

# RETAIL SECTOR WEEKLY

## Key Retail News and Commentary

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### REMEMBER...

Concentration can be cultivated. One can learn to exercise will power, discipline one's body and train one's mind.

## Revolving Loans Hurt Banks

The ongoing credit crunch can feel like a battle against garden weeds – remove one problem and another pops up in its place.

Banks have minimized their exposure to high-risk corporate debt by hacking away at the once overwhelming backlog of leveraged buyout debt over the past few months. Yet just recently, other struggling companies have started to turn to their lines of credit for help, leaving banks exposed to junk debt in another – perhaps even riskier – form.

With bankruptcies expected to increase substantially in the coming year and with debt investors unwilling to finance new deals – especially not for companies on the verge of going out of business – these lines of credit have the potential to become a trouble spot for the banks and brokers who've extended them.

Revolving credit facilities are similar to credit cards in that companies are expected to tap them for working capital and then pay it back, rather than use the debt to keep their business afloat.

Banks have avenues to deny companies this form of credit, as demonstrated by Bank of America Corp.'s recent decision not to renew a \$1 billion credit agreement with Sears Holding Corp. and the cancellation by the bank and HSBC Holdings PLC of \$265 million in letters of credit to Talbots Inc. Both Sears and Talbots have been trying to rebound from successive quarters of poor earnings, so it

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## Talbots: Retailer of the Week

We are downgrading Talbots to an "E" high-risk credit with a "negative" outlook. Talbots created quite the wave of news in recent weeks. The loss of two of the company's key letter of credit facilities shows how the credit crunch in the US economy can impact retailers as well. The company claims that it was able to negotiate open credit terms with its vendors, which is probably true in some cases. However, it is certain that the company will lose out on some products, especially if the operations for the company continue to deteriorate. The massive loss for the year can partially be explained away by a goodwill impairment charge of \$134 million and a trademark impairment charge of \$15.6 million, totaling \$149.6 million. The annual loss surely ran deeper, however, showing that the company's operations have really begun to struggle with the slowdown in consumer spending. The marriage of J Jill and Talbots just doesn't seem to be working. Talbots needs to find a way to get its operations under control quickly before it slips further.

The \$20 million per quarter payment on the debt is creating quite a strain on short-term operations and liquidity. The company is not generating enough funds from its retail sales to cover the payments and it is sucking the company dry from a liquidity standpoint. Thankfully, Talbots still had plenty left available on its revolver at year-end.

For 2008, the company is expecting revenues to grow around 3% to approximately \$2.36 billion. With just \$329.1 million in inventory on the books at year-end, we hope the company is correct when it says it has negotiated open credit terms. Comps are expected to fall slightly for the year, with both J Jill and Talbots expected to fall about 1%. Based on current outstanding shares, Talbots is projecting another loss of \$31.8 million for the year. This could prove costly given the \$80 million in current debt coming due in the next twelve months.

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## Revolving Loans Hurt Banks (Continued from page 1)

makes sense banks wouldn't want to be exposed to any more of their debt.

But lenders can't simply back out of these agreements whenever they'd like and, in the risky debt markets, revolvers are often committed to for up to seven years. In the next 12 months alone, the bankruptcy rate is expected to rise from 1% to 2% to as high as 7%, meaning a large number of companies could be forced to turn to their bank lines of credit in the 11<sup>th</sup> hour.

Some companies are already relying on these facilities simply to stay in business. Linens 'n Things, which recently delayed a bond payment as it attempts to stave off bankruptcy, had drawn about \$200 million from its revolver as of year end, compared with \$37.8 million a year earlier. The company is expected to continue to tap that revolver to compensate for its limited cash flow.

Even more unfortunately for the banks, many of these lenient revolvers have been extended to companies in the troubled retail sector. Banks are holding lax lines of credit for such companies as Claire's Stores Inc., Rite Aid Corp., Dollar General Corp., and Michaels Stores Inc., all of which have debt trading at or near distressed levels presently.

To put it in numeric terms, Dollar General, which is solidly junk-rated company, has a \$1 billion revolver with an interest rate of 150 basis points over Libor. With Libor now around 2.9%, that translates into a 4.4% yield on debt for the company at a time when, according to Reuters Loan Pricing Corp., the average loan with a similar credit rating trades around 697 basis points over Libor, effectively yielding about 9.87%.

