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**MANAGEMENT DISCUSSION SECTION**

Operator: Good day everyone, and welcome to the Q1 2010 Krispy Kreme Doughnut (sic) [Doughnuts] Earnings Conference Call. Today's call is being recorded.

It is now my pleasure to introduce your host, Brian Little. Please go ahead.

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**Brian K. Little, Director, Corporate Communications**

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Good afternoon everyone. Welcome to the Krispy Kreme 2010 First Quarter Earnings Conference Call. As the operator mentioned, my name is Brian Little. I am the Director of Corporate Communications for Krispy Kreme. Also on the call for Krispy Kreme today is Jim Morgan, President and the Chief Executive Officer, and Doug Muir, Executive Vice President and Chief Financial Officer.

During the call today, Mr. Morgan will comment on the Company's performance, and Mr. Muir will give an overview of the financial results released earlier today. Following Derek's comments, the operator will open the lines to take your questions.

As a reminder, a copy of our earnings announcement is available in the News Release section under the Investor Relations tab at our website, krispykreme.com. Also, this conference call is being webcast, and will be archived on our website for one year. A transcript of this conference call will also be available there. Investors, analysts, and shareholders are directed to these online public resources for the most up-to-date Company information. Krispy Kreme Investor Relations can be reached via email at [ir@krispykreme.com](mailto:ir@krispykreme.com).

Our comments today should be considered forward-looking in nature, and are subject to various risks, uncertainties and assumptions. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated or expected. Key factors that may have a direct bearing on Krispy Kreme's operating results, performance, or financial condition are discussed in Krispy Kreme's Form 10-K for fiscal 2009 and other periodic reports filed with the US Securities and Exchange Commission.

I will now turn the call over to Mr. Morgan. Jim.

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**James H. Morgan, President and Chief Executive Officer**

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Thank you, Brian. Good afternoon to everyone, and welcome to today's call. As you know, we released our first quarter results earlier today. We reported operating income of \$5.8 million, up from 5.6 million in the first quarter last year. We did this despite the fact that this year's result included \$2.4 million of lease termination costs related principally to two stores in Michigan that we closed in the quarter.

We had net income of 1.9 million, which reflected those lease termination costs, as well as an additional 1.1 million of expenses relating to amendments to our credit facilities, compared to net income of \$4 million in the first quarter last year.

While we are pleased with the improvement in our first quarter operating results, we still have a way to go in order to produce the financial results that we think are achievable. As we've said before, there'll be setbacks and there'll be bumps along the road. But we will continue to build a business that achieves consistent and predictable results. We are on the right track, and our results are beginning to show that. The signs of progress we saw in the first quarter actually make me more

enthused than ever about our long term prospects. And in fact I would say in my most professional jargon that that was actually a pretty doggone good quarter.

With that as an overview, I would like to update to you on our progress to-date, and provide you with a glimpse of things to come. Then I will turn the call over to Doug, who will discuss our financial performance for the quarter.

Our strategic initiatives are the focus of every operational decision we make at Krispy Kreme. And I have challenged every member of our team to make sure that they do something every day that will advance one of those strategic initiatives. We remain enthusiastically focused on them. And believe that fiscal 2010 will be the year in which it will become apparent that we have begun to seize the opportunities that will lead us to a bright and successful future. Our incredible employee base remains committed to the success of this Company. And our progress to-date is due in large part to their commitment, their loyalty and their passion for excellence.

Our employees are by no means the only members of our team. We and our franchisees continue to share our expertise with each other as part of our ongoing efforts to communicate and brainstorm together. We know that the success of this Company is directly tied to the success of our franchisees. And we remain committed to a positive relationship with them, built on mutual respect and dedication to each other and to this incredibly powerful brand.

Additionally, we are listening and responding to what our consumers are telling us. A constant theme is that 'you need to be more convenient to me'. That is the demand we are taking very seriously. And we believe our small store concept, paired with a broader menu, will be the foundation that meets that need, and sets the stage for our domestic growth in the years ahead.

