

RETAIL SECTOR WEEKLY

Key Retail News and Commentary

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Remember...

Work is either fun or drudgery. It depends on your attitude.

Unemployment Rate Soars

The nation's employment report, considered a pivotal measure of economic activity, delivered startlingly bad news about the economic outlook last week, renewing fears of a recession and in the blink of an eye changing the discussion from interest rates possibly moving higher to the potential for further easing in rates.

The shocking news came in the form of the unemployment rate for August, which soared to 6.1%, the highest in nearly five years. The rate has steadily climbed this year from a cycle low of 4.4% and now sits just below the peak of 6.3% seen during the last recession.

One economist said his forecast of a 7% unemployment rate before the economy manages a recovery might be too low.

The report had a major impact on financial markets. The dollar weakened in foreign-exchange trading, while stocks dropped sharply after the data were released but showed signs of a rebound by midday.

Nonfarm payrolls decreased by 84,000, the Labor Department reported, more than the 75,000 drop expected by economists surveyed, marking the eighth straight monthly drop in payrolls.

The factory, especially the auto industry, shed jobs in August. Employment services, considered a bellwether of future labor market trends, also had sharp losses.

The weak labor market is sure to rekindle fears of an incipient recession among investors and consumers alike. Federal Reserve policymakers are watching closely.

Economist have been warning that the economy appeared to be stalling, but Wall Street was dazzled late last month by the strong 3.3% growth reported in the government's first revision of its estimate for gross domestic product during the April-June quarter.

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Retailer of the Week: Pacific Sunwear

We are **downgrading PacSun to a "D" moderately high-risk credit with a "negative" outlook.** In the past, Global Credit Services has pulled no punches when we speak of aggressive share repurchase programs. There is a time and a place for such activity, while some firm's fit the bill better than others. PacSun is one situation where we feel the firm did a large amount of damage to its balance sheet. In the second quarter, PacSun used \$52.9 million for this purpose. The purchase sucked the company of nearly all of its cash, leaving just a small balance on the books at the end of the quarter. The firm didn't even have enough cash to complete the purchase, and was forced to tap its revolver as well. The debt is still very low for PacSun, which eases some concern. The lack of cash is certainly alarming, however.

The first half of the year was hurt largely from the closure of the One Thousand Steps and demo banners. The company has taken large accelerated depreciation charges and also took a very large charge for discontinued operations. The large one-time items charges should cease in the second half of the year. The major concern now is the fact that, despite being finished with the other two problem banners, the PacSun banner has failed to produce much on its own. The

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Unemployment Rate Soars

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Other aspects of last week's jobs report underscored weakening conditions in the labor market. Payroll losses in the previous two months were 58,000 larger than previously estimated. Aggregate hours worked fell 0.1% in August, the fifth straight monthly decline. Hours worked in the factory sector plunged 0.9%. The jobless rate rose for a clear-cut reason: People lost jobs.

According to a separate survey of households, employment fell to 145.6 million, off 342,000. Unemployment rose by 592,000, to 9.4 million, and the labor force fell by 8,000.

The weak report should postpone any Fed-engineered rate hike. Although some Fed officials have been agitating for a tightening sooner rather than later, most analysts believe it will be difficult for the Fed to justify raising rates in face of labor market weakness.

The Global World of Sports and Footwear

Collective Brands Inc. has signed an agreement with Kuwaiti franchise operator M.H. Alshaya to open Payless ShoeSource stores throughout the Middle East. Payless and Alshaya said they believe the region could ultimately support more than 200 stores.

Also, **Collective Brands'** net income of \$8.2 million was 67% below the prior year's \$24.7 million for the quarter ended Aug. 2 and includes \$36.2 million in pre-tax charges related to the trademark infringement litigation that Collective has lost to Adidas and settled with K-Swiss. Excluding the litigation charges, PSS earnings would have been \$33.6 million, up 35%. Collective also recovered \$7.5 million in an insurance settlement related to the K-Swiss litigation.

Dick's Sporting Goods management believes market conditions will slightly deteriorate through the end of next year. Dick's predicted more private label expansion in its stores, at the expense of tertiary brands rather than its main branded suppliers. DKS is also seeing considerable pricing pressures from Asia, but the impact has been more pronounced from branded vendors. Dick's reiterated that it is finding expansion into Texas its biggest market challenge against Academy, but said it is gaining traction and has no plans to retrench. It sees the potential for 60 stores there (10 now) as

part of its 800-store national plan. Other key markets for expansion, with existing units in parentheses, are California—90 stores (15 now); Florida—40 stores (8); Washington—17 stores (0); Arizona—20 stores (3); New York—45 stores (28); Illinois—37 (19); and Georgia—22 (11). It is also looking for a location for a West Coast distribution site. It may also look for a fifth site in CO or the western Midwest if fuel prices get to the \$4.75 or more range.

