FINAL TRANSCRIPT

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NAFC - Q1 2007 Nash Finch Company Earnings Conference Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen and welcome to the Nash Finch First Quarter 2007 conference call. The company has asked me to advise you that this call will include forward-looking statements which involves risk and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements. Factors that could cause such differences are described in the Nash Finch press release and the in the company's filings with the SEC including its Form 10-K for fiscal 2006.

The company also notes that this call may include references to certain non-GAAP financial measures, as the term is used in SEC Regulation G, such as consolidated EBITDA. Reconciliations of non-GAAP financial measures to the most comparable GAAP financial measures are provided in the Investor Relations portion of the company's website under the captions Presentations and Supplemental Financial Information and in the schedules to the company's earnings release which can also be found in that same portion of the company's website under the caption Press Release.

It is now my pleasure to turn the conference over to the company's Chief Executive Officer, Mr. Alec Covington. Go ahead, sir.

Alec Covington - *Nash Finch Company - CEO*

Thank you, Josie, and good morning, everyone. Joining me today is Bob Dimond, the company's Chief Financial Officer, and also Kathy Mahoney, the company's general counsel.

First, I'm going to turn the call over to Bob and he'll review the financial results for the first quarter and then I'll be back to talk about some additional comments regarding the first quarter and also some updates on some of the more strategic items that we're focused on within the company. So at this time, I'd like to turn the call over to Bob Dimond.

Bob Dimond - *Nash Finch Company - CFO*

Thank you, Alec, and good morning, everyone.

Our total sales in the first quarter were $1.032 billion, relatively flat to the prior year's sales of $1.035 billion. Our strong sales in our military segment offset the sales declines in our retail segment which was caused primarily by the stores closed last year and customer attrition in our food distribution segment. This marked significant improvement from the year-to-year sales declines reported in the fourth quarter of 2006 of -2.2% and the third quarter of 2006 of -2.6%.

The following is a breakdown of sales by our three business segments. First, sales in our food distribution segment were $614.8 million this year, down 0.9% from $620.5 million last year. You should note that the sales decline between the first quarter 2007 and the first quarter 2006 was greatly reduced from the decline reported in the fourth quarter run rate of -2.7% the prior year.

Sales in our retail segment were down 10.4% to $135.6 million in the first quarter this year, versus $151.4 million last year, reflecting last year's store closures. Retail same store sales were -0.3% in the first quarter 2007. This compares favorably to same store sales in the first quarter last year of -4.1%.

As mentioned previously, our strong military segment sales momentum continued in the first quarter. Military sales were $281.8 million in this year's first quarter, up 7.2% versus $262.9 million last year.

Our gross margin for the first quarter 2007 was 8.8% of sales compared to 8.9% of sales in last year's first quarter. The decrease in gross margin in the 2007 period was primarily due to the sales mix shift between business segments. A higher percentage of the overall 2007 sales occurred in the food distribution and military segments versus the retail segment which has a higher gross profit margin. The decline in gross profit attributable to this shift was approximately 30 basis points of sales in the first quarter.

Our selling, general and administrative expenses, as a percent of sales for the first quarter 2007, were 6.4% of sales compared to 6.8% for the first quarter 2006. Similar to gross margin, the SG&A margin benefited from the fact that our retail segment, which has higher SG&A expenses as a percent of sales than our food distribution and military segments, represented a smaller percentage of our total sales in 2007. The decline in SG&A expense attributable to this shift was also approximately 30 basis points of sales in the first quarter.

Net earnings for the first quarter 2007 were $5.3 million or $0.39 per share. This compares to $3.9 million or $0.29 per share last year.

I'd like to remind you that we provide a schedule at the end of our earnings releases which details our quarterly EBITDA results in terms of consolidated EBITDA as defined in our bank credit facility. As we discussed last quarter, you'll hear Alec and I primarily discussing our earnings progress in terms of EBITDA going forward. You'll recall that one of the key financial targets identified by our new strategic plan is to drive improvements in our EBITDA margin.

With this in mind, EBITDA for the first quarter 2007 increased to $25.2 million or 2.4% of sales compared to $24 million or 2.3% of sales last year.

The following is a breakdown of EBITDA by business segment. First, EBITDA in our food distribution segment was $20.6 million for the first quarter 2007, an increase from $20.4 million in last year's first quarter. In our retail segment, EBITDA for the first quarter 2007 was $6.8 million, up from $6.7 million in the first quarter 2006.

And finally, EBITDA in our military segment was $9.9 million in the first quarter this year versus $9.2 million last year. As you can see, for the first time in several quarters, we delivered increases in EBITDA in all three business segments compared to the prior year.

Now turning to the balance sheet, you'll see that we paid down approximately $15.3 million of revolving and long-term debt during the first quarter. We had $145.5 million of debt outstanding on our senior debt facility and had $104.9 million of availability under that facility at the end of the quarter.

The leverage ratio of debt to EBITDA was 3.24 times at the end of the first quarter. The company was in compliance with all financial covenants at quarter end and we believe we have enough head room to stay in compliance going forward.

