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# EDITED TRANSCRIPT

JCP - J C Penney Co Inc CEO Commentary on Open House Tour -  
Webcast

EVENT DATE/TIME: SEPTEMBER 19, 2012 / 6:45PM GMT



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## PRESENTATION

**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

Welcome, and thank you for coming. As I mentioned downstairs, you are in a -- you might call an art studio. It's a place where we're creating the JCPenney of the future. I really appreciate your coming. As we said, we wanted you to come because, we can talk about it all day, but until you feel a space or understand, it's really hard to understand what it's for. And we're interested in making sure, as people make their long-term economic decisions that affect their families and friends and funds, we have got to make sure they understand where we're headed. This is the fourth time, I believe, in the last eight months that I've talked to you. In January in New York, many of you were there, we laid out the vision for how we're going to reinvent JCPenney and hopefully retail. In May and August, we came to New York and updated you on our progress through the quarterly results. More short-term.

Today's purpose is longer term. So today I want to talk about where we're headed, because this is about the new JCP. All right, so we've got to look out further as to where we're going. As I said when I came, though, I didn't believe it would be good to come to JCPenney to improve the business model. The goal has always been to transform it, because for a lot of years, people here have been working really hard to compete well, and we've had great leaders. Allen Questrom was one of the best retail leaders in the department store era, and he came here and put his stamp on JCPenney. Mike Ullman came here, spent five or six years. Mike ran Macy's.

But trying to improve it over time, we did lose market share. And I believed, as you know, that eventually, the promotional model runs its course. Because the more you promote, the only way to beat a promotion is a bigger promotion, and ultimately, you don't have access to any new ideas from a merchandise perspective, other than those you can create by yourself. Because nobody's going to put their brand in a place that they'll devalue it, or take 50% or 60% off and sell it on coupons. So ultimately, stores are about merchandise, and if you want to win, you've got to reinvent the content and the service and the presentation. So when I came, we concluded, we're not here to improve, we're here to transform. And the goal is this, I even said this since January. Like I said, now you're in our house, and I can tell you what we're doing. We're going to create America's favorite store, and you guys all had a chance to see it today. To see it beginning.

Like I said, it's an art project. Every time I come here, it's a little bit better. But this is something we're going to create. And we're going to redefine the way America shops through a whole new interface for retail and a new experience. We're going to transition, as you know, from a promotional model that Penney's is, that Mervyn's was, that Kohl's is, that Macy's a little bit is, to what we call a specialty department store. I talked about what a specialty department store is in August, but now you've had a chance to experience it. I'd like to take a few minutes and walk through, intellectually, what it is, so you'll really understand what you just went through. There's three simple ideas in our store design. There are Shops, there's a Street, and there's a Square. Today stores are just filled with racks, right, that's what we've got, a lot of merchandise. The heart of this is the Shops.

The way to think about it, we're creating a new interface for retail. It's like when Steve talked about the iPhone, that iPhone, Apple created the screen. Apple created a lot of the technology that runs that phone. We all know that why we love our phone is our apps. The way to think about it is, all those boutiques are the apps. What JCPenney is creating is a new interface. All right? So the secret is the shops, right.



And in this store you saw today, you experienced 17 shops. Eventually, there will be 100. It's a lot of shops. And each of them will be pure. Meaning if you're in the Disney shop, you're going to feel like you're in the Disney store. If you're in the Joe Fresh shop, you're going to believe you're in the Joe Fresh store. Everything down to the people, how they're trained, the signing, the experience, the hangers, the hang tag are 100% the shop. If they're not, we're not being authentic, because that's what's going to make people believe. If all of a sudden this thing has a standard JCPenney hanger, standard JCPenney sign, I'm not going to know if I'm really in a Joe Fresh store or a JCPenney version of a Joe Fresh store. People want to connect with Joe Fresh. They want to connect with Disney. Everything will be 100%, as you see. We're going to have 100 shops when we're done, and you saw 17 of them.

The Street. You just walked on it. It's amazing how simple the idea is, but to me, how magical it is. Up until now, stores have merchandise. And they've got aisles. We expanded that aisle by five feet, that's all. And remember, our cost of real estate is about \$2 a foot. We don't pay a lot. We get really good deals.

And what do we do? That allows us to inhabit it with activities that let people get inspired, like a mannequin, refreshed, like a quick cup of coffee to continue shopping, or a treat, like yogurt. Or sit down at a bar and just check out the sports scores, because Peyton Manning threw his third interception, whatever it might be. But you don't have to leave the store to continue on with your life. All we did was made that five feet wider, and because we moved to new technology, where like Apple, like Nordstrom, like a lot of people, we can check out anywhere, anytime, from anyone, and we'll do that February 1 next year, and we've got our JCP bars, we can replace where the checkouts were with seating. That's how we put in the little cafe like by Caribou, you've got a place to sit. It's all coming from free space, because we embraced technology in our year of transformation. So The Street is a new idea for retail.

You just got a glimpse of The Street. In our completed store, it's a half mile long. And you started to see today, there are different activities in every Street. So in the kids area, we had our Lego table. If you'd been to the Mall of America, one of the most popular things, they've got their theme park. I have never been there, and I've been there hundreds of times, because when my kids are young, we would go out there all the time. The kids are all over those Lego tables, building Legos. We took one of those nodes that used to be a cash wrap, we've got a place for kids to create while mom shops.

We've got technology. We've got iPad tables and we've got Mac tables. At the Apple store, we put in one little table with four Macs, and I can tell you, I can't tell you how many times people come. My kids' favorite store is the Apple store because they thought about him. You put The Street together, all the kids' activities, when it's time to get shopping you know where the kids want to go? They want to go where they can, we thought about them, they get a little candy, maybe a little yogurt, mom can find what they want. That's The Street for kids. But The Street and the home area will be all different. Because your needs when you're shopping for home are very different than buying apparel. I think you're starting to pick up what goes on.

It's free. It doesn't cost a lot of money to buy a couch. But with a high speed Internet, you create a place for someone to catch up on their smartphone that they feel comfortable doing, while they're with someone can shop. So The Street, new interface for retail. When we're done, I want the customer to think of JCP as The Street. Because the brands are all the shops. Right?

