The Kroger (NYSE:KR) Q4 2012 Earnings Call March 7, 2013 10:00 AM ET

Executives

Cindy Holmes - Director of Investor Relations

David B. Dillon - Chairman, Chief Executive Officer and Member of Proxy Committee

W. Rodney McMullen - President, Chief Operating Officer and Director

J. Michael Schlotman - Chief Financial Officer and Senior Vice President

Analysts

Stephen W. Grambling - Goldman Sachs Group Inc., Research Division

Andrew P. Wolf - BB&T Capital Markets, Research Division

Mark Wiltamuth - Morgan Stanley, Research Division

Ajay Jain - Cantor Fitzgerald & Co., Research Division

John Heinbockel - Guggenheim Securities, LLC, Research Division

Meredith Adler - Barclays Capital, Research Division

Jason DeRise - UBS Investment Bank, Research Division

Karen F. Short - BMO Capital Markets U.S.

Edward J. Kelly - Crédit Suisse AG, Research Division

Kelly A. Bania - BofA Merrill Lynch, Research Division

Gregory Hessler - BofA Merrill Lynch, Research Division

Operator

Good day, ladies and gentlemen, and welcome to the Q4 2012 The Kroger Co. Earnings Conference Call. My name is Kirstie, and I'll be your operator for this -- for today. [Operator Instructions] As a reminder, this call is being recorded for replay purposes. I'd now like to turn the call over to Ms. Cindy Holmes, Director of Investor Relations. Please proceed, ma'am.

Cindy Holmes

Thank you, Kirstie. Good morning, and thank you for joining us. Before we begin, I want to remind you that today's discussion will include forward-looking statements. We want to caution you that such statements are predictions, and actual events or results can differ materially. A detailed discussion of the many factors that we believe may have a material effect on our business on an ongoing basis is contained in our SEC filings, but Kroger assumes no obligation to update that information. Both our fourth quarter press release and our prepared remarks from this conference call will be available on our website at www.thekrogerco.com.

After our prepared remarks, we look forward to taking your questions. [Operator Instructions] Thank you.

I will now turn the call over to Dave Dillon, Chairman and Chief Executive Officer of Kroger.

David B. Dillon

Thank you, Cindy. Good morning, everyone, and thank you for joining us today. With me to review Kroger's fourth quarter and full year 2012 results are Rodney McMullen, Kroger's President and Chief Operating Officer; and Mike Schlotman, Senior Vice President and Chief Financial Officer.

Kroger had an outstanding fourth quarter and an outstanding year. We accomplished a lot in fiscal 2012. We delivered on ID sales growth, we exceeded expected earnings per share growth, we increased FIFO operating margin and we increased our dividend 30%. Kroger's unique value offering of better service, great products and enjoyable shopping experience and lower prices continues to resonate with a full range of customers. The result is an industry-leading 37 consecutive quarters of positive identical sales growth. In this morning's press release, we provided you with details to make it easier for you to do an apples-to-apples comparison and understand how we look at our business internally. Table 6 in our press release was designed to help you understand the details behind the growth figures we reported.

We delivered value to shareholders by increasing our dividend and exceeding our own earnings per share guidance through the combination of solid operating results and share buyback. We returned more than $1.5 billion to shareholders through dividends and stock buyback in 2012. Our associates delivered an outstanding year that underscores Kroger's growing connection with customers remains the key to shareholder value creation. In a moment, Rodney will outline how we got there, and Mike will discuss the numbers.

First, I'd like to give you some insight into what our customers are facing today. Consumer confidence was fragile throughout the year, and it hit its lowest point this January as customers voiced heightened concern over taxes. We believe 4 factors will continue to affect consumer confidence: the overall state of the economy, fluctuating gas prices, payroll taxes and government policy uncertainty. These factors are causing sales comparisons between days and weeks to be highly variable. But overall, we continue to have strong ID sales trends.

We remain confident in our ability to deliver growth despite the economic uncertainty. Our team has delivered strong results by executing our Customer 1st Strategy over the last 5 years. And as you know, the last 5 years has been highly volatile, and we have continued to consistently deliver through that time. A cornerstone of our Customer 1st Strategy is the value our associates deliver to our customers. Our customers are stressed at the pump, they look to our Fuel Points program for meaningful savings. And when families have less to spend in restaurants, our ready-to-heat and ready-to-eat meals help them eat well at home.

When you want convenience of finding everything you need plus a little in one place and save time at the checkout, nobody does it better than our family of stores. So whatever the economic and operating environment, Kroger is situated to deliver on our growth targets for 2013 and beyond. Our ability to do this is what makes Kroger a compelling investment.

Rodney will now provide deeper insight into our business performance and share our year-end market share statistics with you. Rodney?

W. Rodney McMullen

Thank you, Dave, and good morning, everyone. We exceeded our expectations for the quarter and the year, thanks to our associates performing to deliver growth. We are implementing our long-term growth strategy, which includes: targeting capital to grow our business in new and existing markets, leveraging dunnhumby insights to solve varied customer needs through both traditional and digital channels and continuing our share buyback program.

We continue to make good progress, adding square footage in 4 fill-in markets, and we've identified others based on various metrics. We have narrowed the list of new markets for future expansions. In 2013, we plan to build, expand or relocate 45 to 50 supermarkets compared to 44 in fiscal 2012.

At our Investors Meeting in October, we identified 4 key performance targets for shareholders to measure our success. I'd like to spend a few minutes discussing the results of each metric. On identical sales, we are very pleased with our fourth quarter identical supermarket sales growth of 3% without fuel. We focus on identical sales because it provides the strongest measure of our relevance with customers over time. Our identical sales without fuel and pharmacy were consistent throughout the year. We are very pleased with our identical sales trends through the year, given the fact that inflation declined during the year and tonnage growth improved throughout the year.

Consistent with our guidance at the start of 2012, pharmacy sales benefited overall sales in the first half of the year. This was due to strong growth in our pharmacy business, including attracting and retaining Express Scripts business. As also in line with our guidance at the start of the year, identical sales trended down as prescription drugs came off patent. These events will be important to keep in mind as you estimate our quarterly sales expectations for 2013. Mike will provide our guidance shortly.