It certainly will be interesting to see what interest rates we will be seeing on the renewals of revolvers coming due this year, especially in retail.

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## Rating Changes and Outlooks

Company	S&P Credit Rating		S&P Credit Outlook		GCS Credit Rating
	Current	Prior	Current	Prior	Current
GAMESTOP CORP	BB	BB	POS	STA	B-
155 EAST TROPICANA LLC	CCC+	B-	NM	NM	E
SAKS INC/FKA PROFFITTS INC	BB-	B+	POS	NM	C
OMNICARE INC	BB	BB+	NEG	NEG	D
LINENS HOLDING CO	D	CCC+	NM	NEG	F+
BRODER BROS CO/SPORTSWEAR DISTRIBUTOR	B-	B	NEG	NEG	F
DILLARDS INC-HQ	BB-	BB	STA	NEG	D
LINENS HOLDING CO	D	CCC+	NM	NEG	F+
OFFICE DEPOT INC	BB+	BBB-	NEG	NM	D+
BROWN SHOE COMPANY INC	BB	BB	NEG	STA	C+
MACYS INC (FKA FEDERATED DPT STORES)	BBB-	BBB	STA	STA	D

**Did You Know...?**

Moody's Investors Service expects 11% of non-financial corporate debt issuers globally to trip a covenant this year, with North American companies most vulnerable.

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## Bankruptcy Blotter

... Citing the present retail climate, the specialty nature of the company, as well as the limited financing available, **Sharper Image** has elected to sell the business and assets at auction. It is the company's intention to complete the sale process and seek approval of the sale by the court by the end of May.

... Separately, **Sharper Image** reported that its sales for the month ended March 31, 2008 were \$19.2 million generating a loss for the period of \$6.2 million including \$1.7 million of reorganization items.

... **Movie Gallery, Inc.** was not able to deliver its fiscal year 2007 financial statements to its lenders on April 21<sup>st</sup> as required in its \$150 million DIP facility. The company now has 30 days to comply before an Event of Default occurs.

... A judge has ordered creditors and possible bidders for **Pacific Lumber Co.** into mediation to resolve a dispute that has kept the logging company stuck in bankruptcy with no clear exit. Bondholders of Pacific Lumber subsidiary **Scotia Pacific** and hedge fund **Marathon Asset Management** are grappling to win control over the company's assets.

... **Ski & Sports Center** of South Easton, Massachusetts, doing business as **Ski Outlet** was pushed into involuntary Chapter 7 bankruptcy by petitioning creditors **Quiksilver Rossignol Group, K2 Corp., Spyder Active Sports** and **Fisher Sports USA**. Ski and Sports Center ceased operations on April 9<sup>th</sup> and sold its assets at public auction on April 16<sup>th</sup>.

... The **Golf Etc.** franchisee operated by **Paul and**

**Christine Howard** in Apple Valley, Minnesota filed for Chapter 7 bankruptcy sporting \$287,400 in unsecured claims and \$647,146 in unsecured debt.

... Staring into a hole of continued losses and lingering negative cash flow, the independent accounting firm for **Wilson's the Leather Experts Inc.** reported that it has "substantial doubt" about the company's ability to stay in business. In addition, the company's line of credit has been frozen pending an acceptable business plan and projections to its lender.

... **Interstate Bakeries** has requested a delay in its reorganization plan hearing yet again, though the company did not propose a new date for the hearing. The company and the **Teamsters** have been at an impasse since October over work and welfare concessions that the company says are vital to its exit from bankruptcy. Negotiations continue.

... In other news, **Interstate Bakeries** continues to lose money. For its third quarter ended March 8, 2008, the company reported a loss of \$67.8 million, compared with a loss of \$42.2 million during the same period a year ago. Revenues during the quarter fell 6.4% from a year ago to \$806.3 million.

... It seems like everyone is getting into the act when it comes to bankruptcy reorganizations. The **United Auto Workers** wants **Dana Corp.** to shell out \$2.5 million to cover a success fee the union wants to pay its financial adviser, **Potok and Co. Inc.**, for its role in the company's reorganization.

Feedback?

Questions?

Suggestions?

