

RETAIL SECTOR WEEKLY

Key Retail News and Commentary

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Did You Know...?

Sales in the joint women's/ girls' plus-sized clothing and men's/boys' big and tall clothing market are expected to balloon nearly 41% over the next five years, according to Plus-Size and Big and Tall Clothing in the U.S., a new report from Published Facts. The hefty market demand is primarily due to the country's growing obesity rate.

Vote May not Lead To Strike

Will they strike or won't they?

Even though Southern California grocery workers have given their union the go-ahead to call a strike, that doesn't mean a walkout or an employer lockout is imminent, Wall Street analysts and labor experts reported last week. In fact, the strike authorization vote helped jump-start stalled talks toward a resolution.

It's all part of a high-stakes, elaborately choreographed form of theater seen when a supermarket employment contract comes up for renewal. But there are some differences in strategy this time.

The Albertsons, Ralphs and Vons chains may have been looking for a sign of just how committed the union's rank and file were to the idea of another potentially devastating work stoppage, observers said. That would give the grocers a better sense of how hard they could push for more concessions in contract negotiations, which had broken off.

Talks had bogged down over wage and health insurance issues.

For its part, the United Food and Commercial Workers International Union is following a new script.

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Retailer of the Week: Cost Plus Inc.

Really poor performance all around led the operating loss for Cost Plus to leap from just over (\$4.8) million for the first quarter of fiscal 2007 to (\$16.8) million for the first quarter of fiscal 2008, representing an increase in the operating loss of just about 350%! In addition, the ongoing poor performance is starting to manifest itself into what was a fairly strong balance sheet. With this entire sub sector of retail doing very poorly, including leading chains Pier 1 and Bombay Company, Global Credit is very pessimistic about potential future operating performance. With this latest spurt in losses, Global Credit is downgrading Cost Plus from a "D-" to an "E+", now reflecting a fairly high amount of credit risk.

BACKGROUND

Cost Plus is specialty retailer of casual home furnishings and entertaining products. The Company also offers food and drink to set itself apart from the competition. The Company operates under the Cost Plus and World Market trade names with the latter mostly for West Coast store locations. Despite all of its financial woes, Cost Plus continued to expand fairly rapidly opening five net new stores in the first quarter of this year with 292 stores in 34 states in operation as of May 5, 2007. However, only seven net new sites are planned for the remainder of the year as heavier losses have now forced management to reconsider their expansion strategies.

FINANCIAL PERFORMANCE

Even with many efforts initiated to revive consumer traffic, Cost Plus saw lower average tickets and slower store counts. In addition, the sizable comp store sales decline in this year's first quarter led to the deleveraging of occupancy related expenses against a lower sales base. In turn, this had a sizable negative impact on margin dollars and the corresponding percentage.

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Bankruptcy Blotter

... **Hancock Fabrics** reported sales for the period from May 6th through June 2nd were \$27.9 million, generating a loss for the period of \$5.7 million.

... In other news, **Hancock Fabrics** dismissed **PricewaterhouseCoopers LLP** as its independent registered public accounting firm. The company has engaged **Burr, Pilger & Mayer LLP** as its new independent registered public accounting firm.

... **DJM Realty**, the real-estate arm, of **Gordon Bros.**, purchased the rights to sell the leases at 61 soon-to-be shuttered **Rag Shops** stores for at least \$2.75 million following a bankruptcy court ordered auction. Earlier this month **Hilco Merchant Resources LLC** paid \$16.2 million to conduct GOB sales at the Rag Shops' stores.

... **Schulze Asset Management, LLC** has made a \$38 million "going concern" bid for substantially all of the assets of **Tweeter Home Entertainment Group, Inc.** Schulze would also assume \$8 million of Tweeter's "cure costs" as well as provide the company with a \$10 million Junior DIP line of credit. The bid includes the purchase of Tweeter's 18.75% interest in **Tivoli Audio, LLC**. Separately, **Whippoorwill Associates, Inc.** and **Bay Harbour Management, L.C.** have teamed up to make a \$10 million bid for just Tweeter's Tivoli ownership interest. An auction is scheduled for July 10th.

... **Tower Records** reached a settlement with **Great American Group LLC** and **Hudson Capital Group LLC**, providing Tower with \$3.1 million in a dispute over the valuation of inventory sold during GOB sales conducted by Great American and Hudson. A hearing on the settlement is scheduled for July 11th.

