

FINAL TRANSCRIPT

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NAFC - Q4 2007 Nash Finch Company Earnings Conference Call

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CORPORATE PARTICIPANTS

Alec Covington

Nash Finch Co. - CEO

Bob Dimond

Nash Finch Co. - CFO

Kathy Mahoney

Nash Finch Co. - General Counsel

CONFERENCE CALL PARTICIPANTS

Mark Churchill

Piper Jaffray - Analyst

Karen Howland

Lehman Brothers - Analyst

Regina Russell

JP Morgan - Analyst

PRESENTATION

Operator

Good morning, ladies and gentlemen and welcome to the Nash Finch fourth quarter and fiscal year 2007 conference call. As a reminder, today's call is being recorded. The Company has asked me to advise you that this call will include forward-looking statements which involve risks 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 in the Company's filings with the SEC including its Form 10-K for fiscal 2006.

The Company also notes that the 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 on the Investor Relations portion of the Company's Web site under the caption, "Presentations and Supplemental Financial Information" and in the schedules the Company's earnings release which can also be found in that same portion of the Company's Web site 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. Please go ahead, sir.

Alec Covington - Nash Finch Co. - CEO

Thank you, James and good morning, everyone. Joining me today are Bob Dimond, the Company's Chief Financial Officer and Kathy Mahoney, the Company's General Counsel.

As we've done in the past, Bob will step us through the financial results of the quarter and the year and then I'll be back just a little later to express a few thoughts on the quarter, the year, our strategic plan and some other matters. Go ahead, Bob.

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Bob Dimond - Nash Finch Co. - CFO

Thank you, Alec, and good morning, everyone. Total sales in the fourth quarter 2007 were \$1.069 billion compared to the prior year sales of \$1.099 billion or a decrease of 2.7%. Fiscal 2007 sales were \$4.533 billion as compared to \$4.632 billion last year, a decrease of 2.1%.

The fourth quarter and full year sales declines were primarily due to the previously announced transition of a large customer in the food distribution segment to another supplier. It's important to note that after excluding the sales decrease attributable to this customer, total company sales actually increased by 0.9% in the fourth quarter which was a 190 basis point positive swing from that experienced in the third quarter of minus 1%. It was nice to see this swing to a positive sales comparison relative to the prior quarter trends where sales comparisons to the prior year had been negative.

Net earnings for the fourth quarter 2007 were \$8.5 million or \$0.62 per diluted share and this compares to a net loss of \$26.4 million or \$1.96 per diluted share last year. Net earnings for fiscal 2007 were \$38.8 million or \$2.84 per diluted share, as compared to a net loss of \$23 million, or \$1.72 per diluted share for 2006.

I'd like to remind you that we provide a Supplementary Schedule at the end of our earnings release which details our quarterly EBITDA results in terms of consolidated EBITDA as defined in our bank credit facility. You'll recall that one of the key financial targets identified in our strategic plan is to drive improvements in our EBITDA margin and with this in mind, EBITDA for the fourth quarter 2007 increased to \$30.2 million, or 2.8% of sales compared to \$23.9 million, or 2.2% of sales last year.

EBITDA for fiscal 2007 was \$128.8 million, or 2.8% of sales, compared to \$102.7 million, or 2.2% of sales, for fiscal 2006. We're very pleased with the year-over-year increases in EBITDA realized during the quarter and fiscal 2007 periods which benefited from improvements in both gross margin and SG&A expenses.

I'd ask that you refer to the table on page 2 of the earnings release which details the significant items that affected both pretax income and EBITDA. Pretax income for the fourth quarter periods included significant items totaling \$2.6 million in 2007 and \$39 million in 2006 and EBITDA for the fourth quarters included significant items totaling \$2.6 million in 2007 and \$5.2 million in 2006. Pretax income for the full year periods included significant items totaling \$3.3 million in 2007 and \$63.7 million in 2006.

Finally, EBITDA for the full year periods included significant items totaling \$2.4 million in 2007 and \$11 million in 2006.

I'd now like to drill down into each of our business segments. The following is a breakdown of sales by our three business segments for the fourth quarter.

Sales in our Food Distribution segment were \$635.2 million in the fourth quarter 2007, down 4.7%, compared to \$665 -- \$666.5 million last year. Excluding the decline in sales of \$39.3 million attributable to the customer who transitioned to another supplier, Food Distribution segment sales increased 1.3%, which is a 200 basis point positive improvement from that experience in the third quarter of minus 0.7%, so we're very encouraged by this swing to a positive trend compared to the previous quarters.

The sales momentum in our Military segment continued to be strong in the fourth quarter with sales of \$299.2 million in this year's quarter, up 3.7% versus \$288.5 million last year. Our Retail segment sales were \$134.9 million in the fourth quarter of 2007 as compared to \$144.1 million last year which primarily reflects the closure of three stores since the beginning of the year. Retail same store sales decreased 1.2% in the fourth quarter 2007 and were down 0.8% for fiscal 2007 versus the prior year.

Now regarding EBITDA, the following is a breakdown of EBITDA by business segment for the fourth quarter.

Our Food Distribution segment EBITDA was \$26.1 million, or 4.1% of sales in the fourth quarter of 2007, an increase of 29.2% compared to \$20 million -- \$20.2 million or 3% of sales in the fourth quarter 2006. Consistent with the previous two quarters,

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the EBITDA margin in the Food Distribution segment increased significantly over the prior year. This was primarily due to more effective management of our inventories, better control of expenses, and improvement in productivity.

EBITDA in the Military segment was \$10.5 million, or 3.5% of sales in the fourth quarter of this year versus \$9.9 million, or 3.4% of sales last year. The improvement in EBITDA was primarily due to the increase in sales.

