounded in Q209. The 3-month moving average in retail sales growth is now back in positive territory in the UK. On top of still significant inflation, this change has been led by volumes back to positive. On this front as well, Continental Europe is lagging behind the UK but the retail sales decline has stabilised.
- While these first signs of hope will take months to materialise, European retailers posted plummeting like-for-like sales growth in Q109. The trend is worse for non-food retailers which are suffering harshly from the recession, ie customers cutting discretionary expenses.
- UK retailers were more reactive to the crisis and achieved the adaptation of their offer to customers' changing needs. UK retailers attracted back some of the customers they lost to hard discounters, by investing and communicating massively in promotions and price discounts. Thanks to their improving price image, the "Big Four" are gaining back market shares.

In this issue: Page

Confidence indicators in Europe: signs of hope

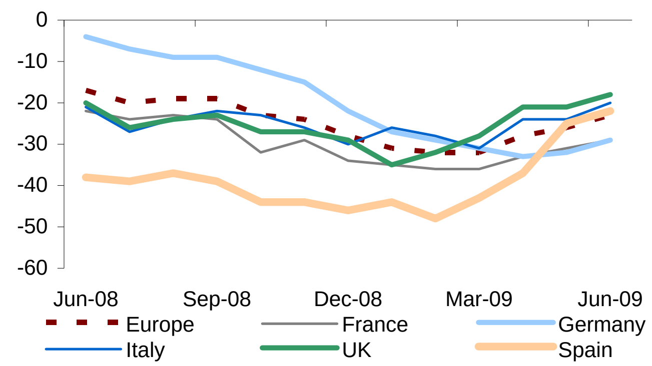
In Q209 consumer confidence picked up globally in Europe. It gained 9 points, ranging from -32 in March to -23 in June. In Q209, it rose at different paces depending on the country. In the UK and in Italy it was at its highest since January 2008. In Spain, the rebound has been remarkable since February 2009 when consumer confidence reached a record-low of -50. However, in Germany and France the recovery of consumer confidence in Q209 seems much slower.

While France and Germany reached a record low in March and April 2009, the UK touched bottom in December 2008, proving that recovery is likely to come earlier in the UK than in continental Europe.

Consumer confidence is still at a historic low but it has improved in Q209 despite a context of continuing depressed markets and job losses. That reflects a contracting economy in the short term but also consumer expectations that the economy may shortly recover from the recession.

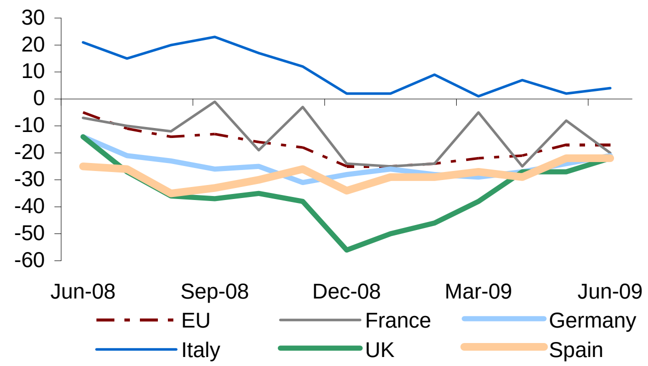
Retailers are gaining confidence too. The retail trade confidence indicator that surveys retailers improved 5 points in Q209, particularly in May 2009 (+4 percentage points). The rise started earlier in the UK in January 2009. In France and in Italy the trend is uncertain and oscillatory.

Consumer confidence indicator in Europe



Source: European Commission

Retail trade confidence indicator



Source: European Commission

The indicator is the arithmetic average of the balances (%) for the present and the future business situation, and for stocks – with inverted sign.

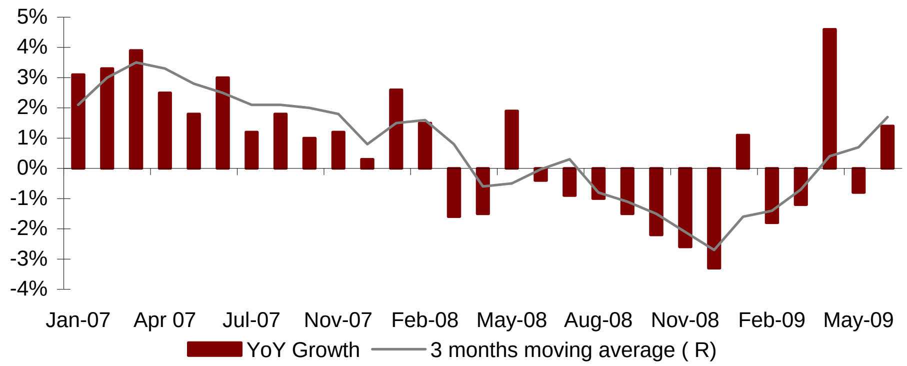
UK: Improving trends

Retail sales and price indicators: picking up

Although the trend was uncertain and polluted by non-recurring items, Q209 was a little more optimistic for retail sales since its 3-month average growth moved into positive territory – up from 0.4 % in April 2009 to 1.7% in June on a like-for-like basis (versus -0.7% in March 2009):

- In April 2009 there was an exceptional uplift in sales (+4.6% YoY) spurred by a sunny Easter and a favourable comparison basis last year.
- The like-for-like retail sales decline has been steadily slowing since February 2009 (-1.8% YoY) as volumes have been falling at a slower pace.

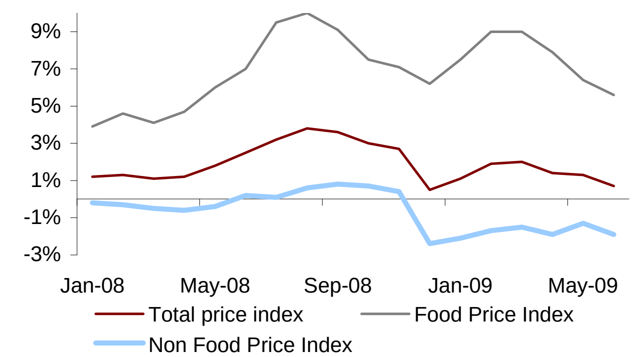
UK LfL retail sales growth



Source: BRC

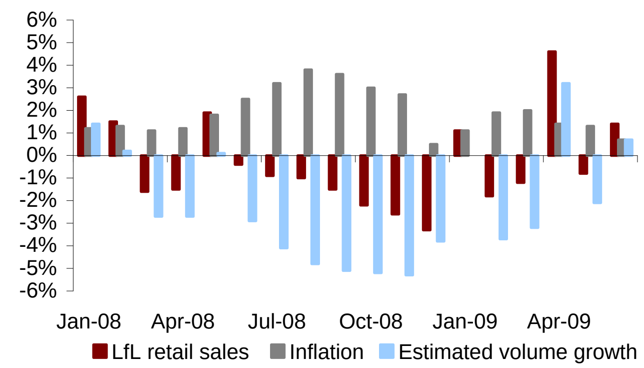
In Q209, inflation has been easing due to a strengthening GBP against the USD in the last two months. The 2-month average change in Retail Price Index (RPI) fell to 1.35% YoY in April/May from 1.95% YoY in February/March 2009. In June, the RPI continued easing, down to 0.7% YoY. The largest downward effect came from food prices which lost 340bp in Q209, shifting from 9% in March 2009 to 5.6% in June 2009. Deflation in non-food remains in an array of -1.5%, more or less 40bp. All in all, the retail like-for-like sales increase seems to have been driven more by volume growth in Q209 than in the previous quarter.

UK BRC Shop Price Index



Source: BRC

UK LfL retail sales growth: inflation/volume



Source: BRC

In FY09/10, UK retailers' performance should be challenged by tough trading conditions in the UK market with intense price competition and continuing deflationary pressure on prices and margins. Food inflation is likely to continue to fall.

The common trend among UK retailers: Changing habits

The recession is challenging the way retailers are doing business. They understood that their relationship with the consumer is undergoing rapid and permanent change. According to Tesco's CEO, consumers are redefining the way they shop and are looking for more transparency from retailers and simplicity when they shop (ie, good quality core product). The key to survival is innovation: spotting the new trends among consumers and moving first, such as focusing on cheap and good value own-branded products.

Price reductions and aggressive promotions is a key to bypass the crisis by attracting customers from low-cost rivals. As a result, the competition is fierce between the "Big Four". Tesco is still losing customers to Asda and Morrisons, and more recently to Sainsbury too. While the crisis is affecting some retailers, others will emerge reinforced.

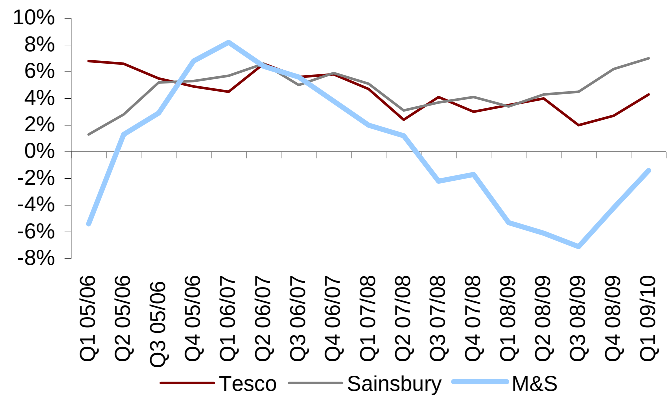
Even hard-discounters have been caught up with the Big Four. Hard-discounters' sales growth has tailed off and fell to 7.5% for Lidl and 8.5% for Aldi (vs previous double-digits rates) whereas that of the Big Four is slightly above: 8.2% for Asda, 8.9% for Sainsbury and 9.3% for Morrisons.