Rolling 4 quarters adjusted FIFO operating margin, excluding fuel and the extra week, increased by 6 basis points compared to the adjusted fiscal 2011 result. This is in line with our commitment to grow the rate slightly over time on our rolling 4-quarters basis. The third target metric is return on invested capital, or ROIC. ROIC in the fourth quarter held steady at 13.4%, the same as last year. We are committed to growing our ROIC over time, even with the higher level of capital spending. Our fourth target metric is market share growth, which we report on annually. We look at market share the way customers would look at it, where they spend their money.

According to Nielsen Homescan data, Kroger's overall dollar share of products we sell in markets where we operate grew approximately 20 basis points during fiscal 2012. The pace of our market share growth accelerated in the back half of the year. This mirrors our tonnage growth during the year. This data also indicates that our share increased in 10 of the 19 marketing areas outlined by the Nielsen report and declined in 9 areas. Walmart Supercenters, our primary competitor in 17 of the 19 marketing areas, outlined by the Nielsen report. Kroger's share increased to 9 of those 17 markets and declined in 8 markets, and overall market share slightly increased. This Nielsen Homescan Data is generated by customers who self-report their grocery purchases to Nielsen. This includes all retail outlets that sell the same products that we sell.

Strong identical sales and cost controls allowed Kroger to leverage operating expenses for our eighth consecutive year. In fiscal 2012, OG&A plus cost plus rent and depreciation without fuel and the extra week were down 48 basis points as a percent of sales. Sales growth in the fourth quarter was driven by an increase in visits per household, loyal household growth and slight increases in units per basket and per month. As a result, total units sold were up solidly compared to last year as I mentioned before.

For the full year, customer visits and monthly purchases were up, while items purchased each trip were down. The number of loyal households continued to increase, as did the number of loyal household store visits. We estimate the rate of product cost inflation declined to 1.7% excluding fuel. Once again, every store department had inflation with the exception of seafood, which had deflation.

Corporate brands represented approximately 27% of grocery department sales dollars in the fourth quarter, and grocery department corporate brands units sold were 33.5%. The mix between national brands and corporate brands fluctuates in any given quarter. Our goal is to give the best value to our customers, and we continue to be a market leader in corporate brands. Corporate brands introduced 588 new items in the grocery department in 2012. Many of these were sold under our new Simple Truth and Simple Truth Organic brands, which had fiscal 2012 sales that exceeded our internal goal by 33%. Obviously, this has been a huge home run.

We plan to continue developing innovative products that solve for unmet needs and that our customers won't find anywhere else in 2013. Our practice has been to disclose our corporate brands' share in grocery category only. The reason for not using a broader base was the introduction of new items in categories where we previously had not been broadly represented. We felt this would have portrayed our growth in a too-favorable light. With this behind us, we plan to begin giving a view of our share across a broader portion of the store in future quarters.

As you know, our commitment to improving the 4 keys of our Customer 1st Strategy, our people, products, prices and shopping experience, sets us apart from many of our other food retailers. While many of our competitors do well in one or more of these areas, very, very few excel in all 4 of them. I'd like to share a couple of examples how we are seeking to improve our connection to customers through the non-price key of our Customer 1st Strategy.

An important area of focus for us is improving our digital connection with customers through our mobile phone app and on the web at kroger.com. We offer Kroger customers the ability to check their fuel points, download coupons instantly to their shopper cart, create a shopping list and order pharmacy prescription refills virtually wherever they are. We know that customers who are digitally engaged with Kroger are more loyal than those customers who aren't, which is why we recently began promoting our digital offering to connect with more customers on our digital platforms. In a short period of time, we've seen visits to our mobile app increase by more than 120% and a 45% increase in traffic to kroger.com and growth in the number of customers who have signed up for online and mobile accounts with Kroger.

Another measure of our growing digital connection is the total number of digital coupons that have been downloaded. In December, we hit a milestone of more than 500 million digital coupons downloaded by our customers. We see only opportunity by improving our offering in the digital arena, particularly as we leverage our world-class loyalty program with dunnhumbyUSA.

Our customers are also eating more seafood as part of their weekly diet, making seafood one of the fastest-growing commodities we sell. To meet this growing demand today and in the future, we support both wild-caught and farm-raised fishery improvement projects around the world so customers can know with confidence that the seafood they buy at Kroger is always fresh, high quality and sustainably sourced. Just last month, we helped launch the Global Sustainable Seafood Initiative, or GSSI, to ensure that certification programs continue to successfully evaluate and validate our suppliers' best-in-class sustainability efforts. Kroger is proud to be the only U.S.-based retailer to hold a seat on the GSSI steering board, and we are also a founding member.

Finally, I'd like to give you an update on labor relations. Our associates play a big part in building customer loyalty. Kroger's commitment to our associates include our dedication to safety, significant investments in training, solid wages and good quality, affordable health care. We have to deliver on this in ways that allow us to operate competitively with the non-union retailers in each of the markets that we serve. Kroger's financial results continue to be pressured by rising health care and pension costs, which some of our competitors do not face. Kroger and the local unions, which represent many of our associates, have a shared objective. Growing Kroger's business and profitability will help us create more jobs and career opportunities and enhance job security for our associates. We were pleased that our associates ratified a series of new labor agreements covering stores in Portland and throughout Oregon and Southwest Washington. Currently, negotiations are underway with the UFCW for store associates in the Indianapolis area. In 2013, we have labor contracts expiring in Michigan, Houston, Dallas, Cincinnati and Seattle.

Now Mike will offer more detail on Kroger's 2012 financial results and our guidance for 2013. Mike?

J. Michael Schlotman

Thanks, Rodney, and good morning, everyone. Obviously, our numbers are a little difficult to dissect this quarter. As I go through our results, there are 3 important comparisons that we want to make sure you understand: first, how we performed compared to our guidance in 2012; second, how we compare our fiscal 2012 results to fiscal 2011; and third, to show you how we calculated our growth rate for 2013.

Net earnings for the fourth quarter totaled $461.5 million, or $0.88 per diluted share. LIFO was $0.09 per diluted share lower than estimated, and a discrete tax item added $0.02 per diluted share to the results for the quarter. These 2 items were not contemplated in our guidance. Excluding the benefit of these items, we exceeded earnings per diluted share expectations by $0.07.