In our Retail segment, EBITDA for the fourth quarter of 2007 was \$4 million, or 3% of sales as compared to \$6.2 million, or 4.3% of sales in the fourth quarter of 2006. The Retail segment EBITDA in the quarter was adversely impacted by a \$2.6 million adjustment related to retail promotional markdowns. Excluding this markdown adjustment, the Retail segment EBITDA would have increased 6.5% relative to last year to \$6.6 million, or 4.9% of sales in this year's fourth quarter as compared to \$6.2 million, or 4.3% of sales during the prior year quarter. This markdown adjustment will not have an impact on future periods.

In summary, total Company EBITDA increased by 26.4% to \$30.2 million in the fourth quarter of 2007 versus \$23.9 million in the same period a year ago. Similarly, total Company EBITDA increased by 25.4% to \$128.8 million for the full year 2007 versus \$102.7 million in fiscal 2006.

As mentioned in our third quarter call, our effective income tax rate for fiscal 2007 was 32.6%. The Company benefited during fiscal 2007 as a result of the closure of an IRS examination covering fiscal years 2004 and 2005. Additionally, the 2003 statute of limitations for most tax jurisdictions expired. These events allowed the Company to file various reports to settle potential liabilities accordingly -- and accordingly, the Company released certain income tax contingency reserves which benefited those tax provision for the full year by approximately \$4.9 million, or \$0.36 per diluted share. We expect the effective income tax rate to return to historical levels in fiscal 2008 at about 40%.

Now, turning to the balance sheet. During the fourth quarter 2007, we repurchased 413,000 shares of common stock for \$15 million. You'll recall that we announced in November that our Board of Directors authorized a share repurchase program for the Company to purchase up to 1 million shares of the Company's common stock up through the end of fiscal 2008.

During fiscal 2007, you'll see that we continued to de-lever the balance sheet by repaying \$35 million of revolving and long-term debt on our senior credit facility. At the end of the quarter, we had a total of \$125 million drawn against our senior credit facilities and availability under our revolving credit facility at the end of the year was \$102.6 million.

Our leverage ratio of total debt to EBITDA improved to 2.42 at the end of fiscal 2007 and this was improved significantly from 3.42 at the beginning of the year and the Company was in compliance with all financial covenants at year end.

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 March 21, 2008 and this will be our 326th consecutive quarterly dividend paid.

Finally, let me comment regarding our progress towards our 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. Just as important, we've also targeted to achieve free cash flow returns on net assets of 10%, a 2% sales growth rate and to de-lever our balance sheet to a debt to EBITDA ratio of between 2.5 and to 3 times.

In fiscal 2007, we realized significant improvements on several of these metrics. Our EBITDA margin improved to 2.8% of sales in 2007, up from 2.2% during 2006, our rolling four quarter free cash flow to net asset ratio improved to 9.2% versus 8.7% during 2006 and our leverage ratio of total debt to EBITDA improved greatly to 2. -- or 2 times in 2007 down a full turn from 3.42 times in 2006. We expect to make improvements on the organic revenue growth metric as we implement initiatives associated with our strategic plan in 2008, in addition to making further progress on other metrics in 2008 and beyond. As we progress towards delivering on these long-term targets, we believe this should translate into driving significant shareholder value.

I'll now turn the time back to Alec.

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Alec Covington - *Nash Finch Co. - CEO*

Thank you, Bob and again, good morning and I was thinking earlier this morning that for four times this year in 2007, I've been glad to come to this call and haven't dreaded it and I actually look forward to it and yet this is once again that I look forward to speaking to you about our quarter and I certainly want to see that continue into 2008.

One of the things that I've said repeatedly during 2007 is that our results were as we'd expected. Quite frankly, we don't have a lot of excitement because we're -- the business is performing exactly as we had indicated that it would and exactly as we had thought it would.

Our EBITDA improved in the quarter by 26%, very significant. For the full year, we improved 25%. Quite a remarkable improvement from where we were a year ago. As Bob mentioned, our EBITDA rate, we have a goal to get to 4%. We've moved the needle from 2.2% to 2.8%. That's a 27% improvement in EBITDA rate during the last 12 months so we feel very good about the progress of the business. We feel very good about the momentum of the business and we feel very positive about the way our team is performing.

I'm particularly pleased with our Food Distribution group and the fact that our sales turned positive by 1.29%, setting aside the impact of the Martin's loss. The fact that our Food Distribution business was so strong and actually helped us to turn the overall Company positive. If you use the same measurements setting aside Martin's we were just under a 1% improvement in overall top line growth for the total Company.

Our Retail comps were better than we'd expected. We came in at minus 1.2 versus the negative 1.6 that we'd had in the third quarter and we had thought that we would probably go as high as 3% in the fourth quarter primarily because we were cycling through some stores that we closed a year ago where we had in some towns two stores that we consolidated into one store. We knew that we would not enjoy that benefit again as we cycled through the calendar.

But we saw that as a result of some promotional activities really more slanted toward perishables in our conventional stores that group has done a good job in helping to improve the results over what we thought that they would be. And secondly, our Avanza units -- our alternative formats really showed some considerable strength in the fourth quarter. So with those things in mind we actually overachieved what we thought was possible in the fourth and actually improved over what we thought we could achieve in the third -- what we did achieve in the third quarter.

Now, I want to talk a little bit about this one-time charge. We did take a one-time charge of \$2.6 million. I want to explain that in some level of detail because I want to make sure that we're not comparing it to things that perhaps we shouldn't compare it to. This is a change of estimate. If you look at the things that we took in charges during 2006, those were things that were related to pain. Those were goodwill write-downs. They were asset impairments. They were inventory impairments due to closing stores a year ago.

This particular charge is none of that. It has no relationship to the way that our retail business or any of our business is running. It is not an indication that we needed to impair anything or that we needed to mark anything down. It is solely and simply a change in estimate. Now let me explain what I mean by that.