According to TNS Worldpanel, in the 12 weeks ending 14 June, UK grocery retailers seem to have ridden out the recession posting a growth at 6.5%.

Another trend spotted amid retailers is calling for fresh funds. Tesco announced a CMBS issue and Sainsbury a capital increase to have more financial flexibility to carry on their expansion strategy. Indeed, there are opportunities to be seized with the property crash in the UK.

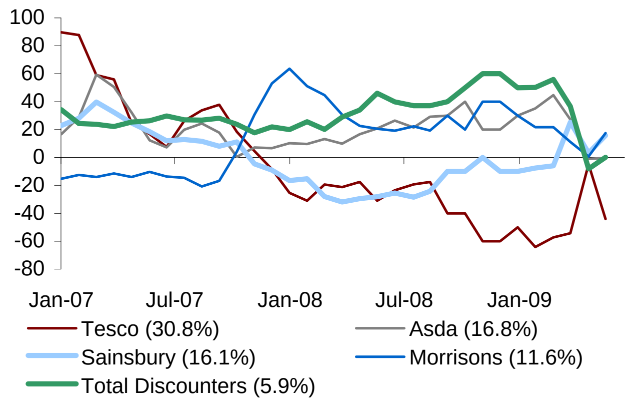
UK Retailers: Performance Monitors

Domestic LfL sales growth



Sources: Calyon , Companies

Market Share growth (in bp)



Sources: TNS Worldpanel as of 14 June 2009

UK Retailers operating trend

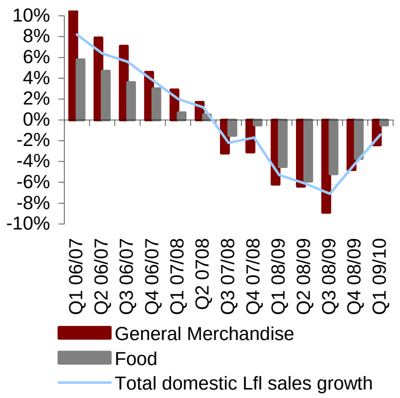
	Released FY 08/09				∆ released vs Bloomberg consensus		Domestic retail underlying operating margin		
GBPm	**Sales**	**EBITDA**	**recurring EBIT**	**Net Debt***	**Sales**	**EBIT**	**FY 06/07**	**FY 07/08**	**FY 08/09**
Marks&Spencer	9,062	1,178	769	2,491	0.38%	-0.22%	11.99%	11.71%	8.00%
Sainsbury	18,911	1,082	616	1,671	-0.65%	0.40%	2.51%	3.00%	3.26%
Tesco	54,327	4,395	3,206	9,600	1.52%	2.70%	5.86%	5.88%	6.23%

Source: Calyon, Companies, Bloomberg

MARKS & SPENCER (BBB- / NR / BBB neg)

Still in distress…

Domestic LfL sales growth

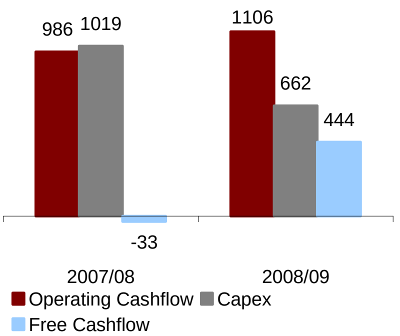


Source: Calyon, M&S

M&S reported deceiving FY08/09 results and lost market share. It did not achieve most of its targeted measures reported last year. The company had announced an improvement in gross margin between 0bp and 50bp whereas it actually deteriorated by 170bp.

In 08/09 global operating margin fell harshly by 370bp (8% vs 11.7% last year) hurt by low performances in the UK where 90% of revenues are made. Indeed domestic like-for-like sales growth (excluding petrol) was negative thoughout 2008/09 with a decelerating trend in Q4. It reached a record low growth rate of -7.1% in Q3 and improved to -4.2% in Q4. The blame goes to the non food activity, with a 9% like-for-like sales contraction in Q3. Added to that, M&S did not achieve a better control of its operating cost base which deteriorated in the UK and impacted operating profit. However, the fact that results were more positive in Q4 may indicate that the anti-crisis measures (promotional and price offers) are starting to bear fruit and have helped to halt trading deterioration.

FCF Generation (GBPm)



Source: M&S, Calyon

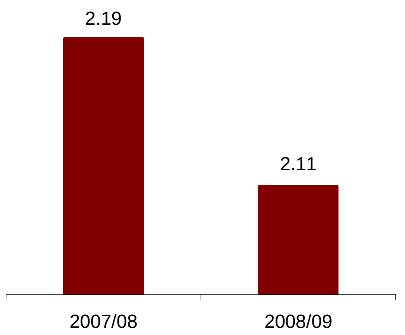
M&S seems to be much more worried about its credit metrics and its ability to generate free cash flows. Indeed, it has seriously cut its capex in FY08/09 (GBP 662m), much more than announced last year (GBP800-900m). M&S slowed its modernisation program and the opening of new stores. Moreover, M&S cut the dividends by a third even though operating cash flows increased (due to an improvement in working capital). As a consequence, net debt decreased by GBP600m to GBP2.5bn, which improved the ratio net debt/ EBITDA.

For 2009/10, M&S is warning of continued pressure on prices and margins, but will try to preserve its profitability and financial structure as much as possible:

- UK gross margin guidance: -125 to -175bp;
- Operating costs -1% in 09/10 (ie, GBP175m savings);
- GBP400m capex (mostly investment in supply chain and technology), ie, a further GBP262m cut compared to last year.

Better than expected Q109/10 figures

Unadjusted Net Debt/ EBITDA



Source: M&S, Calyon

M&S confirmed its recovery in Q109/10: domestic like-for-like sales growth was still negative at -1.4%, but the fall has decelerated by 280bp versus the previous quarter. Analysts were expecting a slump within a range of -1.8% to -3.5%. The food business reported a decrease of 0.5% in like-for-like sales, above forecasts (-4.2% for some analysts). In general merchandise, the contraction reported was at 2.4%, while the consensus predicted a fall between 3%-5%. This surprising performance is mitigated since M&S benefited from a more favourable context (Easter) and a positive comparison basis in May 08.

Although M&S is more confident regarding a consumption trend that seems to be stabilising, it remains cautious about the full year outlook. The environment is expected to remain tough and according to the CEO, there is still a lot to be done in terms of restructuring in the food business.

SAINSBURY (BBB- / WR / BBB)

Well on track!

Sainsbury delivered strong results despite the economic downturn, benefiting from its restructuring plan "Making Sainsbury Great Again". Indeed, domestic like-for-like sales grew all throughout the year (6% in FY08/09 vs 4% last year), performing by more each quarter than the previous. The operating margin has improved by 26bp to 3.3% in 2008/09.

This restructuring programme has weakened Sainsbury's financial structure due to rising expenses:

- Its FFO decreased by 11% to GBP768bn (increase in taxation). However its operating cash flow generation broadly improved by GBP100m in 2008/09 (positive change in working capital). As a result, its free cash flow generation improved though it remained negative at -GBP46m. Capex was unchanged at GBP976m and dividends increased by 10% this year.
- Consequently, net debt increased, slightly deteriorating the solvability ratio: it shifted from 1.49 to 1.55.

The retailer should continue to forge ahead in 2009/10 by reinforcing its position in the retail market: reaching more customers through additional channels (convenience, online,…), offering complementary non-food and service activities, investing in the promotion of its cheap and good quality food, growing supermarket space and having an active property management approach.

Sainsbury released very detailed guidance for 2009/10:

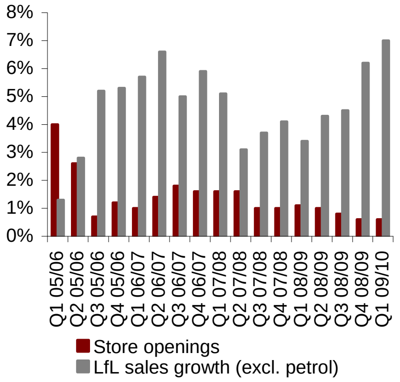
- 2% sales contribution from net new stores, 5% growth in gross new space.
- Offset 75% of cost inflation by cost savings.
- Net debt should range from GBP1.7bn to GBP1.8bn.
- Capex is hovering between GBP800m and GBP900m
- Finally, John McAdam will succeed M. Philip Hampton as Chairman.

A pronounced turnaround in Q1 2009/10

In Q1, Sainsbury posted the strongest domestic like-for-like retail sales (excl. VAT and fuel) since at least the 1990s, up 7.8%, beating analysts' expectations and outpacing its fiercest rival Tesco (+4.3%). These outperforming figures mark a turnaround in the once struggling firm's strategy. It demonstrates Sainsbury's competitive price position thanks to its great investment in price reductions (7,000 products since January 2009).

