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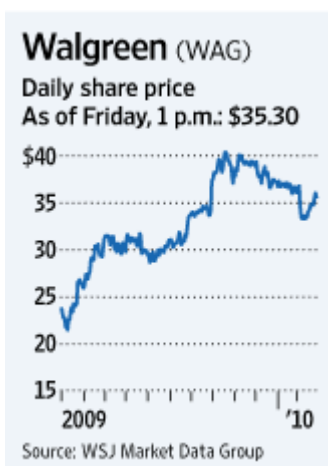
BARRON'S INSIGHT | FEBRUARY 28, 2010

With Acquisition, Walgreen Has a Prescription for Growth

By ROBIN BLUMENTHAL

Walgreen, the nation's largest drug-store chain, is about to take Manhattan and its environs -- with its nearly \$1.1 billion plan to buy Duane Reade, the New York metropolitan area's biggest drug-store chain.

The purchase of Duane Reade's 258 stores, coupled with a makeover of Walgreen's more than 7,100 other stores, could help the Deerfield, Ill.-based company return to consistent double-digit earnings growth, and prove rewarding to shareholders. Earnings per share jumped 20%, to 49 cents, in the fiscal quarter ended Nov. 30, on a 10% rise in revenue, while operating cash flow tripled to \$1.2 billion, year over year.



The Duane Reade deal, expected to close by August, could shave 10 cents from earnings in fiscal 2011. However, "it would have taken us 20 years to get this footprint in New York, with a lower rate of return," says Wade Miquelon, Walgreen's chief financial officer.

Analysts expect Walgreen to earn \$2.30 a share in fiscal 2010, 14% above fiscal '09's level, on a 7% rise in revenue, to \$67.7 billion. The forecast for fiscal '11 is \$2.70 a share.

Andrew Wolf, an analyst at BB&T Capital Markets, thinks Walgreen may be understating the savings it could realize from the Duane Reade deal. Mr. Wolf maintains that the company could make \$2.95 a share in calendar 2011. And he says that the

stock, which has rallied 35% in the past year, to the mid-\$30s, could trade for at least 16.3 times expected earnings -- below its historical average price/earnings ratio of 25, but above today's 11. That implies a share price of \$48.

Walgreen is sticking with its \$2 billion, four-year stock buyback program, which also could help lift earnings per share and the stock. In addition, the company has targeted a 35% dividend-payout ratio -- the percentage of earnings it pays out to shareholders -- compared with 24% now. Walgreen currently pays 55 cents a share annually.

Elizabeth Bramwell, manager of the Sentinel Capital Growth Fund, a Walgreen investor, expects the chain to benefit as more high-margin generic drugs hit the market, starting in 2011. Walgreen

controls 19% of the U.S. prescription-drug market, and operates onsite clinics for companies such as [Walt Disney](#).

It recently struck a deal with [Caterpillar](#) to buy prescription drugs for its employees. Mr. Miquelon says Walgreen has about 200 corporate clients under similar arrangements. With Duane Reade onboard, expect that number to grow.

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