... Workers represented by the **United Auto Workers** union at **Delphi Corp.** ratified, by a 68% to

32% vote, a new cost-cutting labor agreement with the auto supplier, clearing a key hurdle in the company's effort to exit Chapter 11. The agreement, which runs until September 2011, calls for wages of \$14.50 to \$16.23 an hour for all current workers, down from \$27.00 per hour for workers hired before the lower-tier wage scale.

... **Delphi Corp.**, fresh off reaching a labor pact with the **UAW**, has won court approval to push off until the end of the year a deadline for filing its Chapter 11 restructuring plan.

... In other news, **Delphi Corp.** reported a net loss for May of \$45 million, narrowing the loss reported in April of \$66 million. Sales for May rose to \$1.47 billion from \$1.32 billion in April, for a total of \$6.77 billion in sales so far this year.

... **Collins & Aikman Corp.** is seeking court approval for an agreement with **DaimlerChrysler Co.** and **General Motors Corp.** to continue making certain component parts in its plastics and convertibles plants after June 30th, that supports its ongoing asset sales and averts a forced shutdown of its plastic operations. The automakers will foot the bill for funding the continued operations and have an option to buy certain of the facilities by August 31st.

... For the month of May, **Tower Automotive Inc.** reported a net loss of \$4.9 million on sales of \$98.5 million. The net loss included reorganization expenses of \$3.7 million.

... **Pacific Lumber Co.**, saying its available cash is likely to dwindle to just \$123,000 next month, reached a deal to borrow \$75 million from **Marathon Structured Finance Fund L.P.** The loan is contingent on Pacific Lumber repaying \$40 million owed on a pre-bankruptcy revolving loan. A hearing is scheduled for July 19th.

Feedback?

Questions?

Suggestions?

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Management on the Move

... **IGA** named **David S. Bennet** VP, Procurement and Private Brands, a new position within the organization, with responsibility for the procurement of all IGA Brand products and private brands that will be developed. Mr. Bennet most recently held the position of General Manager/Senior Director of Business Development with **Daymon Worldwide, Inc.**

... **Rite Aid Corporation** announced that **Brian R. Fiala**, formerly SVP at **Target Corporation**, is joining the company as EVP of Store Operations. Mr. Fiala will be responsible for all store operations,

reporting directly to **Jim Mastrian**, Rite Aid's COO.

... **Rite Aid** also announced the election of **Michael N. Regan** to the company's Board of Directors, increasing the size of the Board to fourteen. Mr. Regan is the retiring CFO of **The St. Joe Company**, a publicly traded company with significant real estate development and timberland operations.

... In addition to the above, **Rite Aid** appointed **John Coster, Ph.D.**, a health care and government affairs veteran with extensive experience in state

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Management on the Move

(Continued from page 2)

and federal health care programs and regulatory issues, to the position of VP, Federal Affairs and Public Policy. Mr. Coster most recently served as VP, Policy & Programs, for the **National Association of Chain Drug Stores**.

... **ShopKo** appointed **Rod Ghormley** as SVP, General Merchandise Manager – Home. Mr. Ghormley comes to ShopKo from **Amazon.com**, where he served as Divisional Merchandise Manager with responsibility for home textiles, tableware, home furnishings, floorcare, clothing care and organization.

... **The Talbots, Inc.** appointed **Trudy F. Sullivan** as the company's President and CEO, effective August 6, 2007. Ms. Sullivan will also become a member of the Board of Directors. Ms. Sullivan succeeds **Arnold B Zetcher**, who previously announced his intention to retire, but will remain Chairman of the Board through March 31, 2008. Ms. Sullivan most recently served as the President of **Liz Claiborne, Inc.**

... **Charming Shoppes** announced the promotion of **LuAnn Via** to Group Divisional President, with leadership responsibility for the **Lane Bryant** and **Cacique** brands, reporting to **Dorrit Bern**, Chairman, CEO and President. Ms. Via succeeds **Lorna**

Nagler, who was President of **Lane Bryant** and who left the company to pursue other career interests.

... **Tween Brands, Inc.** promoted **Paul C. Carbone** to the position of SVP and CFO and **Kurt E. Gatterdam** to the position of VP, Treasurer, reporting to Mr. Carbone. Mr. Carbon joined the company as SVP – Finance, coming over from **Limited Brands, Inc.** in September 2006.