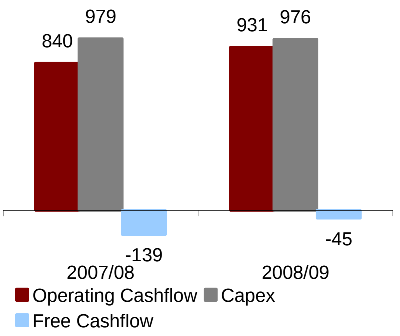
Enhanced by this positive momentum, Sainsbury is now targeting a boost in its expansion strategy (15% space growth, adding more space in two years than in the last five): it is planning to open 50 new stores this year and increase its capex to GBP2bn for the next two years (vs GBP1.6m last year). In order to fund this expansion, Sainsbury raised GBP445m through selling shares (GBP225m) and convertible bonds (GBP190m) in order to preserve its balance sheet structure and put no pressure on the BBB rating.

Domestic LfL sales growth



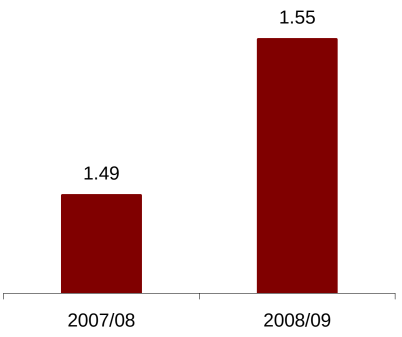
Source: Sainsbury, Calyon

FCF Generation (GBPm)



Source: Sainsbury, Calyon

Unadjusted Net Debt/ EBITDA



Source: Sainsbury, Calyon

TESCO (A / A3 neg / A-)

An aggressive policy to the detriment of its credit metrics

Tesco proved to be quite resilient to the ongoing recession with performance results in FY08/09 in line with last year's expectations.

Domestic like-for-like sales growth (excluding petrol) was 3% in the full year (anticipated: 3% – 4%). However, H208/09 showed deterioration compared to H1: 3.75% in H1, 2.4% in H2. Indeed, Tesco faced tougher trading conditions in H2 (harsh competition from Asda and Morrisons) and suffered from the recession, ie, customers down trading.

Tesco's core business performed well as the domestic underlying operating margin was above analysts' forecasts (expected to be alike): it improved by 35bp, thanks to a boost in sales volumes.

As announced last year, Tesco also continued its aggressive acquisitive strategy in 08/09, with the acquisitions of TPF and South Korean stores Homever. It deteriorated Tesco's financial structure as it was financed by 100% debt:

- Capex reached a record high level: GBP4.7bn (vs GBP3.8bn last year). Thus its free cash flow deteriorated to -GBP600bn from -GBP40m last year, despite its operating cash flow generation having seriously improved (+16%).
- Net debt rose to GBP9.6bn from GBP6.2bn last year. As a result Tesco's solvability ratio deteriorated this year to 2.18 from 1.64 in 07/08.

As a consequence, Tesco had the outlook on its A3 credit rating changed to "Negative" from "Stable" by Moody's as credit metrics seriously deteriorated:

- The volatile capital market and unfavourable currency movements affected the value of Tesco's pension scheme assets in FY08/09.
- The increase in undiscounted operating lease commitments: reported GBP12bn (long-term heavy investment programme in the UK and overseas).

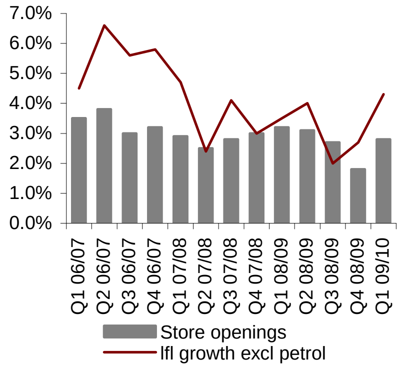
In 2009/10, Tesco's priority will be to streamline its indebtedness by reducing net debt to GBP 8.5bn, primarily driven by lower capex (GBP3.5bn in 09/10) and by cutting operating costs sharply (mostly in logistics).

An encouraging FY 2009/10 start – Annual forecast confirmed

Tesco reported an increase in Q109/10 sales despite the challenging economic climate. Domestic like-for-like sales (excluding petrol and VAT) grew by 4.3%, which is inline with the outlook for the year. Tesco managed to prevent consumers from shifting to lower-cost rivals through its discount food range and in-store promotions. Tesco has also gained customer loyalty thanks to the re-launch of its Clubcard. However, the retailer underperformed its peers – domestic like-for-like sales at Morrisons were up 8.2% and Sainsbury's released a 7.8% increase.

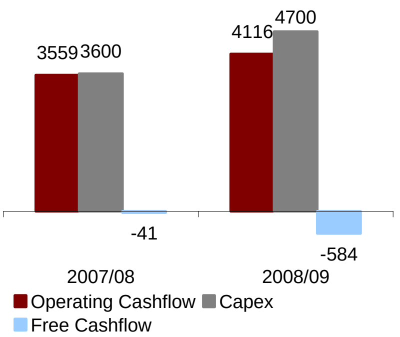
Tesco was also in the headlines after the financial press reported it was selling GBP415.6m of 30Y bonds secured by rental income from 12 retail stores and two distribution centres. The sale-and-leaseback transaction has the traits of a CMBS, although it would seem as though it is not (unsurprisingly) being marketed as such. The deal is being marketed towards the traditional UK sterling corporate investor base, perhaps explaining why Tesco has explicitly guaranteed the notes – the rating of the notes and Tesco were already heavily linked, as Tesco is the only tenant in the transaction, so there was little need for an explicit guarantee from a structuring perspective. If successfully placed, the deal will be the first publicly sold CMBS transaction in Europe, for nearly two years.

Domestic LfL sales growth



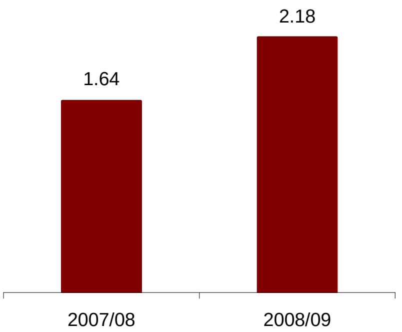
Source: Calyon, Tesco

FCF Generation (GBPm)



Source: Tesco, Calyon

Unadjusted Net Debt/ EBITDA



Source: Tesco, Calyon

Continental Europe: lagging behind

The common trend among European Retailers: Alarm is on!

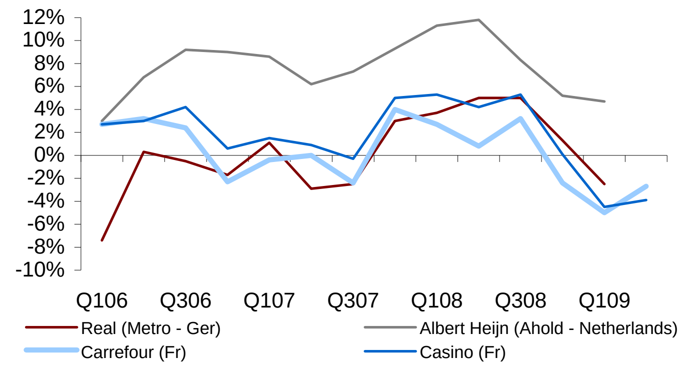
Like-for-like sales growth in entering into negative territory in Q109 clearly shows that the recession is hitting at full stride and is not yet over. The fall that started in Q208 has continued at the same pace for most of retailers (except for Ahold). As expected, food retailers have been more resilient than non-food retailers.

Negative figures can partly be explained by external factors: a decrease in oil prices and negative calendar effects (Easter shifting in Q2). But the major issue is consumers reducing the average price of their basket. For instance, Casino and Carrefour discount banners posted like-for-like sales contracting respectively by 6.2% and 7.8% in Q109 as a result of fewer and lower-value items (also linked to the development of private labels).

In the coming period, credit metrics will remain under pressure: profits and margins should suffer from massive price investment, if equal efforts are not made in terms of cost savings.

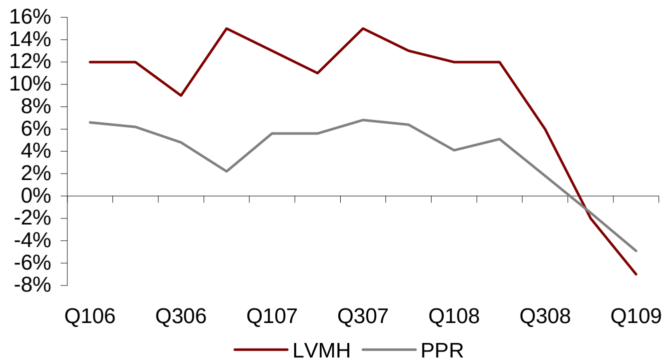
The luxury market should be facing challenges until at least 2012. According to Bain & Co sales are expected to drop 10% in 2009. Then, growth should slightly recover until reaching 2007's level in 2012. The recipe for success in these hard times includes managing costs rigorously. However, consumer trends have changed with the crisis moving to more sober luxury goods.