Also, **Dick's Sporting Goods** intends to open a 44,000 sq. ft. store at Fashion Island in Newport Beach, CA next summer, according to the Orange County Register. DKS already has plans to convert the first Chick's Sporting Goods to its own banner in Q3 with the last 14 Chick's store slated for a banner change in H209.

Forzani blamed extensive renovations at 20 stores for its down comps in the second quarter. Had those doors been operating at "full speed" during Q2, management said, the comp decline would have been eliminated. Forzani was encouraged by an 8.2% same store sales increase (+9.8% in corporate locations, +5.4% in franchisees) for the first four weeks of Aug.

Filson is opening a 2,400 sq. ft. store in the Pearl District of Portland, OR in the fall. The outdoor brand has existing retail shops in Seattle and Denver.

Options and Resources

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Bankruptcy Blotter

Chapter 11 bankruptcy filings skyrocketed by 38% last month after holding fairly steady all year, an increase that may have been boosted by seasonal and retail businesses. In August 1,082 businesses and individuals filed for Chapter 11, versus 786 in July.

Linens 'n Things is looking to extend its exclusivity period to November 28, 2008 with the solicitation period ending January 27, 2009. While the company has filed a Disclosure Statement with the court, it cannot send it out for a vote until approved by the court.

In other news, **Linens 'n Things** Chairman, **Robert DiNicola**, resigned as Executive Chairman of the Board. Mr. DiNicola will, however, continue to serve as a Director.

Mervyn's filed a lawsuit against **Cerberus Capital Management**, **Sun Capital Management** and **Lubert-Alder**, accusing the private equity firms and owners of Mervyn's of stripping the firm of valuable real estate and making bankruptcy a forgone conclusion. Mervyn's claims the firms financed the acquisition with \$800 million borrowed against the real estate, then leased the properties back to Mervyn's at a "substantial rate increase."

Shoe Pavilion and **Wells Fargo Retail Finance** reached an agreement in which Shoe Pavilion will pare down to 63 stores and then place itself up for sale as an ongoing concern, necessitating the closing of 52 locations. The 52 store closures include 24 stores already announced for closing and an additional 27 location in four

states. **Gordon Brothers** was selected to conduct GOB sales at the additional 27 locations, beating out a stalking horse bid by **Great American Group**, with the court approval hearing scheduled for September 11th.

In a status hearing filed September 3, 2008, **Shoe Pavilion** reported that its available cash of the end of August was approximately \$5.3 million, roughly 19.6% below the company's \$6.7 million budget.

The Justice Department is balking at **Boscov's Inc.'s** plan to pay six senior executives up to \$1.45 million in bonuses tied to the department store chain's successful reorganization or sale by early 2009, claiming the company has not shown that the goals set for the executives are difficult enough to achieve to deserve a bonus.

The Trustee for the **Southern Building Products'** Chapter 11 case believes the case should be converted to a Chapter 7 Liquidation because the company's Plan of Reorganization "fails to contain complete and convincing evidence" that it has sufficient cash to pay creditors and get out of bankruptcy.

Interstate Bakeries Corp. is in the "final stages of negotiating a Plan of Reorganization" that would allow the company to emerge from nearly four years of bankruptcy protection as a stand alone business. The final agreement hinges on compromises from several parties, including the company's lenders, its unions and private equity firm **Ripplewood Holdings**.

Did You Know...?

Core capital equipment orders rose 2.5% in July, the Commerce Department reported, with overall new orders up 1.3% in the month.