... **Le Chateau Inc.** announced the departure of **Frank Niro**, SVP, Footwear, who originally joined the company as a consultant in May 2005, to pursue other challenges. The company remains committed to the footwear business.

... **John W. Swatek** was named CFO of **Home Décor Products Inc.**, a multi-channel retailer of kitchen and bath products, appliances and related items for the home. Mr. Swatek previously was SVP and CFO for **Hanover Direct Inc.**

... **Steven L. Korby** was appointed as interim CFO for **CSK Auto Corporation** replacing **James B. Riley**, who resigned to join **Ormet**. Mr. Korby has been serving as a consultant to the company since July 2006 and is a partner with **Tatum, LLC**, an executive services and consulting firm.

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Report

Off the Rack

... **Jones Apparel Group, Inc.** entered into a definitive agreement to sell its wholly owned subsidiary **Barneys New York** to an affiliate of **Istithmar**, a Dubai-based private equity and alternative investment house for \$825 million in cash. The transaction is expected to close in the third quarter.

... A Lebanese private equity firm appears to have reached a deal to buy **Nordstrom Inc.'s** Faconable brand of upscale apparel and accessories for approximately \$200 million.

... **Barington Capital Group, L.P.**, which represents a group of investors that owns over 3.2% of the outstanding common stock of **Dillard's, Inc.** is pushing for a meeting with **William T. Dillard, II**, the Chairman and CEO of the company to discuss ways of increasing shareholder value.

... In the process of restructuring, **Limited Brands Inc.** announced it would double the size of its stock buyback program, cut 10% of its corporate jobs, raise \$1.25 billion of debt, and is exploring alternatives for its **Limited** chain and other core

assets including real estate. The company plans to focus on intimate apparel and beauty products through its **Victoria's Secret** and **Bath & Body Works** chains.

... Reacting to lower than planned sales, **Charming Shoppes, Inc.** lowered its second quarter earnings guidance to a range of 18 cents to 20 cents per share from previous guidance in the range of 25 cents to 27 cents per share. Earnings for the second quarter last year were 24 cents per share.

... **Christopher & Banks Corporation** reported sales for the first quarter ended June 2, 2007 of \$149.4 million, up \$6.8 million or 4.8%, versus sales of \$142.5 for the comparable period last year. However, net income of \$11.7 million for the quarter represented a 20.1% decline versus prior year.

... With its disappointing results for the first quarter and bulging inventories, **Christopher & Banks**

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Off the Rack

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Corporation has lowered its earnings guidance for the second quarter to a range of 11 cents to 12 cents per share, compared to actual earnings of 21 cents per share last year.

... **Calvin Klein, Inc.** plans to launce five freestanding Calvin Klein-branded better specialty retails stores in November 2007 to showcase a full range of men's and women's better apparel and accessories. The stores will be located in Los Angeles, Denver, Bloomfield Hills, Michigan, Atlanta, and Natick, Massachusetts.

... **Kohl's Corp.** removed some lines of its Daisy Fuentes clothing brand following allegations that the Guatemalan factory where the clothes are made is a sweatshop, where workers are humili-

ated and forced to work unpaid overtime.

... Expecting to fully tap its U.S. growth opportuni-

ties during the next several years, **Jos. A. Bank Clothiers Inc.** is beginning to explore opening stores overseas. The company now operates 389 stores in the U.S. with expectations to reach 500 in the near future.

... **Tween Brands, Inc.** launched the roll-out of **Webkinz** plush toys in its **Limited Too** and **Justice** stores just in time for the back-to-school season. The stuffed animals come with a code that allows access to a Web site where users can adopt a virtual version of the pet.

Health & Beauty Aids

... **Rite Aid Corp.** posted net income of \$27.6 million for the first quarter ended June 2, 2007, surprising Wall Street, which had been forecasting a loss for the retailer. Sales for the quarter rose to \$4.46 billion from \$4.34 billion, with comp store sales up 2.3%.

... With the acquisition of the **Brooks and Eckerd** stores finally accomplished earlier this month, **Rite Aid** immediately began to fully convert 23 Brooks and Eckerd "pilot" stores, representing various store designs, and integrating its six new distribution centers. The company's entire soup-to-nuts conversion/integration/rebranding campaign is expected to take 16 months and cost \$425 million.