The company announced on Tuesday that our Board of Directors had declared a regular cash dividend of $0.18 per share to be paid on June 1, 2007. This is our 323rd consecutive quarterly dividend paid.

Finally, let me comment regarding the long term key financial targets identified in our strategic plan. As mentioned earlier, one of our key financial targets is to achieve an improvement in our total company EBITDA margin to 4% of sales. This is important. We have also targeted to achieve free cash flow returns on net assets of 10%, a 2% sales growth rate and to de-levering our balance sheet to a debt to EBITDA ratio of 2.5 times.

During the first quarter of 2007, we realized improvements in the following three metrics; EBITDA improved by 12 basis points over the prior year. Our total company sales growth rate improved to -0.2% versus being down an average of -2.1% during the prior three quarters. And our leverage ratio of debt to EBITDA improved to 3.24 during the quarter, down from 3.42 at year-end.

Our rolling four quarter free cash to net asset ratio decreased from the year-end rate of 8.73% to 7.28% in the first quarter 2007, due to the timing in the collection of our military accounts receivable balance from December 2005 into the first quarter 2006 which provided a benefit to the free cash flow ratio last year.

We're confident that as we progress towards delivering on these goals, that this should also translate into driving significant shareholder value.

I'll now turn the time over to Alec.

Alec Covington - *Nash Finch Company - CEO*

Thank you, Bob. I think a few comments from my side. At first, overall, I think the first thing I would say is that sales were almost exactly as we had expected. We do, obviously, have internal budgets and forecasts and I would say that our top line came in, I mean, just within a few dollars of what we had anticipated relative to our internal plan. I would say that our EBITDA was right on track with our internal plan.

The one thing that I'm very pleased about this morning is that we don't have any notable one-time charges that we have to discuss because, it's always a little uncomfortable when we have to come in with a schedule that tries to reconcile EBITDA because of a lot of one-time charges and we don't have that this quarter. And that, of course, is very positive for us.

Clearly, there are visible signs of improvement in all of our business units. That's what you want to see. So we've been able to get the right team in place; get the people focused around the things that need to be done in all business units so that we don't have one performing well and another one struggling and so on and so forth. So I like to see that in a business. To be honest, that gives me some reassurance that the team's working well together.

I would also say, though, and I think everybody understands this, that we clearly still have a lot of heavy lifting that has to be done. There's a lot of work to be done within this company to really continue to maximize on the opportunities that are ahead of us towards the targets that we've established for ourselves to hit.

I'm also pleased that we have now finished the senior management team line-up. We just added Denise Wilson as the Senior Vice President of Human Resources. Denise comes to us from NRG Energy where she served as an Executive Vice President and the Chief Administrative Officer of the company. She has an extensive human resource background and experiences and is extremely bright and talented. So with Denise on board, we now have a full complement of our senior management staff, all very talented. All very experienced in their own disciplines. All working together properly as a team and all well understanding the targets that we're committed to and the journey that we have in front of us towards hitting those targets.

Now looking at the individual segments of our business for a few moments. First of all, in the food distribution segment, personally I was pleased with the top line result with a decrease that's about 1% less than last year, keeping in mind that it was more than double that decline in the fourth quarter. So the only way that happens, of course, is that there's been some incremental pieces of business that's been added. Part of that has come from a higher level of concentration of purchases from existing customers where maybe they were buying items such as store supplies outside of our network. And now with our new supplies program and some of the other things that we've done, they're now purchasing inside the network. So that's positive news.

We also have, on a regular basis, been adding new customers. A store here, a store there; nothing big, nothing that merits a major public press release, of course, but yet embedded in our network, has been some steady increases and gains of new customer business along the way. Otherwise, of course, the food distribution segment could not have posted those top line results.

In food distribution, EBITDA showed slight improvement in dollars from prior year. That also is good to see that that group is gaining traction. Now that's coming from a couple of different areas. First of all, as we analyze the business carefully, we know that we have a lot of disciplines back in place in inventory management. That's part of how you earn gross margin by properly managing inventories. That's one part of where those improvements has come from.

The second is in vendor management. We have a complete new group and a new leader in that role. And [Gary Spinazi] is Vice President of Vendor Relations. Gary was with the company back some time ago, left and now he has come back and under Christopher Brown's leadership, has put in place a lot of the disciplines that had been lost in vendor management. That's very positive toward the achievement of our gross margin because in order to earn gross margin, managing inventories is critical. And secondly, properly managing the relationships with our vendors is critical.

Now where the gross margin improvement didn't come from is from increases in the way that we sell products to our customers. To the contrary, we have a tracking device within the company that tracks the level of off-invoice promotions that are available to our customers at any one time. And what I mean by that is products that we sell is sold at list cost and then we reduce from the list cost that which is made available to us from the vendor community in promotions that are available on an interval cycle throughout the year. We've actually saw a remarkable increase in the number of promotions that we're making available to our customers.

The second thing, we monitor that's very important about that is the depth of those promotions. And by depth, I define that as the percentage of the promotion as a percentage of the list case cost of the product. We've actually saw an increased depth in this promotions. So, simply said, what that means is is that we're actually selling products to our customers today on a net, net lower price than we were a few months ago and earning a higher gross margin by better managing our inventories and better managing our vendor relationships.