Upcoming Reporting Dates

| Company | Event | Date |
|-------------------------|---------------------|--------------|
| Bakers Footwear Group | Quarterly Results | Sep 10, 2008 |
| Barnes & Noble | Investor Conference | Sep 16, 2008 |
| Burlington Coat Factory | Annual Results | Sep 12, 2008 |
| Circuit City Stores | Quarterly Results | Sep 29, 2008 |
| Family Dollar Stores | Quarterly Results | Oct 3, 2008 |
| Ingram Micro Inc. | Investor Conference | Sep 16, 2008 |
| Kroger Co. | Quarterly Results | Sep 16, 2008 |
| Loblaws Companies | Investor Conference | Sep 16, 2008 |
| Lululemon Athletica | Quarterly Results | Sep 11, 2008 |
| Penn Traffic Company | Quarterly Results | Sep 11, 2008 |
| Pep Boys | Quarterly Results | Sep 9, 2008 |
| REX Stores | Quarterly Results | Sep 9, 2008 |
| Toys R Us | Quarterly Results | Sep 17, 2008 |
| Wal-Mart Stores | Investor Conference | Sep 15, 2008 |
| Zale Corp. | Investor Day | Sep 10, 2008 |

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General Retail News

This August was the third coolest in the past ten years, which positively affected Back to School sales for many apparel retailers, according to WeatherCall from **Planalytics Inc.** Tropical storm activity helped increase traffic at home improvement chains and restaurants, the company said. Shoe Carnival, Dillard's, Lowe's and Talbots, were among the companies that benefited most.

Shoppers are trading down, shopping at fewer stores and shopping closer to home, according to the new *American ShopperScape 2008* report from TNS Retail Forward. This trend favors large discount retailers and power centers at the expense of specialty stores and shopping malls. Respondents cited these top five behavioral changes in the report:

- 75% are planning errands to minimize the distance traveled.
- 58% are going to stores where they can do one-stop shopping.
- 55% are going to stores that are closer to home or work.
- 47% are doing more activities around the house instead of driving places.
- 26% are doing more online shopping.

The Nielsen Company has developed a research tool for relating retail purchases to the in-store media types that drive them according to a report in *Progressive Grocer*. The technology, called P.R.I.S.M. (Pioneering Research for an In-Store Metric) is applicable to food, drug, and general merchandise retailers.

The NPD Group offered insight from its research on current consumer trends in footwear and apparel:

- Apparel and footwear purchases have improved in the last three months with footwear (+7%) outpacing apparel (+0.8%).
- Selling patterns during back-to-school are mirrored during the holiday season, suggesting business will be concentrated during peak selling periods.
- Sales trends for the under-18 and 35-54 year old sets have been robust for footwear, and moderately better for apparel.
- Dining out, travel and apparel are the three top categories where consumers will likely cut back on spending. Footwear doesn't appear as vulnerable since it remains a passion-driven purchase.
- Despite poor overall comps, footwear has been a bright spot for department stores. Category sales in the channel have risen 6% over the last three months.
- Select retailers, focused on tightly managing inventories, are running the risk of under stocking key items.
- Denim category continues to grow, although ASPs are falling.
- Celebrities and testimonials are resonating more with shoppers than brand-specific advertising.

Rating Changes & Outlooks

| Company | S&P Credit Rating | | S&P Credit Outlook | | GCS Credit Rating |
|------------------------------------|-------------------|-------|--------------------|----------|-------------------|
| | Current | Prior | Current | Prior | Current |
| STARBUCKS CORP | BBB | BBB+ | STABLE | NM | B- |
| O CHARLEYS INC | B+ | BB- | STABLE | NEGATIVE | D- |
| BARE ESCENTUALS INC | B+ | | STABLE | | NR |
| REGIONS BANK | A+ | A+ | NEGATIVE | STABLE | NR |
| CBRL GROUP INC / CRACKER BARREL | BB- | BB | STABLE | NEGATIVE | D- |
| BURGER KING CORP | BB- | BB- | POSITIVE | STABLE | NR |

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Hi Tech Entertainment

OfficeMax is adding more computer repair options through its ctrlcenter service. Customers can either drop off a desktop or laptop PC at any OfficeMax store for service or have one of 2,500 ctrlcenter technicians do the work on-site.

Staples, Inc. reported their second quarter, their first since the Corporate Express acquisition. Corporate Express contributed \$673 million to the top line, adding 21% (\$355 million) in North American Delivery division revenue, and expanding Staples international sales by 47% (\$318 million). Excluding the addition, revenues would have risen 2.6%. North American retail revenues were down 1.1% to \$2.09 billion for the second quarter, as comps for the segment pulled back 7%. North American delivery revenues were up 24.7% to \$1.97 billion. Staples continues to forecast "moderate accretion" this year from the acquisition, and low-single digit EPS growth.

Overstock.com, Inc. is upgrading the online auction section of its web site with increased fraud protection and other usability enhancements.