... Increases in prescription sales, especially among profitable generic medications helped **Walgreen Co.'s** third quarter profit climb nearly 20% to \$561.2 million, versus earnings of \$469.2 million for the comparable period last year. Sales for the quarter grew 12.5% to \$13.70 billion.

... In other news, **Walgreen's** began construction on its first Hawaiian store set to open in November to the chagrin of **Longs Drug Stores**, which has long dominated the market. Two more Walgreens stores will open early next year with the company looking at as many as 40 stores in the Hawaiian market. .

... A **ShopRite** store in Neptune, New Jersey saw the grand opening of **ExpressCare**, a retail health

care center, and the first of a planned 42 locations. Six will open in New Jersey and Pennsylvania this summer, with another 12 expected to be operational by next March. ExpressCare has signed agreements with three separate multi-store ShopRite owners.

... **Cardinal Health** completed its tender offer for **VIASYS Healthcare**, with only 88% of the outstanding shares tendered. However, the acquisition will be completed shortly pursuant to a short-form merger procedure available under Delaware law.

... The **American Medical Association (AMA)** is calling for both state and federal investigations into the health clinics operated in retail stores, alleging that the facilities do not offer appropriate or comprehensive care and could put patients at risk. The clinics have become more popular of late, with chains such as **Wal-Mart**, **Walgreen** and **CVS** all getting into the business.

... The U.S. Supreme Court refused to reconsider a lower-court decision in favor of a controversial marketing arrangement between generic drug maker **Barr Pharmaceuticals** and brand-name drug company **AstraZeneca**. The widely followed case goes to the heart of the practice of "reverse" payments and "authorized" generics, under which a branded drug maker will pay a generic firm to keep a generic version of a patented drug off the market or to market an "authorized" version of the patented product.

Did You Know...?

The market for products bought by and for the 25.6 million member teen market will experience a slight growth spurt, increasing from \$189.7 billion in 2006 to 208.7 billion in 2011, despite an estimated 3% decline in the 12 to 17-year-old population.

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Heard in the Grocery Aisle

... **Whole Foods Market Inc.**'s CEO **John Mackey**, in his battle with the **FTC** over his proposed acquisition of **Wild Oats Markets Inc.**, accused the **FTC** of acting in "a biased, adversarial and arrogant manner" and of using "bullying" and "unethical" tactics. Not a good way to win friends and influence people.

... **The Kroger Co.** reported that its first quarter net income was \$336.6 million, up from \$306.4 million during the comparable period last year. First quarter sales increased 6.7% to \$20.7 billion.

... With its improved operating results **Kroger** also reported that it will no longer need to devote a third of its cash to servicing debt, and is stepping up its stock buyback program to \$1 billion. The company has reduced debt by \$32.2 billion while improving EBITDA by \$522 million since 2000.

... In other news, the **United Food & Commercial Workers** Local Unions 408 and 455 in Houston and Local Union 540 in Dallas ratified the new labor contract agreement with **Kroger Co.** The new contract covers 13,000 Kroger associates in 202 stores.

... Officials of **Ahold** expect to complete its pending sale of **US Foodservice** to **Kohlberg Kravis Roberts** and **Clayton, Dubilier & Rice** despite the unit pulling back a bond offering of \$650 million that would have helped finance the \$7.1 billion deal.

... **ShopRite's** parent company, **Wakefern Food Corp.** is in talks with **Stop & Shop**, a unit of **Ahold**, about possibly acquiring nine of **Stop & Shop's** struggling southern New Jersey stores, including markets in Galloway Township, Atlantic and Middle Township, Cape May County.

... After more than 60 years of selling almost exclusively to its **ShopRite** members, **Wakefern Food Corp.** is expanding its wholesale sales to other supermarkets and institutional customers,

both within and beyond its traditional Northeastern market. The company recently began selling more than 300 **ShopRite**-brand grocery and non-food items to **Heinen's Fine Foods**, a 17-store chain based in Ohio.

... Three weeks ago, **Safeway Inc.** quietly opened a stand-alone restaurant in Redwood City, California called **Citrine** without a word of advertising or publicity. The eatery is a test for the grocer, like most food retailers, looking for more ways to sell prepared foods. So far, **Safeway** has kept its name tucked in the shadows of **Citrine** and has commented little on the restaurant.