And then The Square. Now, The Square we haven't mocked up yet. But I want to remind you what it is. It's going to be our dynamic seasonal space. The shops you see here will change all the time, like specialty stores do. Merchandise will come and go, it will get cleared out. When we're all done, and we have 100 stores, we expect 25 to change every year. So there will be more than this many new stores coming in every year. We're going to turn 2.5 times faster than the shopping mall does. Because we've got to keep new concepts coming, or we'll get tired.

But this is a dynamic seasonal space, and that's where you find your unique seasonal items, you'll have light food and beverage and an engaging experience. The Square is a pretty big place. It's about 1.5 Joe Freshes. It's a big space. It will be one of the biggest spaces in our store, and like this will be for example, November, December, the kids normally come to the store and they get their Legos and their candy and their clothes, but at Christmas, this is where mom buys the trim-a-tree, this is where we get Christmas cookies. This is where the kids, instead of building Legos, might create a card for mom and dad, and this is where every kid in America remembers they met Santa Claus. Again, you're leaving marks that will last a lifetime. JCPenney did this really well, and if you go to people, they all say my grandmother used to shop there, my mom used to shop there.



We're going to create that new imprint, long-term in customers' minds. We did that back-to-school, 1.6 million free haircuts. Santa Claus, Christmas portraits, Legos, Sugar Shack.

This is building a relationship with the customer. We're not selling stuff. We're transforming retail. That's The Square. Every two months it changes, different activities. All right. We haven't built that out, next time you come.

When we're done, that will be the new JCP. And you've now felt it. But again, you've seen about 30,000 square feet. When we're done, 130,000, 100,000-some number of square feet. 100 shops. All kinds of streets, you've got The Square.

Now, we really like it and I can tell you from taking a lot of vendors through here and a lot of media through here, like Nina Garcia, when she saw it, she tweeted, get ready America. There's something that we're feeling it pretty good. But as much as I like to rely on intuition, our team went out and actually did some research. And secondly, we've now had shops, we have 12 shops in our store, and I want to share with you what we're learning from customers and real experience that validates that this is a good idea. Right? Because it would be nice to have some evidence. And so just 12 days ago, we conducted some research. So we were building out things, so when the focus groups came through here, what they saw was the area pretty much from Cosmopolitan to Caribou, Joe Fresh was in, and Levi's, but none of the other stuff was built out yet. It was a war zone, if you will.

We took in five groups of shoppers, turned out there was some skeptics on JCPenney, some neutral and some people that love JCP. We didn't ask them in advance who they are. We said we want you to come. The group started downstairs with a pre-tour perception of JCP. We asked one simple question, we've asked them for years. If you had to give three adjectives to describe JCPenney, what are they? Then they spent 90 minutes on a self and then a guided tour of the store, so they were here about 30 minutes longer than you might have been. And then as they left, we said, give us three adjectives to describe JCPenney you just experienced. Right? And this happened 12 days ago.

So I thought I'd share it with you. And what's kind of interesting is here is the pre-tour perception. All right. These are the words and the adjectives that come out. So some of these were what we had hoped for. When I think of JCPenney I think of great value, I think of bargains, I think of quality, I think of loyalty.

But here are the words that really stood out to me. It's a store for kids and older people. It's a little bit traditional. It's old-fashioned. It's for old ladies. It's polyester. There's overstuffed racks. I remember it from my childhood. It's low-end, it's discount, it's outdated, I go there infrequently. There are no high-name brands. It's disorganized.

These were the perceptions of the people who walked in here. And if I were honest with everybody, this was my perception of JCPenney when I took this job. And I think we all know that is probably a perception a lot of Americans have with JCPenney. And this is seven or eight months into our transformation. It takes time to change people's minds, but that's what they thought. Now, we put this disclaimer up because what I'm about to show you I honestly did not want to show you. Because I don't want you to think we've made this up.

But we showed our Board of Directors last Thursday and they said it's only fair that you let people know the truth. And I asked our teams that did the research, it's a Company here in Dallas, did you edit things out. They said no, this is what we discovered. Believe me, this is what it is. These are real consumers who were here. As you listen to them, you're going to think, yes, this is a story, but this is what they said.

So, we talked about four things. What do you think of the overall place, what do you think of the merchandise, what do you think of the pricing, is it too expensive, too light, how would you compare it to other stores? Let's start with a few -- each of these are about two minutes long, but they'll talk about what the consumer said. This wasn't an interview. We just captured them talking to one another. And you'll kind of learn a little bit of what they said. Let's start with place.

(video playing)



Isn't that interesting? Honestly, they told me there was nothing they edited. But people quickly understood the concept of The Street, the Shops, the mall within a mall very clearly. So let's move on to -- that was place. Now we'll talk about what do they think of the products in the store. Remember, all of the products they saw except for Joe Fresh are in our stores now.

So, frame of reference. This was before Giggle, before Sugar Shack, before [DP Hugh], this is basically Liz Claiborne, Arizona, the new JCP, Levi, more Arizona, the IZOD shop, so what they looked at besides Joe Fresh as you listen to them, was what's in our stores today. But listen to how they perceived the product versus what they saw with the attributes before we started. It's kind of interesting.

(video playing)

Okay. So okay, I'll act as an in between right now. But same product, different perception of the merchandise. It's interesting.

The next thing we want to talk about is the pricing. Because one of our big concerns is if you create a store that's too nice, will people see the product must be expensive. So it's real -- this price thing is really important. Don't think I don't under-appreciate the importance of price. I just like Fair and Square prices. How they feel about price is really important. Here's what we heard from these people 12 days ago.

(video playing)

Pricing was not an issue with this group. Interesting. Last thing we asked them was about how would you position -- how would you feel about this versus where else you shop. I just want to start. We included a couple things here that are not me talking. As you know, I would never say a negative word about a competitor.

I've never talked about Macy's or Target or Kohl's in any way, shape or form, other than good for them, because we're going to do our thing. But there are a couple comments here about competitors but this is from customers. I'm going to play it. I think it's the right thing to do. This is not me in any way dishonoring or commenting on whoever they talk about.

