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Webinar Presentation:

J.C. PENNEY COMPANY INC.

Robert C. Pike, Senior Industry Analyst

February 5, 2013

Today's Agenda

1. Economic Overview

2. Company Profile & 3Q12 Summary

3. Financial History

4. Recent Developments

5. Strategic Initiatives

6. Issues & Conclusions

7. Q&A

ECONOMIC OVERVIEW
U.S. Unemployment Rate

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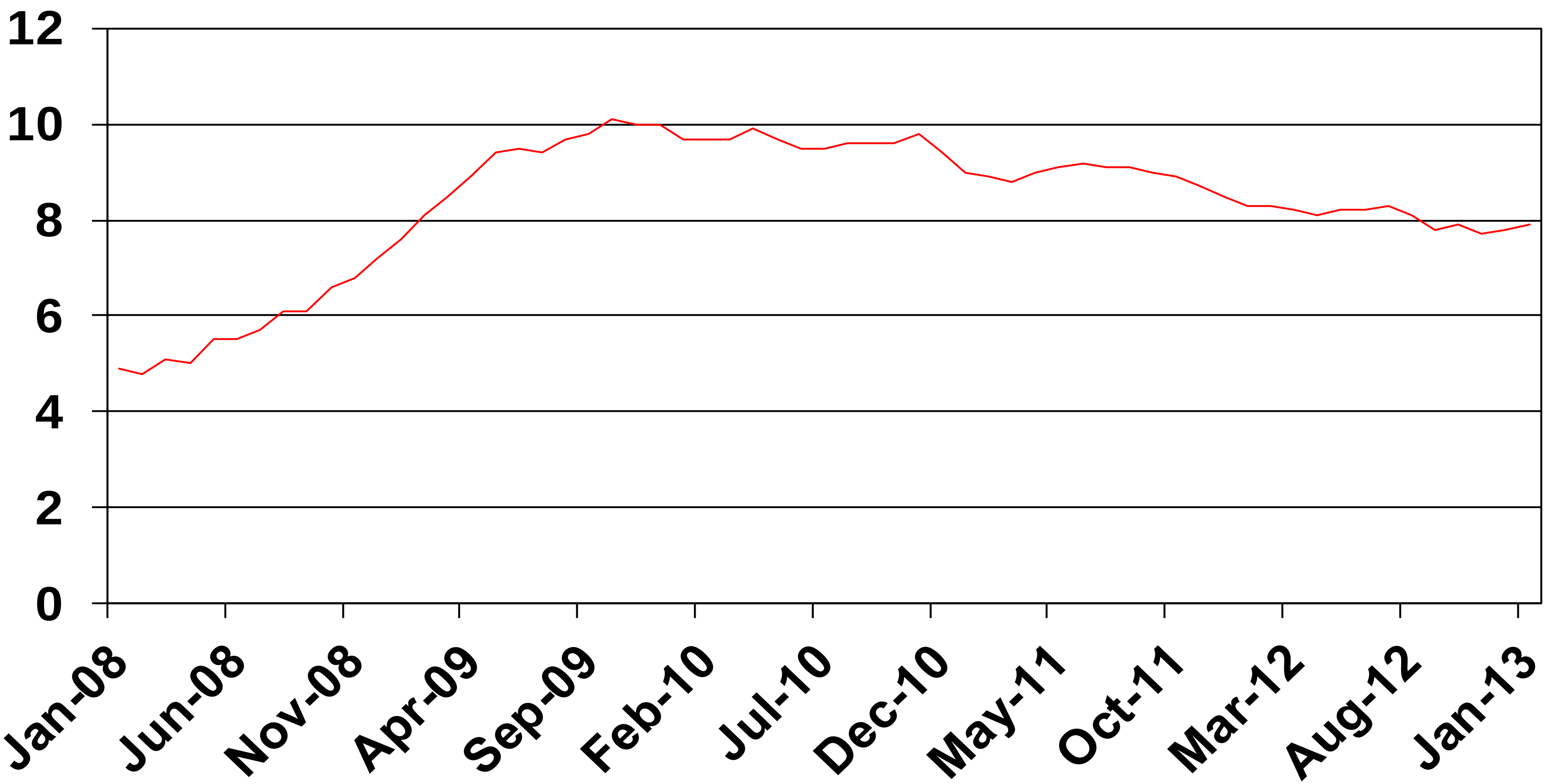

ECONOMIC OVERVIEW
Consumer Confidence

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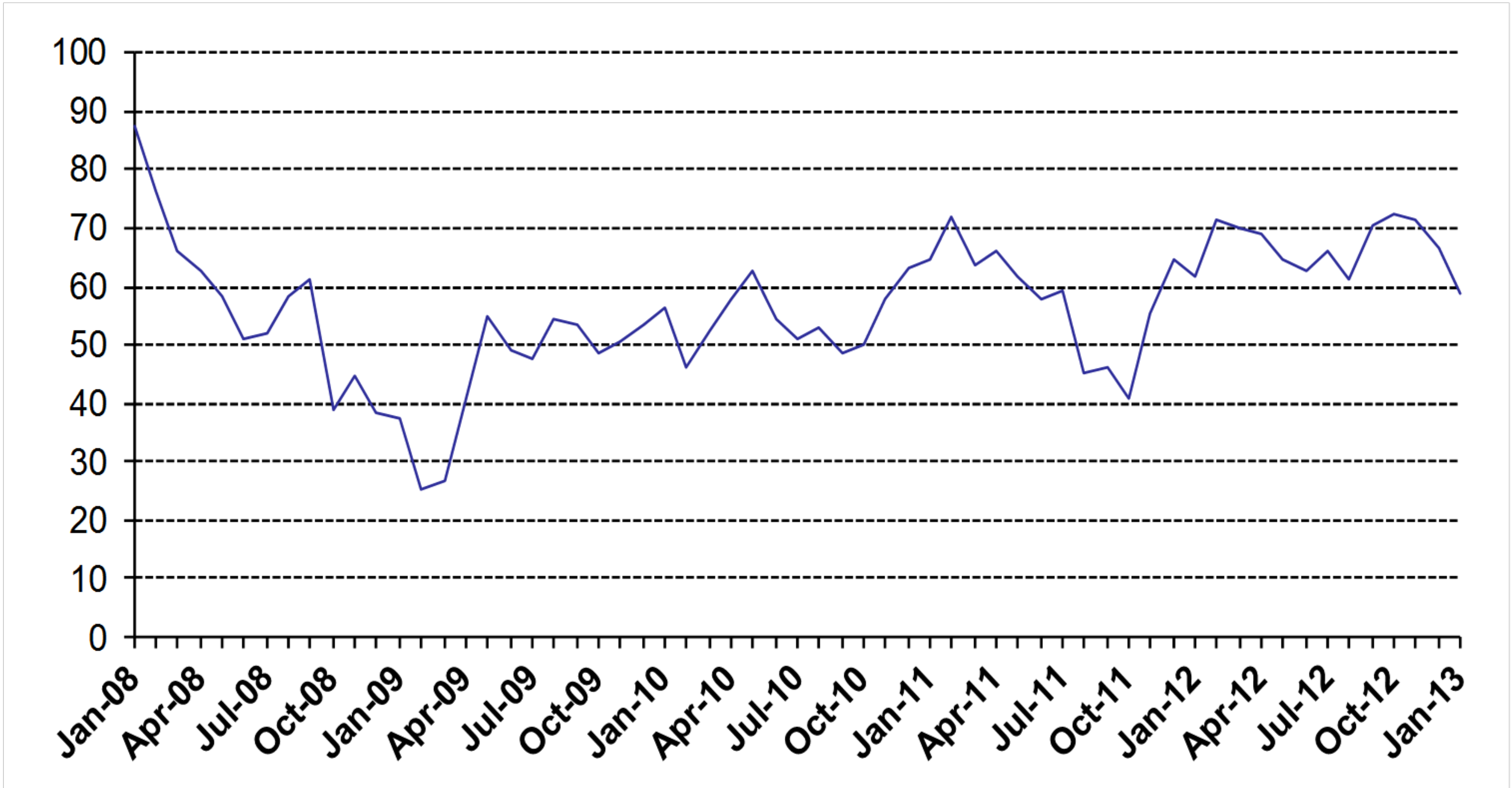

N.B.: January drop attributed in part to the increase in the payroll tax.