So those are the kinds of variables that you want to see move in that collective direction that gives you an indication that the procurement team is really doing a good job. And they are. I think the management team in food distribution is clearly focused on the right things.

Now one of the things, of course, that we regret is that Martin's, one of our largest customers, has made a decision to transition their business to another supplier that was, of course, part of the announcement that we put out in the press release last evening. We regret this decision but, let's be clear, we highly respect the customer. They've been a good long-term customer of ours and [Roundies] before we acquired them. I've known the family for the better part of my life. So I have a high respect for them. This represents a business decision. And this business decision was made by that particular family for reasons which we are not privileged to, nor do we fully understand. In the world that we live in and, of course, with confidentiality agreements, we're not likely to know all of the reasons, nor do we have a right to know all of the reasons upon which they base their business decision.

What I'm also always very concerned about is making sure I understand what kinds of things could have contributed to that. Was it something to do with our relationship? Well the answer to that is unequivocally no. Was there something wrong with the service we were providing? No, to the contrary, Martin's, in just recent weeks, was very complimentary of the job that our Westville, Indiana facility had been doing in servicing their business through some very difficult times. Westville was, that particular area around South Bend was hit with an incredible snowstorm here a number of weeks ago. Martin's called me specifically to compliment our Westville facility on getting the trucks out and taking care of their business in spite of those impediments.

So it didn't have anything to do with service or relationships. It simply had to do with the business decision that Martin's made. And that is the business we're in. I've been in this for 30 years and, fortunately, over the last 30 years, I've been fortunate to see more people come than go but, occasionally, you see them go. And one of the things that you always do is make sure that you handle that transition in a way that makes it easy for the customer return if they ever see the need.

You can see from the press release that we turned in that the margin was low so I don't have to tell you that we didn't have a lot of wiggle room in the relationship before we got down to a loss. So we didn't have a lot of places to move given the low margin nature of the business. And, at the end of the day, as much as I love serving independent customers and that's been my life, I also have a responsibility to make sure that the facilities that we have and the capital that we have employed in this business is allocated in such a way that not only does it do a proper job of serving our customers, but also it does a fair job in serving the needs of our shareholders.

And when those two things aren't possible, sometimes it creates a need for a business change. And that's indeed what we're seeing here. Not reflective of a relationship. They're wonderful people. And not reflective of any kind of service issues, 'cause there just hasn't been any. It just really has to do with a basic business decision that, in the last 30 years, I've seem made to my benefit and sometimes to my detriment and I'm sure that in the course of time I'm here with Nash Finch, we'll see that work both ways as well.

The one thing I would tell you is that I am very, very -- well before I move on, let me go on and just touch on one other point with the Martin's relationship. And that is that this information in its finality came to us only within the last few hours. And it was my opinion, Bob's opinion and Kathy's opinion that we would relay to the public everything that we know. Of course, we're obligated to do that, but it's just the right thing to do to begin with. So we did release very quickly all the information that we had, as quickly as we had it.

Sometimes in these kinds of transitions, people change their minds on what they think is possible. And I would only say that as recent as within the last hour, I've had some discussion that leads me to believe that some of that business, particularly in the perishable areas, we have a really powerful meat program out of Westville. And an even more extensive variety of bakery and deli products that are not readily available. And in my own heart of hearts in the last few hours, I questioned whether they would be able to replace that variety with the new source of supply. And as it turns out, it may be that some of that perishable business may be retained, but again, that's just new news here in the last few hours. There's nothing definite. But I would say that the meat and bakery, deli, the perishable business associated with Martin's represents roughly one-third of the overall volume that we did with them to begin with.

So I should tell you everything that I know. So we have stated that it is our belief that we may lose all of the business, but there is some possibility that roughly one-third of that business could be retained. I don't know. These things are fluid. If you've ever been through this in a transition of a customer, you know what I'm talking about. And, of course, we're perfectly willing to retain any portion of that business that we can properly serve the customer and also properly serve our shareholders.

So we would certainly be positively inclined to do so if that would be of service to Martin's. And we'll report next quarter. We'll certainly have a lot more clarity on that. We'll bring the group back up to speed with what those results are because I think we'll understand a little bit more by then what the true finality of this situation might be. The transition timeframe for that business appears to be sometime after the first of June, so my expectation is that the transition of that business may extend into July and August so it may be a little bit into third quarter before we get it all transitioned out, whatever part actually goes out.

Now having said that, I was at our Westville facility yesterday. I met with our employees through the evening, last evening, face-to-face, to make sure that they were communicated with very fairly. I would tell you that first of all, I have a strong attraction toward the Westville, Indiana facility. It has an excellent location first of all, because it's located adjacent to Chicago. And if you've been around the food business very much, you know that a great deal of product originates in Chicagoland, if you're in the food business.