(video playing)

That's my favorite comment in the whole thing. We're here, when I was at Apple, our goal was to enrich lives. It was using technology to help people get more out of themselves and out of their technology. Our goal here is to help Americans live and look better every day and we do that through the products we carry, the experiences we offer, through things like free haircuts, but that last comment, which said I felt valued, we don't have to treat people like they're poor, just because they're on a lower-income budget. And if we can get that across to people, that's magic. And I was pretty encouraged by that. So that's the focus group.

Now, if you go back, that's where we started. On the way out, we asked them tell us the words to describe JCPenney. And the list was here. Nothing's out. Creative, sophisticated, not a lower middle-class store anymore, vibrant, organized, good value, trendy, updated, higher quality at lower prices, modern, fun, open, innovative. Wow. We spent 100 years building out the list on the left, in 100 minutes the perception changed.

It shows the power, in my opinion, of rethinking everything. It's pricing, it's products, it's presentation, it's place, it's people. That's the magic of reinvention. That's the magic of transformation. That's what we're here, to create America's favorite store. It ain't going to be easy. But you can tell from them, I mean, I felt -- I've watched a lot of these videos. Most of them were doing their focus group thing. They were a little bit smitten. You saw the sparkle in the eyes of a lot of people, and that's pretty encouraging.

That gives us encouragement. A lot of encouragement. But the other thing that does is we have shop performance now. As you know, we started the year with two shops, Sephora and Mango. August 1, we added six more, and as of September 1, we had 12 shops. We now have 12 stores inside of JCPenney. You've been to our stores. You've seen them. We know how they're doing.



We gave you a little bit of feedback on that in August, after the first 10 days. We're now seven weeks into some of the shops. We're three weeks into others. It's way too early to draw conclusions. But we ought to be reading the data, and the high level conclusion is the collective shops are comping 20% better than the rest of the store. Simple math. All right.

Now, let's go through a couple of them. I want to talk about four or five in particular, because they represent the kind of shops that we'll have. Sephora, as you know, is our first shop, opened in 2006. We're in our seventh year with Sephora. A huge question to me, what happens to a shop over time. Our thesis, our dream, our hope, is not unlike when a retailer opens a new store, they go through a period of five or six years of comps as people discover they're new in the marketplace and I learn to shop there, and I changed my shopping habits. That's the history of retail. Most retailers will comp about 20% a year for five years to get to their full maturity, and then you go compete. You, who have studied the industry, know that.

Sephora is now in its sixth year. Sephora this year will comp double digits, with our traffic, as you saw in the first half, down 10%. So the point is, Sephora continues to improve. We have about just under 400 Sephora stores. We're adding 75 a year. The reason that's going at that pace is because it's really hard to do cosmetics well. We carry 55 or 60 brands. The employees have to understand everything well. It's a very personal thing. But Sephora had taught us that shops work, that we can do the people right, we can do the environment right and as you know, our partner with Sephora is thrilled with this performance. So Sephora continues to comp in year six, and we're building, in the future going forward, slightly larger Sephora stores. All right.

Levi. Talk about Levi, because as you know, it's one of our first shops that opened August 1. Levi's is the one, probably, if I were to say, I'm most proud of, I'd say Levi. Because we not only put in a great way to shop, we create a new experience called The Denim Bar. We staffed it with knowledgeable people. Levis is now running double-digit comps, and we just went through the most competitive season for Levi, back-to-school. That's when everyone promotes Levi's. That's when the coupons come out. That's when the sales come out. We went through the whole back-to-school at an everyday price, at our low everyday price. Levi's is comping in the double digits. We're the fastest-growing Levi place in America.

We are selling fashion like we never have, new fits, that's in the men's area. In the women's area, where we really took an approach, a curve idea some of their fashion, it is growing so fast it's not really fair to give a comparison. But if you walk through, we're out of stock, we're chasing it. Both Levi shop for women's and men's are doing well above where we planned. Our IZOD shop just set three weeks ago. I think many have already talked about it. It's off the charts. This is growing a little over 50% over last year's IZOD. It has a little more space. So it should grow faster. It's well above our plan.

But why it's important is we're not here to just create great products for our customers. We want to be the world's favorite place to put their brands. And so the fact that a brand like IZOD, which is a mature brand, can grow over 50% in a place and have a great environment, is pretty powerful. So this shop's doing great. It's high priced. We now carry much more styles than we have had in the past but obviously that's going to create some interest in the marketplace, because if you follow these big companies, it's hard to eke out comp store growth when you do business the same way. We are editing to create shops, and be the best at what we carry. IZOD's doing exceptionally well.

Liz Claiborne, we acquired this brand a little over a year ago. I think it was last October. It's important to us. We've expanded the size. It's doubled. But we've given it more space. This is an example of we take one of our own assets, the Liz Claiborne brand has been around a long time, and it's doing really well, and we're proud of that. You see that in our store.

And finally, the one I'm really -- it's the JCP. What this really represents to me is a whole new idea. We've never had this before. Just three weeks ago, we said we're going to take the key essentials of your wardrobe and we're going to put them in one place with high quality fabrics, things like you saw in the video, cotton cashmere, at price points that are a little above where we've been in the past, but we're going to present it right, and the JCP women's is off the charts, selling through. We're chasing. The men's is a little slower than we planned. The women's shop is really successful, the men's is a little behind. And the men's, we've got some in-stock issues. The men are buying down the smaller sizes because it's a little more fashionable, and we look at it as our colors might be a bit advanced, purples and oranges, and we're learning. The men's is a little slower. The women's is off the charts.



I talked about Arizona and the others. You get the idea. Shops are working. That's my only message. Our vision to go to specialty shops is encouraged by the focus group and by the performance in our stores. All right. There they are. That's the six I talked about. Now, we have 12 today.

We'll have 40 a year from now. A year from now we'll have -- I can't do the math that quickly, but 2.5 times what you experienced today. What's interesting is, I showed you this in August. Here's where we started the year. Here's today. It's about 10% to 15% of the space is a shop, they are kind of random, you kind of bump into them, but 90% of the store looks kind of like the old JCP. Next holiday, that's how much the store will be done. And as you see, between shops, there's a shop. So we think with just better merchandising, picking the brands right, without investing money, we get credit for a shop, even though we haven't built it out.