Our work has only just begun, as we strive to accomplish the task required to grow the business over the long-term. In the first quarter of fiscal 2010 we accomplished much that has moved us in the right direction. And I would now like to speak to just few of those accomplishments.

First, the measured growth of our international business continued in the first quarter, as the first Krispy Kreme shop in Malaysia opened in April. That shop is the first of 20 Krispy Kreme shops our franchisee plans to open in that market over the next five years. We remain very enthusiastic about our international growth prospects, not only for this year, but for many years to come. The number of new international store openings this year won't meet the extraordinary total of 114 openings we had in fiscal 2009. But we are very content to spend this year absorbing and building on the commitments our international franchisees have made to our brand, and dedicating additional resources to operational and marketing support to franchisees around the world.

Second, in the United States I think there's greater excitement among our franchisees about our potential than at any time since I've been a part of the Krispy Kreme management team. Franchisees are dedicating resources to open new locations. And I think those commitments will continue if we as a franchisor continue to commit our own resources to opening new locations, and proving the validity of the small retail shop concept.

Third, on the Company store side, we are negotiating lease agreements to construct three more small retail shops, which we expect to open in the coming months in the Raleigh, North Carolina, Louisville, Kentucky and Columbia, South Carolina metropolitan markets. We are committed to becoming more convenient for our customers by establishing smaller retail locations in higher traffic areas, which allow us to bring our signature products closer to consumers.

The initial sales numbers for the two new small retail concept shops we opened already this year are very encouraging. But it is way too early to declare success. However, we do feel good about the initial results, and we'll keep you posted as we gain more experience in developing and operating these small retail concepts.

Fourth, during the first quarter we continued our Company shop renovations and upgrade projects in order to enhance consumer appeal. We expect several more shop renovations to be finished by the end of the calendar year. All renovated shops will also include the installation of our Kool Kreme soft serve concept that is now being tested in five of our Company store locations, with two more locations to introduce Kool Kreme later this month. We continue to believe that Kool Kreme has the potential to provide significant operational leverage, by addressing both daypart and seasonal-part challenges.

Fifth, we have completed the development of the first baked products that we plan to begin testing this fall. They include bagels, muffins, cinnamon and pecan rolls and Danish pastries. We view these potential new products as complementary to our core product, which is and will be our one-of-a-kind doughnut. Our research tells us that the morning daypart is growing, and there's opportunity in providing a wider variety of for sale, portable menu items. Additionally, presenting a variety of baked products that complement our existing menu gives consumers more options and, therefore, more reasons to visit our shops. This is a limited test that will be initially conducted at one of our Company shops here in the Piedmont Triad of North Carolina.

Sixth, we are making progress in strengthening shop operations, including execution of the QSR basics through enhanced training and development tools we are introducing into the system. We are arming our employees with the skills they need to provide an outstanding consumer experience. And they are leveraging their learnings to create an exceptional guest experience in our shops. We are committed to ongoing investment in the training and support of our employee base, as our in-store teammates are the face of Krispy Kreme to thousands of customers each and every day.

Seventh, we are making progress in stabilizing and reinvigorating our off-premises business. We have seen significant signs of improvement in the markets in which we have most fully implemented a new off-premises operating model. And we think these gains can not only be extended, but also can be replicated as we expand introduction of the new model to the rest of our organization.

Eighth, and finally, we will soon begin ramping up an expanded broadcast media strategy in select markets where we have reached sufficient scale to make use of broadcast media economically feasible. Those markets include the Piedmont Triad region of North Carolina and the metropolitan area of Nashville, Tennessee.