Office Depot has agreed to refund \$2.5 million to the State of California after an audit of the state's office supply contract found \$14.2 million in "off-contract" items that Office Depot sold to the State without providing the expected discount.

Zones, Inc. "go-shop" period has ended with no other parties expressing interest in acquiring the information technology reseller. The company's merger with Zones' CEO Firoz Lalji's Zones Acquisition Corp. announced in July is now free to proceed.

Amazon.com, Inc. subsidiary ACI Gift Cards introduced Amazon Gift Codes On Demand for corporate gift card programs. Participating companies can skip physical gift-card fulfillment overhead and create e-mail or html gift cards as needed.

Microsoft Corp. is deploying its own "Microsoft Gurus" to computer retailers like Best Buy and Circuit City to help customers with their PC purchases. There will be 155 Microsoft Gurus by the end of the year, with more to come if the project is successful.

Did You Know...?

The Institute for Supply Management nonmanufacturing index rose to 50.6% in August from 49.5% in July, indicating that more companies are expanding than contracting, and beating analysts expectations.

Management on the Move

Winmark Corp. appointed **Tony Ishaug** CFO. Previously, Ishaug was CFO and COO of the Department 56 division of Lenox Group, Inc.

Movado Group, Inc. President and CEO **Efraim Grinberg** will be named Chairman with the retirement of company founder and current COB Gedalio Grinberg at the end of FY2009.

Hibbett Sports COO **Nissan Joseph** has departed due to philosophical differences. A search for a successor is underway.

REI hires **Bill Baumann**, previously Chief

Information Officer (CIO)/EVP of Technology for Tower Records, as VP of Information Technology.

Zumiez promoted **Lynn K. Kilbourne** to President. The former 10-year Banana Republic executive joined ZUMZ as EVP/GMM in 2004.

The Home Depot has named **Matt Carey** EVP and Chief Information Officer. Carey was SVP and CTO at eBay prior.

Abercrombie & Fitch Co. director **Allan A. Tuttle** passed away suddenly on August 31.

Heard in the Grocery Aisle

Metro Inc. has renewed its stock buyback plan enabling it to repurchase up to 6 million of its Class A Subordinate Shares between Sep 5, 2008 and Sep 4, 2009.

Latest update on **Whole Foods'** dustup with the **FTC**: The U. S. Court of Appeals has asked the FTC to respond to Whole Foods' petition for an "en banc" hearing in front of the whole court. FTC's brief is due late this week.

Supervalu has launched a new private label premium food line called Culinary Circle. The line includes over 150 items including on-the-go meals, hors d'oeuvres, desserts and breads and is priced 10 to 15 percent lower than competing national brands.

Giant Food Stores is celebrating 85 years in business this month with special savings, events and promotions.

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Mass Merchant Musings

Target is the latest retailer to use "pop-up" stores to generate buzz and penetrate new markets. Called Bullseye Bodegas, the retailer will open four stores selling designer merchandise in vacant storefronts in Manhattan from September 12 - 15.

Wal-Mart Stores Inc. will open an Asian headquarters in Hong Kong to oversee operations in China, India and Japan. Wal-Mart has 101 hypermarkets in China, along with other outlets.

Also, **Wal-Mart** has launched the new Wal-Mart Smart Network in-store TV system. The new

system uses Internet Protocol Television (IPTV) technology which will allow control of more than 27,000 screens in more than 2700 stores. Content can be varied by store, department and time of day.

Duckwall-Alco Stores announced a \$3.5 million consulting agreement with Accenture to evaluate certain company practices and implement a plan to increase operational efficiency.

Target subsidiary Target Commercial Interiors completed the previously announced purchase of Walsh Bros. and U.S. Business Interiors.

FYI for the DIY

Prices of single-family homes across the country are still falling, but the declines are slowing, according to one of the leading housing market indicators. Numbers released by Standard & Poor's showed a 15.4% decline in the second quarter of 2008, compared with the same quarter of 2007. The declines were less than economists had forecast.

Construction spending fell in July, according to the U.S. Commerce Department, down 0.6% to a seasonally adjusted annual rate of \$1.084 billion, 4.8% below the \$1.14 billion recorded in July of last year.

MSC Industrial Direct Co. subsidiary Sid Tool Co. has sold its interest in a parcel of Nassau County, NY land to Esco Management Corp.

Lowe's is testing new stores in formats smaller than its usual minimum of 94,000 sq ft. The new stores are from 66,000 to 80,000 sq ft according to a report from *Dow Jones*. Company management said that 103,000 sq ft stores are often sufficiently large, but Lowe's largest stores are 117,000 sq ft.