We think the impact of the shops will be much greater next holiday than now, where it's kind of spread out in the store. That's kind of our program. And obviously, shop interest is growing. Once the vendors and people have seen the shops come in, they understand that we truly can execute, that we truly are going to commit to our pricing, that we truly can do the best thing for the brand. And that's why as an example we announced Disney this morning. To have a brand like Disney, which probably has as high of brand standards as anybody out there, pick us and say I trust them with my brand, we're pretty proud of that. If you look at the kind of brands we have, just six, seven weeks ago we launched Levi.

Since that time, Dockers, Haggar, and Disney have committed to putting shops inside JCP. Seven weeks later. None of those were anything more than a conversation until Levi's was in the store, and the brands came down here to look. If you go and you went through, and you can go back later, look at Dockers, it's not about brown pants. It's giving Dockers a chance to build their brand. There's tops and bottoms and shirts, it's a whole different way to shop.

Haggar is back in the clothing business. When I was at Mervyn's in the 1980s, we sold a lot of Haggar suits. The world went more casual, thank God. I like that. But Haggar wants to be in the clothing business. We are going to enable them to do that.

And Disney. Disney, one of the great American brands, would love to get their customer, their products into more places. Then we've got store brands like Sephora. It doesn't have to be just a brand. A wholesaler.

There are retailers out there that are looking for a way to expand, and so we've talked about Joe Fresh is coming next. By April 1, 700 Joe Freshes in JCPenney. Joe Fresh, the number one apparel retailer in Canada, five years after it launched inside grocery stores. Three stores in Manhattan, including Fifth Avenue. They concluded they could spend 15 years trying to get products into the US, or on April 1, they could reach most of America through JCPenney. Joe Fresh.

Bodum, one of the great companies in Europe, known for coffee and tea, you saw the products here. How do they go to the US? They're in Crate & Barrel, they're in Starbucks, but their brand in Europe is much more robust. We'll have Bodum shops in all 700 stores next spring. Giggle, a start-up. If you've been to Soho, if you've been on Chestnut Street in San Francisco, if you've been in Santa Monica. They're a real good editor of baby products and we don't do very well when it's time to buy a baby gift or get started or new maternity. We've got to find a way to catch these moms before they get started to get gifts. Giggle, a start-up doesn't have a lot of capital, but suddenly, they're in 700 JCPenney stores. And we're now beginning our relationship with the customer at the time they're having their first child.

Retail partners pick us because it's a very low cost way to get to market. You can imagine after the Joe Fresh announcement, the phone rings, because there are a lot of retailers in the world that have got to figure out, I've got to go to China. I'm hearing about India. There's a lot going on in the Middle East, some great malls. What do I do in the US, where do I invest? Well, here there's no rent. There's no build-out. You've got your brand. Interesting alternative. Designers, Michael Graves, Jonathan Adler, Terence Conran, and more. So many designers, love their products, but they just get a few racks at a store. They get a shop.

And then we've got our Street partners. People like Caribou Coffee based in Minneapolis, great coffee, beloved in the Twin Cities and several markets. How do they grow? A great way to get to a bunch of stores. Sugar Shack, a little candy store, created by a mom who has seven children, set up a hobby. It's the favorite candy store in Menlo Park, California. Her dream was to do that. Now she gets a chance to have this idea go across the country and create a place for kids to experience her aesthetic. [Pichugo], 44 stores, Italian yogurt like Grom in New York City. It's a great treat.



We want to find things, not unlike Marvin, the great Marvin Traub did years ago, that we discover and bring to the market because they're interesting, because we haven't seen them before. DP Hugh, if you haven't been there go stop by. A couple of Minneapolis natives, who had a dream about how to make it easier for you to look better, color their hair without having to go to the salon and spend four hours on a Saturday and spend \$60 to \$80, and it's really cool. We want to help people live better and look better. You can buy the makeup at Sephora but you can buy the hair coloring and learn how to do that, because a couple in Minneapolis have invented a great concept, and we somehow happened to discover it. We think that's really fun to bring those kind of things to life.

So from big brands to big stores to designers to little ideas, we're unlimited. Once you go to world of shops, they all just kind of fit in. And in many ways, the more interesting they are, the better the store becomes. That's a few of them. We've got room for 100. We're going to save some space, because we want to get to the best ideas long-term.

100 shops inside JCPenney, I said this before. It's pretty incredible to contemplate this. That's a lot of stores. The average 1.2 million square foot mall has 100 stores. But do you know, when people go to a mall, they only go in four stores on average. Why? It's a commitment to go in a store. You've got to open the door. You've got to go introduce yourself to someone. You've got to buy before you leave. Not that it's not a good experience.

When you go to a mall, think of how many places you truly get to. We're creating that many choices within 130,000 square feet instead of 1.2 million, that you just kind of seamlessly move in and out, and you hardly know what you're doing, but you don't have to check out before you leave, because we have innovative ways to check out when you're done. Or when you want. And so we think it provides the best of a specialty store, with a modern interface that makes it really convenient to get into more stores when your time is short. We think it could be America's favorite store. It ain't going to be easy. It's going to take a lot of time. But that's why we're here.

To get there, the only way to be where we are was to have the courage to endure a year of transformation. It's been a really hard year for all of us. There are no short cuts to success. And we're going through that. The biggest change we made was our pricing strategy. Right. We're going Fair and Square. There are no coupons. There are no sales. The sales are going to be what they're going to be, and why did we do that again? Because we knew you win through products.

We're going to get people to want to put stuff in our new specialty department store. If you walk through today and said I might like to go to Joe Fresh, that's because we had the courage to go through a year of transformation. If you walk through and say I might like to buy Giggle, that's because we had the courage to go through a year of transformation. If you want to buy Bodum, it's because we had the courage to go through a year of transformation. The only reason DP Hugh and everything and Disney is here is because we protect the integrity of these brands, and that's an important long-term thing. Ultimately as Mickey or Terry or anyone will tell you, it's all about the goods, and we're getting the goods. But it's because we're willing to go through pain. Running sales down is painful. Reducing your expenses \$1 billion to get to a new business model is really painful.