This has to do with the estimate that we use in calculating our promotional ad markdowns in our stores on a weekly basis. Historically, Nash Finch has used more of a capitalized method to calculate those markdowns. In other words, if we had a promotion in a given week and that promotion cost \$80,000 then that \$80,000 cost became part of the inventory costs. And what that meant was is that until we had completely turned the inventory in our stores we would never fully reflect the cost of that promotion in our financials. Therefore, it was possible and I saw evidence of the fact that in some cases we would run a promotion in one period and it might still show up financially in yet the following period because it took that long to cycle through the inventories.

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Now that is one way of doing the estimate. There was nothing wrong with the way Nash Finch has done that estimate. It's just something that I personally don't agree with and it's something that I wanted to change so that we could better run our business and hold our retail team more accountable for those promotions and match the actual costs up with the exact period in which it was run.

So the change that we're going to now or that we have already gone to is one whereby when we run a promotion we take the expense against that week and within that accounting period so that everything matches so it becomes more of a sales related charge instead of an inventory charge. So that is the difference. I think it was the right thing to do. I think it is the right thing to do. It is a one-time non-recurring charge. Again, it has nothing to do with any impairment of our inventories or anything else. It's solely a change in estimate. A one-time charge and something that's non-recurring that we did and I felt was beneficial to allow our retail team to better run their business and match their promotional decisions against the financial performance within the period in which the promotion occurred. It's as simple as that.

Now as Bob mentioned, we purchased 413,000 shares of Nash Finch stock at an average price of \$36.27, so we began to act on the Board's decision to enact a share repurchase program as soon as it was practical. We saw good opportunities to create shareholder value in that. As I mentioned at the end of the third quarter, we use a very simple discount and cash flow method to determine when and how we believe we should be buying stock and obviously we believe that using our methodology that that was a good decision and a great way to create shareholder value and create a good return for our shareholders and I think that's indeed what we've done.

We've also reduced debt by \$35 million for the year. It did go up a little bit in the fourth quarter as we began to spend some maintenance capital and invest a little bit more heavy into inventory as well as buy back stock but only by about \$6 million. The other point I would make regarding free cash flow, we had indicated at the end of the third quarter -- at the end of the third quarter we were setting at a 10.9% return on free cash flow to net assets. That was actually an overachievement of our goal of 10%. We had indicated that we thought we could hold that range by the end of the fourth quarter. That did not happen. It slipped to 9.2% and that only happened because of the calendar and timing.

Something that we just didn't see when we were doing our analysis and that is regarding our Military business. In our Military business, there are very specific calendar dates in which we receive payment for shipments and it just so happens that the way the year cut off we were just short of being able to take and get additional payments for the receivable. So if you look at our accounts receivable on our balance sheet you see that it's up about \$11 million from prior year and that's nothing more than a timing issue in the way that we get paid for our Military shipments. And as a result of that, that brought our free cash flow metric down to 9.2, still a great number. We see nobody in our average peer group that even comes close to accomplishing that. Still better than we ended a year ago, but a little bit short of our 10% goal only because of the calendar. Nothing to do with anything else.

Now usually when we have these calls we usually see that several reports come out into the marketplace after the call when we've had time to answer questions and explain our business. Today was a little bit different because we did see some reports come out and talk a little bit about and analyze our numbers before we have the opportunity to discuss it and answer questions and that's fine. I have no problem with that but I do want to talk a little bit on a couple of things that I did read this morning.

One had to do with the fact that if we took the tax benefit of roughly \$0.10 a share for the fourth quarter if we deducted that from the achievement that we had for the quarter then we would have indeed missed the Street expectations. But there's a couple of thoughts that I would have on that point and just to be clear and fully transparent. In the third quarter, we explained that we had a tax benefit so I don't think that was any new news to anybody who was making estimates. We have a brilliant tax department. Paul Bischel and his team is just doing an excellent job in managing our tax exposure. I think they'll continue to do a great job and any chance we get to avoid having to have our shareholders unduly pay income tax that's exactly what we're going to do and that benefits not only free cash flow, but it benefits EPS even though we don't talk a lot about EPS because our metric is set on EBITDA.

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Even if that were the case, if we wanted to try to rationalize that tax benefit of a dime, well then I think we have to look at the other items that were detrimental to EPS during the quarter and one that I would bring up is a LIFO charge which was almost double what it was a year ago. It was actually up \$2.5 million from the prior year. That actually impacted not cash -- had no impact on EBITDA because LIFO is a non-cash item. LIFO is our friend. LIFO is a mechanism that allows us to avoid paying undue tax on inflation that we have in our inventory and any time that I get an opportunity to invest in inventories in such a way that we can generate either a better deal for our customers or an extended deal for our customers or gross profit for ourselves, I'm going to do it. It's the right way to run our business from a cash perspective.

But when I do that, it creates more inflation in our inventories and creates a higher LIFO charge and so be it. LIFO is a non-cash item. It's there to help us avoid paying undue income tax and when you take that impact that actually had a bigger detriment to EPS at \$0.11 than the tax gain at \$0.10 so we really can't just take one single item and try to rationalize and say that we made it or we missed it. We either need to accept the numbers as they are or not and when we look at EPS and when we look at EBITDA or when we look at any other kind of measurement, I can't find any measurement that says that we didn't have anything but an excellent quarter and met every single objective that we had indicated to the market and I truly believe when the analysis is done that we certainly not only met our Street expectations, I think we're slightly ahead of Street expectations for the quarter and also for the year.

And again, I'm happy to discuss and analyze that in anyway possible with any parties that would like to discuss it because we want to make sure that everybody understands our numbers. Sometimes there are complications and we're not exactly an easy company sometimes to understand. That's why we want to have these calls and we're always available to help discuss and reconcile any item that's not clear to anyone that looks at our numbers or looks at our press release. As I see it, we made continual -- continued visible signs of improvement in all business units and I just couldn't be more pleased with the quarter and with the year.

Specifically in Food Distribution, I'm particularly pleased with our growth momentum. We've been working hard on that. The team has been focused on it. We've all been focused on it and it's now happening and we're very pleased.