Food retailers' domestic LfL sales growth



Sources: Calyon , Companies

Consumer retailers' worldwide LfL sales growth

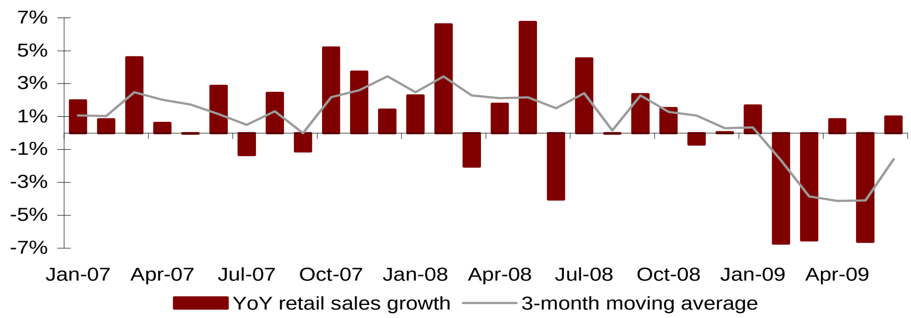


Sources: Calyon , Companies

Retail market in France

The trend was quite oscillatory in Q209, with retail sales growth moving from a positive to negative territory. In May, retail sales collapsed and reached a record low level of -6.5% in Q1. It followed a slight positive growth rate in April, at 0.8%, benefiting from the calendar effect (Easter was in March last year). In June, retail sales growth was once again positive at 1%, which drew the 3-month moving average up to -1.6% in June, from an enduring -4% level in the previous three months.

Monthly evolution of retail sales growth (YoY)

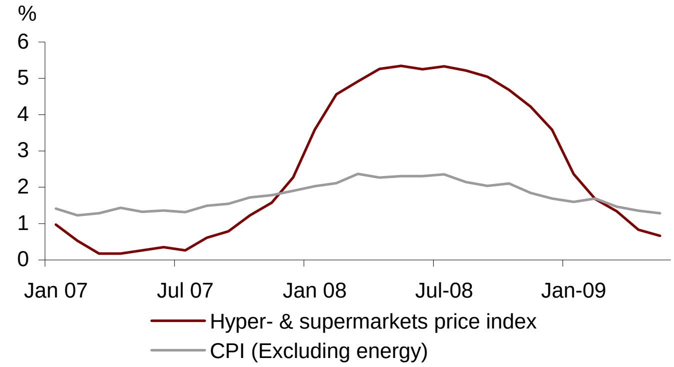


Source: Calyon, Banque de France

In Q209 retail sales growth was fostered by volume rather than prices, translating the measures of price cuts. In June, growth was 30bp higher in volumes than in value.

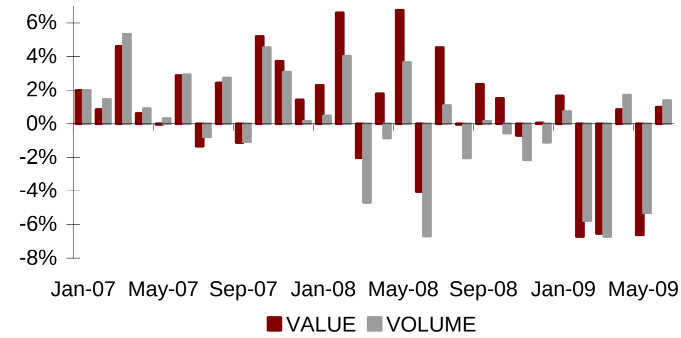
In parallel, the retail shop price index fell sharply in Q209. The 3-month average in Q209 was 0.7% versus 1.8% in Q109. In June 2009 it was at its lowest since August 2007 at 0.5%, looming largely on retailers' sales and margins. In February 2009 the Retail shop Price Index had trended below the Consumer Price Index.

Consumer versus Retail Price indexes in France



Source: INSEE

YoY Retail Sales Growth: Value vs Volume

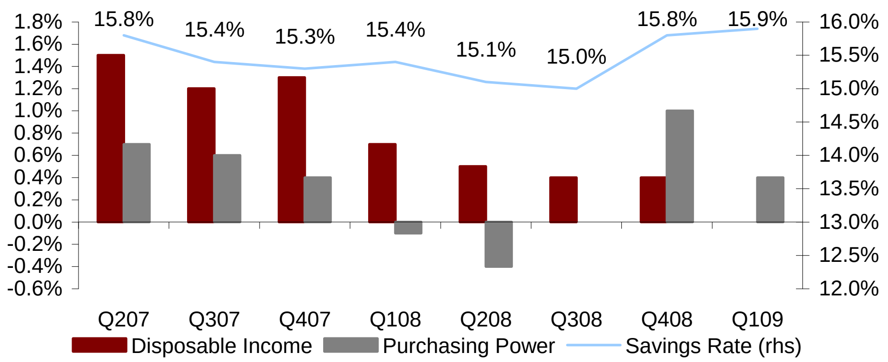


Source: Banque de France

The trend should continue weighing on retailers' performances at least until September 2009, without assuring a swift rebound of volumes in the near term. Eurozone inflation may soon be flat and should turn negative this summer, alleviating consumers' purchasing power. Moreover, purchasing power should be helped by the increase in social allowances and tax reductions granted by the government in 2009. According to INSEE, French household purchasing power is expected to rise by 1.1% in 2009 (versus a 0.6% decline in 2008 caused by rise in oil prices), whereas gross disposable income will fall by 1.3% in 2009.

However, with the negative effects of unemployment, consumption is still jeopardised as households remain cautious and are more willing to save. The saving ratio was 15.9% in Q109 and is in a rising trend since it jumped by 80bp in Q408 to 15.8%.

Evolution of French households' purchasing power and disposable income (QoQ)



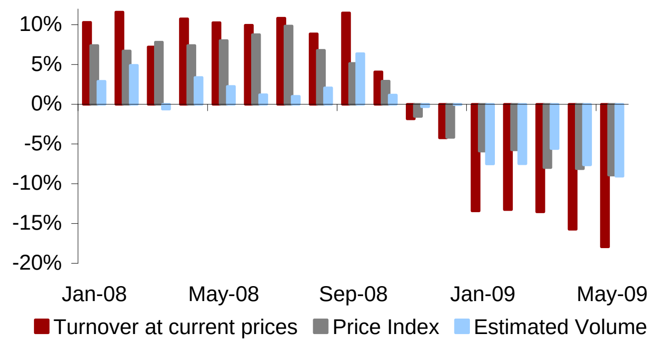
Source: INSEE

Retail market in Germany

German retailers are in phase with French retailers: they are in the same cycle of the crisis. Recession is slightly steeper for French Retailers whose like-for-like sales decrease reached 6.5% in May 2009, versus a 3% to 4% decline in Germany. In Q209 inflation was flat, which means that the fall in sales was a result of weaker volumes.

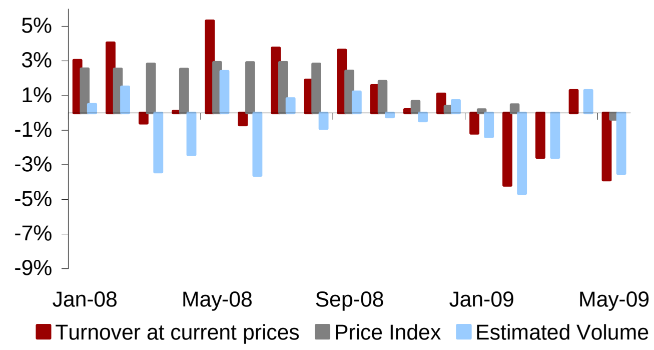
The wholesale trade turnover YoY change is a representative measure of the trends in retail as it indicates those in upstream branches. The situation has worsened in Q209 reaching an 18% contraction in May. As a contrast with retail sales growth, the contraction is fuelled by a severe decline in prices that started early 2009. It has almost doubled since December 2008, shifting from a 4% fall in the price index to 7%. This reflects the pressure exercised by retailers on suppliers.

Wholesale Trade Turnover YoY Change (%) – (calendar and seasonally adjusted value)



Sources: Calyon , Statistisches Bendesamt Deutschland

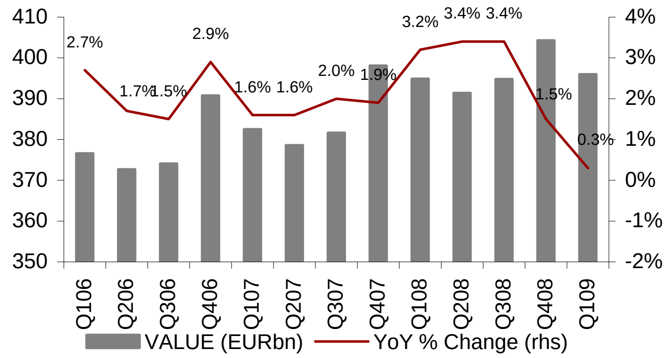
Autos/ Retail Sales Growth YoY (%) – (excl. VAT)



Sources: Calyon , Statistisches Bendesamt Deutschland

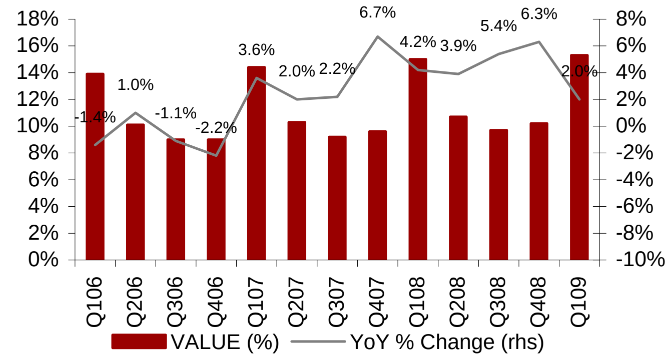
Therefore, the economic background is not expected to improve in Germany. Added to that, household disposable income shifted from a 3.4% YoY growth in Q408 to nil in Q109, which is likely to impact consumption, all the more since the saving ratio reached a record high of 15.3% in Q109.