This is actually really fun. I love doing that. But it's been very hard year, but we're going through it. As we told you in August, as Ken Hannah told you in September, we're planning the back half to be very similar to the first half. I don't want anyone -- this is all about long-term but I want to make sure you understand. We are planning the business to continue where it is, because we're depromoting. It's great to have 10 shops. That's 10% of the floor. It's not going to make a difference enough. Taking off the coupons, depromoting will impact the business much more than a handful of shops performing well.

You can do the math. If the shops comp 20% and they're 10% of the space, that's plus 2%. If you're down 20% it's not going to move the needle. You need critical scale. Understand? We had a back-to-school, that continued like it started. We were pretty pleased with it. The last two weeks have been much tougher than we planned.

We're now in September, it's a lot like March was for us. We're now, before the season begins, it's been a little warm, kids are back to school, we don't have a coupon to bring them in to buy. We don't have a sale to get started on fall. We've got to trust that when the weather turns, when the time's right, that they'll come back. We're hoping that happens. But we had a pretty good August, tough last two weeks.



We've have 13 weeks to go. You're probably thinking it's two quarters. 13 weeks and two days. Because the last ad we ran was December 26th. And then if you remember, January's a clearance month for us. We reticketed to the new pricing. 13 weeks and two days and we'll be done with our year of transformation, and then we run up against, hopefully, people understand your pricing better, shops, more traffic, better marketing, we start to grow again. But we've got to get through the year. But I want you to understand, there was no choice than to choose a year of transformation to get to here, and in the long run we're going to be better off, because we're going to jump start on the new JCP.

End with a thought about my time at Apple. I have watched this movie before. When I joined Apple in 2000, Apple was a Company with dwindling less than 3% market share selling computers. Everyone said to me, what are you doing there? Remember, Michael Dell said, what would you do? He said I'd give the cash back to the shareholders and close the business down, and Michael's a smart guy. But he represented a thought that most people didn't think was that crazy. We were there.

Apple went through 2002, I think it was, sales were down 38%, as we dreamed about becoming a digital device Company. But Apple invested during that downturn. That's when Apple started to build its chain of stores, that's when Apple transitioned to Intel, that's when Apple started its App division, that's when Apple imagined and built the first iPod. We went through that. The stock didn't get up to where I joined until 2004. I spent 4.5 years at Apple, the stock lower than where I started, not a very good time for my wife. Why did we do this? But it worked out okay. But it wasn't easy. Just like this isn't easy. But transformation's never easy.

I remember the day we opened our Soho store. How many have you been to the Soho store, down in Lower Manhattan. That opened on July 17th, 2002. It was a day after MacWorld. That's when Apple was kind of at the bottom, and Steve had really worked hard with myself and a few other people in this room to design that Soho store. We were really proud of it, and it was a day after MacWorld.

I made the decision to open at 8.00 AM. I thought that was kind of a good time open a store, it will be crowded. It turns out nobody in Lower Manhattan was up at 8.00 AM, Steve came over to the opening and he was kind of in, not one of his better moods. Most of the time, he actually was a lovely guy, very upbeat. And there were about 50 to 100 people in line for an Apple store opening in Manhattan. At that time, we didn't believe could we make money building a big store like that? Steve and I talked about a half hour.

He said, nobody cares. There are days I feel like just giving up. Nobody cares. He had read all the reviews from Walt Mossberg and David Pogue in the New York Times. He said nobody understands what we're doing. Nobody cares. Sometimes I just want to give up. And he said maybe the store's not going to work. It wasn't a good day. I said all right. Steve got in his car and went back uptown. He was staying at the Four Seasons.

I was stuck with the store, so I had to stay. About 11.00, Soho started to wake up, and people started to come and we had a person at the door. You know with traffic counters, you want to validate those, so we started clicking. From 12.00 to 1.00, 1,000 people walked through the door, from 1.00 to 1.30, 800 people walked through the door. I called Steve at the Four Seasons, I said, Steve, you've got to come back. He says, I don't want to come back, I've already been there. I said, I want you to come back, and Steve drove down. He actually arrived around 1.30.

If you've been in that store, there's a glass bridge behind the Genius Bar you can stand on. That was one of the great -- it was actually really hard to design that in a lot of ways. Steve and I stood on that bridge at 1.30. He didn't leave the bridge until 8.00 PM, 6.5 hours. He immersed himself in his customer, what he loved. And we went to dinner at Nobu and talked about it and Steve got back in the game.

It's really hard to transform things. It isn't always fun. But that's what we're going of to do, and I've seen this movie and I'm really excited to see how this one plays out, as well. That's what we have for you today. I'd love to take some questions if we could. Thank you. Please.

If you want to get a question, you've got to stand with a microphone and they are -- handheld. Why don't you provide a handheld. Thank you.

## QUESTIONS AND ANSWERS

**Bernard Sosnick** - *Gilford Securities - Analyst*

Bernie Sosnick, Gilford Securities. You told us about the success of Levi's and everybody could see it. Could you give us an idea of what the overall sales of denim were during the back-to-school season?

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

We had a great denim period. I'm not going to go into numbers, but the denim overall was great, and if you know, Levi's made a commitment to put in Dockers shops right after back-to-school, so clearly it worked for them and it worked for us. Again, I'm not going to get -- trust me, I wouldn't get out here and say the numbers were good, unless they were. We've looked at -- I'll give you another number. We went through a study, what do we think the incremental sales of denim were. So we looked at, because we took a little more space, about 250 more square feet to put the Levi shop in, and we edited Lee down a little bit, and we made a couple of changes to Arizona, and that would take it down about 5 points. So 25, if I had to be specific, went to 19.3. There's some impact. The big picture we're trying to say is shops work. All right. I'm just trying to get -- without getting lost in detail, but I'm not going to tell you something that isn't true.

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**Unidentified Audience Member 1** - *Analyst*

Hi. The store looks great. My questions are around mobility, for you to roll it out from one store to hundreds. And specifically around labor and training people from putting clothes on hangers to racks, and now you have things assorted on tables more like a specialty store, so doing that. Then secondly, on inventory and buying inventory for shops on a shop-by-shop basis versus a whole store and how you're managing through that, and how you're going to get there?