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## Hi Tech Entertainment

... Bankrupt specialty retailer **Sharper Image** has put itself up for sale. The company is expected to go to the auction block to sell all of the company's assets. It is expected that the company will be sold by the end of May. The company also filed operating results for the month of March and has lost \$6.2 million since it filed for bankruptcy.

... Rumors were swirling this week in speculation that Dell may be interested in acquiring **Radioshack**. Dell has yet to find a meaningful retail footprint, and many feel that Radioshack's more than 4,000 stores would give it just that.

... **Blockbuster** is weighing its options in regards to the \$1.3 billion bid that is on the table for **Circuit City**. Blockbuster has said that a hostile takeover is unlikely, but that it was still talking to investors. Circuit City shareholder Mark Wattles

is urging the company to open up its books and show Blockbuster what it needs to make the bid formal.

... **Office Depot** has teamed up with Indian retailer **Reliance Industries** to provide office products and services to customers in India. The pair also bought **eOfficePlanet**, a dealer of office products and services to corporate customers in India.

... **Ingram Micro** reported that net income for the first quarter was \$64.1 million, up from \$37 million for the same quarter last year. Revenues for the quarter rose 4% to \$8.58 billion.

... **Amazon** reported that first quarter profits rose 29% to \$143 million as revenues rose 37% to \$4.14 billion.

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## Management on the Move

... **Kroger** named **Angel Colon** as the head of its multi-cultural business development program.

... **Sweetbay Supermarket** named **Lori Malcolm** as its vice president of human resources. Mrs. Malcolm was most recently the senior director of human resources transformation at **Wal-Mart**.

... **Mark Foote** has resigned his position as the President and Chief Marketing Officer of **Loblaws**. **Alan Leighton** has been promoted to the company's presidency. CFO **William Wells** and vice president of food **Petro Satriano** also left the company. **Bob Vaux** will be interim CFO. **Frank Rocchetti** will be the firm's new Chief Marketing Officer.

... **Winn-Dixie** announced that **Jim Carrado** has been named vice president of neighborhood marketing.

... **Wal-Mart Stores Inc.** nominated **Gregory B. Penner**, a general partner at **Madrone Capital Partners** and **Ame M. Sorenson**, EVP and CFO of **Marriott International** for election to its Board of Directors. **Jack Shewmaker** and **Roland Hernandez**, long-time members of the Board are not standing for reelection.

... Ending its six-month search, **Home Depot** named **Frank Bifulco** SVP – Chief Marketing Officer replacing **John Ross**, who had been handling the role on an interim basis and who retains the position of VP – Advertising. Mr. Bifulco previously served as the Chief Customer Officer and President of **Hasbro North America Sales**.

... **Five Star Products Inc.** filed a Form 8K with the SEC announcing the departure of **Neal W. Collins** from the company. No other details were provided.

... **Hibbett Sports, Inc.** promoted three managers to VP positions in the areas of merchandising, legal and real estate. **Michael McAbee** was named VP of Merchandise Planning, having been with the company for almost 6 years. **David Benck** was named VP and General Counsel, having served with the company since 2005. And, **Jeff Gray** was named VP of Real Estate, having served with the company for over 17 years. Looks like titles this year instead of bonuses.

... **David Mussafer** will not seek reelection to the Board of Directors of **Kirkland's, Inc.** Effective upon the expiration of Mr. Mussafer's term, the Board will reduce the number of Directors comprising the Board to seven members.

... **The Pep Boys – Manny, Moe & Jack** named **Mike Odell**, the company's COO, as interim CEO following the resignation of **Jeff Rachor**, who left to become a principal in an automotive dealership venture. There are no plans at the present to begin a search for a new CEO.

... In other news, **The Pep Boys** appointed **Ray Arthur** to the position of CFO. Mr. Arthur most recently served as EVP and CFO of **Toys "R" Us Inc.** from 2004 to 2006.

... **Advance Auto Parts, Inc.** named **Kevin Tobin** to the position of SVP, General Manager, Financial Services, responsible for building market competitive, differentiated and innovative financial services products and services. Most recently Mr. Tobin served as EVP and Managing Director at **HSBC Card and Retail Services**.