We have our sights and have had for some time our sights firmly focused on the Chicago market for growth and development out of Westville. That has been our focus. That will continue to be our focus. It's an excellent location for us. It's a very strategic location for us. And I believe it is one whereby we have the ability to grow volume. And grow volume in a way that not only allows us to properly serve the customer but also allows us to be property accretive to our shareholders. So that will be our focus. It is an excellent facility. We own the plant there. It was built by Eagle Food Centers a number of years ago. It's a fantastic facility. And beyond all of that, and more important than all that, it has an excellent and extremely productive work force. So we have quite a strong competitive advantage in comparison to the Chicagoland market in terms of distribution. And we want to leverage that and really exploit that here over the next couple of years.

So that is, of course, a set back to the top line of our company and a set back to Westville. But as I said to the group last night, that doesn't change my opinion of Westville. I've been in this business a long time. And I know what the opportunities there are and we fully intend to exploit those over the next couple of years.

Now can we bring that level of business back as quickly as this transitions out? Well no, of course not. But if I wasn't confident of our ability to do that over the longer term, I'd say so. But in some locations, I would have difficulty in rebuilding that volume over time, but in that particular location, I think we have some tremendous opportunities over the next couple years.

Now for the food distribution, in looking at the second quarter, they're going to be focused on three things in some level of intensity. First of all, we have been focused on continued top line improvements. They've been doing a good job in that area. We need to continue. The pipeline is quite strong and I expect to see continued improvements in customer additions during the second quarter.

We want to continue to focus on improvements in inventory and vendor management. That group, as I mentioned earlier, is gaining traction. That's the reason for the gross margin improvements. I know that I've said, probably more times than you've wanted to hear, how important it is to have people that are truly experienced in merchants managing that inventory. I think you can now see the evidence of what I've been talking about.

The third is I want to see an increased emphasis on operating cost reductions. Now to be fair to the group, the operating cost in that particular segment was below prior year. But yet it's my belief, and our belief as the senior management team including Christophers and Jeff Poores who directly operate this business, that we need to see that accelerate. And so that'll be a continued emphasis or stronger emphasis for us in the second quarter because I'd like to see us show even quicker and more accelerated operating cost declines in that particular business unit. That's available to us. We know it. We see it. It's a matter of making sure that we see it materialize at a faster pace. Again, they are below prior year in operating cost but, again, not quite up to what we think should be there and what is possible.

In the corporate retail segment, I was delighted to see that our comparable store sales were negative only by a negative 0.3 as compared to a negative 0.70 in the fourth quarter and negative 1.8 through all of 2006. We saw a slight EBITDA improvement in dollars and rates. And the rate moved to 5% from 4.45.

The major reasons for all of that is, first of all, we closed underperforming units last year. You're aware of that. And that automatically gives you a lift in comparable store sales. Obviously, it would if you close the right one. But also beyond that, the group is really doing a good job in improving the efficiency and the dollars that they're spending in merchandising. And that is really helping to drive our top line results in a more efficient manner. So the markdowns are being spent in a proper way. The merchandising dollars are being spent wisely. And as the efficiency of all of that is much better than it was a year ago and therefore, you see improvements in the gross margin.

Now embedded in that, you will also see that we've increased labor in those stores. That was intentional. I wanted to put labor back in those stores, particularly in the conventional units in order to better serve our customers. We put in programs such as all check lanes open between the hours of 4 and 6 in the afternoons. That's paying big dividends for us. We're getting a lot of good remarks from our customers in that regard. Our service departments are more staffed and better staffed than they were. So that's all part of doing the proper job in retail. So we've reinvested some of that margin improvement back into additional labor to better serve our customers. Service is, of course, a key differentiator for us against the big box retailers that we compete with.

So I think management in that area, that management team in retail, they're all making good decisions. In the second quarter, their focus will be to maintain a strong focus on sales comp improvements. We have to recognize that throughout the year, we'll have more competitors that are going to open. So that becomes a more intense battle every month that you go throughout the year. On the other hand, we began to cycle through competitors that opened a year ago. So balancing those two and continuing to see improvements is a struggle in this business, of course. But I think that this group is continuing to show good results but I'm cautious about how well they'll be able to do that throughout the remainder of the year given the fact that we know we're going to have additional competitors open. So they're focused on that maintaining the sales comp improvements. But that'll be a difficult task for them.

They're also continued on the focus of continuing to open and expand in the alternative format area. Our Avanza units in Denver are performing quite well. We see additional opportunities in some of the areas throughout the rest of our network to capitalize on that same opportunity. We'll begin to do that in the second quarter. We opened a second Food Bonanza which is our extreme price impact format which is operating at a [shell] price plus 10% at the cash register type format. We have one in Omaha. We just opened one in Ottumwa here a few weeks ago in March and so far so good.

So making sure that we focus on alternative format to get these units well-defined in their market position is a critical part of our strategic plan. We have to do that carefully. We have to do it without spending a lot of money. And I think you see that we're doing that. And we'll continue to focus on that in the second quarter.

Now the military segment for a second is one that I just couldn't be more delighted with. First of all, they produced over a 7% increase in growth through new customer additions. That's just organic growth which is the best kind of growth you can have. So that's indicative of the fact that our vendor partners are happy with us. The military bases are happy with us. And they continue to award us more business.