Also, 4Q12 U.S. GDP fell 0.1%, below an expected increase of 1.0%.

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Profile

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- **Founded: 1902 – National department store chain**

- **HQ: Plano, TX (approx. 159K employees as of January 2012)**

- **Store Count (a/o 10/27/12): 1,115, in U.S. and Puerto Rico**
  - Change over Last 12 Months: negligible (+1 net increase)
  - Change since 2007: +4.5% (+48 net increase)
  - Approximately 39% owned; remainder under operating leases.
  - Formats (avg store size - approximately 101K square feet):
    - J.C. Penney – 1,105 stores
    - The Foundry Big & Tall Supply Co. - 10 stores (started 2010)

- **Distribution Facilities:** 26 distribution centers, warehouses and fulfillment centers in 17 locations (approximately 70% owned)

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Profile, con't.

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- **Product Mix:**

		(% of Sales)
Women's Apparel	-	25%
Men's Apparel & Accessories	-	20%
Home	-	15%
Women's Accessories (incl. Sephora)	-	12%
Children's Apparel	-	12%
Family Footwear	-	7%
Fine Jewelry	-	4%
Services & Other	-	5%

- **Principal Competition:** Kohl's, Macy's, Bon-Ton, Belk, Dillard's, Target, Wal-Mart and Sears, but also off-price discounters like TJX and Ross Stores.

- **Private/Exclusive Brands (approximately 52% sales):** jcpenney, Liz Claiborne, Okie Dokie, Worthington, St. John's Bay, The Original Arizona Jean Company, Ambrielle, Decree, Linden Street, Article 365, Uproar, Stafford, J. Ferrar, jcpenney Home Collection, and Studio by jcpenney Home Collection, among others.

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Key Executives & Major Shareholders

Name	Title	Ownership
Ronald B. Johnson (new)	President & CEO	3.6%
Michael W. Kramer (new)	COO	N/A
Kenneth H. Hannah (new)	CFO	N/A
Pershing Square Capital Management LP (W. Ackman)	Shareholder (Director)	18.0%
Vornado Realty Trust (S. Roth)	Shareholder (Director)	10.8%
State Street Corp.	Shareholder	9.4%
Evercore Trust Company	Shareholder	6.7%
JCP Savings, Profit-Sharing & Stock Ownership Plan	Shareholder	6.3%

N.B.: All directors and executive officers as a group own approximately 32.0%.

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3Q12 Summary – Operating Performance

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- **3Q12 Total Sales: $2.93B [$14.53B over last 12 months]**
  - **(26.6%) YoY decrease from 3Q11 [(17.2%) YoY decrease for LTM period]**
- **3Q12 Same-Store Sales: (26.1%) YoY change [(22.3%) YTD]**
- **3Q12 Gross Margin: 32.5% [vs. 37.4% in 3Q11]**
- **3Q12 EBITDA: ($186MM) [$146MM over last 12 months]**
  - **($402MM) YoY decrease from 3Q11 [(89.1%) YoY decrease for LTM period]**
- **3Q12 EBITDA Margin: *Negative* [vs. 5.4% in 3Q11]**
- **3Q12 Free Cash Flow: ($389MM) [vs. ($489MM) in 3Q11]**

N.B.: FCF would have been worse in 3Q12 except for $99MM of favorable working capital changes (mostly increases in payables) vs. $544MM of working capital buildup (mostly increased inventory) in 3Q11.

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3Q12 Summary – Operating Performance

- **Sales**:
  - Comp-store sales plunged b/c of a 12% decline in traffic and 2% fall in conversion rate.
  - Total transactions, total unit volumes and average customer ticket each declined. But average number of units per transaction rose.
  - More “clearance” merchandise sold at lower average prices than “everyday low-price” merchandise, which sold at higher average prices.
  - The company discontinued the “month-long” values part of its new pricing strategy in August. This deterred many customers who had regarded month-long value specials as another name for “sale.”
  - Internet sales dropped 37.3%.
  - The exit from catalog business in FY2011 also hurt sales.

- **Product Performance**:
  - *Good* – None.
  - *Bad* – Everything. Men’s and women’s apparel saw the smallest same-store sales declines, while home products experienced the worst.

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3Q12 Summary – Operating Performance

- **Profitability**:
  - EBITDA was negative primarily because of the drop in sales and gross margins.
  - Gross margins declined due to (1) higher markdowns and inventory reserves, (2) unfavorable change in product mix (i.e., more clearance merchandise; less everyday low-price), and (3) vendor resistance to cost concessions.
  - Additionally, SG&A failed to decline as fast as sales did.
  - Higher-margin private-label and exclusive brands declined as a percentage of total sales.

- **Free Cash Flow**:
  - CFO and FCF were deeply negative because of a $320MM net loss (adjusted for $197MM gain on sale of assets) and the near-doubling of CAPX to $341MM, primarily for the company's aggressive store remodeling program.
  - A portion of this deficit was funded with $279MM of asset sales.
  - Adjusted for asset sales, working capital changes and financing activities (mostly $243MM of debt repayment), the company burned through $488MM of cash during the third quarter, alone!

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3Q12 Summary

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Year-to-Date Asset Sales

• 2.0MM of 2.2MM Simon Property Group REIT L.P. Units (July 2012):	$248.0MM
• Leveraged Lease Assets (3Q2012):	$146.0MM
• Interests in Four J.V.s that own Regional Malls (3Q2012):	$ 90.0MM
• Interests in CBL & Associates Properties REIT (3Q2012):	$ 40.0MM
• Building (3Q2012):	$ 3.0MM
Total:	$527.0MM

N.B.: The company recognized a $412MM gain on the sale of these assets.

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3Q12 Summary - Liquidity

- **Cash (a/o 10/27/12): $525MM [vs. $1.09B a/o 10/29/11]**

  (N.B.: Cash has declined $982MM over past nine months; $1.51B without asset sales.)

- **R/C Available: $1.29B of $1.50B Asset-Backed Facility*, due April 29, 2016 (Admin Agent = JPMorgan Chase)**

  - ***No* outstanding borrowings at the end of 3Q12.**
  - **$214MM of letters of credit issued.**

- **Total Liquidity: $1.82B [vs. $2.18B a/o 10/29/11]**

***Collateral = first lien on credit card receivables, accounts receivables and inventory. Borrowing base = 85% of eligible accounts receivable, 90% of eligible credit card receivables and 90% of the liquidation value of inventory, net of certain reserves. Facility increased to $1.75B on 1/31/2013.**

N.B.: The only financial covenant applicable to this facility is a minimum fixed charge covenant of 1.00:1.00 that applies only if availability falls below the greater of (1) $125MM or (2) 10% of the lesser of (i) the total commitment and (ii) the borrowing base in effect at the time of measurement.

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3Q12 Summary – Debt & Leverage

- **Debt:** $2.97B [vs. $3.10B a/o 10/29/11]

- **Net Debt:** $2.44B [vs. $2.02B a/o 10/29/11]
  - Net Debt increased by $845MM since the end of FY2011.

- **Rent-Adj Debt-to-EBITDAR:** 12.0x [vs. 3.4x a/o 10/29/11]

- **Principal Components of Debt**
  - $0.0MM outstanding on $1.5B Asset-Backed R/C, due 2016
  - $2.87B Various Series of Notes & Debentures, due 2015-2097
  - $97.0MM capital leases & notes payable

N.B.: Only $22.0MM of debt matures before the end of next October.

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YTD Restructuring Charges

• Home Office & Stores (headcount reduction):	$105MM
• Supply Chain Consolidation (DC closing/severance):	$ 19MM
• Software & Systems (asset writedowns/disposal):	$ 36MM
• Store Fixtures (writedowns/disposal):	$ 60MM
• Management Transition (retention/severance):	$ 36MM
• Other (e.g., closure of PA call center):	$ 13MM
Total:	$269MM

N.B.: These charges follow $451MM of aggregate restructuring and management transition charges recognized in FY2011 for supply chain consolidation ($41MM), catalog & catalog outlet store closings ($34MM), severance ($41MM), a voluntary early retirement program ($179MM), executive management changes ($130MM) and other miscellaneous items ($26MM).