... **Rakesh Gangwal** was named as the new lead independent director at **Officemax**, replacing **Gary G. Michael**. Mr. Michael did not stand for reelection. Gangwal will also serve as the new chair of the committee of outside directors.

... **Steven R. Morgan** resigned from the President's post at **Gamestop**. He will be leaving the office on May 2, 2008. Mr. Morgan's duties will be distributed to other members of the management team.

... **James Muehlbauer** was named as the permanent CFO at **Best Buy**. Mr. Muehlbauer had been serving as the interim CFO since the departure of **Darren Jackson** in September. Muehlbauer was previously CFO of Best Buy's US operations.

... **J. Wayne Weaver** has retired from the Board of Directors at **Stein Mart**. Mr. Weaver has been a member of the board since 2001, citing his age of 72 as the reason.

... **M. Adam Boucher** has resigned from his post of COO at **Wilson's the Leather Expert**. The resignation is effective April 25, 2008.

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## Health & Beauty Aids

... **Walgreen** has announced it has renewed its contract with **Horizon Lines**, its primary shipper to Puerto Rico.

... **Walgreen** announced that it was adding **Colleen Booth-Rothchild's** "c.booth" bath and body products.

... **Shoppers Drug Mart Corporation** completed an amendment to its existing credit facility that ex-

pires in June 2011, increasing its size from \$550 million to \$800 million. In conjunction with this amendment, its commercial paper program has been increased from \$300 million to \$500 million.

... **MedCath** announced revised full-year revenue guidance of \$620 to \$630 million for fiscal 2008, which ends in September.

## Specialty Items

... With its significant vendors providing product on a cash-with-order basis, **Linens 'n Things** is looking to buy a few weeks of breathing room as it works to secure a substantial capital infusion.

... In a related development, **Linens 'n Things** retained banking firm **Financo** as well as **Conway, Del Genio, Gries & Co. LLC** as financial advisers to devise a plan that in the next 30 days satisfies vendors, bondholders, creditors and its employees.

... **Overstock.com** reported a 27.1% year-over-year increase in sales to \$200.7 million for its first quarter ended March 31<sup>st</sup>. For the quarter, the company reported a net loss of \$3.9 million, down 81.7% from a \$21.4 million loss for the first quarter last year.

... **Aaron Rents, Inc.** reported revenues for its first quarter ended March 31<sup>st</sup> of \$437.3 million, an increase of 12.7% versus sales of \$387.9 million for the comparable period last year. However, due to heavy start-up costs from several new stores opened late last year, the company's net income for the quarter dropped 15.2% to \$24.8 million from \$29.2 million in the prior year.

... **Borders, Inc.** will open its second stand-alone **Paperchase** shop in the U.S. May 2<sup>nd</sup> in Glendale, California. **Borders** acquired **Paperchase Products Limited** in 2004 and has since added **Paperchase** shops in over 320 **Borders** superstores throughout the U.S.

... **Haverty Furniture Companies, Inc.** will release its first quarter financial results on Wednesday, April 30<sup>th</sup>. Be sure to look for **Global's** updated

analysis and assessment shortly thereafter.

... **Ethan Allen's** income fell 49.7% to \$8.8 million for its fiscal third quarter ended March 31<sup>st</sup> as sales slipped 4.3% to \$235.9 million.

... **Furniture Brands International** acquired 11 **Thomasville Home Furnishings** stores from four dealers, bringing its company-owned count to 23 stores. Terms of the acquisitions were not disclosed.

... **The Pep Boys - Manny Moe & Jack** informed the SEC that its annual report on Form 10K would not be filed within the prescribed time frame due to additional work relating to accounting for taxes and an assessment of its internal controls over accounting issues. The 10K is expected to be filed by May 15<sup>th</sup>.

... **CSK Auto Corporation** reported sales for its fiscal year ended February 3, 2008 of \$1.852 billion, down 2.9% versus sales of \$1.908 billion in the prior year. For the year, the company reported a net loss of \$11.2 million versus net income in the prior year of \$6.3 million. As reported earlier, the company is in the process of being acquired by **O'Reilly Automotive**.

... Meanwhile, **O'Reilly Automotive, Inc.** reported sales for its first quarter ended March 31<sup>st</sup> of \$646.2 million, up 5.4% versus sales of \$613.1 million for the comparable period last year. However, net income for the quarter was \$46.3 million, short of expectations and down roughly 4.3% versus the prior year's net income of \$48.4 million.