EBITDA improved and one of the reasons why EBITDA improved is because our export business really exceeded our expectations. And exporting is a good part of that business. We didn't really expect it to be a growing part of the business, but it's turned out to be growing at a little faster rate than we'd anticipated. And the export business is typically more profitable at an EBITDA level than the domestic business. So that's part of what's driving those improvements. And we're just delighted with what's happening there. The management team is just doing an excellent job, led by Ed Brunot, who we installed in there last year as the leader. And then a group of really experienced and really seasoned veteran management members that many of which has worked for Nash Finch since we owned it. But many of which worked for [Jerry Jerrod] and the group of owners who owned it prior to Nash Finch acquiring it back in the late '90s.

Now the second quarter, that group is going to continue to push for organic growth. Not only have they had good results in the first quarter, but as we look at their pipeline, we think there's improved results that we'll see also in the second quarter. So that's good news.

And just like food distribution, we've asked them to put an increased emphasis on operating costs reductions. We think that there's opportunity for productivity improvement. And, yes, the operating cost is not worse than it was a year ago. It might be slightly better than it was a year ago. At the end of the day, those of us who study that business and Ed, who leads that business, understands that there's opportunities to improve that productivity and reduce some of the operating cost on the operating side that will make that business even better. And we really want to exploit that in a more aggressive way than we did in the first quarter.

Regarding Operation Fresh Start, which is our strategic platform for the future. We added two new team members to kind of round out our efforts there. Dennis Hanley, we announced during the quarter, had joined the company as Vice President of Alternative Formats. Dennis is someone that I worked with in another lifetime. He is very experienced; very seasoned and is working very hard to exploit the opportunities we have available to us in our Hispanic format and in our extreme value format. He's doing that now. He'll continue to ramp up those efforts throughout the year.

Howard Befort just joined as Senior Vice President of Merchandising. He is specifically charged with the strategic initiative which we refer to as our center store program. Howard comes to us with 30 years of experience in merchandising and marketing from Safeway; is just a really seasoned executive to put into that role and already is gaining traction having only been here just a few weeks.

So that is moving and we have now a good solid team in place to lead those strategic initiatives. I've mentioned before that we have a desire to improve the efficiency of our perishable network west of the Mississippi. And that would be where we would start. That perishable network study is currently underway. We have some interesting initial findings but we have nothing to report at this particular conference call, but you can expect to hear more about those developments later this year as we finalize those plans and begin to act on those a little bit later.

Regarding the center store program, we have established test sites. We have communicated with those test sites who they are and communicated with the customers so that they're aware of where we'll be launching the center store program at. For right now I would prefer not to name those sites because of competitive reasons, but we have two initial sites that we're going to launch. And those vendor discussions are currently underway. Our category management team are meeting with the vendors right now as we speak, renegotiating our product cost relationships in order to support the program properly.

Private label expansion, as I mentioned, was essential toward the success in this program. That's already happening. We've launched an organic line of product under the Our Family label as well as an expanded line of premium labels that helps to increase the penetration of private label in our stores which helps support this program.

And our pricing department has been fully established and is well underway in developing the pricing matrix that's necessary to drive the overall center store program. So all of that is moving well. But we move carefully and cautiously to make sure that each step we take is on solid footing. We don't need any surprises. So we move very carefully and we're managing that process very close within the senior management team.

We also, as I mentioned before, have installed new systems and consistent systems among all of our facilities to support our military distribution business. As I mentioned before, some of that military business is shipped from some of our Nash Finch facilities, our food distribution facilities. We want to make sure that to the customer it looks no different than shipments that are coming right out of MDV. So that now has been done so that all of our processes and all of our customer service matrix is consistent with what we do at MDV. That is really drawing some great accolades from our vendor partners and from our military partners. So that's been a good move for us. It has dramatically improved our shipping quality.

So we continue to pursue organic growth not only at our Norfolk facility, but we're actually seeing growth in our Nash Finch facilities as well as a result of this. And along with that, we're continuing to review acquisition opportunities that may make themselves available in the military segment of our business because we would be very comfortable with absorbing something that would meet our risk profile and also be accretive to our business there.

In corporate retail, as I mentioned, we converted another store to our Food Bonanza program in March and the initial results are encouraging but hey, it's only been a few weeks. So we don't really have enough under our belt to really see what kind of sustainable results might be available from that, but we're encouraged by what we see so far.

Now I guess in summary, while we regret the pending loss of some of the Martin's volume, we're clearly pleased with the first quarter results overall. There's signs of improvement visible in all of the business segments. It's clear that as we move forward, Operation Fresh Start with our strategic plans, we continue to move carefully, but we are moving forward. We're simply dedicated to our being the premier partner to our independent retailers and regional chains. It's simply what we intend to do.

We remain committed to our long-term goals. That's 2% organic growth. Again, we have to get the strategic plan implemented. Of course, the news that we would lose some of the Martin's business puts us one step behind and we have to now gain more to even do that. But I don't have any hesitation in believing that we'll still be able to achieve the 2% organic growth beyond the implementation of our full strategic plan. I think that's even more readily clear to me with what I saw in terms of growth in the first quarter.

The 4% EBITDA to revenue; we're moving now toward that direction by reducing our costs and improving the way we manage inventory. That's exactly what we told you we would do.