Comparing our fourth quarter results to the prior year, net earnings per diluted share in the fourth quarter grew 22%. To calculate this, we excluded the extra week from the fourth quarter of 2012 and adjusted fourth quarter 2011 for the UFCW pension plan consolidation charge and to make LIFO comparable between the 2 quarters. This is illustrated in Table 6 of our press release.

We recorded a $41.2 million LIFO credit during the quarter compared to a $73.4 million LIFO charge in the same quarter last year. We reminded you in the third quarter that we manage the company without regard to our LIFO charge, and many of the items we discuss are on a FIFO basis. So when we develop our expectations for any given year, we estimate LIFO last. The reason for this is LIFO is merely an accounting convention. If LIFO is lower than the prior year, our EPS growth rate will be higher than our targets. And if LIFO is higher than the prior year, our EPS growth rate will be lower than our targets. This is why we excluded the benefit of our lower-than-expected LIFO charge when comparing to guidance and calculating growth rates.

FIFO gross margin excluded retail fuel operations and the extra week decreased 43 basis points from the same period last year. Operating, general and administrative costs plus rent and depreciation, excluding retail fuel operations and the extra week, declined 70 basis points as a percent of sales compared to the prior year's adjusted fourth quarter.

Before I move on to discuss Kroger's full year 2012 results, I'll share some data on our retail fuel operations. We disclosed many items with and without fuel due to its effect on operating costs and gross rates, but we view fuel as a core department that over time is expected to contribute to earnings per share growth. About half of our supermarkets have fuel centers today. In the fourth quarter, our cents per gallon fuel margin was approximately $0.127 compared to $0.121 in the same quarter last year after adjusting 2,000 -- after adjusting for the additional week. For the full year, the cents per gallon fuel margin was roughly $0.139 compared to $0.138 after adjusting for an additional week.

Turning now to Kroger's full year 2012 results. For the full year 2012, total sales increased $96.8 billion or -- to $96.8 billion, or 7.1% compared with the prior fiscal year. After adjusting for the extra week in fiscal 2012, total sales increased to $94.8 billion, or 4.9% compared with the prior fiscal year. Excluding fuel, total sales increased 6% over that same time period. And further adjusting for the extra week, total sales excluding fuel increased 4%. Identical supermarket sales without fuel increased 3.5% in fiscal 2012 compared with the prior year.

Net earnings for fiscal year 2012 totaled $1.5 billion, or $2.77 per diluted share. These results include LIFO being lower than our guidance by $0.08 per diluted share and the discrete tax item that added $0.02 per diluted share in the fourth quarter and the $0.14 per diluted share effect from the credit card settlement and a reduction in the UFCW pension accrual in the third quarter. Collectively, these totaled $0.24 per diluted share and were not contemplated in our guidance of $2.44 to $2.46 per diluted share.

So comparing our performance without these items to guidance, we exceeded the high end of our range by $0.07 per diluted share. Comparing our 2012 results to the prior year, net earnings per diluted share in 2012 grew 16%. In order to calculate this, we believe adjustments to 2012 and 2011 are required. Adjustments for 2012 included the benefits gained from the pension accrual and credit card settlement in the third quarter and excluding the extra week. In 2011, adjustments included the UFC pension plan consolidation charge in the fourth quarter and making LIFO comparable to 2012. This calculation is illustrated in Table 6 of our press release. The fact that we beat our own earnings guidance for the year even after raising it upwards several times throughout the year demonstrates the underlying strength of our core business and the bit of our -- benefit of our share buybacks to increase shareholder value.

Kroger recorded a full year LIFO charge of approximately $55 million. The company's fiscal 2011 full year LIFO charge was $216 million. As Dave and Rodney said earlier, we expect -- currently expect a slightly expanded FIFO operating margin on a rolling 4-quarters basis. On this basis, FIFO operating margin excluding fuel and the extra week increased by 6 basis points. This also excludes the benefits of the credit card settlement and the reduction in UFC pension accrual, both of which incurred in the third quarter of fiscal 2012. We are pleased that we were able to deliver on our commitment, and it remains our goal to continue to slightly improve Kroger's non-fuel operating margin rate over time.

For 2013, our planned uses of cash remain unchanged. We're going to fund capital investments, repurchase shares, pay dividends to shareholders and maintain our current investment grade debt rating. Capital investments, excluding acquisitions and purchases of lease facilities, totaled $2 billion for the year compared to $1.9 billion in 2011. For 2013, we expect capital investments to be in the $2.1 billion to $2.4 billion range for the year.

During the fourth quarter, Kroger repurchased 2.2 million common shares for an investment of $57 million. Since the end of the fourth quarter and through the close of the market yesterday, Kroger has $466 million remaining under the $500 million stock repurchase program announced in October of 2012. Net total debt was $8.6 billion, an increase of $470.6 million from a year ago. Kroger's net total debt to adjusted EBITDA ratio was 2.04 compared to 2 during the same period last year. Our objective is maintain our current debt rating, and we believe a net total debt to EBITDA ratio of 2x to 2.2x will support this objective.

Now I would like to outline our specific growth objectives for fiscal 2013. Kroger anticipates identical supermarket sales growth, excluding fuel, of approximately 2.5% to 3.5% for fiscal 2013. We expect identical sales to trend up during the year as we lap higher inflation early in the year and the effect of generics in the second half of the year.

Full year net earnings for fiscal 2013 are expected to range from $2.71 to $2.79 per diluted share. This equates to the company's long-term growth rate of 8% to 11% from the adjusted fiscal 2012 earnings per diluted share of $2.52, as shown in Table 6 of our press release. To calculate our base, we excluded the benefits gained from the pension accrual and credit card settlement in the third quarter and the extra week, and we also normalized LIFO.