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3Q12 Summary

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Off-Balance Sheet Commitments

• Operating Leases:	$2,916MM
• Purchasing Commitments:	$3,429MM
• Letters of Credit:	$ 214MM
• Simon Property Contingent Capital Commitment:	$ 360MM
• Guarantees & Surety Bonds (insurance & leases):	$ 115MM
• Under-funded Pension:	$ 121MM

GCS Rating / Outlook

- High credit risk, "E" / Negative outlook

Reasons: High leverage, deteriorating operating performance, negative free cash flow, ineffective management strategies introduced over past year and weak competitive position, offset by decent asset protection.

Financial History

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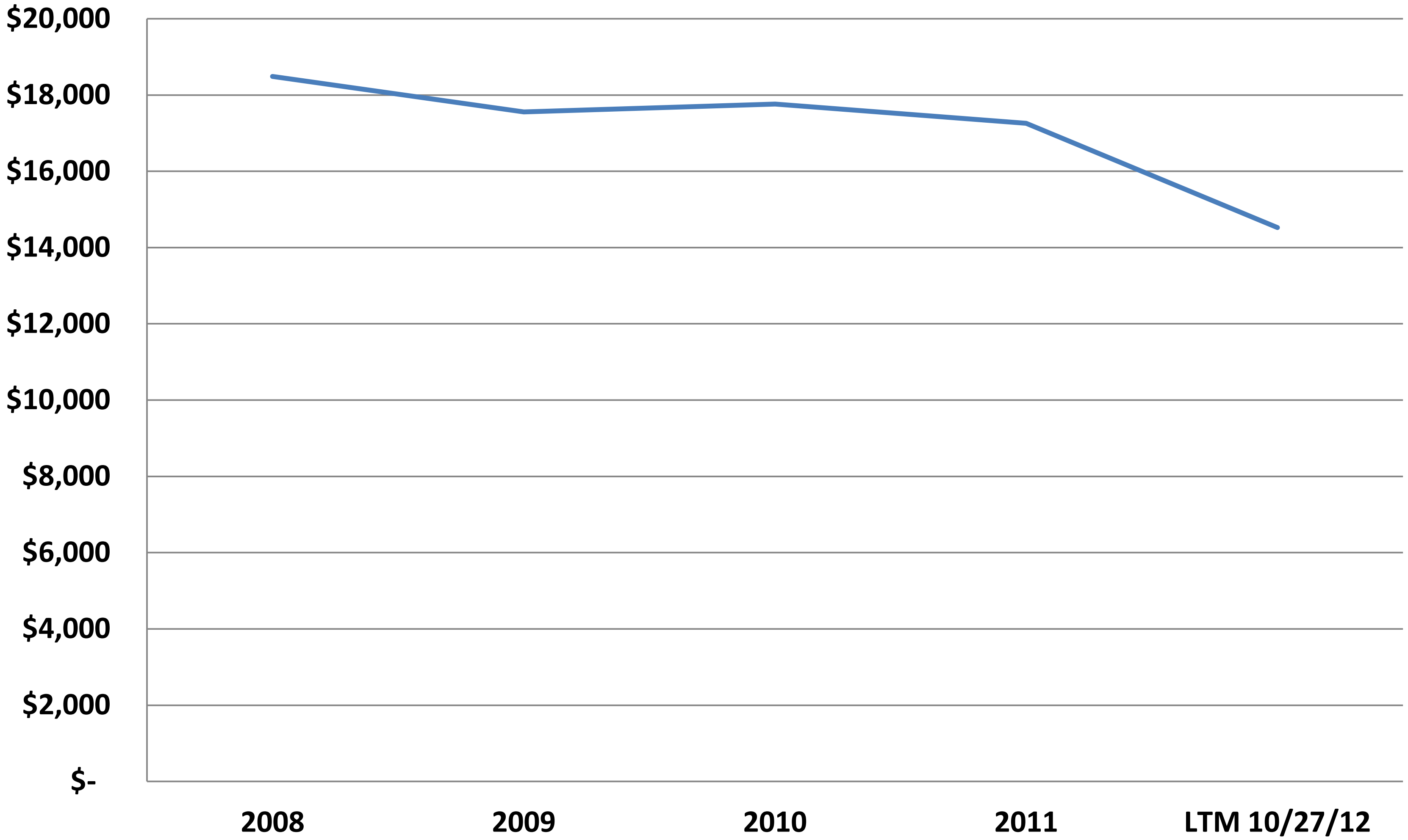
Financial History - Sales ($ in MMs)



N.B.: Steady sales decline despite increase in store base since 2007.

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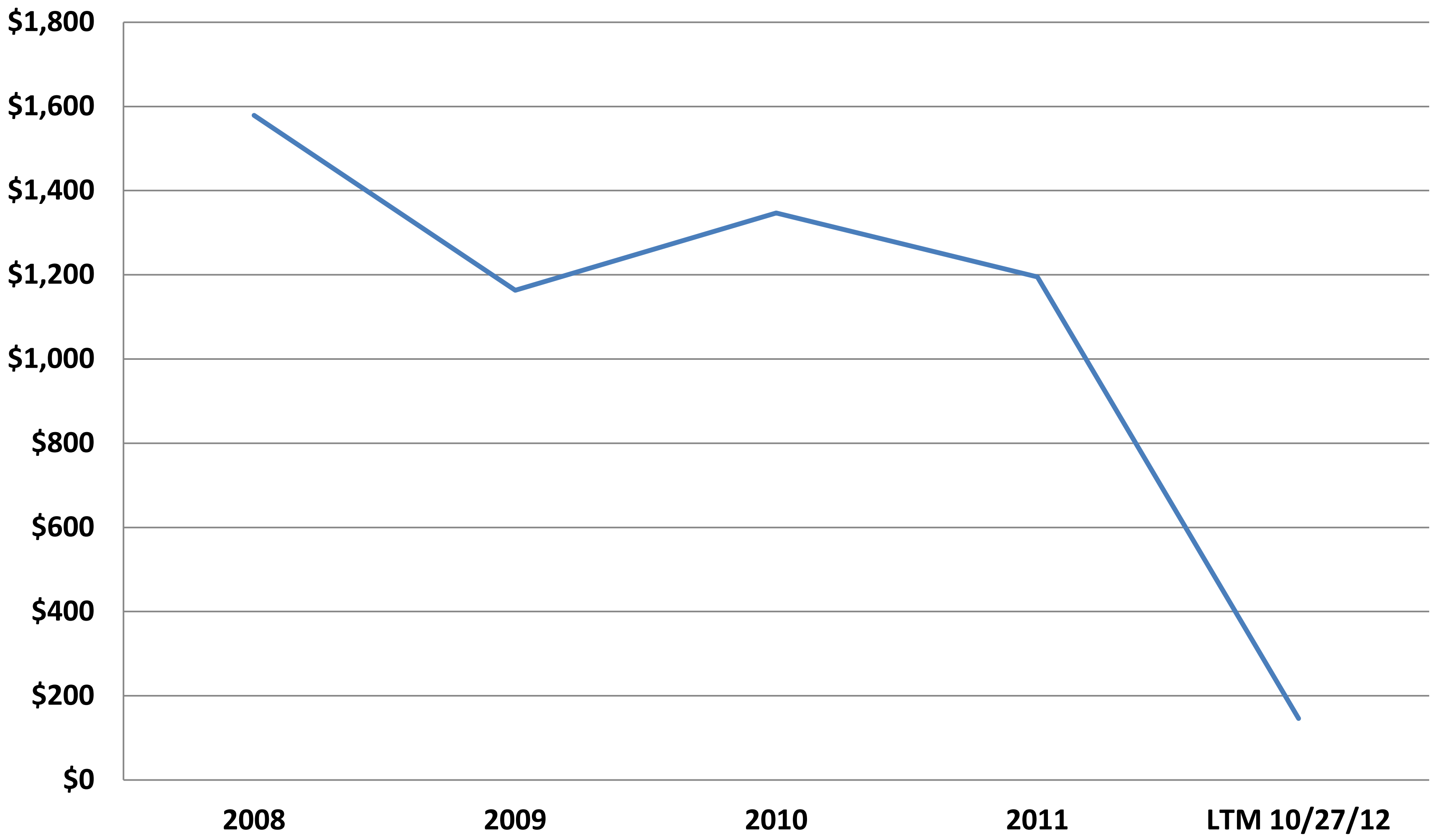
Financial History - EBITDA ($ in MMs)



N.B.: Gradual decline and recovery through recession followed by last year's plunge.