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

It's really hard. Everything we're doing is really hard. For instance our buyers, they're having a blast doing it, but the first time we put in the Arizona shop, the teams realized oops, everything I bought is on display. You can't hide it. Our buyers have to think and buy like specialty store buyers. It's a very different process for newness, versus buying things early in the season, trusting that through a bunch of sales and coupons, they'll eventually go away. The art of what we're doing is much more complicated, and we're getting better every day.

On the people side, our dream is to have specialists and experts in the departments. And we've already proven we can do that through Sephora. The Sephora shop is always neat and organized. I'll challenge you to go to a Sephora store, come to JCPenney, it looks great. It's hard work, but we figured it out. We're doing that in Levi. You go to the Levi stores, when I go, they look really great. Our specialists know a lot about jeans. I'm wearing a pair of 508s today, I'm wearing them because I was at a Sephora conference in Las Vegas and visited a Penney's store. The woman looked at me and said Ron, I would love to help you with a pair of Levis. I said, I'm a little bit older, I want something a little skinny at the ankles. She said, you deserve 508s. I said, what color? She said, I like this dark finish. I bought them. I actually like them. And she did that. So we've got to work hard. It's going to take time, but I think that's actually the easy part. But the key will be to be able to have enough staff to do the work.

So when we started Apple stores, our payroll model was 15 employees. As the business grew, it's at 150 employees now. That's why you see all those people in blue shirts. You earn that payroll, because there's a business model you've got to do. That's where there's a long-term transformation. We have to get better and better and better. None of that will be easy. None of that will be easy.

I'll tell you, all you have to do, if you walk into a JCPenney store today and talk to the employees, if you talked to them in February or March they were as confused as the customer. Why are we doing this? How do I explain this all the time? Today, our employees are exceptionally proud to work for a Company that has the courage to do what we're doing. When we gave out those 1.6 million haircuts, and we helped every kid in America look great when they opened up and went to school that first day, our teams were really proud. And so when you connect with the hearts of your employees, they're going to do great work. Because it's within all of us to do our best work every day. We just need a mission. We need a mountain to climb. We're going to create that mountain.



**Unidentified Audience Member 2** -- Analyst

Thanks for doing this day. This is really interesting and helpful. My question is there's a couple of new threats that have sort of emerged in the last probably five years. Here in the States, fast fashion, retailers like H&M expanding pretty rapidly. The second would be innovative new online retailers. How do you deal with those threats? How do you bring people back into the store that have kind of given up on going to malls or department stores?

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**Ron Johnson** - J. C. Penney Company, Inc. - CEO

Great question. Fast fashion. The fastest-growing segment probably in US retail. How do you deal with it? You compete like they do. What does H&M do? What does Forever 21 do? What does Zara do? They price goods every day. And they compete on the goods. That's what that is. We've got to solve our supply chain to shorten our lead times. We're working really hard at that. The way you compete is you try to emulate what makes that work. So if fast fashion is coming, the worst thing we could do is sit here and say, we're going to buy things for a whole season six months out, put it on the rack and promote its way through and then next year, buy a little better. We're trying to compete with fast fashion.

On the Internet, it's interesting. The Internet is moving quickly and we're working hard at that. We'll talk about more some other day, but there aren't as many unique internet retailers anymore. The flash sales sites, if you haven't noticed, are pretty much having trouble. Most of the Internet success is coming from bricks and mortar retailers who really well integrate their omni-channel strategy. Macy's is doing a fabulous job, it's driving a lot of their growth. Nordstrom is really doing a great job of investing in that web store, the physical integration. So the way you compete is we have to get a dream for how we do that, and really do it well, and we've got a team working hard on that, and we'll unveil more about that when we truthfully get it figured out. But we'll get there. But I'm not worried about Internet only at all. Our product's unique.

Not worried about fast fashion. We're starting to compete better with them. We'll do better going forward. Joe Fresh is a pretty good answer to H&M in my opinion. It's a pretty good answer to Uniqlo. It's a pretty good answer to Zara. We'll compete well there. But those are some of the things that are out there.

Keep moving around. I know there's so many hands up. Please, just -- I'm sorry. Yes.

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**Brian Nagel** - Oppenheimer & Co. - Analyst

It's Brian Nagel from Oppenheimer. A question on the financials of some of these arrangements with your vendors. Give us an idea, how this started with Levi's or if you don't want to mention specific names, fine, how does the financing of these stores within a store-within-a-store concepts work with the vendor? And how is that transitioning now as you start to build some momentum with these shops who sign up for these vendors?

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**Ron Johnson** - J. C. Penney Company, Inc. - CEO

Good question. We work with every vendor and reach an agreement on the terms of the business relationship. We're setting that up, so both of us profit fairly. We want a Fair and Square return for our vendors and ourselves, and in a perfect world we're going to share the proceeds of all the innovation we do. We are committed to having gross margins over 40%. So we're artfully putting together a mix that gets us into the 40%-plus kind of margins, that the good specialty stores do. But there's a lot of margin to go around, because a lot of these people that have to do their own specialty stores, they need 60 to 70 points of markup to be able to deliver their profit, because there's a lot of expense going into that store. So if we need 40%, and they start at 60%, 70%, there's a lot of room to share the profit.

So every deal is done differently. Vendors provide capital to help build the shops. That's really important to us. We buy things at wholesale. There's no funny money. There's no promotional allowance, markdown money, because all that does is lead to more inventory than you need. We've got to make the whole pipeline efficient. And then fairly and squarely share in the profits. And that's why they're lining up.

But all I want to make sure is that we get our 40%-plus. Greed is a really bad thing. We can't say we're the power, therefore we're going to take money out of the vendor's product and put it in ours. If we don't share long-term, we aren't going to have partners. And all I care about is when they have a new idea, they put it in our store. So if Levi's has a new fit or a new finish, and say I'm going to JCPenney because I earn more money selling through JCPenney. If I'm the guy who's grabbing all the money, I'm not getting the new fits, we're not getting the new finishes. So we're going to treat our vendors fairly, we're going to treat them squarely, and we're going to share in the profit of what we create together. It's a principle thing. Bill, are you allowed to ask a question? I'm kidding, one of our great shareholders.