Shareholder return will be further enhanced by a dividend of 2% to 2.5% for a total shareholder return of approximately 10% to 13.5%. When looking at our cadence by quarter, we expect the following: the low end of our growth rate -- we expect quarter 1 to be at the low end of our growth rate, inflation is expected to be lower in the first quarter of 2013, and the growth of our pharmacy business won't be as substantial as last year's first quarter. We expect the second and third quarters to be at the high end to above our growth rate expectations as inflation is expected to become more comparable between the years, and we expect our ID sales to be trending up. For the fourth quarter, we expect lower than the prior year on a 12-week to 12-week basis, due primarily to a budgeted LIFO charge of $13 million versus a credit of $41 million for the fourth quarter of 2012.

We expect our full year LIFO charge to be approximately $55 million for 2013. This is the same as our LIFO charge for fiscal 2012. Where it ultimately ends up could be one of the factors that will determine where we land in the $2.71 to $2.79 EPS range. A higher LIFO charge would move us down in the range and a lower LIFO charge would move us up in the range.

As I said earlier, we expect Kroger's full year FIFO operating margin rate in 2013, excluding fuel, to expand slightly compared to fiscal 2012 results. This morning, we filed an 8-K summarizing the guidance and financial strategy that I just discussed and some additional items including pension contributions and expense and our tax rate expectations.

Now I will turn it back to Dave.

David B. Dillon

Thanks, Mike. And as you can tell, we're very pleased with our financial results for the quarter and the year. Kroger's performance is the result of our associates' hard work and commitment to make each day better for our customers. We grew our business in 2012. And building on that momentum, we expect to deliver the growth in 2013 that we outlined at our investor meeting in October.

Now we look forward to your questions.

Question-and-Answer Session

Operator

[Operator Instructions] Your next question comes from the line of Stephen Grambling from Goldman Sachs.

Stephen W. Grambling - Goldman Sachs Group Inc., Research Division

I remember at the Analyst Day, you had referenced the incremental CapEx would be a pressure to your SG&A in the near term, yet you still held that 8% to 11% range. Is there something as you look out to 2013 that gives you greater confidence than the long-term range and maybe if you can just give us a little more color?

J. Michael Schlotman

Well, the increased capital, it'll have an effect on holding down our ROIC ability to grow that in the short term. We do expect to continue to not have that go down but, as Rodney said, grow it in the near term. As we open the stores, if you look at our guidance, we opened up 44 stores in 2012 and we're projecting 45 to 50 in 2013. So that's not a dramatic increase year-on-year that would have any kind of material effect on -- or from a preopening cost standpoint or the ramp-up of those new stores.

Stephen W. Grambling - Goldman Sachs Group Inc., Research Division

Okay, that's helpful. And then one other quick detail. On the pharmacy business, how should we be thinking about the generic shift impact in the quarter? And I know you referenced that it'll be a little bit less next year, but maybe if you can help us quantify that?

David B. Dillon

Let me make a comment first and then I'll ask Rodney to answer the specific question. But I wanted to make the broad observation that our pharmacy business this past year was outstanding. And I want to make sure that anybody who's touched our pharmacy business in our organization knows how we feel about that. We were absolutely thrilled. So Rodney, you want to comment about the generic effect?

W. Rodney McMullen

Yes. The generic effect kept getting bigger and bigger as we went through the year, and we're just now starting to cycle the beginning parts of that. So the heavy -- the largest effect will be in the first and second quarters. It'll get a little smaller in the third and fourth, but not tremendously smaller. And we also obviously have a few more drugs going to generic. So we believe it will be a headwind from a sales standpoint throughout the year. One of the things that's very positive, as Dave mentioned, we had a great year on pharmacy. And so far this year, we've continued to have a strong script count growth in pharmacy as well.

Operator

Your next question comes from Andrew Wolf from BB&T Capital Markets.

Andrew P. Wolf - BB&T Capital Markets, Research Division

Wanted to ask you, Dave, when you mentioned the variability in sales, I'm not surprised to hear that given all that's going on in the macro environment. But has that increased a lot compare -- I think you had mentioned it last quarter, too, and I asked you about it. But is that something that's -- the amplitude, the amount of variability is increasing. Or is that something to call out that we should think about?

David B. Dillon

I think we've seen it more amplified in the last 6 months or so than it had been, and that's why I called it out last quarter. And I think what we saw this last quarter was much of the same. Now last year was also hampered by the fact that there was a 2-day swing in the calendar because of leap day a year ago and when you come to the first of month or end of the month. And we've now rounded that, so we don't have that issue to contend with. But the issues that I was referring to really is the fragile nature of the consumer, and I think that they ended up swinging with -- almost with that day's news. Now that may be a little bit of an exaggeration, but you can see, as we do our polling, you can see heightened awareness. In January, for instance, on taxes -- I mean, that just shows crystal clear that it was on their minds. And I think it's things like that, that caused them to have that swing in how they approach their own daily living.

Andrew P. Wolf - BB&T Capital Markets, Research Division

So that polling information, that's correlating somewhat with sale -- behavior and people...

David B. Dillon

Well, actually, we're calling out specifically in this case because sometimes, we can see behavior in sales as we did actually see it a couple years ago when the debt ceiling was been debated. But this time, when you look at the payroll tax, lots was written about the payroll tax, and lots of people were assuming. Of course, it's early in that process, so I don't know that we'll feel differently -- could feel differently down the road. But right now, what we see is taxes and the payroll tax and other issues like that on people's minds in a very noticeable way, and we see the variability from day to day, week to week. But we do not see what we think is a dollar sales impact in total on what's happening from the payroll tax.

J. Michael Schlotman

The other thing on top of that is, in some states, government transfer payments, the way those payments are made, have changed, and we haven't yet cycled a year with the new schedule on transfer payments being made to recipients. So that creates some of the volatility as well.

Andrew P. Wolf - BB&T Capital Markets, Research Division

Okay. One follow-up then I'll cede because of your one-question rule. Did the delay in tax payments, do you think that also affected the cadence and the variability in the sales results?

David B. Dillon

It certainly could have. It wasn't a big enough factor that we would be able to -- that we were able to discern it specifically in our minds. But it's one of the factors that I think we would list, and it's what was going on in the consumer's world.

Operator

Your next question comes from the line of Mark Wiltamuth from Morgan Stanley.

Mark Wiltamuth - Morgan Stanley, Research Division

It's Mark Wiltamuth. We saw a number of other retailers show some holiday cautiousness on the part of consumers. Did you see any of that across the demographic cuts that you do as you look at your data?