EBITDA margins. EBITDA showed significant improvement. They generated a 29.2% improvement in the quarter and that's all coming from improved inventory management, improved vendor management. We're showing increased product promotions to our customers still. We're still seeing increased product promotion levels to our customers. In addition to that, a lot of our improvement came from expense reduction initiatives which are gaining traction. So I think this management team under the direction of Christopher Brown and his team is just doing a fantastic job. They're clearly focused on the right things.

I will say that inflation is aiding some of the EBITDA improvement in Food Distribution. We are a distributor. We do make investments in inventory from time to time and during heavy inflationary times our investment inventory tends to go up and that's exactly what we're seeing. So some of that EBITDA improvement is being aided by inflation but a lot of it is being aided by just improvement in inventory management and also a good solid expense reduction in growth that's coming to the top line.

Now during the third quarter call, Bob and I were actually in New York and the question came up regarding any customer contracts or if we had any substantial customer contracts that would expire in 2008. Bob and I didn't have our information with us. We actually hadn't even reviewed that because it was earlier in the year than when we do that. The fact of the matter is is that every year in the wholesale business and in this Company you have contracts that expire. That's just the nature of our business and that's been that way and will continue that way out into the future.

We only have one that has any substantive EBITDA associated with it at all and the answer to that is we do have contracts that expire. We only have one that has any level of substance EBITDA associated with it at all and we're well down the path of resolving and renegotiating that we speak. Anything can happen in these things with business. I've said that before. You can never predict what's going to happen with the customer relationships, with a contract or without a contract but you can see that in our numbers we are gaining momentum so that must be indicative of something that's going the right way.

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Now looking at the first quarter in Food Distribution, we anticipate slightly positive growth setting aside the impact on Martin's which will be \$36.2 million in impact in sales from prior year in the first quarter of 2008. So setting aside the 36.2, we expect that -- continue to see some slight growth. Now we had a really good fourth quarter and I think that was driven by some strong promotional activity that we had in the Food Distribution group so I don't know that we're going to be quite as strong in the first quarter as we were in the fourth quarter but the point is it will continue to be positive in the first quarter.

I will say that we expect by design to have higher than normal inventories in the first quarter. By the time we end the first quarter I do not expect that we will have inventory levels at the same level that they were a year ago. I expect them to be higher. That's not by accident. That's by design. That is again because of the inflationary times we're living in.

We're seeing price increases or have seen price increases that -- and I'm not an economist and I'm not a statistician but I can tell you from my experience I haven't seen this level of price increases since the 1970s. I'm from the south and down there we say you've got to make hay when the sun shines and that's exactly what I've instructed the inventory management team to do when we have the opportunities to make the proper buys to protect the price for our customers and our corporate retail stores and also to enhance our gross margin that's exactly what we should do. Therefore, I expect our inventory levels will be high at the end of the first quarter.

The result of that will be that I believe our free cash flow to net asset measurement will drop in the first quarter. I would expect that it could drop as low as 4.5 to 5%. Again, that will only be a one quarter snapshot. We take a longer view on free cash flow and I expect that by the time we end the year we will have resolved that issue but for right now from a cash perspective, from an EBITDA perspective it's the right way to run this business and I'm not going to let one metric dictate how we -- keep us from making good decisions for our shareholders.

Top line growth remains our top priority and we'll continue to focus on that and we'll continue to focus on Food Distribution on making sure we have the proper emphasis on operating cost reduction. The team has really gained some traction with that. I think there's more that can be done and we'll continue to work on that into the first quarter of 2008.

On the corporate retail side for a second. Comparable store sales as I mentioned improved from a negative 1.6 in the third quarter to a negative 1.2 in the fourth quarter. EBITDA was down from prior year only due to this change of estimate. EBITDA rate would have improved to 4.91 from 4.3 a year ago had we simply not made that change of estimates. That was again nothing that they did. They actually had nothing to do with it. It was a decision that I made and Bob concurred with would be a better way and a more proper way to manage our business and make it easier again to match our promotions with the timing in which they were actually run.

We also had a lot of transition costs that we had to overcome. We obviously have some store activity that is underway as we mentioned and told you at the end of the third quarter we would begin immediately to remodel some stores. We had a lot of transition costs incurred due to a remodel that we had going on in Omaha and those costs are actually in our numbers in the fourth quarter. We talked about that during the last call but the amazing thing about that store is that the more that we tore it up during the quarter the stronger the sales got and it got up to where we -- at one point we had the store completely torn apart and the sales were up 16%.

Now our labor costs was high because we had the place all messed up and we were resetting and tearing it up and moving stuff from one to the other. But the point is is that it appears that Avanza is going to be very well received in the Omaha, Nebraska market. Otherwise, people wouldn't be tolerating the conditions they've had to shop in during Christmas and during the holidays and still award us with such a bold increase in sales. So that also helps of course to drive our top line.

We also, as we mentioned, we had to add people to help with these store rollouts so we have a little bit more overhead. That's again part of what we talked about that would be embedded in our numbers in 2008 because we have to have people to get these things done. And we also reached an agreement with Albertson's during the quarter to acquire a store in Rapid City and

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Scottsbluff, Nebraska. These two stores just happen to fit in the market in which we already have strong market share and Rapid City, South Dakota, Nash Finch under our Family Thrift banner has always been a strong player in the marketplace.

Upon the completion of this acquisition which we expect to close sometime in the first quarter or at the very latest the very first of the second quarter we will assume number one market share above WalMart in the South Dakota market in Rapid City so that is a good move for us. It's a nice little tuck-in acquisition. It's not big. It's only two stores. Again, we're not in the market to go out and buy retail chains but when we have the opportunity to make a very strong accretive tuck-in acquisition that fits with our current business, as we talked about before, of course, we'll be willing to look at that and do that as long as it makes good financial sense. With that, we're getting some fantastic people. A couple of dynamic store managers and so we're pleased to have that coming our way in the not too distant future.