### Did You Know...?

The sales of existing single-family homes and condominiums dropped by 2% in March to a seasonally adjusted annual rate of 4.93 million units. The median price of a home sold last month dropped to \$200,700, a decline of 7.7% from the median price a year ago.

## Off the Rack

... **Charming Shoppes** has said that it's exploring strategic alternatives for its catalog business. The company will do this to focus more on its core brands, which include Lane Bryant, Catherine's and Fashion Bug. CEO Dorrit Bern has said the company has had a number of inquiries from qualified third parties.

... Bank of America has opted not to renew its \$1 billion secured facility with **Sears Holdings**. Bank of America chose not to renew the facility under the existing terms. There was just \$1.6 million in letters of credit outstanding on the facility as of April 18, 2008. The facility was solely written to provide letters of credit.

... A New York mother is suing **Victoria's Secret**. The lady feels that Victoria's Secret stole her idea

for a bra whose straps can be worn in different ways. Katherine Plew claims she filed a patent for the invention in hopes of making some money to help raise her kids. She is seeking unspecified damages.

... **Wilson's the Leather Expert** received a warning for potential delisting from NASDAQ. The company doesn't meet the minimum \$10 million equity values. The company had just \$5 million in equity.

... **Coldwater Creek** had its quarterly fixed charge for its \$60 million revolver reduced. The charge will be reduced for the remainder of the year, and Coldwater Creek also agreed it will not buy back stock before May 2, 2009 and will maintain liquidity of at least \$30 million through April 2009.

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## The Global World of Sports and Footwear

... In connection with **Footstar, Inc.'s** planned wind-down of its business, the Board of Directors of the company authorized a plan to align its workforce with its anticipated staffing needs by reducing the company's workforce by approximately 130 employees, incurring cash charges of approximately \$4.6 million for one-time severance costs.

... **West Marine, Inc.** will release its first quarter financial results on Wednesday, April 30<sup>th</sup>. Be sure to look for **Global's** updated analysis and assessment shortly thereafter.

... With approval by local county supervisors, **Dick's Sporting Goods** cleared the first local government hurdle that will enable it to receive \$8.25 million in tax breaks to construct a new corporate headquarters in Findlay, Pennsylvania. The tax deal still needs to be approved by local school district officials and the County Council.

The U.K.'s biggest sporting goods retailer, **Sports Direct International Plc** expects to meet earnings expectations despite challenging market conditions. Management is confident of reaching full-year EBITDA of \$294 million.

... **Bass Pro** will reportedly open its fourth Outdoor World in Georgia in the fall of 2009. The 100,000 square foot store will be an anchor in a proposed development in Augusta.

... **Shoe Tellers, Inc.** and **A Perfect Dealer, Inc.**, in association with **New Balance Athletic Shoe, Inc.** opened its second and largest store in the Greenburgh section in White Plains, Westchester County, New York. The New Balance Westchester store is over 4,000 square feet.

... **GSI Commerce Inc.** reported a 33.7% increase in net revenues for its first quarter ended March

29, 2008 to \$195.5 million, though the on-line performance of its sporting goods retail partners was mixed. Investing in acquisition and infrastructure for building the business, the company reported a loss for the quarter of \$9.6 million, versus a loss of \$2.3 million in the prior year.

... Based on results for the first quarter, **GSI Commerce** lowered its guidance for income from operations from a modest profit of \$1.5 million to a possible loss of \$1.5 million, down from a forecast in mid-February of income of from \$3 million to \$6 million.

... **Big 5 Sporting Goods Corporation** will release its first quarter financial results on Wednesday, April 30<sup>th</sup>. Be sure to look for **Global's** updated analysis and assessment shortly thereafter.

... **Cabela's** is reportedly moving forward with its planned Billings, Montana store in June. The development project was suspended in January.

... **Hibbett Sports, Inc.** will release the results for its first quarter ended May 3<sup>rd</sup> on Thursday, May 22<sup>nd</sup>. Be sure to look for **Global's** updated analysis and assessment shortly thereafter.