David B. Dillon

Well, of course there were some signs of caution. But on the other hand, actually, we were pleased with our holiday selling period and the weeks that followed, actually, too. So I would say nothing that should be called out at this point. Rodney, you want to add anything to that?

W. Rodney McMullen

No.

David B. Dillon

No.

Mark Wiltamuth - Morgan Stanley, Research Division

And Mike, if you could maybe quantify your health care and pension headwinds because you still have a strong earnings growth story here, but it sounds like there are some headwinds we just can't see behind the scenes.

J. Michael Schlotman

Well, health care and pension headwinds are always out there. We -- in the 8-K, we filed what we expect our contributions to the union funds to be for pensions, and that dollar for dollar is an expense item. Whatever we contribute is an expense. The other item that's out there is the amount of expense we expect for the company-sponsored pension plan. And that's actually a little lower next year than we would have originally expected. But those items are always out there. It's one of the reasons why our identical sales performance is so important. And our goal is to be able to grow identical sales faster than our underlying costs are going so we can make the operating profit margin growth be what we expect.

Operator

Your next question comes from the line of Ajay Jain from Cantor Fitzgerald.

Ajay Jain - Cantor Fitzgerald & Co., Research Division

Maybe I'll address this to Mike Schlotman. I noticed your D&A was lower compared to last year, and I think it was down more materially if you account for the calendar shift. So just wondering, is there any change in your schedule? Can you just talk about what's driving that decrease? And what's implicit in your 2013 guidance for D&A expense?

J. Michael Schlotman

I wouldn't say there's anything specific that winds up being in there. Some of it's just reflective of some older stuff becoming fully depreciated. As you know, when you look at our CapEx, keep in mind not everything we spend capital on gets depreciated because we like owning our properties. So therefore, we buy the land, and that doesn't wind up in depreciation. So it doesn't affect that. We would expect the depreciation to be up a little bit in 2013 compared to 2012 on an apples-to-apples basis.

Ajay Jain - Cantor Fitzgerald & Co., Research Division

Okay. And just as a follow-up, maybe you guys mentioned it earlier and I might have missed it, but I just wanted to ask if you could comment on the intra-quarter ID trends?

David B. Dillon

Yes. The ID trends grew. By the 13th period, they were the strongest of the quarter, which is our last period of that quarter. And in fact, you didn't ask about it, but I'll add the additional 4 quarter -- or 4 weeks, rather, 4.5 weeks that we've had since that time. If you take the 13th period and the 4.5 weeks since that time, they both were about the same, and they both exceeded actually slightly above what our sales range guidance is for the year 2013. So we're pleased with that. We did have some weather in the last few weeks that has positively helped our sales. But even if you take that out, I think we were solidly -- certainly above the midpoint of what the guidance is that we gave.

Operator

Your next question comes from the line of John Heinbockel from Guggenheim Securities.

John Heinbockel - Guggenheim Securities, LLC, Research Division

I wanted to drill down a little bit on sort of the market share performance. So if I'm right, the share gains have moderated a little bit, say, from '11 and '10. Is that just because the prior gains were unsustainable and where we are now is more sustainable? Or I don't know how you've dove into that and taken a look at that. And then as part of that, if you then looked at loyal households, you looked at different customer groups and/or different competitors, is there something where, as you dice it, the market share gains are actually stronger or accelerating with certain customers and again, certain competitors?

David B. Dillon

Let me take a shot at the market share question, and then I'll see if Rodney wants to bring that and the loyal households together. But on the market share, I would encourage you not to think of it as an accounting number and with precision. I would think of it as more a directional picture. It's a very helpful indicator of where things are headed, but I think it's more important really to look at it in combination with other things. So the first thing we noted on our market share was that it has been growing in the second half of the year so that you can assume that the comparison for the year, that we're -- we may have had -- we had some -- we did have. In fact, we talked about some of the struggles we had with tonnage early last year, and that's changed. Our tonnage through the last half of this past year was strong. And in fact, as I indicated on the sales so far in the 4.5 weeks we've had it in this quarter, our tonnage continued strong, too. So if you combine the sales trends we've experienced, the tonnage we have experienced with what the ACNielsen material shows us, it's certainly directionally strong. Yes, it may be a little bit less than what it had been, but I don't -- in terms of market share. But I don't think it's a meaningful variance. I don't think that the numbers are that accurate that we can see that kind of variance in them. Rodney, you may want to add to that, and feel free to comment on the households.

W. Rodney McMullen

Yes. I would -- I agree completely. And as Dave and I both mentioned, and I mentioned earlier, we've improved during the year. So actually, the last half of the year, the gains were better than the overall year. When you look at customer segments, the value customer early in the year, we were very soft on share with that type of customer, and it's improved nicely. But that would have been the -- earlier in the year, that would have been a very soft area of our share by segment. If you look at more a traditional and upscale customer, those customer gains were really, across the year, and continue to be very nice.

John Heinbockel - Guggenheim Securities, LLC, Research Division

And when you guys look at -- to Dave's point, you think it's -- share and comp together is probably a good matrix to use. And the levels we're at today, you're comfortable with. I would also think as the capital program picks up, share will pick up. Maybe there's some cannibalization, but share should pick up as you roll out more stores, correct?

David B. Dillon

I would agree with all of that. I would add to the metric. I would add tonnage, too. So I'd look at ID sales, tonnage and then what the ACNielsen material shows. And I'd look for the intersection of what those 3 things together are telling us. That's how we look at it.

W. Rodney McMullen

And there's not one single number that gives you all the answers, and that's one of the things that your comment really highlights, is you really need to look across more than one to get a feel overall. But at the end of the day, we felt very good about the progress we made on share gain last year in all markets.

Operator

Your next question comes from the line of Meredith Adler from Barclays.

Meredith Adler - Barclays Capital, Research Division

I would like to actually talk a little bit more about tonnage. I thought there were comments that you were making last year that the tonnage weakness was, to some extent, a result of high inflation at the beginning of the year. And then produce was deflationary, so you started to see some tonnage improvement. Is it fair to think about it in that sort of broad sense about the consumer and pricing? Or do think that whatever happens with tonnage is just based on what you guys do?