Off the Rack

After a better than expected second quarter, **New York & Co.** raised its earnings guidance for the year to \$.52 to \$.60 per share from \$.44 to \$.54 prior guidance.

A New York man was charged with selling \$80,000 of **stolen bras on eBay**. George Tutaya purchased the Victoria's Secret bras from a professional shoplifting ring.

JCPenney launched a website for Australians shoppers to buy products in AUS\$ direct from the United States. Few U.S. retailers target

overseas markets for e-commerce, but a weak US\$ makes prices very attractive, especially for luxury brands which often have well-padded exclusive local distribution.

Sears Canada Inc. is opening four pop-up stores at four Canadian universities. The 900 sq ft stores will feature student-targeted items such as housewares, electronics and cosmetic.

Nordstrom, Inc. has opened its latest location, a 138,000 sq ft store at The Oaks in Thousand Oaks, CA.

Specialty Items

1-800-Flowers.com, Inc. has amended its credit agreement with a syndicate of lenders. The new \$293 million facility is comprised of

\$165 million of revolving credit and a \$128 million term loan.

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Health & Beauty Aids

Cardinal Health has completed the previously announced sale of subsidiary MedSystems to Linden LLC. The divestiture was part of Cardinal's ongoing efforts to refocus on its core business.

Canadian pharmacy **Shoppers Drug Mart** is testing a new high-end beauty products concept called Murale with two stores to open in 2008.

Walgreens subsidiary Take Care Health Systems has opened four clinics at Indianapolis, IN Walgreens stores, its first in the area, and two clinics in Louisville, KY.

Also, **Walgreens** recently crossed the one million members mark in its Prescription Savings Club.

Another institutional shareholder has questioned as too low **CVS'** offer for **Longs Drug Stores**. **CtW Investment Group** has asked the Longs board for details of any agreement between the companies to conceal

the value of Longs' real estate portfolio and, if there is none, to disclose the information.

Meanwhile the Hart-Scott-Rodino waiting period for the **CVS/Longs Drug Stores** deal expired on September 5.

Drugstore.com, inc. is partnering with **Rite Aid Corp.** to launch a new Rite Aid online store for selling OTC products including Rite Aid's own brand. The web store will open later this year. Additionally, the companies have altered their existing agreement for prescriptions ordered online for pick up at a Rite Aid store. The LPU rights will be transferred to Rite Aid who will pay drugstore.com \$10 million in ten monthly installments.

Boston may **ban cigarette sales** at pharmacies and on college campuses, the *Boston Herald* reports. The new rules up for consideration would also tighten the existing restaurant smoking ban.

Did You Know...?

The productivity of U.S. non-farm businesses was revised to 4.3% in the second quarter from an estimate a month ago of 2.2%.