Again, this management team is making very good decisions during the first quarter. They're going to continue to focus on their aggressive perishable marketing promotions that they're running in our conventional stores that seems to be working evidenced by the improvement that we're seeing in comp store sales.

When we look at the first quarter, I will tell you that our top line sales, our comparable store sales will go positive in the first quarter. I couldn't tell you exactly how much but I wouldn't doubt that they wouldn't be as much as half percent positive from the negative 1.2 that they are today but I want to warn you that has nothing to do with the market. That has nothing to do with the stores. It is only because that Easter is coming a little bit earlier this year so we'll have the benefit of Easter in the first quarter and then we'll have the negative impact of not having Easter in the second quarter.

Now if you take out the impact of Easter we expect that in the first quarter our true comparables will be about negative 1 so we do think we'll see a slight improvement over the fourth quarter at negative 1.2. We think it will be negative 1, but in terms of the way that you'll see it, it will be positive but only because of Easter. So when you see that remember what I told you about the comps and the calendar. That also means that we will exaggerate the negative comparable sales in the second quarter so that's just the way life works with Easter. One of the holidays that kind of moves around on us between quarters and just so happens it's in the first quarter this year.

In our Military business, sales increased 3.7% over prior year due to new customer additions. EBITDA improved 6.1% for the quarter and 6.7% for the year as compared to 2006. Again, this team is showing good progress with expense control initiatives. Management under the leadership of Ed Bruno is just doing a fantastic job with a great team. In the first quarter, they'll continue to push for organic growth. That's what they've done extremely well in the past and they have begun to make real progress on reducing operating costs as is evidenced in our numbers for the year so we expect that will continue into 2008.

Now we have a few other matters that I want to touch on. I would -- there is an 8-K filing I think that is already out that has to do with my change of control agreement. There is nothing that has changed about my relationship with the Company. If you'll remember back in March, we filed an 8-K indicating among other things that I had asked the Board to enter into a new change of control agreement that would have substantially reduced benefits because I felt like that was the right thing to do and the Board agreed.

What happened was as simple as this. The form that was attached to that particular 8-K filing was just simply the wrong form and so we needed to get that cleaned up and so we filed a new 8-K with the proper change of control form attached to it so that we got that corrected. I guess, Kathy, we filed that yesterday. So that whole thing is nothing more than that but I wanted to bring it up.

Secondly, we have decided as a Board -- our Board has focused on good governance and making sure that we are shareholder friendly as an organization and as a company. As you will recall at the end of the third quarter we announced that the Board had unanimously made the decision to declassify the Board so that all of us would stand for election each year. This particular quarter we made a decision as a Board that we would reduce the size of the Board so that we could make sure that we were

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efficient and that we have a streamlined process and that our Board organizational structure is as cost efficient to our shareholders as it can possibly be.

Therefore, we will along with proposing to the shareholders that we declassify the Board, and all of this of course has to be approved by our shareholders at the Annual Meeting, but in addition to proposing to declassify the Board, we will propose a reduction of the Board size. The Board size had previously been a range of 9 to 17 members. The new proposal to the shareholders will be a range of 7 to 12 members. At the current time, we believe that we can manage the responsibilities of the Board with 7 of the 9 that we have -- 7 of the 11 that we have today so the slate will be made up of a subset of our current directors and so that is what that's all about. The 7 to 12 range is more I think appropriate and more consistent with where we see trends today.

The Board feels and believes it is a more cost efficient way to run and govern and get our business done. However, it also allows us flexibility that if our Company became much larger or more complex we have the ability to increase that size if we're missing some sort of skill set that's needed sometime in the future. So today with the Company no bigger than it is we're not a very large company we believe as a Board and the Board believes that they can get their job done with 7 and that will create savings to our shareholders and provide a more streamline process as I believe is both shareholder friendly and representative of the Board's desire to be transparent and provide good governance to our shareholders.

Now, moving on to our strategic plan. We talked about a lot of initiatives that we were working on in 2008 and we would continue to work on at the end of 2007, but I want to touch on a few of those.

In corporate retail as I had mentioned before we had one conversion that we want to make and are making from a -- one of our conventional stores over to Avanza. The first of those will be completed on March 5th and that's the one that I was mentioning earlier in Omaha and again so far so good in terms of the way we've been received there. The second is Greely, Colorado. That one will be done by the end of July and then our first major everyday value conversion, that's our larger format will be completed by the end of June in one of our Wisconsin stores.

Regarding our initiatives in Food Distribution. Our category management systems that we talked about at the end of the third quarter have largely now been selected and some already put in place. We've completed the first seven category reviews. We've been able to reduce the costs substantially to our customers and in turn we've been able to reduce retails in those seven categories so that we're now more in line with big large box retailers. We're seeing in those categories that our unit sales are up and our sales in those categories is off a little bit because -- simply because of the discounts that we put into place into the products and the way that we've been able to work with the vendor community. But we're very encouraged and our retailers are ecstatic in that particular test division by what they're seeing so far. We should have this largely completed in the test site by year end. Maybe a little bit into early '09 and we'll begin to roll that out to the rest of our food divisions thereafter.

In Military. This organization is launching a new identity and marketing program. They've done some beautiful work to reinvigorate the logo and the marketing aspect of the business. They continue to focus on their perfect order index to take waste out of the operation. We're going to soon have our first in-house black belt in place to drive the Sigma process. They've already begun the process mapping for procurement and receiving and they're already discovering ways in which they can improve their operation and service to our customers. And we've began the process, as I mentioned at the end of the third quarter, of recruiting additional bench strength in preparation for growth because it's always been our intention to grow the military business and if we're going to grow it both organically and acquisitively we've got to be sure that we have the right bench strength and the succession plan that will allow us to do that and that of course is underway right now.