... **Sobeys Inc.** reported sales for the fiscal year ended May 5, 2007 of C\$13.03 billion, up 2.5% versus sales for the prior year of C\$12.72 billion. Net income for the year was C\$173.4 million, down 8.5% versus prior year. Subsequent to year end **Empire Company Limited** completed the acquisition of **Sobeys** through the purchase of common share not already owned by **Empire**.

... **VG's Food & Pharmacy** is buying two **Farmer Jack** stores in Fenton, Michigan and one in Shelby, Michigan, from **A&P**. **VG's** intends to re-open one of the Fenton locations and the Shelby store under the **VG's** name in July, but acquired the other Fenton site as a real-estate investment.

... Following years of planning, **Ukrop's Super Markets, Inc.** is set to open its first store in Southwest Virginia. The new 58,700 square foot store will be located in the Ivy Market shopping center in Roanoke. The company now operates 29 supermarkets.

... **Seven & I Holdings**, parent of **7-Eleven**, plans to invest about \$2.4 billion in the next four years to open 1,000 convenience stores in the U.S. and revamp existing outlets. The Japanese company has not been aggressively investing in its 6,000 U.S. stores in the past few years. **Tesco** is already having an impact on the U.S. market and it hasn't opened a store yet.

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FYI for the DIY

... **MSC Industrial Direct Co., Inc.** reported sales for the third quarter ended May 26, 2007 of \$431.1 million, a 30% increase over sales of \$329.8 million for the comparable period last year. Net income for the quarter was \$45.8 million, a 23.6% increase over the prior year.

... **Griffin Land & Nurseries, Inc.** settled a lawsuit that had been filed by a dozen Guatemalan workers recruited by a labor contractor. Although specific terms of the settlement will remain confidential, **Griffin** has agreed to provide the workers with

financial compensation out of concern for the hardship they allege they experienced.

... In other news, **Griffin Land & Nurseries** reached an accord for a settlement with the land use commission of the Town of Simsbury, Connecticut for a proposed residential development. **Griffin** has agreed to increase the amount of open space in the development and to accept a significant reduction of the number of residential units.

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Specialty Items

... **The New York Stock Exchange**, with the intention to initiate delisting procedures, suspended trading on **The Bombay Company, Inc.'s** common stock. The company expects is taking steps to arrange for its shares to be quoted on the OTC Bulletin Board.

... For its fiscal first quarter ended June 2, 2007, **Bed Bath & Beyond Inc.** reported sales of \$1.55 billion, an 11.3% increase versus sales of \$1.40 billion for the comparable period last year. Net income for the quarter was \$104.6 million, a 4.2% increase over the prior year, reflecting the soft retailing environment, especially sales related to the home.

... On June 25, 2007, **Cost Plus** entered into a secured five-year Credit Agreement allowing for cash borrowings and letters of credit of up to \$200 million. The Agreement includes three options to increase the size of the revolver by up to \$50 million in the aggregate.

... With operating results not meeting expectations, **Jo-Ann Stores** will open only six stores this year, compared to 26 stores opened last year.

... **Pier 1 Imports Inc.'s** Fort Worth headquarters building is too big, too grand, too magnificent and too expensive to be occupied alone by the trouble company, according to the company's new CEO. Options are being discussed regarding the 460,000 square foot building.

... **IKEA** officially began operating fully its state-of-the-art southeastern distribution center in Savannah, Georgia. The 685,000 square foot facility

represents the first phase of a project that eventually will expand to 1.7 million square feet.

... Four-store **Bloom Bros. Furniture** is closing after failing to earn a profit last year and so far this year. Liquidation sales have begun and the company intends to honor contracts with customers and vendors.

... **Golden Acquisition LLC**, a newly formed private equity firm run by executives of asset disposition specialist **Hudson Capital Partners**, emerged as the second major investor in **Domain Home**, joining **Synergy Enterprises**.

... **AutoZone** opened its 4,000th store in Houston, Texas. AutoZone opened its first store in Forrest City, Arkansas on July 4, 1979 and today has stores in all 48 contiguous states, the District of Columbia, Puerto Rico and Mexico.

... After a rough 2006, **The Pep Boys - Manny, Moe & Jack** has posted a profit two quarters in a row, giving rise to turnaround stories. Investors have responded pushing up the company's stock recently to a 52-week high, and up 47% since the beginning of the year.

... **Guitar Center, Inc.** signed a definitive agreement to be acquired by affiliates of **Bain Capital Partners, LLC** in a transaction valued at \$2.1 billion including assumed debt. Under terms of the agreement, stockholders will receive \$63.00 per share in cash, which represents a 26% premium over the company's closing price on June 26th.