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**Unidentified Audience Member 3** -- *Analyst*

Now he's nervous. It's not actually a question. One of the things we learned at the Board meeting, it's up to you whether you want to share it or not, I found it very powerful, which is, I think it would also motivate people to go to Stonebriar. What do we do at Stonebriar? What's changed there, what are the numbers on the change early, but what's the impact and what are we doing about it?

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

Well, all right, so thank you, Bill. It's very clear, we learned the moment we set up our first shops here, that presentation changes perception. So we asked the question, in this year of transformation, how do we dramatically improve the presentation in all of our stores? So when I'm not here at 7 in the morning, when I'm in town, I'm at Stonebriar and every day we have our great visual team and our merchants together and we pick a new category and we go through and we try to artfully create as close to that as we can, within our budget. And so if you go to Stonebriar you'll see the nicest JCPenney store merchandise you've ever seen. It's not as good as this, but it's a really good improvement.

And we're working really hard to roll that presentation out to all of our stores by November 1, because we're seeing very positive results in that store. I'm not going to share the numbers, Bill, because it's one store and I can share that with you because it's going against the district, but I don't want to say anything that might lead people to think we're going to automatically perform that much better in November. But our goal is, while we have one eye on the future, we want one eye on the present, and so we're working really hard on our presentation of all of our stores. If you go to Stonebriar today you'll see a much improved JCPenney store. All right. Thank you.

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**Unidentified Audience Member 4** -- *Analyst*

Thank you so much for the overview in terms of merchandising. Could we just shift for a minute in terms of sort of infrastructure? One of the biggest infrastructure changes is about to start early next year in the IT world for the Company. Can you talk about that, and sort of the redundancy that you're building in, and how you're going to go about it, because you're the first major retailer to try RFID across the board, no-holds-barred type of thing.

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

Systems; really important. Fortunately, Kristin Blum, who leads our systems effort as you know went to Abercrombie years ago and did a heart transplant of their systems, and she has told us in many ways that was more complicated, because they had international stores and a variety of things, but this is not easy. We've got an experienced team. We're basically, as you know, we have today, we run the business on nearly 500 systems. Because they're so outdated and customized, 95% of the money we spend goes to updating nothing to new, and so we're going to be rolling out full Oracle Retail and that's going to take three years. It starts next year with merchandise planning, and those kind of information systems, but then we're going to connect all that with our point of sale, with experience in the stores we have to work really hard on. It's going to be hard.

RFID, I think, will be the easy part because we're actually very experienced at RFID. Penney's has been one of the leaders in RFID for the past four or five years. We have about 40% of our tickets on RFID now. We've been using RFID to help replenish a lot of basic categories for years, and we've seen the operational benefits from that. The challenge will be when we move to the customer, and we let customers start to check out with RFID, and that's where we've got to be a little careful. You've got to be careful from shortage and shrinkage. We've got to be careful in a lot of ways, but

we're going to get there, because it's the right thing to do. Because having full RFID lets us have perfect control in counts of our inventory. It lets us know within a few feet where everything is, when we have to find it for the customer. It lets us replenish more accurately and more quickly, but it also lets the customer check out in 25% of the time. And the transaction is the worst part of the retail store experience, and it has been forever. We're working really hard on redundancy and a variety of things to get through that transition.

But if you read our prospectus, the attorneys, there's a risk factor in there, because this is not easy. But we're going to be a leader in this stuff and so we're working really hard. We've got a great team and we're going to start rolling out. We'll test it all. What you saw here today is really just an artificial front end. We haven't figured out exactly how that flow will work. We're working through it. We'll be ready to go next spring, with both personal checkout and checkout in pockets.

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**Unidentified Audience Member 4** - - *Analyst*

You do the whole front end next spring or will you try to phase it in geographically?

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

We will continue to have our cash wraps in all stores next year. As we get to a new store, we're going to take them out, like we said, and we'll get our cashiers untethered to get out and do service, which we think is better, but we will let everyone check out with their phone or iPod starting February. So every employee is going to have an iPod in their pocket, which they can use to check out a customer next spring. But we'll also have the redundancy of the cash wrap. We think that will make us more efficient as we watch the percent go to check out anywhere, anytime, anyone, we'll reduce the number of cash wraps, we'll pull employees out, so that will be a hopefully smooth transition. It won't be like wow, there's no checkouts. That would be risky. When we did this at Apple, we went through a period, where's the cash wrap? That was hard. We've got to get through that.

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**Paul Lejeuz** - *Nomura Securites Intl - Analyst*

Paul Lejeuz, Nomura. Ron, when you first started on this transformation, correct me if I'm wrong, I thought your vision was that it would be all stores, like literally all stores would kind of look the same in terms of shop-in-shops. Lately you've been talking a lot more about 700. Today, we heard about Disney's going to be 500-plus. So what's changed? What do those other stores look like that won't have the complete shop-in-shop assortment? And a situation like Disney, is that a 500-plus store test that maybe could grow over time? What happens to a store that wouldn't have a Disney shop? Is everything else just a little bigger, could there be some other brand that wouldn't be in another store? I'm just trying to put all of those pieces together.

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

Paul's got a great question. So we have just under 1,100 stores. For years, we've thought of the Company, we have 700 stores, approximately. Might be 693, I forget exactly, that tend to be major market, large stores. Those stores tend to be 80,000 square feet, up to -- one is nearly 300,000 square feet. But we've got a range of sizes, one of our long-term challenges. When we think of America's favorite store, in all the shops and The Street and The Square, it's got to have enough size. So therefore, it's got to be 80,000 square feet or more or it just doesn't have the critical mass.

