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PRESENTATION

Gary Balter - *Credit Suisse - Analyst*

Welcome to the Office Depot presentation. We are very lucky today to have Steve Odland as a speaker and I have a little complaint for Steve, though, before we start because when he joined AutoZone, stock was about $27 and it tripled. If you look at Office Depot so far, we only have a double. So, Steve, there is a little bit more pressure on you here to give us at least one more from that 19.

This is -- when we look at what's going on with inefficiencies, whether in government or other places, sometimes you wish that he wasn't at Office Depot and he was actually somewhere in the U.S. government cutting costs. Because if you look at the story both at AutoZone and Office Depot, I think what separates them -- and you know we have a buy emphasis while we're being bullish in the interim.

This is -- what he has been able to do with this company is kind of look at the three divisions. Look at the corporate and say this is an area we should be investing in. This is scenario where we shouldn't. And we see it not just as we saw AutoZone was expense driven, but here we're seeing top line growth. We're seeing strategic investments. We think with Europe still very low relative to the opportunities that are there, with the BS or BSG, or whatever it is currently called, doing pretty well but still some room to grow, and then with retail starting to show the turns as they go -- as they do the M2 format, we think there's still a lot of upside to this company and the earnings, and we think we have the right person to kind of deliver that upside, and it is our pleasure to introduce Steve Odland.

Steve Odland - *Office Depot - Chairman & CEO*

Thank you, Gary. Actually, the stock quadrupled, to be clear. But as everybody knows, past performance is no predictor of future performance. So it's irrelevant, anyway.

Welcome, everybody. The first obligatory slide, I hope everybody has read the risk factors and 10-K. There will be a test on it in the breakout sessions.

For those of us who are not familiar with Office Depot, Office Depot is the leading supplier of office products and services around the globe, especially the largest international player. Annual sales now are $14.3 billion, trailing 12 months. We operate in 23 countries, and we are multichannel virtually everywhere with stores, catalog, Internet and contracts.

We do have the three divisions, North American retail, North American business services, and then International incorporated only 20 years ago. So a relatively young company, started with one store in Florida. It's been listed since '91 and, of course, an S&P member since '99.

The product put out mostly in the supplies area about -- over 60% in supplies, but technology is growing rapidly now with 26% in the furniture for the balance. The story here, though, it is really our multichanneled approach. We have over 1000 stores now in the United States and Canada, mostly in the United States. In North American business services, it is the catalog business, the contract business, and then also e-commerce. I'll get into this in more detail.

Internationally, we have mostly catalog commerce and e-contract. We do have some small retail businesses in Japan, France, and in Hungary. We are now one of the world's largest Internet retailers. This isn't commonly known, but according to sources, we're the third largest Internet retailer in the world, with nearly $4 billion dollars in sales, after Amazon and Dell. So that gives us a great channel there.

This is how we break out, and I think most of us think about Office Depot as a specialty retailer, but less than half of our business actually is in retail. Most of our business is indirect around the world and that splits out the direct business that fits into about half through orders accepted over the phone versus orders accepted over the Internet.

So a way of thinking about the Internet business is how we accept orders, and that is how we categorized. But if you think about the Internet as an information source, it certainly is an electronic catalog source of this -- a resource for virtually everyone and, of course, we provide that in our stores, as well.

Our strategies are in each of the divisions to grow, and in North American retail we want to do that. We believe we can continue to improve store productivity beyond where is today, as well as continue our store build out.

In North American business services, it's a marketshare game, although, as I'll show you in a moment, that business and that industry is growing between 3 and 4%, so there is organic growth on top of marketshare.

And then internationally, as you know, we have been focused on trying to improve the profitability as we integrate past acquisitions, grow our European contract business, and then begin to expand geographic presence there.

The business from a U.S. market standpoint is large, and it is growing about $323 billion, all the numbers that we thought would be industry numbers that are public. The delivery business is the smallest portion of that today, but at the same time a fastest-growing portion.