Looking ahead to the balance of the year, we are entering the summer months which historically have resulted in a seasonal slowdown and weakened results than we typical post in the first quarter. I do not expect the seasonal challenges to be any more intense this year than in years past. And I believe we are better prepared from a marketing standpoint this year to focus on products that have greater appeal in the warmer months of the year. I am also eager to see the results of our expanded testing of Kool Kreme, our new soft serve offering. On balance, I am optimistic about our results, both for the second quarter and for fiscal 2010 as a whole.

In summary, we have made progress on a number of fronts in the last couple of quarters. And the strategic initiatives we instituted during calendar year 2008 are beginning to gain traction and yield results. Although there is still much we need to accomplish, we are pleased with our performance for the quarter. And remain committed to improving our performance in the quarters and years ahead by doing what it takes to achieve sustainable, predictable and profitable growth for the benefit of all of our constituencies, being our employees, our franchisees, our guests and our shareholders.

I'll now turn the call over to Doug.

**Douglas R. Muir, Executive Vice President and Chief Financial Officer**

Thank you, Jim, and good afternoon everyone. We reported operating income of 5.8 million in the first quarter this year, compared to operating income of 5.6 million in the quarter last year. This year's first quarter was adversely affected by 2.4 million of impairment and lease termination charges, which relate principally to two stores we closed during the quarter; while last year's first quarter benefited from a credit of \$645,000 on the impairment and lease termination line. Excluding these charges and credits, operating income rose to just over 8 million this year, compared to about 5 million last year.

We reported net income of 1.9 million, or \$0.03 a share this year, compared to 4 million, or \$0.06 a share in the first quarter last year. This year's results were weighed down by the 2.4 million of charges I just mentioned, as well as by another 1.1 million of charges related to the amendments to our credit facilities we previously announced. That \$1.1 million of charges related to the credit agreement amendments is included in interest expense in the income statement. Last year's results benefited not only from one-time credits to lease termination costs, but also a non-recurring gain of about \$930,000 related to the disposal of investments in two franchisees. If you exclude the effects of all of these charges and credits, our bottom line was about 5.4 million this year, compared to about 2.5 million last year.

We continue to have weak economic conditions domestically. And economic weakness also is apparent to a greater or lesser extent in international franchise markets. The uncertainties associated with a weak global economy have resulted in a stronger US dollar, which adversely affects our international royalty revenues. Changes in the rates of exchange between the US dollar and the foreign currencies in which our international franchisees do business, adversely affected our international royalty revenues by about \$700,000 this year compared to the first quarter of last year. I would note, however, that the adverse effects of currency movements in the quarter were not so severe as we had budgeted.

An uncertain economy makes revenue forecasting particularly challenging. And given those uncertainties, we have attempted to plan and budget conservatively for the coming year. Our results for the first quarter were ahead of plan, and we feel that we are off to a good start in fiscal 2010. On balance, we think the year-over-year comparisons are positive, and we are pleased by the improvements in our results. But as Jim says, we're not satisfied with those results. We can, and will do better over the longer-term. And we expect that there will be some unevenness in our results from quarter-to-quarter as we move toward our goal of achieving predictable, consistent and rewarding financial results.

I'd like to take just a moment to speak to our financial position and liquidity. During the quarter, we repaid \$20 million of principal on our term loan, reducing its balance to 54 million. Even after that significant use of cash for debt reduction, and paying \$2 million of fees related to amendments to the credit facilities, we finished the quarter with 21 million in cash. In addition, there is also \$9 million of unused borrowing capacity on the revolver. So right now we feel pretty good about our liquidity, and about our financial ability to execute the plans Jim spoke of.

Operator, at this time we are ready to take questions.

**QUESTION AND ANSWER SECTION**

Operator: Thank you. [Operator instructions] We'll go first to Jay Garrett with Ahab Capital.

<Q>: Hi, thanks. Just a couple of questions. I was wondering if we could start with your gross margin. Specifically, it looked like COGS were down significantly both year-over-year and sequentially. Could you just talk about a couple of the bigger impacts that you noticed there in the quarter?