Did You Know...?

As part of an effort to appease concerns over its trade surplus with the U.S., China reduced the tax refunds to exports of 2,831 products, including shoes and apparel, as of July 1st.

The Global World of Sports and Footwear

... **The Finish Line, Inc.** reported a net loss of \$3.9 million for the fiscal first quarter ended June 2, 1007, versus net income of \$4.4 million for the comparable period last year. Net sales for the quarter decreased slightly to \$288.3 million compared to \$289.0 million last year.

... With disappointing revenues through the first two months of the second quarter, **West Marine Inc.** reduced its earnings forecast for the year to a range of 24 cents to 34 cents per share versus previously issued guidance in the range of 45 cents to 55 cents per share.

... Having unloaded seven of its eight resorts in recent months, **American Skiing Co.** is shedding its corporate skin as well. The company's remaining assets, principally The Canyons Resort outside of Park City, Utah, will become the property of **Oak Hill Capital Partners**, a private equity firm

that was American Skiing's majority shareholder.

... **GSI Commerce Inc.** announced the pricing of \$125 million unsecured 2.5% Convertible Senior Notes due June 1, 2027. This represents an increase of \$25 million from the transaction size announced previously.

... **Stride Rite** reported that net income for the second quarter ended June 1, 2007 fell to \$14.2 million compared to net income of \$16.9 million for the comparable period last year. The latest quarter includes pre-tax expenses of \$800,000 related to its **Robeez** integration costs and the pending merger with **Payless ShoeSource Inc.** Sales rose 8% to \$209.2 million.

... **Payless ShoeSource, Inc.** and **H.H. Brown Shoe**

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The Global World of Sports and Footwear

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Company, Inc. signed a multi-year agreement making Payless the exclusive retailer for the **Dexter** brand of footwear and accessories in the U.S. and the rest of the Western Hemisphere.

... Some analysts believe that **Quiksilver** may divest its **Cleveland Golf** unit given current market price pressures in the golf club segment and Quiksilver's oft stated focus of building a **Rossil** branded soft goods business and reducing its debt level. Quiksilver owns 64% of Cleveland and is believed to be able to get upwards of \$100 million for the golf company.

... As of July 1, 2007, the start of its fiscal year, **Collegiate Pacific** will be known as **Sport Supply**

Group, Inc. and its ticker will change from BOO to RBI.

... According to **Corporate Research International's** second quarter RealPeopleRatings.com survey of consumer perceptions, **Dick's** and **Stride Rite** stores offered the best customer service in their respective retail segments.

... The monthly **U.S. Census Bureau Report** put the sporting goods sector's sales at \$2.86 billion against \$2.82 billion last year for the month of April. Through the first four months of the year, sales totaled \$10.64 billion, up a healthy 5.5% from last year.

Options and Resources

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Did You Know...?

The Federal Reserve left the federal funds rate at 5.25%, where it has been for the past year. Analysts believe the Fed officials could remain on hold through the rest of this year and well into 2008.

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Mass Merchant Musings

... Research firm **NPD Group** will provide **Wal-Mart Stores Inc.** and its **Sam's Club** unit with consumer tracing data, according to an agreement announced last week. Information, including what was bought, the prices which were paid and where the purchases took place, will be collected from NPD's panel of over 3.5 million consumers. The agreement comes as Wal-Mart is working to improve its lagging comp store sales.

... In South Florida, **Sears Holdings Corp.** has remodeled 13 **Kmart** stores featuring a new Internet café and the addition of **Sears** brands like Craftsman, DieHard and Kenmore.

... **Target** will build its second online fulfillment center on a 100-acre site in Tucson, Arizona. **Diamond Ventures** and Target will jointly develop the site, which is expected to open in spring 2009.

... In other news, **Target** and **Disney** have signed a deal that will give Target exclusive rights to a full line of **Little Einstein** merchandise from Disney starting in July.

... **Vonage** may be embroiled in a fierce patent struggle with **Verizon**, but that has not stopped the VoIP provider from expanding its retail reach, agreeing to have its products and voice service sold through **Meijer**. Meijer will offer several

Vonage-enable products in its 180 locations.