This is an interesting slide though, and again it is public data. But if you look at how the market is split out, the three players in the office superstore category only account for about 10% of the marketshare. You have got everything from other specialty retailers, which includes direct businesses like Dell, Gateway, and so forth, to contract specialists, supermarket drug channel, so office supplies are really split out in a lot of different areas and our segment is relatively small. So as we think about marketshare possibilities, there are a number of these sectors that are naturally declining with a high level of fragmentation.

The North American business is growing. It has a lot of opportunity to go forward. Some of it is in markets. So you've seen us rejuvenate the Taking Care of Business campaign this year, and as that has been successful for us, and then also launched NASCAR.

But an interesting way to think about the retail business is that it is really a direct business. So 80% of the volume we sell through the stores are actually -- it's actually sold to small businesses, small and medium-size businesses. So the whole concept of comps is an interesting concept in this business because, A, we're opening new stores in fill-in markets so there is that aspect of attrition to comps, but there is also more importantly a lot of multichannel shoppers. Our best customers are multichannel customers so they purchase at retail. They purchase direct through the VSC area where we deliver to them and actually we would rather convert them from retail direct, a more profitable way to deliver it.

So as we continue to improve our business and deepen our marketshare within these given customers, we want to move them over and move them up from the retail business to the direct. But the whole notion of comps is an interesting one for us as we go forward.

One of the ways that we're growing our business and working in the margins is through private label. Everybody probably talked about that today. We have our last quoted numbers were about 18 to 20% of our total company in private brands, but we have really developed a number of terrific brand names in this company.

Office Depot is one of them, of course, but in writing instruments we have Foray. In the furniture business, we have the Christopher Lowell brand. Christopher Lowell is a furniture designer where we have proprietary furniture design that has worked terrifically well for us. In the areas of technology, we have the Ativa brand and so forth.

So we're able to margin up and offer a good, better, and best range in our category management development through our private brand approach. Private brand doesn't always need to be the entry-level. What is interesting is to our category management efforts, in some cases, you'll see private brands form the good and the better ranges as well. In some other categories you will see good, better, and best, all delivered through private brands. So it is an interesting ability in this business to leverage the margin up from that standpoint.

We have expanded our new store openings. We have opened 100 stores in '95. We said that we will open about 100 stores this year. We would like to see more, and we think that we can open at least 1000 more stores, on top of the 1000 we have opened already in North America. We have presence in 49 states and most Canadian provinces, although our Canadian business is quite a bit smaller than our U.S. business.

One of the things that we're doing is refreshing our entire store base. We have one of the oldest store bases in the industry. We also have one of the oldest designs, and we're working off of the very original design, 20 years old. The M2 prototype, or Millennium 2, for those of you who have been around the company for awhile, has been in the works for the past couple of years. We have been testing and refining it. We now have settled on a final prototype and the design, and we're rapidly rolling as of this quarter in order to get that prototype across the entire South and 49 stores that we have open.

The prototype will run us about $225,000 to $250,000 per store to renovate the stores. We are pleased with the results, both in the top line as well as the margin, the margin being impacted by adjacencies, as well as the operating efficiencies that come from the M2 design. So now is the race, and it will probably take us the next three or four years to get through the entire store base in order to get the M2 in.

We also have our shopper card, called the Advantage Card. We will be relaunching it as the Worklife Reward card. That is a name change only, but the point here is that we have millions of customers now in our database to whom we are doing a direct, one-on-one marketing through electronic means, e-mail campaigns, and so forth, as well as direct-mail where we are able to customize the offer. This is working very well particularly in small businesses where we can reach those businesses and customize the awards. They tend to be our best shoppers who are loyal, higher shopping cards and so forth.