So we have 400 stores that tend to be smaller, tend to be small town. Now, we're putting a lot of the merchandise into those stores. Like JCP and others. Sephora, for example, we just opened up I think it's in Sioux Falls, South Dakota, it's doing really well. It's the only place they'll ever be able to buy Sephora, probably in South Dakota, in Sioux Falls. But, we're being very careful about those small stores. They do about 20% of our revenue. Well, maybe not. About \$2 billion in revenue in those 400 stores. We don't want to put an investment in those stores until we're sure we get the return. The key is to get them merchandised but everything we're learning about presentation at Stonebriar is going to those small stores on November 1. So we want to make them better. But they will not be going through this exercise in the current planned roll-out.



Now, on how many concepts go to which stores. In our perfect world, we would like to put everything into about 700 stores, but because some of are smaller, there are some concepts that don't go all the way to 700 stores. Sephora, we talked about, because the training requirement, takes more time. Disney, we would love to put in more stores over time, but the teams negotiating came out with 580, or whatever the number was. Remember, Disney already has about 200 of its own stores. Disney's a really smart company, and what they loved about us was our demographics overlap perfect with Disney. They looked at all the retailers and it turns out the Penney's demographic was the most parallel with Disney. I think they're trying to manage a distribution network that includes their own stores, their licensed partners, our own stores, and we concluded that was the right number. Most things will be 700 stores.

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**Paul Lejuez** - *Nomura Securites Intl - Analyst*

What happens with those 200 stores?

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

Then we just add it, but we have choices. We'll do other things. We're going to, over time -- there will be things that we test. We'll take a shop and put it in our bigger stores, and we'll find out ones that should go to all stores. It's not unlike if Steve Roth were here, or one of the landlords, all their malls are different sizes. Some are 2 million square feet, some are 600,000. Some have room for 50 specialty stores, some have room for 200. Some strategies go into all stores, some go into some. It happens over time. So we view ourselves as creating a specialty department store. We want as much common store for impact and marketing as we can, but there's room for exception. And we'll kind of artfully work that out.

All right. I'm not sure how much time we have for -- two more questions, and we'll get three more because you've had your hand up, young lady the whole time. You can go first.

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**Deborah Weinswig** - *Citigroup - Analyst*

Deborah Weinswig from Citi. Number one, can you update us on marketing? And secondly, as I think about sales opportunities, it seems like the minute I came off the escalator and saw Giggle, they have a great registry. With everything you're doing in Home, could you talk about the registry opportunity, as well?

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

We have a new registry strategy we haven't announced yet, it's called Present Company. It's really cool. I probably shouldn't have said that. Present Company applies to babies. It applies to gifts. It applies to kids. You'll learn more later. It will be perfect for something like Giggle. You'll go register anywhere in the store, but these new service bars are a great place to do it.

(technical issue)

On the marketing side as you know, we did not do a good job in the spring with our marketing. Customers found our pricing very confusing, the three types of price and we made the change to go to basically everyday prices and clearance, and thank God we did. We are out of the pricing confusion business. You guys don't read about it, customers don't talk about it. The challenge now is to make sure they understand the value. That's a long-term challenge. We went from confusion to comprehension, but now the challenge is how do you make sure people believe the value's right.

I've concluded in discussions with the team, that you earn trust over time on value. I could go out and shout as much as I wanted to, trust me, we've got great prices every day, and no need to use a coupon. Great prices every day. Other people mark it up just to mark it down. All people are going to say is yes, yes, yes, prove it to me. So we shifted our marketing, Deborah, and we said we're going to change the message to things we're getting really good and important at, like the new brand partners. Like The Shops. Like free haircuts for kids. We're now treating our pre-prints that you



get in the mail with more frequency, and it's about the products and the price and the brands we carry, and our mantra is brand, product, price. We want to seize that branded department store, branded specialty department store. So we made a lot of changes in our marketing to try to get that across. Thank you, Deborah. Last two questions, please?

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**Unidentified Audience Member 5** - - *Analyst*

(inaudible – microphone inaccessible)

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

We're going to be a store for all Americans, right? We want to have, like the videos show, that was a pretty good cross section, I thought. Someone looked a little Neiman shopper, someone looked a little lower income, there was a good variety there. We'll continue to bring people there. We want everyone to shop at JCPenney. But the core is to take our current customer base and over time increasingly get people with a little more income, a little younger, to find that this is a store for them, because our customer base has been maturing. If you look at Home today we have the oldest Home customer of Target, Walmart, Macy's, Kohl's. Why is that? Well, we're the oldest store, and we've been around a while. We've got to get a younger customer. That's going to happen in a very evolutionary way.

As you've seen with our shops today most of the shops are supporting our current own private labels. America's big brands like Levi, Dockers, Haggard. At the same time, we'll sprinkle in a few things like Jonathan Adler and Michael Graves. That's going to be a judgment that Liz Sweeney, our Lead Merchant, myself, all of us make together as to what brands will create the right mix and that's kind of an art. And over time, we'll try to get that right. Last question was right here. Thank you.

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**Erika Maschmeyer** - *Robert W. Baird & Company, Inc. - Analyst*

Erika Maschmeyer from Baird. Could you talk a little bit about your learnings from adding The Shops, and how much faster are you now at putting them in, has there been a hit from having them, and I guess how are you going to minimize the impact from having the stores under construction?

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**Ron Johnson** - *J. C. Penney Company, Inc. - CEO*

I think The Shops turned out pretty darn good. For our first effort, the outcome of The Shops, most people look at the Levi Shop, the IZOD Shop, wow, they could execute a shop. That's good. We did it in our budget. However, the time while it was under construction, was a little bit of an eye sore for our customer. We had white walls. We didn't do a good job of letting them know something exciting's coming.

We want to shorten the duration it takes to build a Shop. We want to make it less of an interruption. It clearly impacted the business a little bit. We're out of the shop construction business until next January. We start our move into Home and we're trying to judge as to when to do it quicker and a little less interruption. Does that make sense? We've got a lot to learn there. We'll get it right over time.

All right. Well, thank you very much for coming, and I really appreciate your coming all the way down to Texas because I really wanted you to see what we're trying to create. We're going to have some time. You might want to browse around a little bit. We'll have buses here that leave at different times, after what you've heard. There's still time to get yogurt, candy, coffee, whatever you need, if not, the buses will be downstairs. They'll take you to Stonebriar, but before you get up, Kristin's going to give a few words on directions and I'll say good-bye. Thank you.



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