David B. Dillon

Meredith, I think it's actually both, personally. We were -- I think we admitted a little surprise in how quickly tonnage returned when inflation subsided. I thought it would take longer than it did. And so obviously, that has -- it has something to do with the fact that inflation subsided. But I also would like to think that we positioned ourselves really well to take advantage of that situation by the investments we've made in price and with the improvements that we continue to make in the other 3 keys in our stores. So I really think it ends up being both.

Meredith Adler - Barclays Capital, Research Division

Okay, great. And then I wanted to -- you had great success in terms of controlling expenses in the fourth quarter, and congratulations on that. I know there's always a whole lot of different things you're working on, but is there anything that particularly stood out in the fourth quarter? And did the extra week, which we had guessed would benefit $0.07, and it benefited by $0.11, did the extra week contribute particularly much to that improvement in SG&A -- or OG&A?

J. Michael Schlotman

Yes. Thanks, Meredith, for the comment. And on the OG&A improvement that I mentioned on the call, it was adjusted for the extra week so we did not get any benefit in the number that I shared. In terms of specifics to call out, it was really broad based. It's almost every division of the company, and it's really core operations. Obviously, having good tonnage growth and identical sales gives you some tailwind, so we had that across the whole company, which was helpful, but just very good execution on our strategy and the things that we've identified. I wouldn't highlight one, Mike or Dave. I...

W. Rodney McMullen

No, I agree with you. It's actually refreshing that there's not one to highlight. That means there's a lot of things contributed to it, and the fact that it's broad based can make it sustainable.

David B. Dillon

And I do tend to look at that number over a longer period. One quarter is good. The number Rodney used in his -- in the prepared comments was the full year number, and I think that's a better reflection of how we did. Now that's still pretty darn good. But I tend to look over a long haul because the longer the period, the more likely that what you did is sustainable. And the things we did were really process-oriented. And changes that our customers actually either prefer or don't notice, either one.

Meredith Adler - Barclays Capital, Research Division

And then my final question would just be about labor, and maybe you could talk about -- you don't have to talk about any individual contract, but in terms of generally the negotiation, are you able to stick with kind of the total numbers you want to get in terms of labor cost increases, balancing the health care, pension and wages?

David B. Dillon

Well, there's 2 balances we actually -- probably more that we try to make each time. First -- or probably second is the one you mentioned, is balancing the health care costs, pension costs and so forth, and those are going to continue to be issues that need to be addressed. But the first balance that we actually try to address is on one hand, we do have the natural tension of wanting and needing to keep our expenses down low as a company. On the other hand, we genuinely want our associates to be fairly paid, certainly paid based on what the market rates are and so forth. We have a workforce that we've very proud of, and we don't look at this as something that is some opposition argument. We're trying to actually work on their side on this argument. We're trying to find a way to balance the business needs with what our associates need. So that's how we think of the labor. Now, Rodney, you may have some specifics.

W. Rodney McMullen

No.

David B. Dillon

That's it.

Operator

Your next question comes from the line of Jason DeRise from USB (sic) [UBS].

Jason DeRise - UBS Investment Bank, Research Division

It's Jason DeRise at UBS. I wanted to ask a question on guidance, and I guess it's multipart and so I'm going to put them all together, and then what you're able to share will be great in terms of the color. So obviously, we have the square footage piece of that, but it's not a net. So I'm wondering if you can share what you're planning in terms of closures. Obviously, you're not going to be able to share what acquisitions you're planning on doing, unless you want to. Feel free to. And then in terms of the FIFO x-fuel gross margin, if you can share some thoughts on what you think between the gross margin element and the SG&A leverage? And then I guess the other ones that aren't mentioned directly but are going to be important in understanding this is the fuel contribution expected and the buybacks expected. So basically, the question is asking for more color on the guidance.

J. Michael Schlotman

The square footage at this point in time, we always give what we expect gross square footage to do. Our model is not built needing any acquisitions to make our numbers, so that's why we always say excluding acquisitions. If there were something out there that worked, it would be something that's additive to our results because we don't need to do anything to have -- to reach our growth expectations. Relative to the closures, while there are certainly a handful that are out there, that's something that occurs throughout the year as we constantly look at our portfolio of assets and look at what stores may need to close. I don't have a specific number for that at this point that we would -- that I would be willing to disclose. Relative to...

Jason DeRise - UBS Investment Bank, Research Division

Can I ask if it would be a -- we would expect a net positive number? Because I mean I guess, last year, there was a positive gross number out there, but it...

J. Michael Schlotman

It's been a net positive for the last several years. Sometimes, what happens is we -- there have been occasions where we've closed a couple smaller stores and opened up one bigger store. And it looks like our store count goes down, but that bigger store is actually more square footage than the 2 stores we closed on a combined basis. So that certainly helps. When you look at the FIFO fuel gross margin and without fuel gross margin and SG&A leverage, we don't give specific guidance on those line items. We always expect to get SG&A savings that we'll invest back on our 4 keys, whatever line that key might fall in the income statement. And our overall goal was to grow our operating margin for the year slightly from the prior year, and that would remain our goal for this year. And relative to fuel contribution, I would say, typically, when we go into a year and when you, for instance, when you look at the fourth quarter of the year, it was only $0.01 difference without the extra week between the 2 years' fourth quarters. So the growth in that is not something that's a huge driver of the 8% to 11% earnings per share growth rate.

W. Rodney McMullen

Usually, we just use what, Mike, a 3-year rolling average in terms of the actual results and use that as a base point.

J. Michael Schlotman

Right. Look at gross margin per gallon over the last 3 years, and that's about where we start.

Jason DeRise - UBS Investment Bank, Research Division

Okay. All of that's useful. I guess, in terms -- just to follow-up on the gross margin element. Within this last quarter that you talked about, I guess it's your inflation cost that you're talking about at 1.7%, but your large national competitor was talking about how their basket inflation was 0.8%. So I mean, if you're passing through that, most of that 1.7%, there's a gap there. I know a lot of people in the market are trying to interpret how the new 8% to 11% guidance -- what that means in terms of your aggressiveness in price or if you're pulling back. So if you can share some thoughts on that, if maybe your pricing isn't as aggressive in the quarter as it has been relative to your competition?