The other thing that we have just begun is global sourcing, so even though we have a significant amount of private brand, it's mostly locally and domestically sourced. So we have an enormous opportunity to take that sourcing and begin to look at all of our business, not just as separate businesses like we have with European business, Japanese business, American business, and so forth. But it is really for all of our global business together and begin to globally source that through China and other places. So we have just -- that to have an impact on going forward over the next few years as we mature our global sourcing efforts.

Cost management is an area that Gary touched on. It is something that is near and dear to my heart and if you look at Office Depot's structure, first there [isn't] really any other benchmark out there, best in class benchmark, you can see we have a long way to go from a cost structure standpoint.

I don't see anything in the -- structurally impeding our ability to move our cost simply is the fact. There is no silver bullet. So I thought as occurred in the fall in the past year, year and a half, on the hundreds of different projects that we have going on, and I have listed these, and any one of them seems immaterial, although all of these up on the screen today are million dollar plus cost savings opportunities.

We are not sharing all several hundred with everybody, but the point is that they are collectively making a big impact on our business that you have seen through our past results.

In the North American business solutions area, we are expanding our sales effort in a number of different ways. The first one is telephone account management or TAM, and that simply is not a -- it's not rocket science, but it simply is putting a sales force on the phone and calling on small and medium-sized customers, which has proven to be very effective at bringing in new business and doesn't require physical salespeople to go out, and you can get much higher return and get penetrations into smaller businesses for very low cost. So that is a very efficient way. Also we found it has increased the buying frequency with our existing customers.

So as whereas we thought about it first as a prospecting tool, it now has become an efficient way to drive recent purchases by calling them. We do have about a 1500 contract salespeople on the street and that group is working on the large, medium to larger size accounts, so there's an enormous sales effort out there.

The other thing we're working on is category expansion, and we renamed the division the Business Solutions Division in order to focus them on finding solutions which will improve services. So you will see us expanding even more services and increasing share as well.

A couple of examples of category expansion has been the janitorial category, but we also are expanding our Design, Ship and Print activities into the direct area; whereas they have been up to this point focused more on the retail areas. So more to come on that.

Turning now to international, you can see these three pie charts are depicting the size of the markets in the various countries in Europe, Latin America, and Asia. The numbers are tough to get and so they are really wide estimates. I think the important thing to note, though, is that we have big categories and big opportunities outside of North America. We have a pretty well developed business today in Europe, about $3.5 billion business, with new businesses beginning in Asia. We have the Japanese business and we just acquired majority stake in the Korean retailer called Best Office, which eventually will become Office Depot brand.

And obviously there are some bigger markets over there which we have worked on from a development standpoint. We also have businesses through Joint Ventures in Latin America. So we have pretty well established businesses of over 100 stores in Mexico and Central America through joint venture with Gigante down there. So that is 50-50 joint venture, so that doesn't get consolidated into our numbers, even though it is a sizable business that is profitable and growing.

Obviously, there are a lot of expansion opportunities to look at. The red is where we are today and the gray, where we are not. And the thing that drives our business are the small business formations, and as you see the liberalization of economies around the world, the growth in small business is booming in areas like China and India, and they form long-term opportunities for us.

We have focused on a number of growth initiatives in our existing businesses, primarily in Europe, and it has gone to a managing director strategy. We have hired a managing director who's in his six-week in Europe and so it's going okay. Last quarter we grew our European business by 2% in local currencies. That is a lumpy situation, and in Europe we still have the economic situation. So I would just caution that we still have a long way to go in Europe to improve that business.

We're trying to convert it from a country structure that was put together through several acquisitions into a Pan-European business that is totally consolidated. You can see us focusing on things have worked in the DFC here and North America, like telephone account management, like an increased sales force, and trying to bring a -- what has been a direct catalog culture to a more selling orientation.

We also are integrating our efforts to private brand from, as I said before, separate country kinds of orientation to more of a global structure, and we are launching Royalty programs there, as well. So a lot of opportunity, but Europe still has a long way to go.