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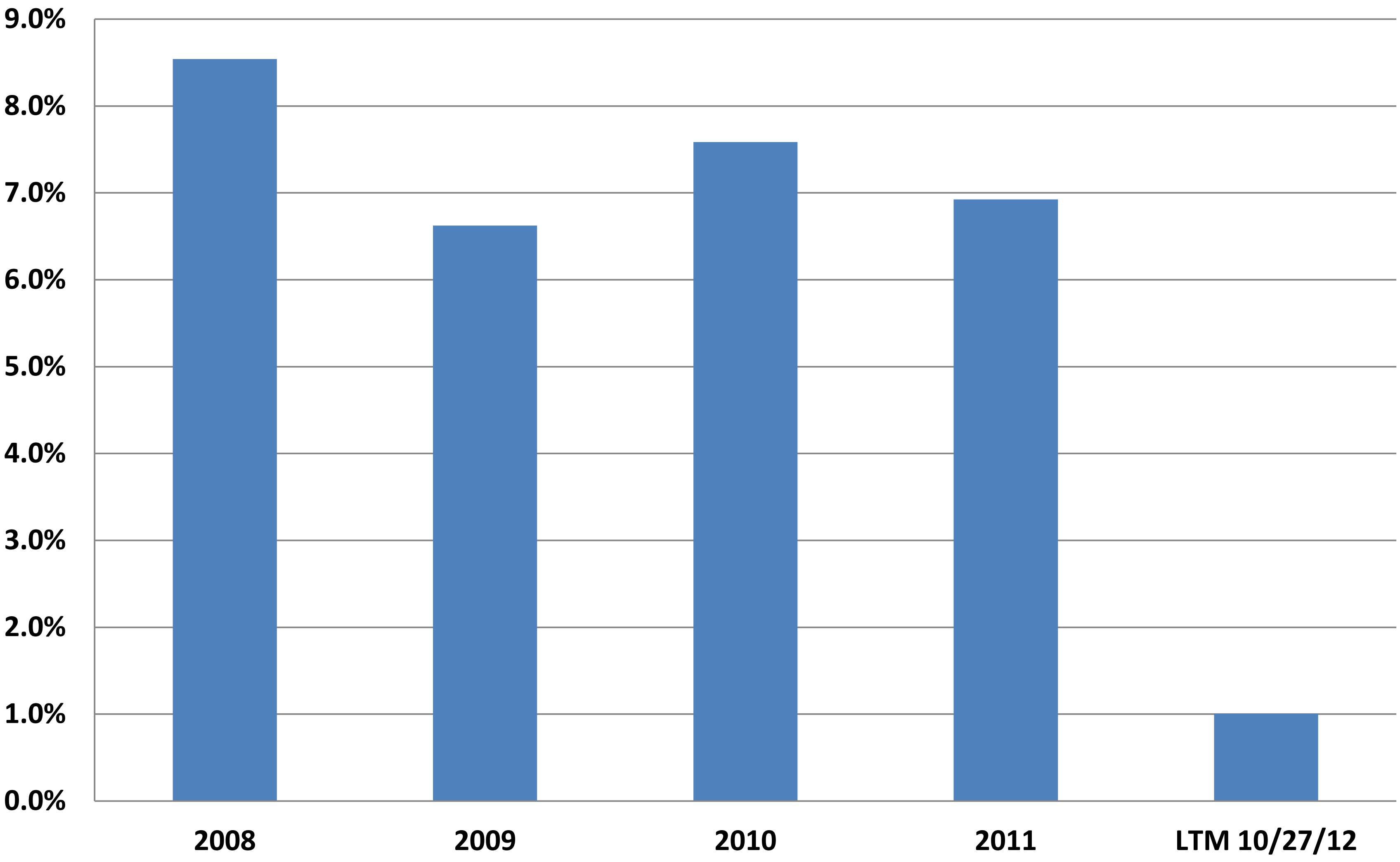
Financial History - EBITDA Margin



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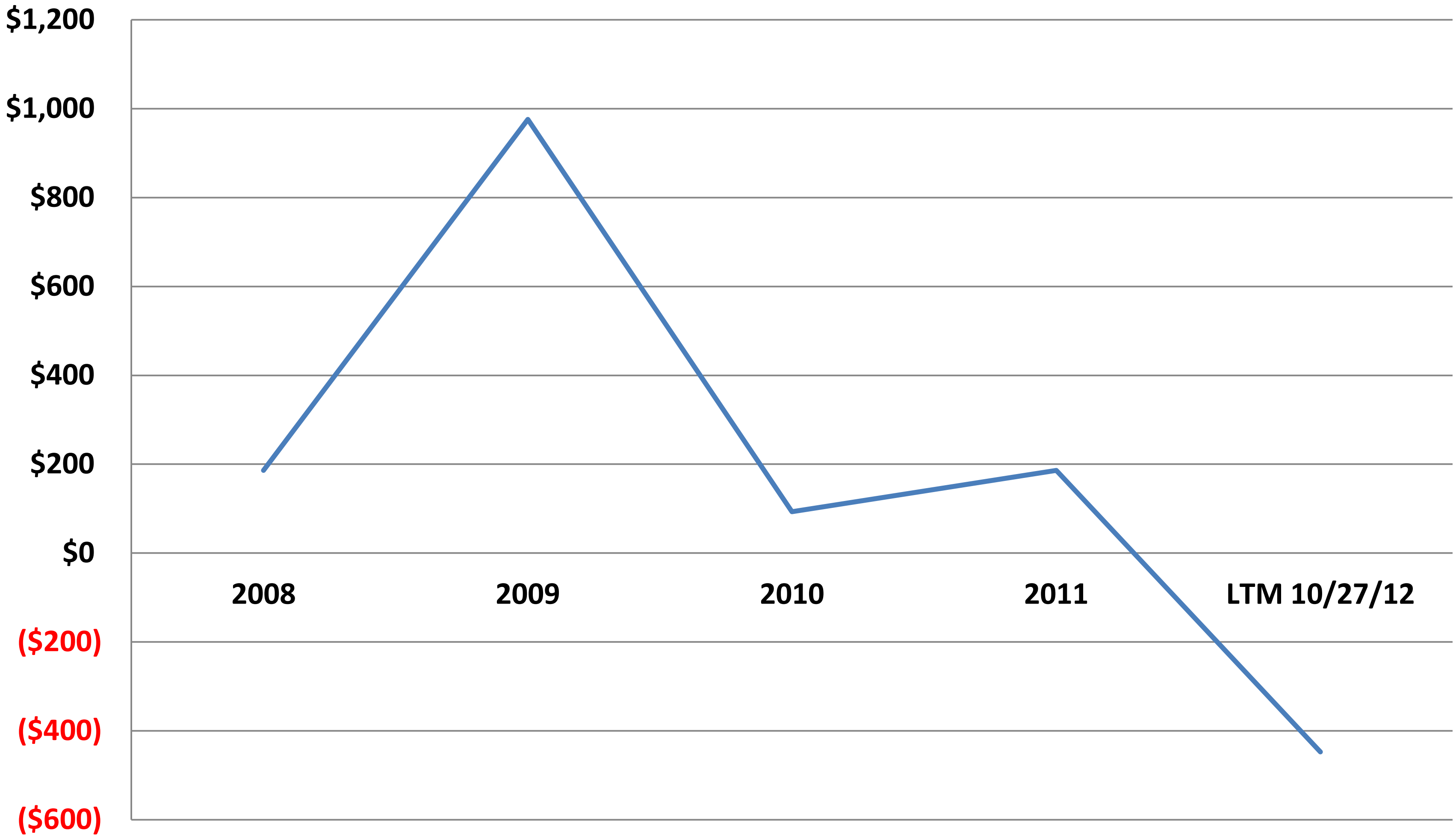
Financial History - Free Cash Flow ($ in MMs)



N.B.: Spike in 2009 due to sharp cuts in CAPX, inventory liquidation, and stretching of payables and accrued liabilities.