In summary, we saw continued improvement visible in all of our business segments, not only in the fourth quarter but throughout the year. Our Operation Fresh Start initiatives continue to move carefully forward. We remain dedicated to our being the premiere partner to independent retailers and regional chains throughout this country and I think that's becoming more visible and more know every single day. We remain committed to our long-term goals of 2% organic growth. We're not there but we've made a lot of progress. 4% EBITDA to revenue, we're not there but we're 27% further there than we were a year ago. 10% return on free cash flow. We've been able to achieve that and an EBITDA leverage of 3 or less which clearly we are at.

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Our key focus areas is growth in our distribution business, continued improvement in our expense control, solid execution of our strategic initiatives and focus on providing targeted returns on our investments as we invest in both our share repurchase program, our internal investments that we're making in our business and acquisitions such as the one that we made and the small deal that we did or are doing with Albertson's.

Now keep in mind the following things and I said this at the end of the third quarter and I just want to remind again. 2008 does have 53 weeks so that -- we need to make sure that that's modeled properly. We expect to see sales to be negative during the first half and flat for the year. That's exactly what we said at the end of the third quarter and I'm more confident today. Obviously, with the recent results we're seeing in Food Distribution that we'll achieve that then at the end of the third quarter.

We anticipate only slight improvements in EBITDA rates and I want to emphasize slight improvement like a hair improvement in the EBITDA rate going into 2008 and I mentioned before at the end of the third quarter the reasons for that slight improvement is that we've got a tremendous amount of transition costs associated with these strategic investments. We have to overcome that and we will. We have a lot of startup costs associated with these new stores. We have to overcome that in our numbers and we will and in spite of that we'll still produce a slight improvement in EBITDA rate for all of 2008 and keep in mind that the 53rd week would be incremental to everything that I've discussed, of course.

Regarding our free cash flow measurement. As I mentioned at the end of the third quarter, we will negatively impact the free cash flow and net asset measurement by the strategic investment that we're making but we're going to provide visibility each quarter of how much capital that we spent on strategic projects so that we can continue to show you the job is being done in true free cash flow to net asset base. So we'll continue to provide that and provide full visibility of that. Of course, we have also the impact that I mentioned in the first quarter because we will be negatively impacted by design because we are going to have heavier inventories by the end of the third quarter than we might have anticipated before we realized the high inflationary period that we're in right now.

Again, we are pleased with the quarter and the year. I certainly congratulate our team on a wonderful year. I thank our customers and vendors for their support in helping us to do this and most importantly for this call thank our shareholders for their continued confidence in our ability to do the job, to keep our word and deliver the results

And, James, with that, if you could help me, I'd be happy to take questions and comments from the overall group.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS).

And we'll take our first question from Mark Churchill from Piper Jaffray.

Mark Churchill - Piper Jaffray - Analyst

Hey, guys.

Alec Covington - Nash Finch Co. - CEO

Hey, Mark.

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Mark Churchill - Piper Jaffray - Analyst

Can you give us some more detail on some of the investments you're making with Operation Fresh Start and when do you think you'll actually start seeing the returns on those?

Alec Covington - Nash Finch Co. - CEO

Yes. We mentioned at the end of third quarter that we're primarily investing in three areas. One is our distribution and logistics by putting in more of an upstream, downstream distribution approach starting in the East and ultimately taking that to the West. The second is investing in systems that we really needed to drive our whole center store project to really drive world class category management. Third, some investments in some of our formats in order to move that needle forward by expanding our Avanza format and then remodeling some of our conventional stores into what we refer to as our everyday value format. Mark, that's a larger 45,000, 50,000 square foot store which is greatly exaggerated in its perishable offerings and to be honest we shrink a little the grocery offerings but it also has a much stronger price impression than the core of the store.

Now we've indicated that in 2008, among those three categories we would invest roughly \$25 million and that in addition to that we would need about our typical \$25 million for maintenance CapEx. So we have committed that between the two we would not spend more than \$50 million in total toward our strategic investments unless for some reason we saw some early signs that we were wildly successful and that we needed to accelerate that for some reason. So we're being very cautious. We're being very thoughtful. In all of those investments, Mark, we demand a 15% IRR and we're very diligent and thoughtful about that so we choose our projects wisely. But that I hope gives you a bit of flavor of how we're approaching the investments.

Mark Churchill - Piper Jaffray - Analyst

Yes, that's helpful. And then on the retail side, outside of the -- are you seeing actually first anything else on the acquisition landscape outside of the Albertson's that you acquired?

Alec Covington - Nash Finch Co. - CEO

We don't have anything today that is anything of substance to discuss. I would tell you that again at the end of the third quarter we said that was one of the things that we hoped would be something we could accomplish more in 2008 than we did in 2007. I think the credit markets and the market probably works in our favor that we might be able to get some things done this year that might have been a little bit more difficult to have gotten done a year ago. I think for those that have a strong balance sheet and access to capital those companies such as Nash Finch is in the best position to be and acquire for those that might want to divest their companies and leave their business.

I would tell you though that the types of acquisitions that we would consider and that we would be looking for as I've said before, I'm not looking for a homerun. I just want to look for a few base hits and when we can find a strong perishable company or a specialty food company or a meat business that would complement our existing business within our current geography where there's a lot of synergies, those are the kinds of deals that we would be most interested in.

We don't have anything to talk about today and also I might mention that to the extent that we could determine a proper acquisition in our military business. We've always been open to considering that but those are the kinds of things that we're looking for. Something that we can manage properly, manage the risk, integrate properly and where we don't bet the ranch on one single deal. So that is about the best I can tell you Mark regarding that.

Mark Churchill - Piper Jaffray - Analyst

Okay. And then do you have any plans yet for retail openings or closing this year?

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Alec Covington - *Nash Finch Co. - CEO*

We don't. I mean we obviously have these two Albertson's stores that will be incremental to the store base that we have. We review that not even just by quarter but we review it by period to see if there's anything that makes sense in terms of stores that where we've got a lease that's expiring or store that's underperforming. The only -- we do have a store where we've got a lease expiring and to be honest the profitability in that store just isn't worth renewing the lease so we expect that in the second quarter we may close one store but it's a small store and we haven't advised all the parties involved yet of our intentions to do this so I don't want to be more specific than that but it will be of no consequence to the overall retail division.