W. Rodney McMullen

It's really a little bit of apples and oranges. What we measure is our estimated inflation based on using government statistics on inflation by category at the mix of business we have. If you look at the actual basket that customers are buying from us, it would have a completely different inflation rate, and it would actually be meaningfully less, especially if the customer has pharmacy in their basket, it's substantially less. So it's -- those 2 are really apples and oranges. And what we try to give on an inflation rate is more based on our sales mix and some of the government statistics out there.

Jason DeRise - UBS Investment Bank, Research Division

Do you feel that you maintained or improved your price position during the quarter?

W. Rodney McMullen

Our internal measures would all show that we've improved our relative price position versus all our major competitors, not just the one that you mentioned.

David B. Dillon

And we have no expectation that, that will change.

Operator

Your next question comes from the line of Karen Short of firm BMO Capital.

Karen F. Short - BMO Capital Markets U.S.

Back on the inflation and the LIFO for a minute. When you guys gave your guidance for the LIFO charge for the full year in your third quarter call, it seemed like you kind of expected inflation to come in where it came in for the year. So I guess I'm confused about the credit this quarter. And then looking to next year, I guess what are your expectations on inflation for next year? Because given the LIFO charge for this year, just kind of going back to your P&L in prior years, it would look like you're kind of expecting like 1-ish percent.

J. Michael Schlotman

Yes. In the -- at the end of the third quarter when we gave our expectation for LIFO, our expectation at that time was that our full year LIFO charge would be $125 million. So through 10 periods, we had expensed enough to have 10/13 of $125 million behind us. So when the year wound up at only $55 million by the time we got to the end of the year, we had almost $95 million, a little over $95 million accrued. So we had to reduce that number down to the $55 million, which led to the credit in the fourth quarter. That make sense?

Karen F. Short - BMO Capital Markets U.S.

Yes, that makes sense. Okay. And then for next year, your inflation expectations?

J. Michael Schlotman

Relative to next year, at this point in time, we're estimating LIFO to be at $55 million for next year, just like this year. As we sit here today, with inflation in the 1 percentage kind of range, maybe a little over, depending how pharmacy winds up affecting that, we think that's the best guess at this time. The other thing to keep in mind is inflation throughout the year has no effect on LIFO. So the fact that last year was very high early in the year and then it trended down throughout the year doesn't really affect LIFO. It is a single day point in time calculation of how many products do I have this year, what was last year's price and this year's price on that particular day. Now that's a little bit of a Reader's Digest version of how the calculation works, but it gets you close.

Karen F. Short - BMO Capital Markets U.S.

Okay, that's helpful. And then wondering if you'd be prepared to give CapEx allocation for next year?

J. Michael Schlotman

You mean how much capital investment we plan to make? Or...

Karen F. Short - BMO Capital Markets U.S.

No, the allocation in -- I mean, you gave the dollars in your 8-K, but wondering if you could give the allocation?

J. Michael Schlotman

You mean allocation by what we're sort of spending on stores and things like that?

Karen F. Short - BMO Capital Markets U.S.

Category. Yes.

J. Michael Schlotman

Well, I wouldn't get into the exact dollar amount of allocation, but we also gave guidance that we expect to do one -- a few more stores, new relocate and expands in 2013 compared to 2012 and probably a comparable number of remodels.

W. Rodney McMullen

Most of the dollar increase would be driven by the store-in program that we've outlined incrementally.

J. Michael Schlotman

And the other thing to keep in mind is as we're increasing our capital spend to focus on existing and some new fill-in markets as well as exploring new markets, it takes a while for those stores to open. So we'll be spending dollars in 2013 that wind up being 2014 store openings. So the growth in that store count takes a while because the spending happens so far in advance of that. So it'll be a slow growth or a slow build into the higher store count.

Karen F. Short - BMO Capital Markets U.S.

Okay, that's helpful. And then just a last question, maybe if you could give some color on both the competitive and the acquisition environment? It seems like, on the acquisition side, there may be some assets coming up or presenting themselves shortly? And then comments on the competitive environment?

David B. Dillon

Well, on the acquisition environment, I would just give you the comments we've made before. We don't generally comment. What we've tried to do is share with you our philosophy how we approach that, and that really hasn't changed at all from the past. As to the competitive environment, I would characterize it as we have recently, it's still a hotly contested market, a very competitive kind of a business. That's the nature of our business. But I see people making rational choices. I don't see it as performing irrationally, which is a good thing in our minds and, I presume, in yours too. Rodney, anything else you want to add to that?

W. Rodney McMullen

No. No. No.

David B. Dillon

Okay.

Operator

Your next question comes from the line of Edward Kelly from Credit Suisse.

Edward J. Kelly - Crédit Suisse AG, Research Division

So I was hoping we could dig into the gross margin, the FIFO gross margin a little bit this quarter. It was a little bit lighter than what I thought it was going to be. And I think if you were to look at it and remove the generic benefit, my guess, and this is where I'm hoping you could help, but my guess is the selling gross margin this quarter is probably weaker than what we've seen otherwise this year. So could you maybe just give us some more detail on selling, what's going on, on the shrink side, maybe the non-selling side and how this -- how the margin played out versus what you were expecting?

W. Rodney McMullen

It really played out very close to what we were expecting. And as you know, one of the things that we always work on is making sure we balance with our expense improvements. And any given quarter, you can't always get a balance perfectly. But for the year, we work really hard to get those 2 balanced. And it's driven as much by balancing those 2 pieces. If you look at it versus what we were expecting, it was very close to what we were expecting. Obviously, the generics improved gross margin, selling gross margins for the quarter. But overall, we were pleased with where it ended up and felt good about the balance. And we felt good about our relative price position in the market from a competitive standpoint.

J. Michael Schlotman

Rodney, I agree. And when you look at operating profit margin, which is what we always focus on, the fact we grew it by 6 basis points when really through 3 quarters year-to-date we were slightly negative, demonstrates the strong cost control. And the fact that we really -- as Rodney said, our -- we executed the plan we had, and it came to fruition in the fourth quarter because a lot of what occurred was somewhat planned. It was planned. So...