<A – Douglas Muir>: Jay are – you're looking at the consolidated results, and not -

<Q>: Yes.

<A – Douglas Muir>: this particular segment? Yeah. A couple of things are going on there, and there's – and I'll highlight just a few of them. Number one is the cost of doughnut mix and shortening are substantially lower this year than they were in the first quarter last year. And our operating margin in the Company stores business is benefiting from those lower costs.

The second thing that's going on is that we are achieving some benefits from not operating in the first quarter this year some stores that were operating last year. So we're finally seeing some benefit of having closed stores that were sub par performers.

Another factor that has helped us is we're a big consumer of gasoline. And our gasoline costs were considerably lower in the first quarter this year than they were a year ago. Gas prices have kicked up a little, so I don't think the benefit will be quite so big in the second quarter. But the year-over-year comparison in gasoline that we look for in the second quarter is still going to be a very positive one. There are some other things going on in there, but those are some of the really big ones that affected results for the quarter.

<Q>: Okay. Thanks. And can you talk about what percent of total cost of goods sold doughnut mix and shortening consist of?

<A – Douglas Muir>: It's hard to --

<Q>: I'm sure it varies from quarter-to-quarter but --

<A – Douglas Muir>: Yeah. And we've also got cost of – our consolidated number we report is a direct operating expense number, which has a bunch of stuff in it besides the cost of mix in the stores. It's also got all the other operating expenses in it. But you can generally figure if you look at the restaurant side and in the Company store segment, that cost of – the total cost of materials, labor and packaging is typically going to run in the range of about, call it, depending on the store, 55 to 60% of sales, roughly.

<Q>: Okay. And then I had another question regarding your working capital. Congratulations on a nice source of cash there. But specifically the two line items that changed to a positive this year was a change in accounts payable and accrued liabilities, as well as other long-term obligations. Could you roughly comment on those?

<A – Douglas Muir>: I sure can. We took charges of -- the 2.4, or 2.2 million of lease termination charges we took in the quarter, about a million of that, I believe, wound up in accounts payable and about another million of it wound up in other long-term obligations. So from a cash point of view, that 2.2 million did not go out the door in the quarter. And that's why you see the add backs. That's the biggest single reason you see the add backs in those lines in the cash flow segment.

<Q>: Okay. And then lastly, just more of a strategy question. I know Jim commented on it earlier, on the convenience piece. And I noticed just looking at your factory-to-satellite ratio, specifically internationally you have such a high satellite-to-factory – you have almost 2.3 satellites per factory store. And then the opposite is the case, really, domestically. I'm just wondering if maybe you can comment on the profitability, not specifically but just generally speaking, the profitability of having more satellites to factories? And where you see an optimal mix down the road?

<A – James Morgan>: Jay, it's Jim. I'll start on that. Doug might want to add to it. There's sort of -- and what you see, which is very accurate with the international versus domestic, there's a bad news and a good news there. The bad news is they figured out that's how much better that ratio would be earlier than we did over here. And they have paced us on that -- and set the pace on that. And the good news is that means we've got a lot of factory capacity here domestically, both Company stores and franchisees, from which we can support a good number of satellites, a good number of smaller stores.

So I would tell you it's going to depend on the size of the stores. But we could certainly have in most areas a handful of satellite stores for every factory store that we've got out there, and I think be in pretty good shape. Now that'll depend, Jay, on whether the satellite stores are fresh shops or hot shops or smaller. We do, do smaller factory stores. For example, the one we did in North Winston a couple of months ago was what we call a 65, just a smaller producing machine. But that in general, I think, is where we're heading.

<Q>: And can you control that from a franchise standpoint?

<A – James Morgan>: I don't know about the word control, but I think that what -- we're all seeing it pretty much the same way. So I think slowly but surely -- one of the really bright parts of this past couple of quarters is the communication we've had with our franchisees where they're seeing the opportunity the same way we are. I think they're going to wait and let us lead and do a better job of proving the merits of it. But yes, I think control, by setting the example and by showing the economics of it, they will join with us. And I think that we'll all be heading in that same direction. As a matter of fact, a number of them have already come to us with some development plans for new stores. And that's what's in our ability to approve.