Mark Churchill - *Piper Jaffray - Analyst*

Okay. Thank you very much.

Alec Covington - *Nash Finch Co. - CEO*

Thanks, Mark.

Operator

(OPERATOR INSTRUCTIONS). We'll move on to our next question from Karen Howland from Lehman Brothers.

Karen Howland - *Lehman Brothers - Analyst*

Good morning. I was actually a little surprised to hear that you are acquiring two retail stores. Going forward, do you expect to focus to be more on the distribution side?

Alec Covington - *Nash Finch Co. - CEO*

Well Karen, I mean as we said at the end of the third quarter we're interested in anything that is a tuck-in acquisition that fits nicely and makes sense with our business regardless of what that is. We've indicated though that our emphasis we're making larger acquisitions. They're going to be more slanted toward distribution than other parts of our business. However, when you're offered an opportunity to acquire market share within a market that you're already strong that just makes all the sense in the world to do so we don't rule out making acquisitions if it makes sense on the retail side.

You may see us actually acquire some stores that we may intend to divest to a customer later if we can help grow our food distribution business, so we'll look at all sorts of opportunities but what you shouldn't expect to see is that we would go out as I mentioned earlier and acquire some retail chain. That's just not our focus. We have those opportunities come available but we decline them because it just doesn't fit with the strategy in which we have today. But for us to allow really good assets to be acquired by a competitor in a market in which we're in would not be doing the right thing for our shareholders when we can saturate and increase our market share in the given market in which we're already in.

Karen Howland - *Lehman Brothers - Analyst*

In looking at acquisitions in the future, would you be willing to go beyond that 3 times -- 3 times to EBITDA if an attractive acquisition was out there or is that kind of where you see it capping out at?

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Alec Covington - *Nash Finch Co. - CEO*

Well, I mean, again, we use the 3 as a pretty strong indication of our intentions. I would never say that we wouldn't go more than that but I would tell you that as we take the leverage up the returns have also got to go up and the risk has got to be managed. So from my perspective, as we began to think about higher leverage then we also have to think about how do we manage low risk and how do we generate higher returns because you when risk effect a large deal it really demands that you have stronger returns than something that you can take in on a tuck-in acquisition that has build-in synergies and is easy to do.

So I don't know that I see us doing that, Karen, but clearly, if it were something that creates shareholder value and something that was manageable and something that made sense and the only thing standing in our way was the fact that we needed to go beyond the 3 range to get it done then I don't think I would sweat that a lot.

The other thing I would say is if we do acquisitions right, I don't know that I always see that there should be a substantial jump in leverage if you're buying cash flow because the cash flow management is part of what helps keep that ratio in line. So by definition, if you're acquiring something and your leverage ratio is jumping dramatically it can only mean that you paid a lot for it or that there weren't enough -- the synergies just going to take quite a while to come. And I don't really see us doing a deal where we've got to wait a long time to get the synergies to justify the returns and get our leverage ratio back down where it needs to be.

Karen Howland - *Lehman Brothers - Analyst*

That's great. Thanks for that additional color. When you talk about the acquisition environment out there, I know you said there's nothing to announce right now but I've always kind of viewed that to get that 4% EBITDA margin you'll likely have to make an acquisition in the distribution space. Are there more conversations going on or is it still very similar to how it was last year that people are looking at from the other distribution companies that are bought whether it be the performance food groups or U.S. Food Services and just looking for too much money at this point?

Alec Covington - *Nash Finch Co. - CEO*

I would say that -- I don't know that there's been a 180-degree turn. What I would say from conversations is that I think that there's a much more of a realization of the difficulty in the credit markets these days. And that if you're -- you've got a lot of people that have recently made large deals so they're sitting on the sidelines and you've got others, private equity that is not able to perhaps be as active as they have been in the past. So what I'm seeing is that if you're a Nash Finch and you've got a strong balance sheet and strong access to capital and a solid performing business you're probably a pretty rarity right now and you're probably a good dance partner.

So we're seeing -- I'm not having as many people -- last year all I heard about was the U.S. Food Service deal. I couldn't get past hello without hearing about the U.S. Food Service deal and I'm not having that happen. I think business people by in large are pretty astute and they see the markets and they see what's going on out there and they realize that if they need an exit strategy or they desire an exit strategy there's not as many people out there today as there perhaps was a year ago and that's causing discussions to be a bit more reasonable. Having said that, I want to emphasize that we don't have anything that is underway or imminent or anything that we're even close to pursuing but we continue as we've mentioned in the past to discuss opportunities with a variety of parties that we think would make sense for both of us.

Karen Howland - *Lehman Brothers - Analyst*

And looking back at the strategic initiatives that you have for this upcoming year. I know you said it was about \$25 million of capitalized costs associated with that. What do you expect the startup costs -- the expense startup costs to be and the transition costs?

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Alec Covington - *Nash Finch Co. - CEO*

I don't have that broken out and some of that it's so embedded into some of our operating numbers it's not as easy to separate as you might think because you have people that are running a distribution center doing their day job and then they're also managing part of the planning for the upstream downstream. So at the end of the period, we see it -- we see a little bit more pressure in certain areas but we've provided for those from a budgeted perspective in the way that we built our numbers.

The way we've built our plans for 2008 and I'll continue to emphasize that our commitment to the marketplace was to eke out a very small fractional hairline improvement in EBITDA rate while at the same time fully absorbing all of these strategic costs and our transition costs and we manage that as we go. I mean in some cases we don't always know what the costs is going to be but that's just management. Sometimes you have to manage one part of your business to offset something else and to make it all pull out the right way. We just fully understand that we've got to absorb those costs and we can't go backwards while we're doing this. We have to continue to go forward even if it's in teeny-tiny steps.