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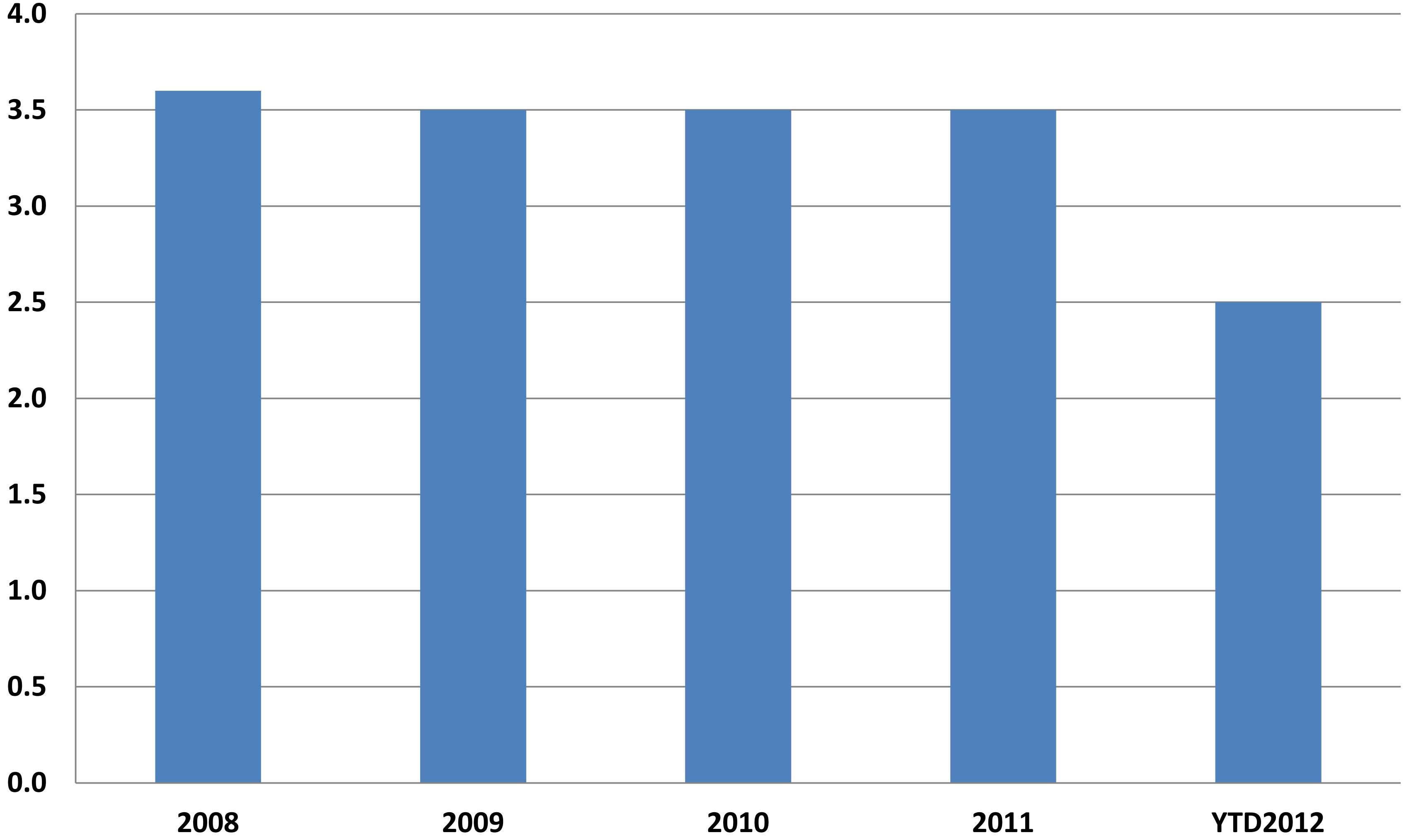
Financial History - Inventory Turnover



N.B.: Recent drop reflects failure to adjust merchandise mix and marketing in response to sales decline.

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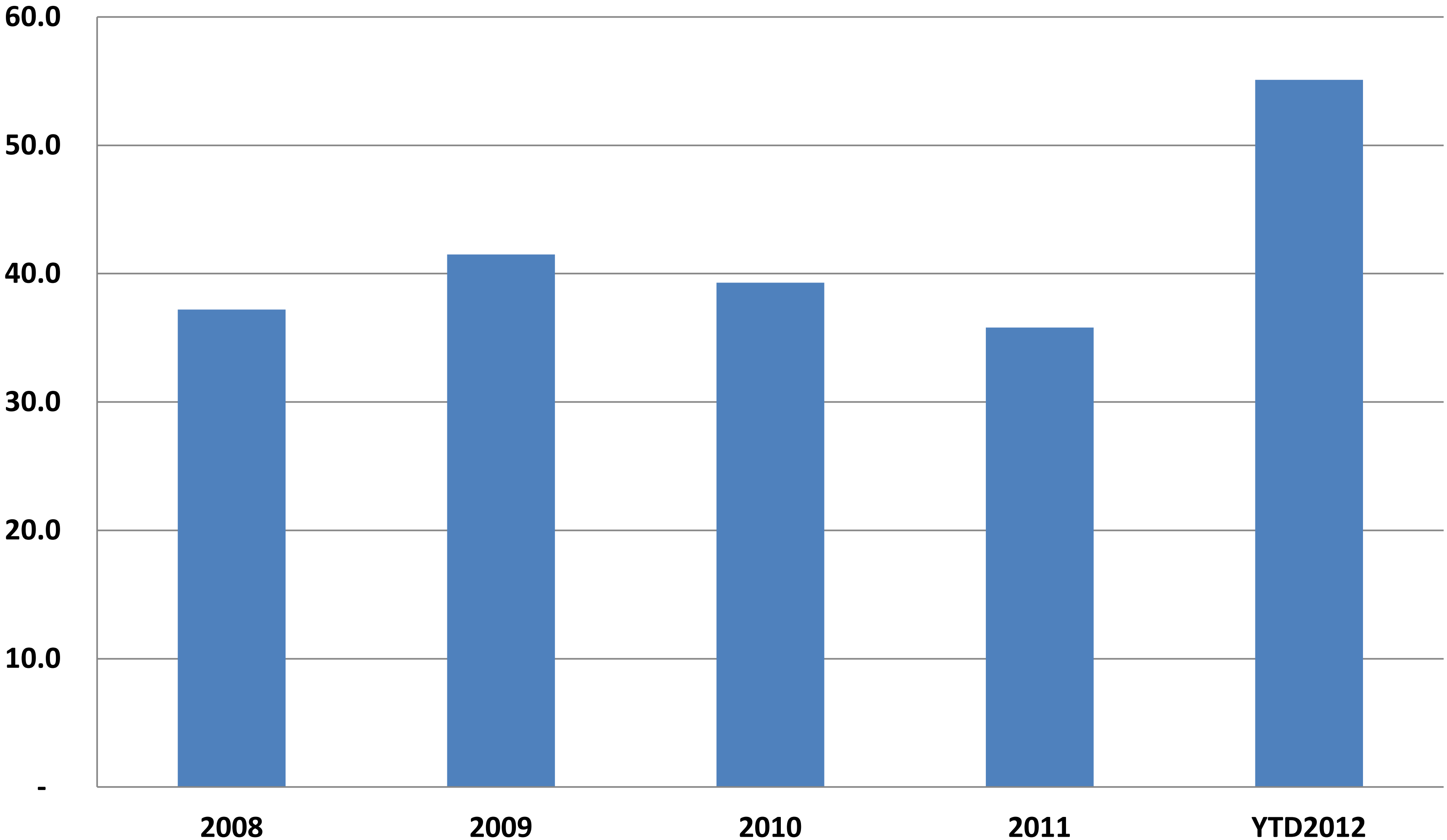
Financial History - Payable Days



N.B.: Recent rise reflects attempt to minimize negative CFO by using increased trade credit.