... **SKECHERS USA, Inc.** reported an 11.6% increase in net sales for the first quarter to \$384.9 million, a new first quarter record and the second highest quarter in the company's history, from \$344.9 million in the comparable period last year. Net income for the quarter was a record \$32.8 million versus net income of \$23.9 million last year.

... **DSW** announced the opening of three stores in Atlanta, Georgia; Dulles, Virginia; and Noblesville, Indiana, with plans to open at least 30 stores this year. In addition the company opened a new web site, DSW.com that allows online shopping.

### Did You Know...?

The Mortgage Bankers Association said its seasonally adjusted index of mortgage applications for the week ended April 18<sup>th</sup> fell 14.2% to 637.6. Borrowing costs on 30-year fixed-rate mortgages, excluding fees, averaged 6.04%, up 0.30 percentage points from the previous week.

## Mass Merchant Musings

... **Wal-Mart** continues its reign as the largest corporation in the U.S., having retained the top spot on Fortune magazine's annual Fortune 500 ranking. Wal-Mart also led the general merchandisers category where it was trailed by **Target** (No. 31) and **Sears** (No. 45).

... **Wal-Mart** is making another go at the fashion business and has been "striking deals" to bring in new brand name designers and apparel. It seems likely the new move into fashion is related to the tightening economic climate, looking for the right balance between cost and style.

... Excluding discontinued operations (mainly

**Value City), Retail Ventures, Inc.** reported sales for its fiscal year ended February 2, 2008 of \$1.872 billion, up 9.7% versus sales of \$1.707 billion for the prior year. Operating income for the year was \$63.5 million, down 36.2% versus operating income of \$99.5 million in the prior year, as competitive pressures reduced gross margins by 142 basis points.

... **Toys "R" Us** rolled out a line of environmentally friendly toys that encourage "Good Green Fun." Marketed under the Toys "R" Us brand, the exclusive line includes natural wooden toys, natural cotton plush animals and organic cotton dolls.

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## FYI for the DIY

... **84 Lumber Co.** arranged two new financing packages that will give it access to \$590 million over five years to help it weather the housing market downturn. The new financing was arranged through **Sun Trust Bank** and **Wachovia Bank** and is not tied to covenants based on the company's earnings.

... Despite the decline in the housing market and overall economy, **Ace Hardware** reported revenues of \$3.97 billion for its fiscal year ended December 29, 2007, a 1.0% increase over prior year revenues of \$3.93 billion. Net income for the year was \$86.9 million, down from record net income of \$94.5 million in the prior year.

... **Interline Brands, Inc.** will release its first quarter financial results on Tuesday, May 6<sup>th</sup>. Be sure to look for **Global's** updated analysis and assessment shortly thereafter.

... For its first quarter ended March 31, 2008, **Sherwin-Williams Company** reported sales of \$1.782 billion, up 1.5% from sales of \$1.756 billion for the comparable period last year. Reflecting the continued housing slump and the effect of acquisitions, net income for the quarter was \$77.9 million, down 30.3% versus last year's first quarter net income of \$111.8 million.

... **United Rentals, Inc.** will release its first quarter financial results on Tuesday, April 29<sup>th</sup>. Be sure to look for **Global's** updated analysis and assessment shortly thereafter.

... **Tractor Supply Company** reported sales for its first quarter ended March 29, 2008 of \$576.2 million, up 2.9% versus sales of \$559.8 for the comparable period last year. Typically the company's slowest quarter, a warmer February and a late spring as well as a progressively more challenging economic climate, led to the company reporting a net loss for the quarter of \$1.2 million

versus net income in the prior year of \$5.0 million.

... Reflecting its first quarter results reported above, **Tractor Supply** revised its full year sales expectations downward to a range of \$2.98 billion to \$3.04 billion from its prior guidance of \$3.01 billion to \$3.08 billion. The company currently expects earnings to be slightly below the low end of its previously provided range, of \$2.54 to \$2.62 per share.

... **Wesco International, Inc.** reported sales for its first quarter ended March 31, 2008 of \$1.465 billion, up 1.0% versus sales for the comparable period last year of \$1.450 billion. Net income for the quarter, however, was down 7.1% to \$44.8 million versus \$48.2 million last year.

... In other news, **Wesco International** reported that it would not submit any further bids for **Industrial Distribution Group, Inc.** over and above its current bid of \$11.75 per share. IDG reported that it had received a higher bid.