The 10% return on free cash flow, of course, because of some aberrations a year ago in accounts receivable, that is a bit more challenging this year in this particular quarter than a year ago. But yet we're going to report each quarter and be held accountable for those results each quarter as we said that we would.

And our EBITDA leverage remains a critical part of our goal as well, at 2.5 and, as Bob mentioned, we made a substantial improvement in debt reduction during the quarter which we think is very positive.

And also I guess my final comment would be, amidst all the things that are positive and moving, there still remains a lot of heavy lifting that we have to do during 2007 and beyond to get this company fully directed toward the goals that we've established for the company.

Now with that, Josie, if you wouldn't mind, I would appreciate the opportunity to accept some questions from this group.

QUESTIONS AND ANSWERS

Operator

Thank you. [OPERATOR INSTRUCTIONS] And our first question is from Meredith Adler from Lehman Brothers. Go ahead please.

Karen Howland - *Lehman Brothers - Analyst*

Hi, gentlemen. It's actually Karen Howland calling. Congrats on the great quarter.

Alec Covington - *Nash Finch Company - CEO*

Thank you.

Karen Howland - *Lehman Brothers - Analyst*

Looks like fundamentals really are improving considerably. I was hoping to touch base on the retail network for a moment. And in the margin, if you look at it sequentially, as far as the improvement, a significant improvement from the fourth quarter. I know in the fourth quarter, you were indicating that investments and promotion and labor really depressed the margin. Is it safe to say that the improvements in the pricing and the merchandise spend offset all of that? Is there anything else going on in those numbers?

Alec Covington - *Nash Finch Company - CEO*

Well I would say that there's a couple things. One is the mix is beginning to change in the retail stores, Karen. The mix, when I came here, was too heavily weighted toward promotional activities. So we measured the sales in the retail stores regarding how much is going out the front door related to ad items and how much is related is to just typical, everyday low priced items. Now what Mike Mills and his team has been able to do with clever merchandising and better price promotion items, better everyday low pricing programs in the store, they've been able to move the needle on that mix which is critical.

Secondarily, they've been able to improve the mix in the perishable areas which is also helpful. So I would say it's a combination of improved mix change. And I would say it's also, as I mentioned before, doing a much better job at wisely spending those markdown dollars to try to drive footsteps through the front door. It's that combination that's doing that, Karen, overall.

Karen Howland - *Lehman Brothers - Analyst*

Great. And then sticking with the retail side, I read in Supermarket News recently that there's speculation that you might be buying some of the Farmer Jack stores from A&P. I'm sure you can't comment directly on that. But I was wondering if you were to be looking at some retail stores, would you be buying them -- are you looking to buy for your own corporate stores or is it to help one of your independent customers out? How would that work? Are you looking to expand your corporate?

Alec Covington - *Nash Finch Company - CEO*

Yeah, no. I think that if we were to do something like that, it would be in direct conflict to what we have said with our strategic plan. So if you were to see Nash Finch move in any direction relative to being involved in any part of a retail acquisition, it would be solely to benefit our retail customers and to expand our presence in that area.

What we are doing, always, is working with our independent retailers to allow them to act as a collective group in pursuing whatever opportunities might be available in the marketplace. So I would not expect to see us directly for any length of time buying and owning and expanding our retail network. But more involved in some fashion in helping to expand the retail stores that are owned and operated by our customers; and our involvement might be very limited or sometimes temporary, but I wouldn't expect to see us expand directly through our corporate retail group in that regard.

Karen Howland. Okay. Great. Thanks for that clarity. And in keeping with retail, are the alternative formats comping and are their performance better than the conventional stores?

Alec Covington. Yeah. There's so much noise in those numbers and, honestly, there's so few of them right now, that it's hard to get a handle around that because in some cases, they're doing wildly well and in others, they're not so well. And we're changing some merchandising strategy. So there's not a consistent theme that I can give you on that. I will say that our test site in Omaha, Nebraska has continued to post sales gains well in excess of anything that we see within any of the rest of our retail group.

And I would also say that it is apparent that there remains a lot more opportunity in our Avanza format that was originally identified by the company. And so I think those are the two key drivers for the alternative formats, Karen. I can't give you a solid trend because we're making so many moves that it's just all over the board and some of those aberrations are coming off of dramatic increases over a dismal performance a year ago. So it's not a true trend that we can really speak to intelligently.

Karen Howland - *Lehman Brothers - Analyst*

I recognize that it's still pretty early, I was just hoping to get some indication of how they're performing versus the rest of the stores.

Alec Covington - *Nash Finch Company - CEO*

No, they're performing -- I would say they're performing, in some cases, better. But then in Denver, where we have the two Avanzas, we're still doing very well in Denver, but then we have a lot of company there now with Azteca and Sbarro and others that have joined the marketplace there. So it's not quite as positive as it was, say, two years ago, but still a very strong market share presence and a very dedicated following in Denver. So it's varied according to the market.

Karen Howland - *Lehman Brothers - Analyst*

Great. Thanks. And then within the distribution, I know you're saying the Martin's business is about $3 million EBITDA to the Westville facility. 'Cause that's a unionized facility, right?

Alec Covington - *Nash Finch Company - CEO*

It is a unionized facility, correct.