... **Costco** reported earnings of \$223.9 million for its third quarter ended May 13, 2007, a 5% drop from the comparable period last year. Included in this year's results is a \$30.2 million charge to its sales-return reserve, the result of an internal study prompted by rampant returns on high-ticket consumer electronics.

... For the third quarter ended June 2, 2007, **Family Dollar Stores, Inc.** reported sales of 1.65 billion, up 5.4% versus sales of \$1.57 billion for the comparable period last year. Net income for the quarter was \$60.4 million, up 6.1% versus last year.

... **ShopKo** broke ground earlier this month on the construction of the first new ShopKo store to be built in six years. The new store in Suamico, Wisconsin, signals a new growth phase for the company which has plans to open several more new stores in the coming years, while remodeling existing stores with the company's new and updated look.

... **FAO Schwarz** opened a new section in its store on Fifth Avenue in New York that allows girls to customize their own Barbie dolls. The "boutique" will occupy 1,500 square feet in the store.

Did You Know...?

The Retail Sector Newsletter has increased readership each week since publishing began?

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Rating Changes and Outlooks

S&P Rating Changes				
Company	Credit Rating		Credit Outlook	
	Current	Prior	Current	Prior
TOYS R US INC - NEW CO	B	B-	STABLE	NM
LIMITED BRANDS INC	BBB-	BBB	NEGATIVE	STABLE
TOYS R US INC - NEW CO	B	B-	STABLE	NM
FINLAY ENTERPRISES INC	B	B	NEGATIVE	STABLE
FINLAY FINE JEWELRY CORP	B	B	NEGATIVE	STABLE
RESTAURANT CO (INC)	B-	CCC+	STABLE	NM
JO ANN STORES INC	B-	B-	STABLE	NEGATIVE
LOEHMANN'S HOLDINGS INC DE	B-	B	STABLE	STABLE
JACK IN THE BOX INC DE /FKA FOODMAKER INC	BB-	BB-	STABLE	NEGATIVE
DAVE & BUSTERS INC	B-	B-	STABLE	NEGATIVE
KROGER CO,THE	BBB-	BBB-	POSITIVE	STABLE
VISTAR CORP	B	NM	STABLE	NM

Vote May not Lead To Strike

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There have been no loud parking-lot rallies in front of supermarket shoppers. Union officials have stayed out of the public eye, opting for telephone news conferences attended by carefully selected workers telling their own stories.

The change partly reflects the union's formal break with the AFL-CIO in June 2005 and its jump to the Change to Win federation, experts said.

During the 2003-04 strike and lockout, the union received national labor movement support, but mostly after the grocery workers were already on the defensive. Now, as part of Change to Win, the Southern California operation is getting more help upfront from national union officials in planning strategies.

Another change has been in the use of local religious and community leaders.

The new approach appears to acknowledge that shoppers might lose their patience with another bitter labor impasse much sooner than they did last time, during the 141-day strike and lockout that left many union members with staggering debts and cost the employers an estimated \$1.5 billion.

The union has coalesced around how much its members have suffered through the healthcare agreement from the last contract. Half of those hired since the strike and lockout have no health insurance, one-third are covered by a spouse or a parent, and 10% rely on public health programs. Just 7% of recent hires are getting insurance from the chains.

Executives at the three chains said labor agreements recently had been reached elsewhere, sometimes shortly after strike authorization votes. Union workers and Kroger Co., for example, ratified a three-year contract last Monday for stores in Dallas and Houston that had been hung up over health coverage issues.

In California, the contract for 65,000 workers from Bakersfield to the Mexican border has been extended twice since its March 5th expiration date.

Ralphs is a division of Kroger, Vons and its Pavilions stores are owned by Safeway Inc., and Albertsons is owned by Supervalu Inc.

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Hi Tech Entertainment

... **Circuit City** is consolidating and relocating two distribution centers into a new fulfillment facility in Scranton, Pennsylvania, that will optimize online orders.

... **Best Buy** now says that the number of stores in the U.S. and Canada could approach 1,800, up from its prior plan for 1,400. Currently the company operates 1,035 Best Buy, Future Shop and Pacific Sales stores in those markets.

... **Blockbuster** plans to close 282 stores in the U.S. this year to improve operating margins and expand domestic share. The company's effort to accelerate closures of underperforming marginal stores comes as the company is spending heavily to beef up its online-rental business to compete with **Netflix Inc.**

... **GameStop Corp.** will redeem all \$120 million of the outstanding bonds remaining under its Senior Floating Rate Notes due 2011. The company

expects to incur a one-time charge of approximately \$3.8 million in the third quarter associated with the redemption.