... Also exhibiting the results of the continued housing slump, **Builders Firstsource, Inc.** reported sales for its first quarter ended March 31, 2008 of \$270.5 million, down 34.2% versus the comparable period last year. For the quarter, the company reported a net loss of \$15.8 million versus net income in the first quarter last year of \$232,000. On the positive side, the company's cash on hand covers approximately 75% of its current liabilities.

... The EPA issued "stop sale, use or removal" orders to **Home Depot, Lowe's, Wal-Mart, Ace, Do-It-Best, True Value, Sam's Club, Meijer** and **K-Mart** for certain illegal, unregistered and misbranded pesticides distributed by **Scotts Miracle-Gro Co.**

### Did You Know...?

High prices for food and fuel, weak income growth and falling home values pulled down consumer sentiment as the U.S. consumer sentiment index declined to 62.6, the lowest level in 26 year, from 69.5 in March.

## Options and Resources

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## Talbots: Retailer of the Week

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\$ FIGURES IN MILLIONS	2/2/2008 (FY08)	2/3/2007 (FY07)	Year-over-Year Change
<b>Liquidity Ratios</b>			
Cash and Equivalents	\$25.50	\$35.90	-29.08%
Cash and Equivalents % Current Liabilities	5.75%	8.36%	-261 bps
Working Capital	\$208.8	\$262.6	-20.49%
Current Ratio	1.47x	1.61x	-14 bps
<b>Leverage Ratios</b>			
EBITDA / Interest Expense	2.61x*	6.22x	-361 bps
Total Debt	\$389	\$514.6	-24.41%
Total Debt / Equity	85.54%	80%	554 bps
Total Liabilities / Total Assets	69.74%	63.21%	653 bps
Total Liabilities / Tangible Assets	89.66%	88.14%	152 bps

\*For analysis purposes, we excluded the \$134 million goodwill impairment charge and the \$15.6 million trademark impairment charge due to the non-cash nature of the charges. Actual EBITDA was (\$55.9 million) for the year.

Revenues for the fourth quarter ended February 2, 2008 were \$587 million, down 8% from the fourth quarter last year. The fourth quarter last year contained an extra week of revenues. Consolidated comp store sales were down 6% for the quarter. By segment, Talbots saw revenues fall 10.4% to \$388 million on a comp store reduction of 6%, while J Jill revenues fell 5.5% to \$86 million on a comp store reduction of 6.3%. Direct marketing revenues were down 0.9% to \$113 million. Certain industry commentators have claimed Talbots lacks the styles its core customers are looking for. The lack of products and the slowing economy caused the company's gross margin to drop 290 basis points for the fourth quarter. Talbots also couldn't initiate any strong cost-cutting methods to combat the environment, and SG&A rose 220 basis points as a percentage of revenues. For the quarter, Talbots posted an operating loss of \$183.2 million. Of that loss, \$149.6 million was a result of a charge for impairment of goodwill and trademarks. Even excluding the charge, it is clear that the company's operations are in a slump. Without the charge, the company's operations still would have lost \$33.6 million, a painful holiday season. The company's operations certainly are not generating the funds needed to keep paying the \$20 million debt principle payment. For the fourth quarter, after \$8.2 million in interest and a \$20 million tax benefit, the company posted a loss of \$171.4 million. These are not the types of results we look for in the holiday season.

Revenues for the year-ended February 2, 2008 were \$2.29 billion, up 2.6% from last year. Last year contained an extra week of revenues. Consolidated comp store sales were down 5.5% for the company. Revenues at the Talbots brand fell 4.4% to \$1.53 billion, driven by a comp store decline of 5.7%. J Jill saw revenues 35.5% to \$327.6. The most current year had the benefit of an entire year of J Jill, while last year only had from May 3 and on. Comps for the segment fell 4.6%. Direct marketing revenues were up 11% to \$427.9 million. Talbots' gross margin dipped 210 basis points for the year. Additional markdowns were again the culprit, as the company was fighting a tough retail environment with products that didn't seem to be appealing to its core customers. SG&A expenses also took a sharp turn for the worse, rising 240 basis points as a percentage of revenues. The falling comps were not handled well, and the company says it will be decreasing its marketing costs going forward to help combat the disappointing revenues. For the year, Talbots posted an operating loss of \$186.4 million, a swing from \$75 million in profits last year. Again, even if we exclude the \$149.6 million in asset impairment charges, it is apparent the company's operations are going through a very rough stretch. The company still would have lost \$36.8 million on the operating line. Even if we are extremely nice and exclude the \$9.3 million in restructuring charges, we still can't find a way to say nice things about the operations this year. For the year, Talbots posted a loss of \$188.8 million. One thing is certain: the company needs to find a way to get its operations under control before the situation worsens.