German households' disposable income (EURbn)



Sources: Calyon , Deutsche Bundesbank

German households' saving ratio



Sources: Calyon , Deutsche Bundesbank

Continental European Retailers: Performance Monitors

European retailers' operating trend

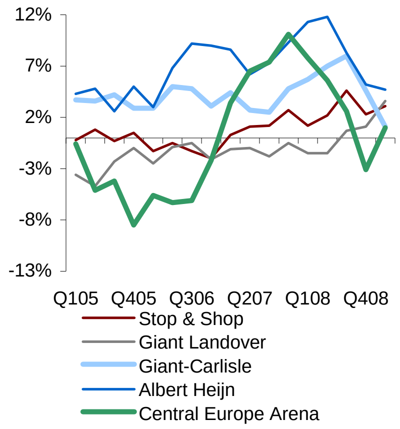
	Q109		Q209	
Total Group	**Sales** (EURm)	**LfL %**	**Sales** (EURm)	**LfL %**
Ahold	8,654	6.2%		
Carrefour	22,717	-4.0%	23,443	-2.2%
Casino	6,624	-1.4%	6,823	-0.5%
LVMH	4,018	-7.0%		
Metro	15,167	1.1%		
PPR	4,777	-4.9%		

Source: Calyon, Companies

AHOLD (BBB / Baa3 / BBB-)

Showing early signs of recovery in the US

LfL Sales growth by banner



Source :Ahold, Calyon

In Q109, Ahold reported resilient results, beating analysts' forecasts. The restructuring of its business model in the US (accounting for 60% of revenues) seems to be on the right track. Indeed, like-for-like retail sales growth was stronger in Q109 than in the previous quarter, except for Giant Carlisle where growth staunchly decelerated by 350bp to 1.1%. While Stop & Shop's like-for-like retail sales growth slightly accelerated by 80bp to 3.1% in Q1, that of Giant Landover jumped by 250bp to 3.6%.

In parallel, in the Netherlands, although Albert Heijn's organic sales growth decelerated by 50bp to 4.7% in Q1, it outpaced all its European rivals. In the meantime, Albert/Hypernova's (Central Europe) organic growth was quite impressive, demonstrating the first signs of recovery: growth was boosted by 410bp in just a quarter, to 1% from -3.1% in Q408.

The group's underlying operating margin improved by 6bp to 4.78% in Q109. On the one hand, US margins improved by 60bp to 4.62%. On the other hand, this performance was offset by that of Europe where margins seriously deteriorated (-68bp in the Netherlands and -225bp in Central Europe), sacrificed for restructuring measures (price cuts, store remodelling, etc).

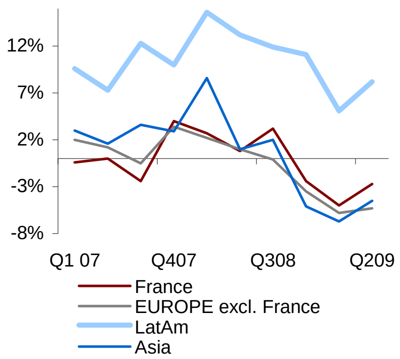
As a result of Ahold's solid performance and strengthened balance sheet, the retailer was upgraded by Standard & Poors to 'BBB / A-2' from 'BBB- pos / A-3' on 24 June. In addition, Ahold entirely bought back its USD690m 8.25% guaranteed senior notes due in July 2010.

Ahold appears well positioned to face the current environment and is so far on track to meet its 2009 objectives (5% organic growth targeted versus 6.2% in Q109). It has been working on its price perception by twice cutting its prices in two weeks on a series of strategic products. In Q2, its EBIT is expected to grow thanks to its EUR150m savings programme, spurring margin improvement in this low inflationary environment (2% in May MoM).

CARREFOUR (A / A3 neg / A)

Strategy is moving into the right direction

Like-for-like sales growth by region



Source: Carrefour, Calyon

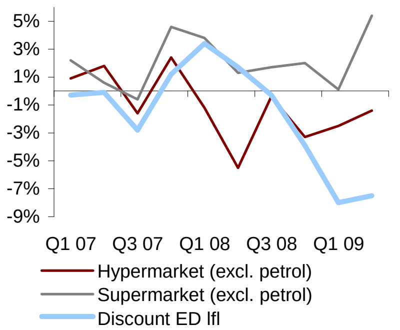
In Q109 Carrefour reported its worst performance since at least 2002. Global like-for-like sales contracted by 4% after a 1.3% decline in Q408. In Europe it reached -5.8% and in Asia -6.7%. Like-for-like sales growth only remained positive in Latin America (+5.1%), although it fell from 11.1% in Q408.

More specifically in France, Carrefour's largest market with 42% of revenues in Q109, organic sales fell by 5%. All formats posted bad figures, ranging from flat growth (excl. petrol) for supermarkets to a 8% drop for the hard discount banner ED. Hypermarkets managed to improve their performance slightly in Q1, gaining 80bp in organic growth to -3.5% (excl. petrol).

In Q209, the group's like-for-like sales growth picked up in every region, moving to -2.2% (vs 4% in Q109). The rebound in France was as swift as in Asia (roughly +230bp), led by supermarkets whose same-store basis sales growth (excl. petrol) soared by 5.4% in Q209. The like-for-like sales (excl. petrol) slump in hypers slowed to -1.4% as traffic also fell at a slower pace (-2.7% in Q2, -3.3% in Q1). The average basket value then increased by 1.3% in Q2, versus 0.8% in Q1. The hardest hit remains the discount banner ED that is still suffering from customers squeezing expenses.

For Carrefour's CEO, the main issue is brand image. During the Analysts' Day held on the 30 June, Carrefour presented its strategic plan to pull out off the crisis:

Like-for-like sales growth in France



Source: Carrefour, Calyon

- First, it will **revitalise the brand** and customer perception. Carrefour's objective is to gain loyalty by being more attentive and satisfying customers needs. The positioning of the brand has to be clear worldwide and the portfolio of banners and products are to be adapted locally.
- Thus, to improve the brand positioning, Carrefour will develop more hard discount banners (ED will be scrapped and replaced by DIA in France for instance) and improve **price perception**. Not only it is planning to invest significantly in prices but it will communicate its promotions even more, spending as much as EUR500m on this over the next 3 years. The marketing campaign will be specific at each store.
- The company will then look at being **closer** to the customer, by opening convenient stores (in town 'Carrefour City' and in rural areas 'Carrefour Contact') on the one hand and by reinventing the hyper format on the other, the latter whose model has tailed off. The change will always include the levers described above (brand, price, positioning, communication…). EUR1bn will be spent on redesigning the stores

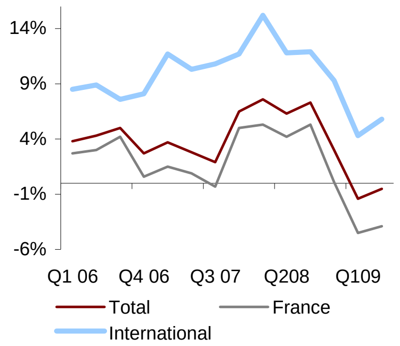
To implement such a transformation programme Carrefour has to reduce its costs. It has announced a EUR4.5bn savings plan by 2012, including EUR 350m in H209, as it overhauls the system. As Carrefour is mainly suffering from being a 'too' heavy and costly organisation, logistics will be at the core of the plan (simplification of the structure, centralisation, negotiation of purchasing conditions with suppliers…). The plan includes EUR1.4bn of savings from reducing inventories by 7 days (from 37 to 30 days). The measures will probably weigh on margins in the short term but should restore sustainable growth after 2012. As a consequence, 2009 operating profit is expected to fall by 15% to EUR2,700-2,800m (from EUR 3,300m). Carrefour will indeed exceed its EUR600m budget of price investment due to an ever more challenging environment than expected.

On 2 July Moody's changed Carrefour's outlook to negative as a result of a weakening in earnings and its publicly announced forecasts for H209.