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Financial History – Cash & Equivalents ($ in MMs)

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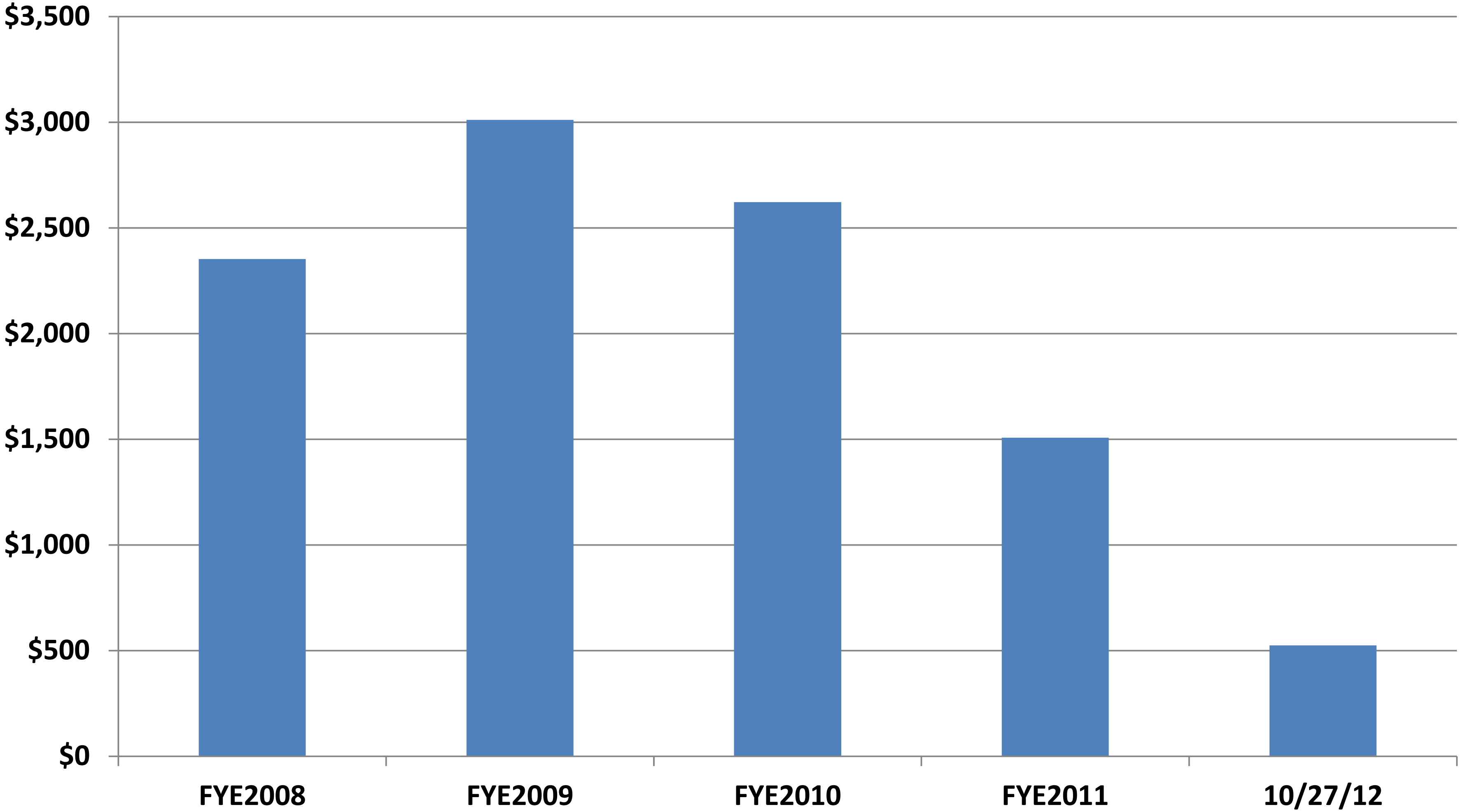

N.B.: Most of $1.5B decline between 2009 and 2011 due to stock buybacks, dividends and brand investments (e.g.s, Liz Claiborne; Martha Stewart).

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Financial History - Debt ($ in MMs)

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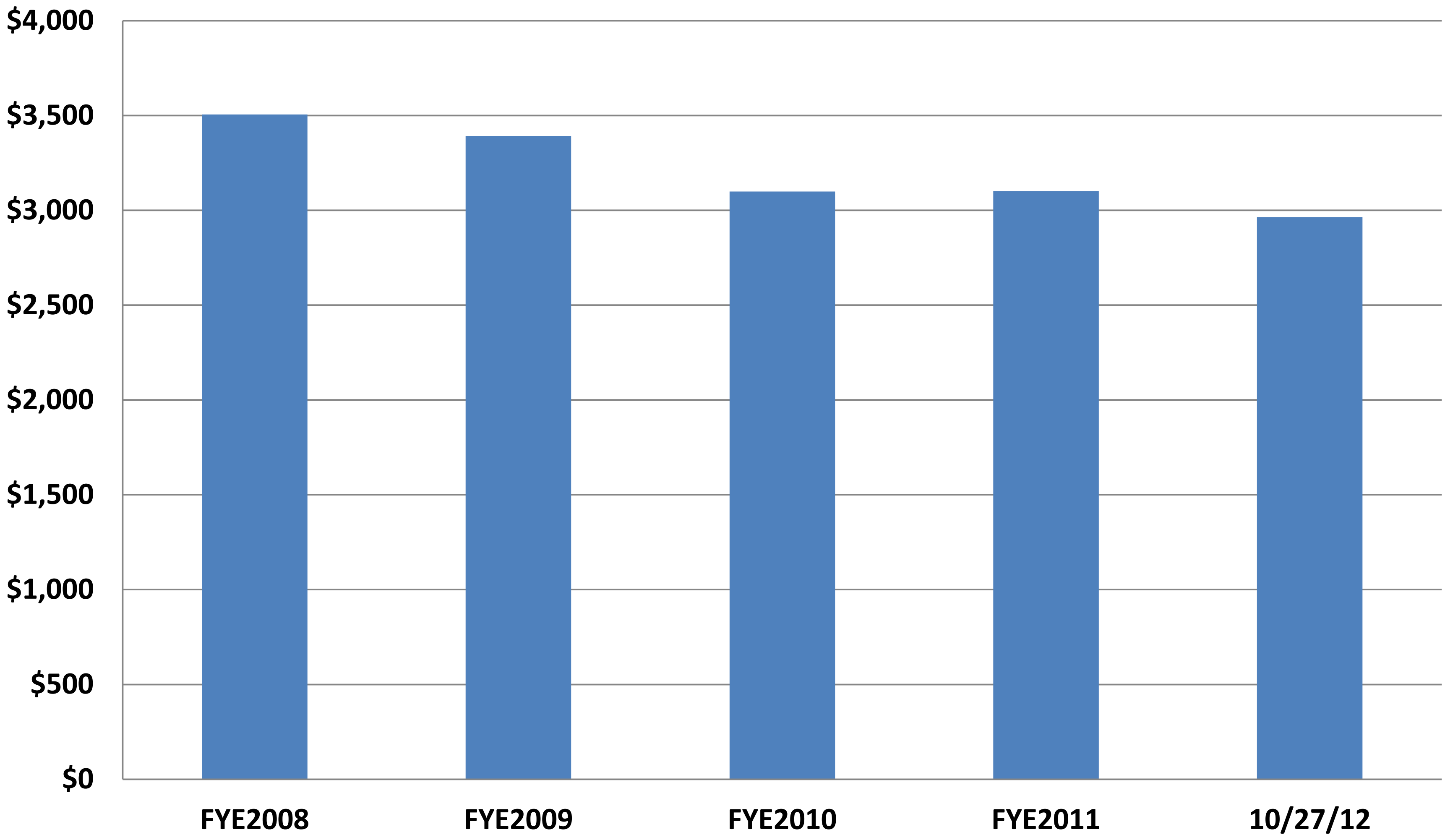

N.B.: Moderate decline in debt has not matched the sharp decline in cash.