(Continued on page 9)

### Did You Know...?

Mother's Day might not be as rosy for mom this year, with consumers planning on scaling back according to NRF's 2008 Mother's Day Consumer Intentions and Actions Survey. Per the survey, consumers will spend an average of \$138.63 this year, compared to \$139.14 last year.

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## Talbots: Retailer of the Week

(Continued from page 8)

Talbots' balance sheet has been facing a double-edged sword in recent periods. The losses have certainly been weighing heavily on the structure, while the \$20 million quarterly principal payments have been sucking the company of valuable liquidity.

At the close of the year, Talbots had just \$25.5 million in cash on its balance sheet. That will be enough to pay for the \$20 million principal payment in the first quarter and not much else. The cash position is down from \$35.9 million last year. The large losses and forced interest payments have really started to take their toll on the company's balance sheet. The liquidity is down by all counts, and the company's working capital has fallen over 20% from last year. There were many LCs outstanding on the company's credit facility, but there was still \$153 million available at year-end. This should at least provide the company with the means to pay its quarterly principle payment.

The company's debt position has fallen, but equity has fallen at a faster clip, more then offsetting the debt to equity ratio. Total debt has fallen from \$514.6 million last year to \$389 million this year. However, the company's equity position has fallen from \$643.3 million last year to \$454.8 million, more then offsetting the debt payments from a comparison standpoint. There will be another \$80 million coming due over the next twelve months, and the company will need to find the cash to pay for this.

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## Heard in the Grocery Aisle

Feedback?

Questions?

Suggestions?

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... **Penn Traffic** has taken a \$4.8 million charge as a result of an attempt to engage in an acquisition, during the past fiscal year. Some analysts speculate that the takeover target was **Tops Markets**.

... **Tesco** is appealing a ruling that required an environmental review of its 820,000 square foot California distribution facility.

... **Supervalu** announced that it would give a \$30 bonus to those customers who redeemed their entire \$300 check at one of the firm's stores.

... **Weis Markets** announced that it would invest \$80 million in its store base during fiscal 2008. The firm plans to use this expanded capital budget to fund 19 major renovation projects.

... During the past few months, Florida-based **Freshco International Supermarkets** has opened locations in Orange City, Kissimmee and Orlando. This Hispanic-themed supermarket now has 6 locations.

... The **United Food and Commercial Workers** (UFCW) has launched a campaign aimed at high-lighting speculation that the Tesco is not doing well.

... A former **Jewel-Osco** store has been converted into a Village Fresh Market, in suburban Chicago.

... **Safeway** announced that it has placed solar panels on two of its California stores. The com-

pany aims to place panels on 23 locations.

... **Winn-Dixie** has decided to countersue 26 current and former employees who filed a lawsuit that alleged discrimination.

... The FTC has gone to court in an attempt to again prevent **Whole Foods** and **Wild Oats** from merging.

... **Ahold** will sell its 73% stake in **Schuitema** to **CVC Capital Partners** for \$293 million.

... The Asian-themed **Lee Lee Oriental Supermarket** announced that it its opening locations on Peoria and Tucson. Arizona-based grocer is looking to capitalize on the growth in the Asian population in the Phoenix market.

... **Houchens Industries** has signed a letter of intent to purchase **Buehler Foods**. Buehler operates 22 grocery stores across Indiana, Kentucky and Illinois.

... **Stop & Shop** announced that it would allow the construction of in-store bank branches in Maine.

... **Acme Markets** announced that it was opening its first environmentally friendly supermarket in Glen Mills, Pennsylvania.

... **Giant Eagle** is offering discounted fuel to customers who purchase multiple DVDs inside its stores.

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