CASINO (BBB- / NR / BBB-)

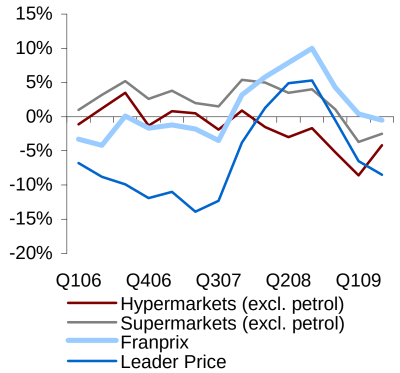
Priority given to margins

The group's organic growth evolution



Source: Casino, Calyon

Same-store sales growth in France



Source: Casino, Calyon

In Q109, the group's organic growth fell into negative territory, with a rate of -1.4% (including petrol), at a slower pace than its main competitor Carrefour (-4%). A good performance abroad (+4.3%, 37% of consolidated sales in H109) has indeed partially offset the 4.5% contraction in French like-for-like sales.

In France, same-store sales growth figures were alarming. The drop was led by hypermarkets with an 11.8% contraction (incl. petrol), all the more serious since it represents a third of their French revenues. Supermarkets have declined harshly, by 6.9%. Franprix/Leader Price also was effected by the recession with estimated same-store sales plummeting by 3.7%.

Internationally, while same-store sales growth was flat in the Indian Ocean and negative in Asia (-1.3%) it climbed by 5.7% in Latin America in Q1, but at a slower pace since Q408 (-20bp).

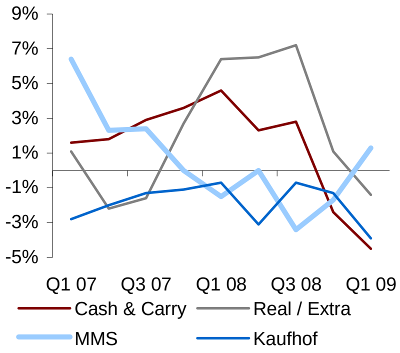
In Q209 the group's organic growth, compared to Q109, materialised in all regions: improving by 90bp to -0.5%. In France, the fall in organic growth was still significant (-3.9%) but it slowed by 60bp versus Q1. In contrast international organic growth jumped by 150bp to 5.8%, demonstrating the strength of its position in emerging markets.

In 2009 Casino should likely continue its focus on margins rather than on market share. It will certainly follow the market trend of cutting prices, but it will mostly give priority to cost efficiency. The full-year target of EUR150m of cost-cutting was confirmed: with more efficiency in the organisation leading to a reduction in the number of employees, logistics optimisation, non-food rationalisation, improved purchasing conditions with suppliers, centralised warehouses with the other group's banners and more. The EUR1bn asset disposal plan was also confirmed by CEO M. Naouri who announced no acquisitions for the next two years.

METRO (BBB / Baa2 neg / BBB)

Dramatic results but a good surprise for the electronics banner

LfL sales growth by banner



Source: Calyon, Metro

In Q109 Metro reported weak results, below analysts' expectations. For all divisions like-for-like sales growth continued on its downward trend, entering into negative territory like most of its European peers except for MMS (+1.3% in Q109 vs -1.7% in Q408).

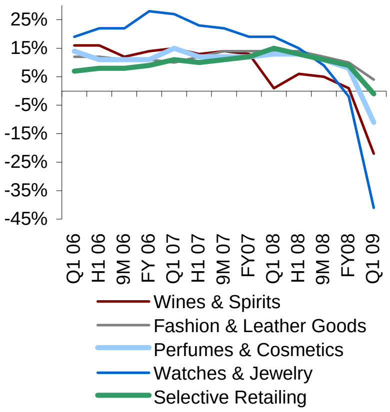
- The Cash and Carry division, which is the backbone of the group (50% of total group revenues), reached the negative rate of -4.5%. Figures were quite alarming in Germany with like-for-like sales plummeting by 7.1%. The repositioning process (ie, a new pilot store with a clear focus on professionals) is still in the pipeline.
- The food retail banner Real also reported negative like-for-like sales growth, contracting 1.4%. It performed badly in Germany (-2.5%), where 75% of revenues are derived, due to fierce competition in the market (hard discounters are implementing new cuts in prices) and declining positive price effects.
- The consumer and electronics banner MMS surprised the market with strong growth in Germany. Like-for-like sales rose by 8.3%. It appears that the restructuring and marketing campaign has borne fruit.

Lately Metro has been in the spotlight, after Arcandor's bankruptcy, showing an interest in acquiring 60 Karstadt stores in order to merge them with its non-core department store chain Kaufhof. It was planning to dispose of the merged business in the medium-term, once it would have become profitable, however negotiations were suspended as the purchase price will depend on the logistics, lease and supplier contracts renegotiation. Additionally the pension provisions (EUR 750m) issue is to be resolved.

Visibility is quite limited for the year as the first quarter is usually not the most important in terms of profitability. No detailed targets were given for 2009, except for capex (a budget of EUR 1.6bn). Capex amounted to EUR245m in Q109 (vs EUR340m in Q108) in line with the year's budget reduction. Metro only confirmed its medium-term forecast of 6% sales growth. Regarding the restructuring programme "Shape 2012", Metro did not communicate any productivity gain or cost savings for the moment.

LVMH (A / NR / BBB+)

LfL Sales growth by division



Source: LVMH, Calyon

Louis Vuitton showing resilience

In Q109 LVMH reported total like-for-like sales that plummeted by 7%. All its businesses published dramatic figures, except for Louis Vuitton that showed remarkable resilience compared to its luxury peers with a positive growth of 4%. That said, selective retailing was slightly negative at -1%. The worst decline was seen in watches and jewellery with a drastic contraction of 41% in like-for-like sales. Wines and spirits suffered from customer down-trading. The division posted a 22% fall in sales on a like-for-like basis. Finally, the perfumes & cosmetics activity (Dior,…), which use to outperform the sector, also reported a strong contraction in like-for-like sales at 11%.

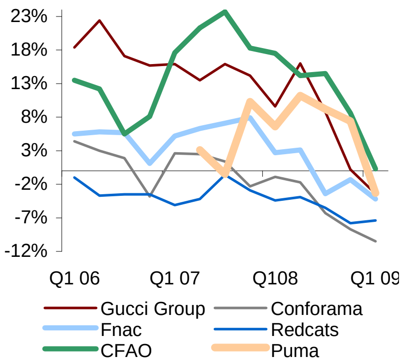
The trend in Q209 should be similar with perhaps a soft improvement in wines & spirits activity. Sales in April were already slightly better.

Although the leader in luxury goods is facing major challenges, there will not be an overhaul of the business model that, in our opinion, is still better positioned than its peers. The strategy is, in the long term, to reinforce brands through using innovation and quality, and the aim is to maintain high margins thanks to rigorous cost monitoring and selective investment.

PPR (BBB- / NR / NR)

Gucci brand, the survivor

LfL sales growth by banner



Source: Calyon, PPR

PPR's like-for-like sales contraction accelerated in Q109. It slumped 4.9% versus 1.5% in the previous quarter. It was penalised by tough trading conditions, especially in mature markets where consumers are reducing their discretionary spending. However, results were above consensus.

The different brands displayed diverging resilience to the downturn:

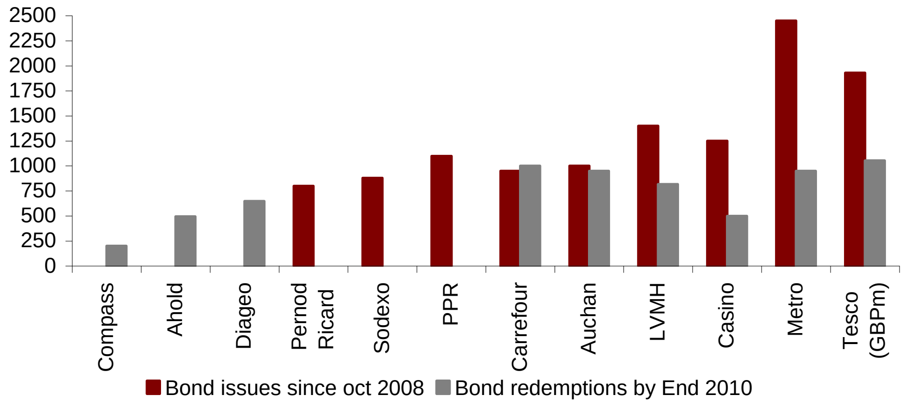
- In luxury goods, Gucci Group posted -3.4% in like-for-like sales growth. While the Gucci brand was resilient with 1% growth (although below the 3% expected), all other luxury brands reported a double-digit sales drop with -10.2% for YSL and -13.4% for Bottega Veneta. Indeed, Gucci benefits from brand recognition and a wide geographical coverage. Moreover the comparison basis was favourable as last year's sales growth was already weak due to supply chain problems. No major changes in 2009 trends are expected.
- The quarter was as tough for mass-market retailers. While Puma and Fnac's like-for-like sales decreased respectively by 3.3% and 4.2%, Redcats and Conforama's decline was much more dramatic with figures near -10%. CFAO, that used to have double digit sales increase, reported flat growth.

In 2009, PPR is looking forward to reinforcing its position in some specific business segments (personal goods). It will thus continue its strong investment/divestment activity, possible thanks to its healthy FCF generation and solid liquidity.