Obviously, some cost initiatives and if you've looked at the European cost initiatives, they are similar to the U.S. but anyone who has looked at our charges that we have phased in over the past, you can see that as we have laid out the simple charges in future years where we are not able to take them all once, they relate mostly to instructional changes in Europe to supply chain -- kind of structure. So we still have a lot to execute from a cost structure consolidation and integration in Europe. So that is going to take us a couple of years. I will show you the chart.

We are a very financially driven company. We want profitable growth only. We want to improve our free cash flow in our margins. We have instituted this culture of thrift, so the one thing about having hundreds of programs focus on cost is that people are really getting it, that we have to save pennies throughout the operation. We have a very disciplined approach now to capital deployment in an economic value-added mindset.

The bonuses for all management throughout the Company are based on an EVA mindset, so it is the components of EVA, ROIC and income. So that I think has focused us on efficient deployment of capital cash flow, as well as the normal P&L focus. The numbers are hard to read. This is the first-quarter results of '06. The numbers were strong. On an adjusted EPS basis, we were up 30%, with ROIC expanding by 240 basis points on a trailing 12 basis. So I am very proud of moving that ROIC in a reasonably short period of time.

Trailing four quarters, you can see sales have been up 5%, earnings per share for four quarters have been up 30%, and of course the 13% ROIC. The diluted shares have come down by a few percent. We actually have continued to work cash off our balance sheet and do our share of buybacks. And you can see when you see the cash in a minute, but cash flow has improved over the past quarter, as well as the past four quarters.

CapEx has been focused on the new stores and some IT, and you can see the share repurchase is $400 million worth in the first quarter, which is $1.2 billion worth of share repurchases since the program began (indiscernible) the last five to six quarters. So from a balance sheet standpoint, you can see the top-line cash has come down as we have worked cash off the balance sheet and contributed to our share repurchase program. Inventories have come down. Working capital has come down.

So we really are focused on managing cash, and you can see then how return on equity has come up between 12% and 16%, and then return on invested capital number again.

This number is hard to see, but we've got it in the K and various reports in the Qs. The point here is that what we try to do is lay out the charges that we have taken cash and non-cash for you, and then we've also laid out what we believe will happen in 2006, 2007, and 2008. There is no new news except the point that I made earlier, which is that the structural changes continue to be out in front of us.

So if you look at what is going to happen here in this year and in the next couple of years, they are related to primarily the supply chain a little bit here in North America, but mostly in Europe as we begin to move those previous acquisitions into one integrated group.

So we had 25 facilities in terms of distribution facilities in Europe today, and we simply need to bring those into fewer facilities. So these charges are what we anticipate cash and non-cash going forth. Hopefully that's helpful as you go through the model.

Performance metrics, we're very proud of them. They've been great. We have a long way to go in Europe to continue this, and we need to execute very well in North America to continue on track.

So the final chart that I'm obviously very proud of is we've added $7 billion worth of market cap over the past year, and the market has recognized -- our focus going forth, though, has got to be on a profitable growth, and these are the areas we've talked about in great execution. We're prioritizing use of our cash flow as follows. Number one, we want to open up new stores here in the U.S., North America, but also some new geographic markets. We will do that in a way that is not affecting the Company's kind of approach, -- our investments have been relatively modest, first and three, and then buying a majority stake in our Israeli joint venture, so I think it's very high return kind of investment.

We do need to make the necessary investments in our core business to drive growth. The store refresh program to the remodel programs to the M2 prototype is very important. We need to get through that. That is going to take some of our capital. Finally, acquiring assets for businesses in our key priority areas. We announced an acquisition of the Allied Office Products business, which is about a $300 million business, largely concentrated here in the New York area, has -- it's in the process of being integrated. We announced this a few weeks ago. So those kinds of things which are easy integration kinds of investments are important.

And then finally, we're using our excess free cash to repurchase shares. So that will remain the order of our deployment of cash flow. With that, I will conclude and open it up to questions.