<Q>: Right. Okay. Great, thanks for your help. Congratulations on a good quarter, and good luck.

<A – Douglas Muir>: Thank you.

Operator: [Operator Instructions] We'll go next to Buzz Zaino with Royce & Associates.

<Q – Boniface Zaino>: Good afternoon folks. Couple of questions here. One, commodity costs are now moving against you, wheat price is moving up. How are you budgeting that? Is this a surprise as these prices do move up?

<A – Douglas Muir>: Buzz, not -- it's not a surprise. The markets have been volatile. We have -- when we think we can lock up prices of wheat or shortening that makes sense, we are not afraid to buy ahead. We have already purchased substantially all of our shortening needs for the remainder of the year. So we're pretty well insulated there. We're not quite so far out on wheat as we are on shortening. So we do have some exposure to rising costs of flour if the economy heats back up, or for some other reason the cost of wheat goes up.

<Q – Boniface Zaino>: Okay. Let me try to figure out the international revenue flow. We can add back in the foreign exchange effect. And that would give you a few percentage increase in revenues, the -- apples-to-apples. But the international franchises -- substantially -- franchisees substantially increased number of stores in the last year. That -- by about a third, I would guess. That doesn't seem to be reflected in revenues.

<A – James Morgan>: Buzz, it's Jim. Probably a couple of reasons for that. I'll give you one. Number one, the great majority of the stores being opened were the smaller stores. And when we – in the last two years we've opened about 200 overseas. I'm looking at Doug to make sure I'm remembering that number right. but -

<A – Douglas Muir>: Round figures.

<A – James Morgan>: 200. And we're coming off, therefore, the honeymoon period on over 50% of the international stores we've got. So that's going to make the – if you're coming off honeymoon periods from big stores and the new stores you're putting online are small stores, then that's going to make those revenue comparisons a lot more difficult for a while here.

<Q – Boniface Zaino>: Okay. And did you shut some -- have the -- international stores during the past quarter? You had mentioned you were getting out of some markets?

<A – Douglas Muir>: The Company sold and re-franchised its four stores in Canada in the fourth quarter. In terms of what international franchisees did, there were a total of six closings in the franchise community outside the United States in the quarter, against about 24 openings as I remember.

<Q – Boniface Zaino>: Okay. And lastly on balance sheet, you have to – what you've been through, it's great to see 21 million in cash on the balance sheet. Do you use that on an operating basis? Or could you use some of that to pay down the continuing debt?

<A – Douglas Muir>: We don't need \$21 million to operate the business. And I agree with you, it's nice to have a substantial cushion for a rainy day.

<Q – Boniface Zaino>: Okay. Now I had said last thing, but here's one other thing. You -- now introducing media spending. How much will that be in certain markets? Will that be a significant factor?

<A – Douglas Muir>: It's not significant, because we're really at this time only looking at two markets that would have a significant effect this year. Again, if TV continues to be as successful as we – as some initial testing we've done suggests it will be, then that spend could go up.

<Q – Boniface Zaino>: Good. Thanks very much.

<A – Douglas Muir>: Thank you.

Operator: [Operator Instructions] And there are no further questions. I'd like to turn the conference back to our speakers for any additional or closing remarks.

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**Brian K. Little, Director, Corporate Communications**

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Thank you operator. As a reminder, this webcast conference call will be archived and available on the Krispy Kreme website at krispykreme.com. There will also be an archived telephone replay available shortly following the conclusion of this call. You will find the dial-in numbers and the access pass code in our earnings release. We thank you for joining us, and have a good evening.

Operator: Thank you everyone. That does conclude today's conference. We thank you for your participation.

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