Conclusion: Undergoing the crisis at different paces

- All in all price positioning has become a key element in such a deteriorating economic environment. A good balance between price investment and cost savings will thus be necessary to preserve margins. In parallel, retailers are adapting shop format and product ranges to accommodate quick changing consumer habits.
- **It appears that the UK and Continental Europe are in different phases of the economic cycle: UK retailers are likely to recover earlier from the economic downturn than their European peers.** The gap in reported like-for-like sales growth is quite significant and it should continue to widen as UK retailers seem to be more reactive to the crisis. Indeed they have replied earlier to changing consumer needs. As a result, they are gaining back consumer loyalty previously lost to hard discounters.
- In contrast their European peers have recently started to implement a new strategy, being more attentive to clients and the way they shop. Consequently, European retailers are lagging behind as the Q109 performances clearly prove.
- Retailers have raised fresh money through bond issues or capital increases in order to gain financial flexibility and finance their expansion in more profitable markets.

2009-2010 EUR bond redemptions (EURm)



Source: Calyon, Bloomberg (as at 13 July)

New benchmark issues in 2008-09

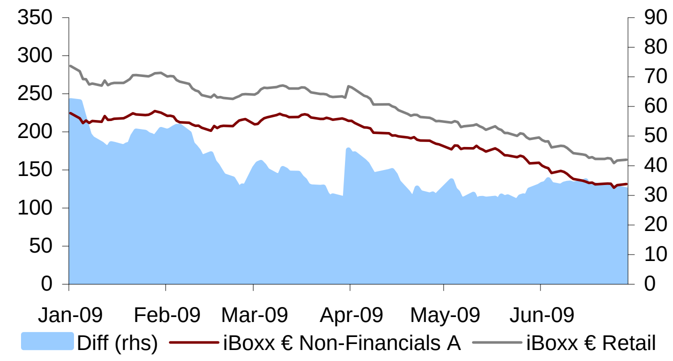
Deal pricing date	Moody's	S&P	Amount (EURm)	Currency	Duration	Maturity Date	Coupon	Spread over mid-swap (bp) - as of 20 July 2009
Auchan								
17-Apr-08	NR	A	800	EUR	5 years	29-Apr-13	5%	67
01-Apr-09	NR	A	500	EUR	6 years	15-Apr-15	4.75%	79
01-Apr-09	NR	A	500	EUR	10 years	15-Apr-19	6%	102
			1,800					
Bacardi								
06-Apr-09	Baa1	BBB	650	EUR	5 years	9-Apr-14	7.75%	268
			650					
Carrefour								
03-Jun-08	A2	A	1,000	EUR	7 years	12-Jun-15	5.375%	80
21-Nov-08	A2	A	700	EUR	5 years	2-Dec-13	6.625%	71
19-May-09	A3	A	250	EUR	8 years	29-Jun-17	4.678%	92
			1,950					
Casino								
26-Mar-08	NR	BBB-	1,200	EUR	5 years	4-Apr-13	6.375%	201
22-Jan-09	NR	BBB-	500	EUR	3.5 years	9-Aug-12	7.875%	206
22-Jun-09	NR	BBB-	750	EUR	5.5 years	30-Jan-15	5.5%	221
			1,250					
LVMH								
28-Apr-09	NR	A-	1,000	EUR	4 years	12-May-13	4.375%	90
19-May-09	NR	A-	150	EUR	8 years	29-Jun-17	4.775%	105
26-May-09	NR	A-	250	EUR	6 years	15-Jun-15	4.5%	103
			1,400					
Metro								
20-Nov-08	Baa2	BBB	500	EUR	5 years	28-Nov-13	9.375%	232
26-Feb-09	Baa2	BBB	1,000	EUR	6 years	5-Mar-15	7.625%	244
18-Jun-09	Baa2	BBB	350	EUR	2 years	24-Jun-11	3.625%	114
07-Jul-09	Baa2	BBB	600	EUR	5 years	14-Jul-14	5.75%	162
			2,450					
Pernod Ricard								
28-May-09	Ba1	BB+	800	EUR	6 years	15-Jan-15	7%	334
			800					
PPR								
16-May-08	NA	NA	200	EUR	4.5 years	16-Nov-12	6.405%	393
16-May-08	NA	NA	200	EUR	5 years	16-May-13	6.536%	387
26-Mar-09	NA	BBB-	800	EUR	5 years	3-Apr-14	8.625%	308
28-Apr-09	NA	NA	150	EUR	8 years	29-Jun-17	6.5%	476
19-May-09	NA	BBB-	150	EUR	8 years	29-Jun-17	6.5%	297
			1,100					
Sodexo								
13-Jan-09	NA	BBB+	650	EUR	6 years	30-Jan-15	6.25%	139
05-Jun-09	NA	BBB+	230	EUR	6 years	30-Jan-15	6.25%	146
			880					
Tesco Plc (GBPm)								
02-Sep-08	A3	A-	1,500	GBP	4 years	9-Sep-12	5.625%	104
02-Sep-08	A3	A-	1,500	GBP	8 years	9-Sep-16	5.875%	104
17-Feb-09	A3	A-	900	GBP	13 years	24-Feb-22	6.125%	152
17-Feb-09	A3	A-	600	GBP	5 years	24-Feb-14	5%	104
			4,500					
Tesco Plc (EURm)								
17-Feb-09	A3	A-	600	EUR	6 years	24-Feb-15	5.125%	91
			600					
Tesco Property (GBPm)								
17-Jun-09	A3	A-	431	GBP	30 years	13-Jul-39	7.623%	268
			431					

Source: Calyon, Bloomberg

Sector performance in Q209

Cash Market

Retail Cash: sector performance



Source: iBoxx, Calyon as of 30.06.09

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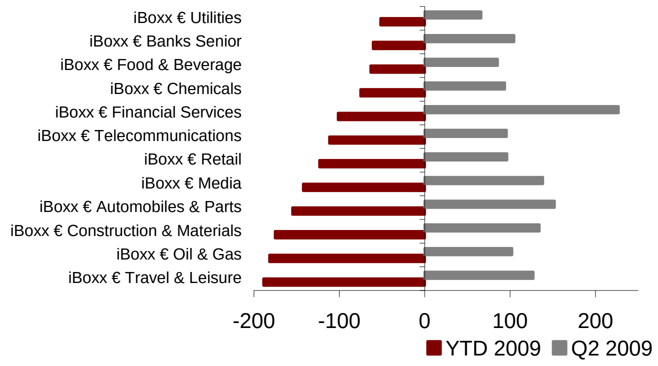
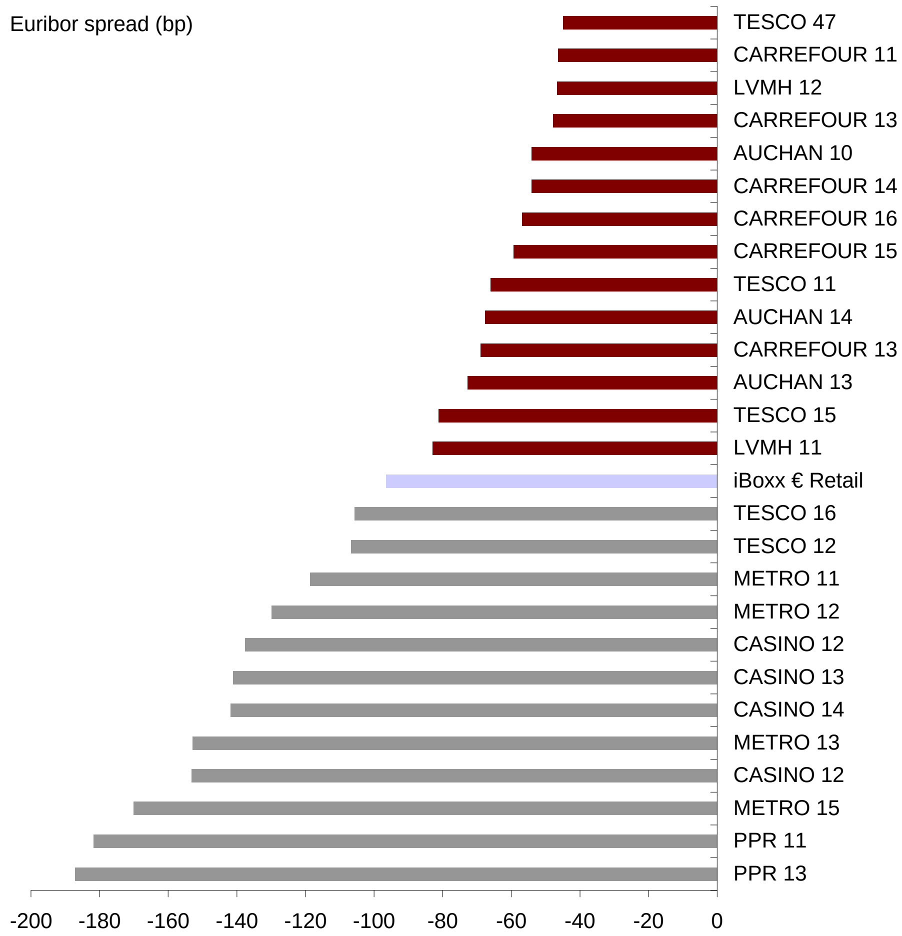
Relative Value