Karen Howland - *Lehman Brothers - Analyst*

And do you expect most of the costs to be spread evenly throughout the course of the year or do you think some of the -- most of these initiatives will be more in the second half of the year?

Alec Covington - *Nash Finch Co. - CEO*

Well, they're going to build throughout the year as we layer on additional projects. However, there's a little bit offsetting effect because there's others such as the Avanza in Omaha. I mean we felt some of that in the fourth quarter. We're going to feel some more of it in the first quarter. Well, that ought to begin to wane by say the third quarter but then we're going to have others that are layering on.

So because of the fact, Karen, that we're layering things on starting projects in the first and the second and third, we're going to see that those costs are going to build throughout the year but again, I still remain steadfast with the fact that I believe that by the time we end the year we will have inked out a slight improvement and we'll still have fully absorbed those costs even though your point is very valid, they will build throughout the year.

Karen Howland - *Lehman Brothers - Analyst*

Okay. And then just one question about the retail business. I know you'd indicated that year-over-year excluding that \$2.6 million charge it would have improved and I could have a flaw in my model but I was under the impression that last year also had a one-time benefit that hit the -- it was like a \$1.1 million of costs so that if you exclude both from both years it actually would be down. Am I -- is that -- inventory markdown?

Alec Covington - *Nash Finch Co. - CEO*

The map as you describe it, Karen, is absolutely right but from an operating perspective the flavor behind that I don't think is so correct because when you look at what we did a year ago, we took a \$1.1 million cash charge because we were closing stores because something was wrong. The business wasn't performing. We were hurting. We had to get out of some operations. To me, that's a whole different proposition from when you take a \$2.6 million charge simply because you chose to change an estimate in your promotional markdowns. There was no pressure to do that. Nothing was wrong. Nothing's broken.

So I think that the issue that we have is that -- we've put it on the same line and that I think causes people to want to compare those two. In reality, I don't really see them as comparable items because I was under no pressure to make the change in estimate

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that impacted the 2.6, but I can assure you that a year ago I was clearly under pressure to do something to stop the bleeding in some of these stores that were underperforming. I just see them as entirely two different things and not apples and apples.

But the math as you describe it is 100% right. There's nothing wrong with the map. My point is is that if I had closed stores last year and I close stores this year those are comparable apples and apples. I haven't closed any stores. Nothing is wrong with my business. I just simply chose to change an estimate in promotional markdowns in order to more effectively manage my business and I think that's hard to compare that a year ago when we were closing stores because we had real problems out there.

Karen Howland - *Lehman Brothers - Analyst*

Oh no, I absolutely I understand that. It's more if I add back both of the charges to make it look on a ongoing basis of what the business excluding these charges should be I have my EBITDA margin actually down a little bit year-over-year.

Alec Covington - *Nash Finch Co. - CEO*

And if that's the way you choose to do the math that's correct. It's just not the way that we would do the math. It's not the way I see the business because there's nothing that has deteriorated in the performance of those stores that's associated with the 2.6 charge. A year ago that was not the case so I just -- I agree that the math is solid. I just don't agree with the method.

Karen Howland - *Lehman Brothers - Analyst*

So you -- I apologize. I'll give a call offline so I can get a better understanding. Thanks.

Alec Covington - *Nash Finch Co. - CEO*

Okay. I explained it as best I know but we'll be happy to go through with you in deeper detail.

Karen Howland - *Lehman Brothers - Analyst*

Great, thanks.

Alec Covington - *Nash Finch Co. - CEO*

Thanks.

Operator

(OPERATOR INSTRUCTIONS). We'll move on to our next question from [Regina Russell] with J.P. Morgan.

Regina Russell - *JP Morgan - Analyst*

Yes. This is Regina Russell on for Steve Chick today. Two quick questions. The first question is related to include inflation and I was just wondering are you able pass those cost increases along to your customers? Specifically wondering about the military division.

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Alec Covington - *Nash Finch Co. - CEO*

Okay. In answering that question the answer is yes. We don't-- specifically to the military business the vendor is in direct control of the costs that the military pays. We really don't have any influence on that whatsoever so for us it's a matter of working off of what we refer to as [grades] so from the military perspective there's no exposure to us on inflation.

Regarding our Food Distribution business, predominately that is also the case. We pass on costs because we are a distributor. We're not holding back on those increases. Having said that, we do the best job we can as a distributor to protect our customers for as long a period as we can by buying inventory before it goes up but absent that there's no impact to us from inflation because again our costs to our customers is based on what we buy it for.

Regina Russell - *JP Morgan - Analyst*

And then second question is related to fuel. Are you able to lock in any fuel costs or have you recently locked in any fuel costs?

Alec Covington - *Nash Finch Co. - CEO*

No, I wish we could. Historically, that's been something that I've always tried to do either through a fuel hedge or fuel contract or both and we were able to do some of that in 2007. If we find an opportunity to do it in 2008 we will but with the way that the oil prices has been selling we haven't seen a logical opportunity to do that so at the end of the day we don't have any of those in place but we will if the opportunity presents itself.

Regina Russell - *JP Morgan - Analyst*

All right, thank you.

Alec Covington - *Nash Finch Co. - CEO*

Thank you.

Operator

(OPERATOR INSTRUCTIONS). Mr. Covington, there appears to be no further questions in our queue. I'll turn the conference back over to you for any additional or closing remarks, sir.

Alec Covington - *Nash Finch Co. - CEO*

All right, I appreciate it everybody participating in the call. One last comment that as we mentioned at the end of the third quarter, Bob and myself to a lesser degree has been working on a new credit facility that we expect to have in place at least by the end of the second quarter. And we expect that facility to replace our current revolver and term note and will be more the size of a \$300 million facility and again we are currently working on that. We expect to have that in place at least by the end of the second quarter.

I appreciate everybody participating in the call and we look forward to coming back and talking about our first quarter results in April. Thank you very much.

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Operator

And that does conclude today's presentation. We thank you very much for joining and have a wonderful day.

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