Karen Howland - *Lehman Brothers - Analyst*

So in addition to the lost EBITDA just from the product sales, presumably there will be some additional labor expenses that are going to be maintained at the facility that don't have sales to leverage on right now, right?

Alec Covington - *Nash Finch Company - CEO*

That's correct. But in our EBITDA analysis, we tried to take a very conservative view of our ability to scale back the operation. So we're very comfortable that the $3 million number would be something that we can meet or overachieve.

Karen Howland - *Lehman Brothers - Analyst*

Okay. Great. Thank you. And then two other just small questions. I noticed in the cash flow statement that there was no dividends paid this past quarter. Is that just a timing?

Bob Dimond - *Nash Finch Company - CFO*

That's just a timing thing. It was paid right after quarter end.

Karen Howland - *Lehman Brothers - Analyst*

So there will probably be two in this upcoming quarter?

Bob Dimond - *Nash Finch Company - CFO*

That's correct.

Karen Howland - *Lehman Brothers - Analyst*

Okay. And then there was a significant jump in other long term liabilities?

Bob Dimond - *Nash Finch Company - CFO*

I think the thing that you're seeing there is the implementation of the [FIN 48] where we needed to re-class as a result of FIN 48, a few items between what used to be in tax reserve accounts down into other liabilities.

Karen Howland - *Lehman Brothers - Analyst*

Okay. Perfect. Well thanks very much for answering all my questions and congrats on the good quarter.

Alec Covington - *Nash Finch Company - CEO*

Thank you.

Operator

Thank you. Our next question is from Blaine Marder, from Loeb Partners. Go ahead, please.

Blaine Marder - *Loeb Partners - Analyst*

Hi, guys. Congratulations, again. Terrific quarter results. Alec, as we kind of work the pig through the python, if you will, with the Martin's business, do you see any Martin's type business in your pipeline in terms of winning accounts like that that could perhaps offset this over the next four quarters, especially as we look in the first half of '08?

Alec Covington - *Nash Finch Company - CEO*

As I look in our pipeline, I clearly see business opportunities that could be equal to or greater than what we will lose as result of the Martin's transition. The issue, Blaine, is always one of timing. Does that business come at the same time that we're transitioning out? It rarely ever matches up. And so I would say that it's difficult for me to put a timing element around that.

What I will say, though, is that as we look throughout our overall network, we've had embedded in our plan a fairly substantial amount of growth that was embedded in our internal plans for the year. And when we ended the first quarter, we actually exceeded those internal plans. And as I look to the second quarter, with the forecast, it's even apparent that we'll do at least as well as we had anticipated. So I think there's growth that is coming. It's a matter of it matching one for one with that. And I really don't see that happening, in all honesty, Blaine. I think eventually we'll make that up and more. But we'll probably see a bell curve with some part of that volume before we see it for the ability to overcome it and move beyond that volume level.

Blaine Marder - *Loeb Partners - Analyst*

Okay. So if I was going to be conservative, the first two quarters of '08, I would assume revenue is going to be down and then we kind of rebound in the back half of '08 such that '08, you might get a little growth overall when we consider the whole year?

Alec Covington - *Nash Finch Company - CEO*

Yeah. That's according to the timing of how quickly it cycles out this year which gives you the comp. And the clarity on when it will cycle out is not quite as clear to me as to will that be closely behind the second or will it delay into the third. Sometimes these things drag on. And how long will we be cycling through that into next year. But I think, today, your assessment is as good as anything I could give you and I would also say that as you look at our trend, and as I look at the initiatives that we have, the progress we're making, it probably will take us longer to make that up on the top line than it will on the bottom line, given the trends that we're in right now. So I think that the business is far more impactful to the top line than to the overall bottom line.

Blaine Marder - *Loeb Partners - Analyst*

Okay. Very good. And then in free cash flow, including the benefits of working capital, you've already produced sort of $20 million this year and you're set to do somewhere between 50 and $60 million at this run rate for '07 and that would get you to your sort of 2.5 debt target leverage. And then if we look into 2008, without the benefit of working capital, you could generate another $50 million of free cash flow. And it looks to be about 10% of your market capitalization. So as you start thinking about using that free cash flow in 2008, what are your thoughts? What is the Board -- what are you thinking? What's the management thinking?

Alec Covington - *Nash Finch Company - CEO*

Yeah. We're, actually, those discussions are underway. We had some really good dialogue with the Audit Committee and with the overall Board on that topic just a couple days ago. And I think you're right. I think we had always indicated that we felt that we could de-lever down through our target range by the end of 2007 or early 2008. And I think your analysis is right on track with what we see. I think that now those discussions are quite interesting because we are kind of going through that sources and uses of cash and you never know what's going to influence your thought process. It's all about what would be accretive to shareholder value and it's about first of all, getting that debt leverage down. Secondly, what types of small incremental acquisitions might be out there that could be very accretive to that cause. Is that a good use of cash? If that's not there, then do we look at dividends? Do we look at stock? What are the kinds of things we would pursue?