Source: iBoxx, Calyon as of 30.06.09

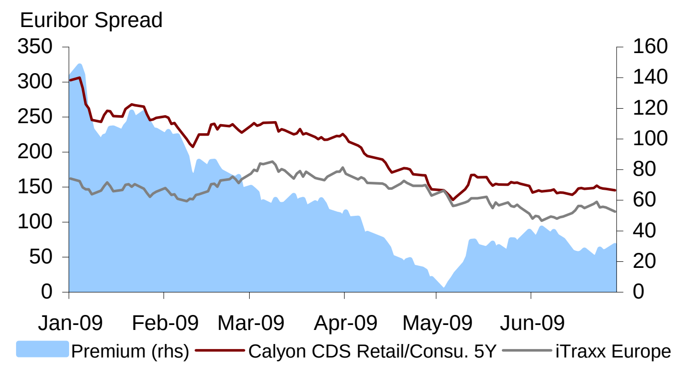
Cash Performance (1 April – 30 June 2009)



Source: iBoxx, Calyon

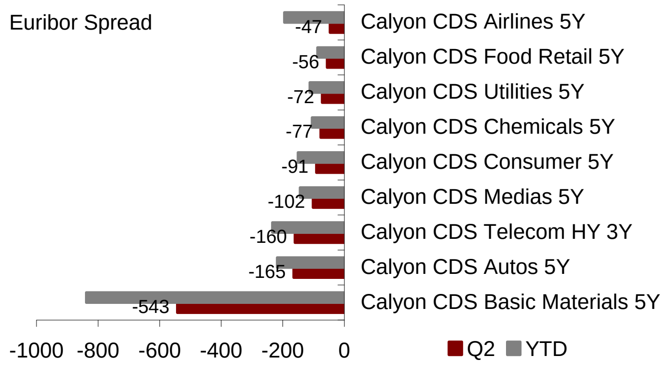
CDS market

CDS sector performance (Euribor spread)



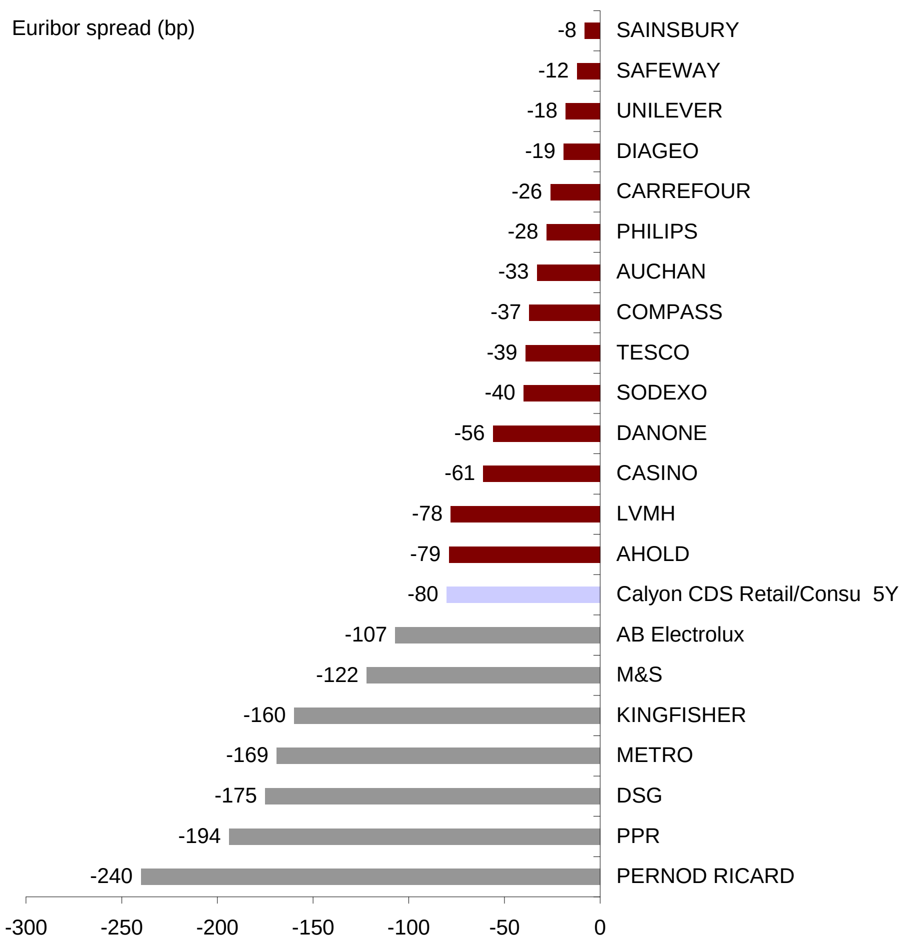
Source: iTraxx, Calyon as of 30.06.09

Relative Value



Source: iTraxx, Calyon as of 30.06.09

CDS Performance (1 April – 30 June 2009)



Source: iBoxx, Calyon

Earnings Calendar

CREDIT RESEARCH

RETAIL/CONSUMER CALENDAR Q309

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July

29 Monday	30 Tuesday	1 Wednesday **Sodexo** 9M/Q3 08/09 Sales **M&S** Q109/10 Results	2 Thursday	3 Friday
6 Monday	7 Tuesday	8 Wednesday	9 Thursday	10 Friday
13 Monday	14 Tuesday	15 Wednesday **Casino** Q209 Sales	16 Thursday **Carrefour** Q209 Sales	17 Friday **Pernod Ricard** FY 08/09 Sales
20 Monday	21 Tuesday	22 Wednesday	23 Thursday **Compass** Q308/09 Sales	24 Friday
27 Monday	28 Tuesday **Ahold** Q209 Sales	29 Wednesday	30 Thursday	31 Friday **PPR** H109 Results

August

3 Monday **Metro** H1/Q209 Results	4 Tuesday	5 Wednesday	6 Thursday	7 Friday
10 Monday	11 Tuesday	12 Wednesday	13 Thursday	14 Friday
17 Monday	18 Tuesday	19 Wednesday	20 Thursday **Ahold** Q209 Results	21 Friday
24 Monday	25 Tuesday	26 Wednesday	27 Thursday **Diageo** FY 08/09 Results **Casino** H109 Results	28 Friday **Carrefour** H109 Results

September

31 Monday	1 Tuesday	2 Wednesday	3 Thursday **Pernod Ricard** FY 08/09 Results	4 Friday
7 Monday	8 Tuesday	9 Wednesday	10 Thursday	11 Friday
14 Monday	15 Tuesday	16 Wednesday	17 Thursday	18 Friday
21 Monday	22 Tuesday	23 Wednesday	24 Thursday	25 Friday
28 Monday	29 Tuesday	30 Wednesday **M&S** Q209/10 Sales	1 Thursday	2 Friday

www.calyon.com *Data releases as of 24 June 2009*

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Claire Poncet Dumont, Franck Bataille

Recommendation System:

Fundamental credit assessment: We evaluate the fundamental credit quality trend of an issuer for the next 12 months.

Calyon's Credit Research evaluates the potential changes of an issuer for the next 12 months and assigns a one year forward rating based on S&P's scale. This rating is to be compared with the average long-term rating assigned by S&P and Moody's.

Internal credit rating: We assign a rating to a company which reflects the assessment of the credit quality by the credit analyst. The timeframe for the rating is one year. As a rating scale we use a scale similar to the one of S&P and Fitch, however, we substitute the rating agencies plus or minus by high and low, ie. the Calyon scale uses AAA, High-AA, Mid-AA, Low-AA, High-A, Mid-A etc.

Performance of credit instruments: We express our expectation of how the 5 year CDS is going to perform vis-à-vis its sector. The timeframe of that recommendation is one month. When the analyst changes a recommendation he/she should indicate in the analysis when the last recommendation was made.

Outperform: CDS spreads should outperform the sector performance.
Sectorperform: CDS spreads should perform in line with the sector performance.
Underperform: CDS spreads should underperform the sector performance.

Credit products rating distribution table:
(as at 17th Jul 2009)

	All covered companies		Companies where Calyon provided Investment Banking Services in past 12 months	
	Count	Percentage	Count	Percentage
Outperform	15	16%	6	40%
Sectorperform	42	45%	15	36%
Underperform	36	39%	4	11%

Disclosures

Company Name	Disclosure
Ahold	None
Aldi	None
Arcandor	None
Asda	None
Carrefour	E, G
Casino	G
Karstadt	
Lidl	None
LVMH	G
M&S	None
Metro	None
Morrisons	None
PPR	G
Sainsbury	None
Tesco	None
TPF	None

A	NOT IN USE
B	NOT IN USE
C	The Company owned more than 5% of the total issued share capital of Crédit Agricole SA as of the end of the second most recent month preceding the publication date of this report.
D	NOT IN USE
E	One or more companies in the Crédit Agricole S.A. group owned more than 3 % of the total issued share capital of the Company as of the end of the second most recent trading day preceding the publication date of this report.
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H	Calyon and/or a company in the Crédit Agricole S.A. group has concluded or is party to a non confidential agreement relating to the provision of investment banking services (except publicly disclosed offers mentioned under G) to the Company during the past 12 months or that has given rise during the same period to the payment of compensation or to the promise to get a compensation paid.
I	This research has been communicated to the Company and following this communication, its conclusions has been amended before its dissemination.
J	An executive director of the Credit Agricole S.A. group is a director or board member of the company.

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