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Financial History - Rent-Adjusted Leverage

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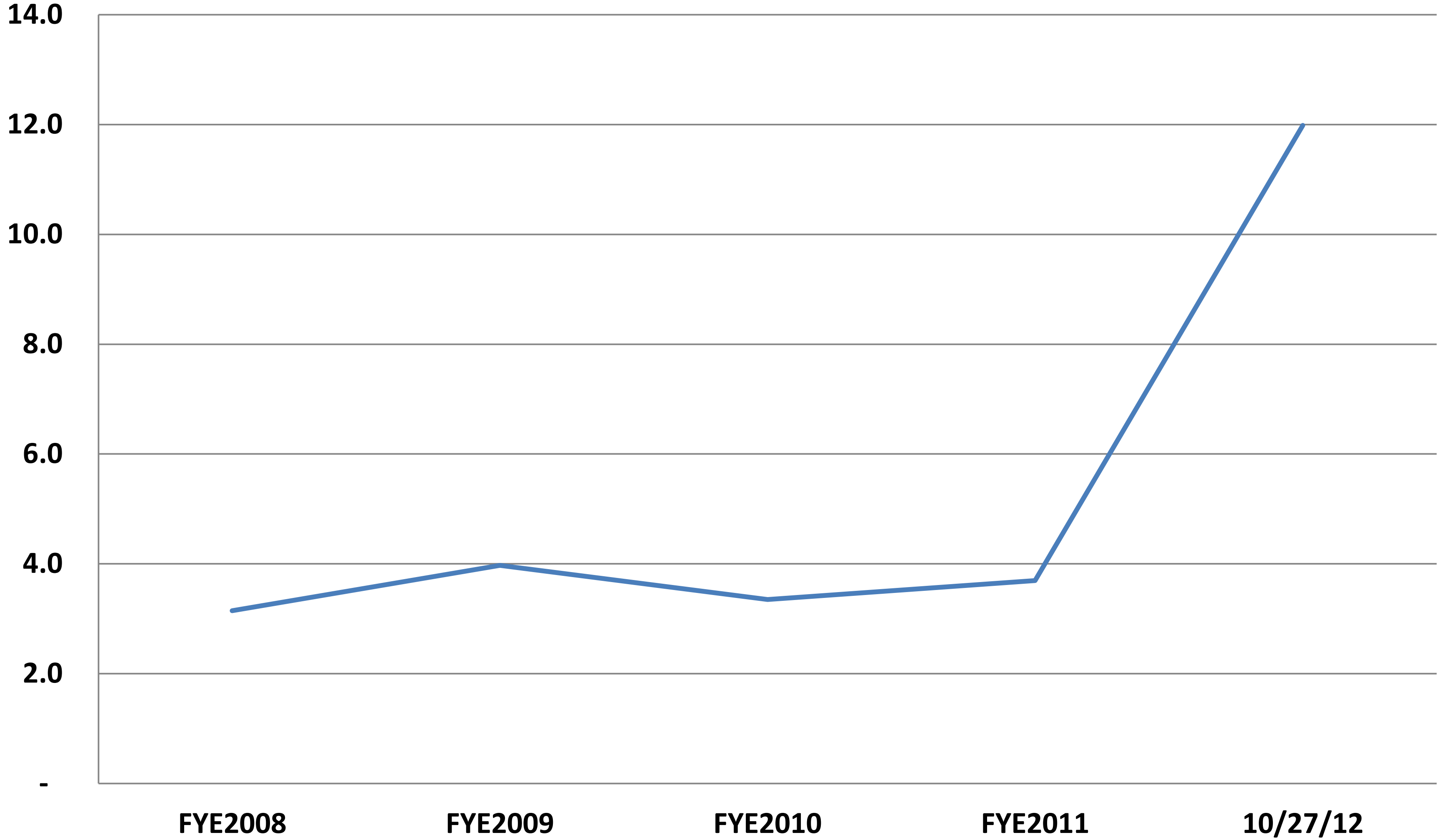

N.B.: Leverage has soared because of sharp deterioration in 2012 operating performance.

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Recent Developments

- **2H2011:** Entered stockholder agreements with Pershing Square Capital (William Ackman) and Vornado Realty Trust (Steven Roth), which together control almost 30% of JCP common stock as well as two director seats.

- **2H2011:** Acquired the Liz Claiborne brand for $268MM, replacing a 10-year licensing agreement that had been entered just one year earlier. The company also made a $39MM equity investment in Martha Stewart Living Omnimedia with a side agreement to sell certain M.S. products exclusively in JCP stores.

- **November 2011:** Appointed new CEO - Ronald B. Johnson, the former chief of Apple Computer's retail division, replacing Myron E. Ulman, III, who remained as Executive Chairman until retiring in January 2012. Over the next several months, Mr. Johnson proceeded to make several other senior appointments, including president, COO, CFO & "chief talent officer," several of which were filled by former colleagues from Apple (and some subsequently fired – e.g., former president, Michael Francis in June).

- **January 2012:** Introduced controversial new three-tiered "Fair & Square" pricing strategy aimed at offering (1) everyday low prices, (2) "month-long" value promotions, and (3) clearance merchandise. This strategy replaced the company's past practice of issuing coupons and regularly marking down merchandise.

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Recent Developments, con't.

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- **January 2012:** Embarked on comprehensive new-store remodeling program that will transform existing floor-plans into a store-within-a-store format filled with separately curated shops and boutiques.
- **February 2012:** Amended its asset-backed credit facility to increase its size by $250MM to $1.5B.
- **March 2012:** Stopped reporting same-store sales on a monthly basis.
- **April 2012:** Embarked on a major cost reduction program intended to save $900MM over 24 months.
- **May 2012:** Introduced a new private-label brand called "jcp."
- **May 2012:** Appointed a new CFO - Kenneth Hannah, formerly the CFO of MEMC Electronic Materials and SVP of Operations at Home Depot.
- **May 2012:** Suspended common stock dividend, saving $175MM/year.
- **July 2012:** Sold substantially all of interest in Simon Property REIT for $248MM.

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Recent Developments, con't.

- **August 2012:** Appointed new controller, Mark R. Sweeney, formerly operational controller of General Electric.

- **August 2012:** Repaid $230MM of 9.0% notes that matured (approximately $21MM / year of interest savings).

- **September 2012:** Sued by Macy's for allegedly interfering with Macy's exclusive marketing arrangements with Martha Stewart Living Omnimedia. Earlier in the year, Macy's had obtained a temporary injunction preventing MSLO from entering its joint venture with JCP.

- **3Q2012:** Sold various assets including interests in REITS, regional malls and leveraged leases for an aggregate $279MM.

- **January 31, 2013:** ABL facility increased from $1.5 billion to $1.75 billion.

- **February 4, 2013:** The company reported it has received a letter from a law firm claiming to represent over 50% of the holders of 7.4% debentures, due 2037, alleging that a default has occurred. Brown Rudnick claims the ABL credit facility entered in January 2012 violated the bond indenture by failing to provide bondholders with a ratable security interest in inventory pledged as collateral under the ABL facility. The company deems this notice of default invalid and has challenged it in Delaware Chancery Count.

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Strategic Initiatives

- **New Pricing Program:** Modified in August to eliminate "month-long" specials, replacing them with permanent markdowns of 20%-30%. This affected approximately 20% of total inventory. Now the Company is experimenting with placing MSRP labels on merchandise next to its lower retail price in an attempt to create the perception of value. Also, it just announced the prospect of holding periodic holiday sales (e.g., Valentine's Day; Easter; Mother's Day). But management insists there's been no fundamental change in strategy.

- **Store Remodeling Plan ("The Street & the Square"):** Approximately 11% of planned floor space has already been transformed to a shop-within-a-shop format. In addition to the long-time presence of Sephora and MNG by Mango, several other vendor/partners have negotiated in-store agreements with the company, including Levi's, Izod and Joe Fresh, among others. Separate shops also are being created for private-label merchandise like Liz Claiborne and The Original Arizona Jean Company.

- **$900MM Cost-Cutting Program:** $350MM from corporate (14% of Plano HQ staff laid off); $400MM from store operations; and, $150MM from marketing over 24 months.

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Issues & Conclusions

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- **Confusing Strategies = Loss of Market Share:**
  1. Traffic and S/S sales trends clearly indicate customer disenchantment with pricing changes. Even management seems uncertain, as it's "simplified" the strategy to an everyday low prices/clearance approach, yet still tinkering with promotional gimmicks (e.g., free haircuts, free holiday portraits, prize giveaways).
  2. Company's billing itself as a "specialty" department store chain, but pricing suggests its positioning itself as an "off-price" discounter.
  3. "The Street & Square" store remodeling has closed off valuable floor space that otherwise might be yielding incremental sales.

- **Product Mix:** Women's merchandise represents <50% of inventory compared to over 60% for many competitors.