... **Donald Trump** and **Staples** announced a licensing agreement, giving Staples the right to use the real estate mogul's name for a line of office furniture.

... Underlining its expansion from online to retail sales, **Dell Inc.** launched desktop and notebook PCs at a **Macy's** department store in New York last week. Dell is hoping that its image as a stodgy maker of desktop and notebook computers is about to end, and it's banking on some new color options and designs to do the trick.

... **Ingram Micro Inc.** will release its financial results for the second quarter ended June 30, 2007 after the market closes on Thursday, July 26th. Be sure to look for **Global's** updated analysis and assessment shortly thereafter.

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Retailer of the Week: Cost Plus Inc.

(Continued from page 1)

Increased expenditures in advertising and store labor did not pan out in improved sales. Therefore, expenses rose despite the lower revenues. Higher borrowings under the Company's revolver and interest under capital leases for property sold now leased back forced the increase in interest expense. This year's first quarter net loss reflected a higher tax benefit.

Income Statement, First Quarter

	2007	2008
Net Sales	\$212 mm	\$207.9 mm
Comp Store Sales	-4.30%	-8.10%
Store Count	272	292
Gross Profit	\$65.4 mm (30.7%)	\$58 mm (27.9%)
SG&A Expenses	\$70.2 mm (33%)	\$74.8 mm (36%)
Interest Expense	1.1 mm	\$1.9 mm
Loss before Tax Benefit	(\$5.9) mm	(\$18.7) mm
Net Loss	(\$3.5) mm	(\$11.1) mm

Balance Sheet

	2007	2008
Cash	\$15.3 mm	\$3.3 mm
Inventory	\$237.2 mm	\$260.3 mm
Current Assets	\$280.5 mm	\$304.8 mm
Total Assets	\$500.5 mm	\$559.9 mm
Accounts Payable	\$38.9 mm	\$53.1 mm
Working Capital Revolver (classified as short term debt)	\$0	\$15.1 mm
Other Long Term Debt	\$65.7 mm	\$35 mm
Total Liabilities	\$192.8 mm	\$279.3 mm
Current Ratio	3.6:1	2.7:1
Leverage Percentage	39%	50%
Working Capital Coverage	8.6 months	7.7 months

Did You Know...?

Sales of new homes fell in May by 1.6% to a seasonally adjusted annual rate of 915,000 units. This followed a 12.5% surge in April sales, which was the biggest one-month jump in more than a decade.

Ongoing losses have forced Cost Plus to burn through most of its cash and now incur borrowings under its unsecured revolver. The Company is considering a larger asset based credit facility to handle holiday needs later this year. There was just \$21.6 million in availability as of May 5, 2007.

During the past twelve months, Cost Plus has sold two distribution centers and entered into sales-leased back agreements. Capital leases for these arrangements stood at \$81.6 million at the end of this year's first quarter. In addition, Cost Plus maintained a \$40 million separate revolving credit agreement to undertake expansion and improvement for one of the distribution centers. In July 2007, the landlord for that particular facility will repay all borrowings and add that amount to future lease payments. At the end of this year's first quarter, there was \$35 million outstanding under this line of credit.

While liquidity, leverage, and working capital coverage remained adequate, all three are clearly moving in the wrong direction. If revolver debt continues to grow while cash balances remain nominal, look for all three to move more towards an uncomfortable level. We also note that is is primarily inventories (and looking bloated at that) that are driving the still strong current ratio.

In addition, while sales are declining inventories are continuing to grow. Cost Plus may see even more margin erosion into the second quarter and beyond. Account payables are up, however, the percentage of inventory financed by vendors and average account payable turns stood at only 20% and 26 days, respectively, at the most recent quarter end. Some of this may be tied to the fact that much of the merchandise is sourced from overseas.

OUTLOOK

A larger secured credit facility will allow for sufficient liquidity for the short term. However, if existing conditions persist into the holiday period and then into next fiscal year, Cost Plus may be facing more dire circumstances. And again, the slow down in housing, rising energy and other prices, and shifts in consumer tastes might point towards no immediate relief for Cost Plus and others in this brutally competitive arena. Therefore, clients should keep a close eye on their exposures and carefully review Global Credit updates and alerts.

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