Edward J. Kelly - Crédit Suisse AG, Research Division

Okay. And on the repo front, share repurchase, how should we think about '13? I mean, it's obvious that you're not probably going to buy back nearly as much stock this upcoming year as you did in the past. Will you still be borrowing to maintain a leverage ratio and then using that to buy stock?

W. Rodney McMullen

Again, the use of our cash flow, including maintaining our net total debt to EBITDA ratio in our 2x to 2.2x range, will really be used for all 4 of the things we laid out, and that's to fund our capital investments; to repurchase shares; maintain and hopefully, over time, grow our dividend; as well as maintaining our current credit rating. So we'll balance all of those needs. Relative to the stock share buyback, we would expect to continue to buy in shares. We obviously didn't buy as much in the fourth quarter as we had throughout the course of the year. That was not any kind of a statement on where our share price was in the fourth quarter relative to the rest of the year. It was really based on the fact that we were cognizant of where our debt levels were going into the fourth quarter, and the fact of the way the rating agencies look at our debt level, things like our $250 million contribution to our EBIT [ph] at the end of the year, it's a very smart thing to do from a tax standpoint because we accelerate the tax deduction. But even though that burns off in the first few months of the next fiscal year, they treat it as debt at the end of the year. So I would have -- it made great return sense to make that contribution and get the tax deduction this year versus next year and balance that with how much free cash flow that leaves me to buy in shares. So we try to balance all of our needs on a quarter-by-quarter basis.

Operator

Your next question comes from the line of Kelly Bania from Bank of America Merrill Lynch.

Kelly A. Bania - BofA Merrill Lynch, Research Division

I was wondering if you could go back to some comments you made a little earlier about the value and the traditional and upscale consumers and how the value kind of improves through the year. I was wondering, one, what do you think has driven that? Have you been catering to that a little bit better as we move through the year? And two, how do you think the volatility -- the mild volatility that you saw in January, how did that impact those different customer segments?

W. Rodney McMullen

Yes, in terms of -- it would definitely have been targeted things that we did looking at the customer. It's one of the things that's such a wonderful benefit of our partnership with dunnhumby. That example was on a value customer, but we'd really look at it on every customer segment. We're constantly testing marketing, direct marketing with different customers and different methods of direct marketing. And when something connects, we do more of it. When it doesn't connect, we don't do it as much. And when we're not satisfied with our performance, we will work and put some extra focus there. So it really was something that we weren't pleased with, we weren't connecting as well as we liked and made some changes to make sure that we did, and that improvement happened. In January, it's really hard -- as Dave mentioned before, it's really hard to see some of the external numbers affecting -- the external things that went on, we don't really see it in our numbers. We believe some of that is probably really driven because we had connected better with some of those customer segments for some of the things we had put in place. What happened at other companies, we really don't have insight into that. But we really didn't see the -- in total, the variability as we mentioned from a day-to-day basis we do.

Kelly A. Bania - BofA Merrill Lynch, Research Division

Great. And then if I can just squeeze in one more follow-up. Can you give any color on the tonnage trends? As you look back over the year between the core grocery categories and the fresh, you mentioned kind of the seafood being strong. But any more color there you can give us?

W. Rodney McMullen

It improved throughout the year, and it was broad based on the improvement in all categories. So it really would be difficult to call out one area being stronger than the other. The only area that I would probably specifically call out is, obviously, pharmacy had great script count growth throughout the year, and our natural foods area had a phenomenal year as well. And it was strong throughout the year.

Operator

Your final question comes from the line of Greg Hessler from Bank of America.

Gregory Hessler - BofA Merrill Lynch, Research Division

So I apologize, I missed a little bit of the beginning of the call. I was just wondering if you could talk about the upcoming maturity, the $400 million maturity in April? Do you plan to turn that out into debt capital markets?

J. Michael Schlotman

Yes. We've talked -- we have not talked about that yet on the call. We actually had a maturity right at the beginning of this fiscal year that we drew down -- that we actually have refinanced with commercial paper on a temporary basis. And then, as you said, we have the other maturity in April. Our expectation would be that sometime in April, that we would term those out. If you look at our SEC filings, we already have a significant amount of that kind of an issuance contemplated and hedged out from an interest rate standpoint, and that coverage goes out until April. So it may not be the exact day. But dependent on market conditions, I would expect, somewhere around that time, we will wind up terming those out.

Gregory Hessler - BofA Merrill Lynch, Research Division

Okay. So that could be maybe up to $1 billion in size. Any thoughts on tenor there? Do you have any preference for shorter-dated stuff? Or should we be thinking about 10s or 30s? Or what are your thoughts there?

J. Michael Schlotman

We'll let the market tell us where the sweet spot is. Sometimes, we may start out with a particular idea. And then we find out, as you start to look at the market on that particular day, that there's a hole on our maturity chart that fits with what the market has an appetite for on that particular day. So rather than lock myself in, when we go to market, we'll let the market tells us what makes the most sense.

David B. Dillon

And before we end the call today, I would like to share a few additional thoughts with our associates who we encouraged to listen in today. 2013 marks the 130th anniversary when Barney Kroger opened his first store in Cincinnati, Ohio. This is an amazing accomplishment, and yet 2 of our banners have been in business even longer: Ralph's division, which is 140 years old; and the Jay C Foods division, which celebrates its 150th anniversary this year.

Our heritage of enduring growth and reinvention gives us great confidence for the future. Each of you played a big part in the success in 2012. Working together as a team, we made shopping more easy and efficient for our customers, and they're giving us credit for all of our hard work. We also helped keep costs under control so that we could invest the savings and lower prices. A special thanks to each of you for your contributions.

This week, we also thank 36 special Kroger associates for their extraordinary efforts for our company and our communities. We honor these associates because they represent strong leadership, courage and character. They live our leadership model and our values by leading effective teams, serving local community organizations, making healthy lifestyle changes and more. You can find more about each of our honorees by watching our live quarterly broadcast tomorrow or reading their inspiring stories at the greatpeople.me website in the coming weeks.

That completes our call today. Thank you all for joining us.

Operator

Thank you. Thank you for your participation in today's conference. You may now disconnect. Good day.