Those discussions are underway and we haven't drawn any specific conclusions, but we are looking at all the alternatives, Blaine, and we see that as an exercise for us, as I refer to it in our initiatives internally, it's financial architecture that we will be examining quite closely and bringing to conclusion here over the several months as we conclude the rest of this year. And we'll probably have more to say about that later in the year. We're not quite prepared to speak to that today. But the trends that you've identified are absolutely right on target.

Blaine Marder - *Loeb Partners - Analyst*

Okay. And just one final question; it's on the retail business. As we look past this year into '08, and the store closures are not going to be as dramatic and that same store sales seems to have stabilized, is it possible you could actually get some earnings, albeit slight earnings, growth out of that business in 2008?

Alec Covington - *Nash Finch Company - CEO*

Well that's clearly our focus. And I would also say that one of the reasons why I'm kind of dead set on doing that is because if we don't do that, then it's a signal that our format differentiation and our conversions to our alternative formats are not working. So I expect to see lift in each of those as we convert them. So I think that is a reasonable expectation and so I happen to agree with that thought process.

Blaine Marder - *Loeb Partners - Analyst*

Fair enough. Thanks a lot.

Alec Covington - *Nash Finch Company - CEO*

Thank you.

Operator

Thank you. And once again, if you folks have any questions, please press star one. And I'm showing our next question is from [Keith Curtis] from [Brent Point Capital]. Go ahead, please

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Keith Curtis - *Brent Point Capital - Analyst*

Hi, guys. Congrats on a great quarter. Question is about the corporate overhead. If you could just comment there. It seemed like you made some headway there and is this a reasonable run rate to think about going forward? Will that move around much from where we are here?

Alec Covington - *Nash Finch Company - CEO*

Yeah. On corporate overhead, that's probably a little bit of a topic that Bob always cringes when somebody brings it up 'cause he knows that I think corporate overhead's way too high no matter where it is. And so I would say that I'm pleased with the progress that has been made in corporate overhead. I would be very disappointed if we saw the trend go back the other direction. And I would be equally disappointed if we don't see continued improvement in that area. So it has our attention, Keith, and I think that there is more leverage there to be had. How much, of course, is up for debate and something that I guess our senior management team finds themselves discussing with me more than they want to, but at the end of the day, it's something that we're very focused on. I don't see it reversing and I'm optimistic that we'll continue to find ways to reduce it because it's critically, absolutely critical that we reduce corporate overhead to continue to improve our competitive vitality and that's part of our strategic initiative.

Keith Curtis - *Brent Point Capital - Analyst*

And when you say continue to improve, do you mean from the 12.1 level we're at now or on a year-over-year basis kind of going forward?

Alec Covington - *Nash Finch Company - CEO*

Well I expect both. I expect on a year-over-year basis that we will continue to see improvements as we've seen in the first quarter. I'd be very disappointed if that trend went the other way.

Keith Curtis - *Brent Point Capital - Analyst*

Right.

Alec Covington - *Nash Finch Company - CEO*

The second is is I think the current run rate, and I give the team a great deal of accolades for the improvements that we've made, but I've also been very clear to say I don't think it's enough. And I think we have to do more. So we're focused on improving it even from the current run rate. Now we don't have -- today, I can't point, Keith, to some specific initiatives that would do that because we're just really beginning to focus. We've been so consumed with trying to make sure that we saw some growth coming on the top line, that we had the margins improving, that we haven't ignored that line, you can see that. But we're now turning our attentions toward those kinds of lines with a great deal more emphasis than we were when we were trying to build a team and trying to get our gross margins straightened out. So I don't have anything specific to say that will be done to reduce that, but I can tell you that I'll be disappointed if we can't continue to improve on even the current run rate.

Keith Curtis - *Brent Point Capital - Analyst*

Yep. Great. And then just lastly; last quarter we talked about a couple of facilities that you guys had planned on closing that you went ahead and kind of put that off on the back burner for the time being as you saw some potential new business in the pipeline. If you could just give us any update there, that would be great.

Alec Covington - *Nash Finch Company - CEO*

Well and I would say that some of that ties back to some of the new business initiatives that are underway right now. Some of it ties back to some of the potential divestitures that are going on in the market place today and how that'll impact our capacity and all is still uncertain. So we're still optimistic that we'll see some growth come through some of the events that are occurring in the market place right now. I would say, though, that we are completing our plans to benefit from a more clever way of running some of our distribution centers and we're concluding those plans. If you remember, at the end of last year, we announced the potential consolidation of some facility and then we reversed that in the first quarter because we said that we found a more clever way of doing it where we didn't have to spend as much capital and where we would get a much higher return. And what we've been doing is finalizing those plans to do that and that will roll out here within the second quarter and we'll be able to speak to that on our next call.

Keith Curtis - *Brent Point Capital - Analyst*

Great. Thanks a lot and keep up the good work.

Alec Covington - *Nash Finch Company - CEO*

Thank you.

Operator

Thank you. And I'm showing no further questions at this point.

Alec Covington - *Nash Finch Company - CEO*

Okay. Well, listen we appreciate the support. We appreciate the dialogue and we'll continue to do our very best to continue to stay on track with our commitments. And I appreciate the attendance in the conference call this morning. Thank you and have a great week.