- **Operating performance:** Sub-subpar. Same-store sales declining at accelerating double-digit pace for past three quarters. Negative EBITDA getting worse. Cash-burn rate (i.e., >$1.3B/year) is unsustainable without asset sales. All this has occurred and worsened since the new strategies were adopted.

- **Excessive Leverage is Climbing:** Company must find a way to reduce debt and cut rent expense. Year to date, the company's turned increasingly to asset sales, which it will probably need to continue to do.

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Issues & Conclusions, con't.

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- **Liquidity:** Ok, for now, but if YTD-cash burn rate does not reverse, company could use up all existing cash and revolver availability within the next 12 months (i.e., $1.0 billion of cash was burned during the first nine months of FY2012, ignoring asset sales, changes in working capital and debt repayment).

- **Aggressive CAPX Program:** Little firm evidence that the "Street & Square" concept is working, though the company claims renovated stores perform better than older stores. Query: are same-store sales trends still negative at remodeled stores? Management's been silent on this question.

- **Long-term Plan/Viability:** Need to perform store-by-store cash flow analysis, and consolidate to much smaller chain. Activist investors need to take more *active* steps to turn around the company (i.e., Management shake-up? Sale of company? Revisit old pricing model? Scale back remodeling program?)

- **Comfort Factor:** Asset protection – fortunately, the company owns a lot of its stores and other properties that should go a long way toward making creditors whole in a worst-case scenario. No real estate is subject to mortgages. As of 10/27/2012, net PP&E plus working capital covered total debt approximately 2.5x and total liabilities almost 100%.

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Comparable Company Analysis

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COMPARABLE-COMPANY ANALYSIS									
Company	Stores	Revenues ($MM)	EBITDA ($MM)	EBITDA Margin	Cash ($MM)	Debt ($MM)	R/A Leverage	Inventory T.O.	GCS Rating
Bon-Ton	273	$ 2,953.9	$ 157.1	5.3%	$ 8.1	$ 1,022.5	7.1	2.0	E-
J.C. Penney	1,115	$ 14,526.0	$ 146.0	1.0%	$ 525.0	$ 2,965.0	12.0	2.5	E
Burlington Coat	497	$ 4,081.4	$ 305.8	7.5%	$ 30.2	$ 1,428.1	6.0	3.1	E+
Belk	301	$ 3,843.7	$ 455.6	11.9%	$ 143.4	$ 417.6	1.9	2.2	C+
Kohl's	1,146	$ 18,955.0	$ 2,823.0	14.9%	$ 550.0	$ 4,578.0	2.2	2.7	C
Macy's	847	$ 27,060.0	$ 3,590.0	13.3%	$ 1,264.0	$ 6,940.0	2.3	2.4	C
Dillard's	302	$ 6,603.7	$ 766.9	11.6%	$ 124.8	$ 851.9	1.4	2.5	C
Ross Stores	1,205	$ 9,358.3	$ 1,383.8	14.8%	$ 625.3	$ 150.0	1.8	5.4	B+
TJX	3,046	$ 24,863.9	$ 3,367.5	13.5%	$ 1,842.9	$ 774.5	2.1	5.6	B+

Comment: JCP has lowest EBITDA and margin. Leverage is highest among its peers.

Questions
&
Answers

ADMINISTRATIVE ITEMS
Contact Information

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ADMINISTRATIVE ITEMS
Upcoming Webinars

- **Tuesday Morning**
  - Wednesday, February 20, 2013 @ 2PM Eastern
  - George Romey, Senior Industry Analyst

- **Nash Finch & Supervalu**
  - Wednesday, March 13, 2013 @ 2PM Eastern
  - Jonathan Kanarek, CFA, Director of Analysis

- **Shopko Stores & ALCO Stores**
  - Tuesday, March 26, 2013 @ 2PM Eastern
  - Dana Melillo, CFA, Senior Industry Analyst

ADMINISTRATIVE ITEMS
GCS Ratings Definitions

GCS RATING	Financial Structure	Liquidity	Cash Flow	Revenues	Operating Profitability
A MINIMAL CREDIT RISK	Strong financial structure – low leverage, strong coverage, high quality capitalization.[1]	Strong liquidity – both cash & short-term investments, as well as proven access to unsecured credit	Strong cash flow – from profitable continuing business, adequate capital investment, strong manage-ment of working capital.[2]	Dependable revenues – organic growth; competitive dominance.	High quality operating profitability – margins better than industry norms.
B LOW CREDIT RISK	Solid financial structure – modest leverage, strong coverage, tangible equity, longer debt capital.	Solid liquidity – both proven access to unsecured credit with committed lines backing any commercial paper; adequate cash, short-term investments.	Solid cash flow – from profitable continuing business, adequate capital investment, solid management of working capital.	Dependable, growing organic revenues – strong competitive position.	Solid quality operating profitability – solid margins vis-à-vis industry.
C MODERATE CREDIT RISK	Stable financial structure – moderate leverage, accept-able coverage, moderate-quality capitalization; some elements of financial structure may pose risks.	Dependable liquidity – committed unsecured bank lines with moderate usage and availability, securitization programs, adequate cash holdings.	Cash flow – from profitable continuing business, capital investment, and adequate management of working capital; cash flow may be erratic some years.	Dependable revenue base – organic growth in line with economic environment.	Operating profitability – margins at or better than industry norms.
D MODERATELY HIGH CREDIT RISK	Risky financial structure – heavier leverage, marginal coverage, lower quality capitalization.	Defensive liquidity – secured bank lines usually in use, availability still sufficient.	Cash flow occasionally negative – capital investment constrained, defensive management of working capital.	Revenue base stagnant – little organic growth, uncertain competitive standing.	Weaker operating profitability – margins at or below industry norms
E HIGH CREDIT RISK	Weak financial structure – heavy leverage, weak coverage, short-to-medium-term debt capital, little if any tangible equity.	Weaker liquidity – secured bank lines mostly in use with little availability; defensive cash hoarding may be evident.	Cash flow frequently negative – capital investment limited, defensive management of working capital; asset sales material ongoing source of cash.	Revenue base declining – weak competitor that's losing market share.	Weak operating profitability or losses – margins below industry norms.
F DISTRESSED CREDIT	Extremely weak financial structure – overwhelming leverage, inadequate interest coverage, impending debt maturities, negative tangible equity.	Little or no liquidity – secured bank lines near limits with no effective availability; defensive cash hoarding.	Negative cash flow – inadequate capital investment, cash conversion cycle lengthening, working capital eroding; marketable assets mostly sold already.	Declining revenues – eroding competitive standing, losing market share.	Operating losses – on continuing business.

[1]Quality of capitalization includes tangible equity and maturity of debt capital. High quality capital includes tangible equity and long term unsecured and subordinated debt. Elements that weaken capitalization include goodwill and debt maturing within next couple of years.

[2]Management of working capital emphasizes the cash conversion cycle: turnover of receivables, inventory, payables and unearned income.

ADMINISTRATIVE ITEMS
Map of GCS Scores & Ratings To Agencies

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Score		Rating		
From	To		S&P / Fitch	Moodys
-	-	0	NR	NR
1.00	1.32	A+	AAA	Aaa
1.00	1.32	A+	AA+	Aa1
1.33	1.65	A	AA	Aa2
1.66	1.99	A-	AA-	Aa3
2.00	2.32	B+	A+	A1
2.33	2.65	B	A	A2
2.66	2.99	B-	A-	A3
3.00	3.32	C+	BBB+	Baa1
3.33	3.65	C	BBB	Baa2
3.66	3.99	C-	BBB-	Baa3
4.00	4.32	D+	BB+	Ba1
4.00	4.32	D+	BB	Ba2
4.33	4.65	D	BB-	Ba3
4.66	4.99	D-	B+	B1
5.00	5.32	E+	B	B2
5.00	5.32	E+	B-	B3
5.33	5.65	E	CCC+	Caa1
5.33	5.65	E	CCC	Caa2
5.66	5.99	E-	CCC-	Caa3
6.00	6.32	F+	CC+	Ca1
6.00	6.32	F+	CC	Ca2
6.33	6.65	F	CC-	Ca3
6.66	6.99	F-	C	C
6.66	6.99	F-	D	D