Second Quarter Scorecard

| \$ in Millions. Quarter ended closest to 7/31/08 | Sales | | | Comps | Net Income | | |
|--|-----------|-----------|--------|--------|------------|----------|---------|
| | 2008 | 2007 | Change | | 2008 | 2007 | Change |
| Apparel | | | | | | | |
| Abercrombie & Fitch | \$845.8 | \$804.5 | 5.1% | -4.0% | \$77.8 | \$81.3 | -4.3% |
| Aeropostale, Inc. | \$377.1 | \$311.2 | 21.2% | 11.0% | \$21.1 | \$14.7 | 43.2% |
| American Apparel | \$133.0 | \$95.7 | 38.9% | 23.0% | \$6.8 | \$4.8 | 41.7% |
| American Eagle Outfitters | \$688.8 | \$703.2 | -2.0% | -9.0% | \$59.8 | \$81.3 | -26.4% |
| AnnTaylor Stores Corp. | \$592.3 | \$614.5 | -3.6% | -10.8% | \$29.3 | \$31.7 | -7.7% |
| Bon Ton Stores, Inc. | \$673.4 | \$708.6 | -5.0% | -5.7% | (\$33.8) | (\$15.0) | -125.3% |
| Cache, Inc. | \$74.0 | \$71.0 | 4.2% | 3.0% | \$2.1 | \$1.3 | 61.5% |
| Casual Male Retail Group | \$113.5 | \$113.5 | -0.0% | 0.3% | \$1.9 | \$2.5 | -23.7% |
| Cato Corporation | \$231.0 | \$219.0 | 5.5% | 2.0% | \$12.1 | \$12.5 | -3.3% |
| Charlotte Russe Holding, Inc. | \$193.2 | \$180.3 | 7.2% | -6.5% | \$6.6 | \$10.1 | -35.2% |
| Charming Shoppes, Inc. | \$648.6 | \$694.4 | -6.6% | -10.0% | (\$3.7) | \$20.9 | -117.7% |
| Chico's FAS, Inc. | \$405.2 | \$436.0 | -7.1% | -15.9% | \$6.7 | \$38.7 | -82.7% |
| Children's Place | \$338.0 | \$290.5 | 16.4% | 9.0% | \$0.0 | (\$28.1) | 100.0% |
| Citi Trends, Inc. | \$115.7 | \$96.8 | 19.5% | 6.5% | \$2.8 | \$0.6 | 353.9% |
| Coldwater Creek Inc. | \$241.4 | \$253.5 | -4.8% | -13.7% | \$3.1 | \$8.7 | -63.9% |
| dELIA's, Inc. | \$58.1 | \$52.4 | 10.9% | 5.2% | (\$5.0) | (\$5.1) | 2.0% |
| Dillard's, Inc. | \$1,646.5 | \$1,689.1 | -2.5% | -4.0% | (\$38.3) | (\$25.2) | -52.0% |
| Eddie Bauer Holdings | \$233.0 | \$227.0 | 2.6% | 8.6% | (\$0.1) | (\$22.2) | 99.7% |
| Gap Inc. | \$3,499.0 | \$3,685.0 | -5.0% | -10.0% | \$229.0 | \$152.0 | 50.7% |
| Gottschalks | \$133.7 | \$145.0 | -7.8% | -7.3% | (\$4.4) | (\$4.8) | 8.3% |
| Gymboree Corporation | \$205.7 | \$182.4 | 12.8% | 1.0% | \$8.0 | \$5.8 | 37.9% |
| Hot Topic, Inc. | \$166.8 | \$161.7 | 3.2% | -0.9% | (\$0.5) | (\$1.7) | 74.0% |
| J. Crew Group, Inc. | \$336.3 | \$304.7 | 10.4% | -0.4% | \$18.1 | \$20.6 | -12.1% |
| J.C. Penney Company | \$4,282.0 | \$4,391.0 | -2.5% | -4.3% | \$117.0 | \$182.0 | -35.7% |
| Jo-Ann Stores, Inc. | \$403.0 | \$388.5 | 3.7% | 3.3% | (\$11.7) | (\$18.4) | 36.4% |
| JoS. A. Bank Clothiers | \$152.7 | \$134.3 | 13.7% | 6.8% | \$8.9 | \$8.2 | 8.1% |
| Kohl's Corporation | \$3,725.5 | \$3,589.2 | 3.8% | -4.6% | \$236.0 | \$269.2 | -12.3% |
| Limited Brands | \$2,284.3 | \$2,624.1 | -12.9% | -7.0% | \$102.0 | \$264.4 | -61.4% |

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Second Quarter Scorecard

(continued from page 7)

| \$ in Millions. Quarter ended closest to 7/31/08 | Sales | | | Comps | Net Income | | |
|---|------------|------------|--------|--------|------------|-----------|---------|
| | 2008 | 2007 | Change | | 2008 | 2007 | Change |
| Apparel | | | | | | | |
| Macy's, Inc. | \$5,718.0 | \$5,892.0 | -3.0% | -2.1% | \$73.0 | \$74.0 | -1.4% |
| Men's Wearhouse | \$545.3 | \$569.3 | -4.2% | -8.0% | \$32.8 | \$54.2 | -39.5% |
| Mothers Work, Inc. | \$152.2 | \$153.2 | -0.7% | 2.4% | \$4.1 | \$1.0 | 310.0% |
| New York & Company, Inc. | \$295.7 | \$285.0 | 3.8% | -2.0% | \$8.7 | \$3.5 | 148.6% |
| Nordstrom, Inc. | \$2,287.0 | \$2,390.0 | -4.3% | -6.0% | \$143.0 | \$180.4 | -20.7% |
| Pacific Sunwear | \$312.7 | \$311.8 | 0.3% | -1.0% | \$2.8 | (\$10.5) | 126.7% |
| Reitmans Limited | \$289.5 | \$291.9 | -0.8% | -4.5% | \$35.4 | \$32.1 | 10.3% |
| Retail Ventures, Inc. | \$459.8 | \$464.6 | -1.0% | -5.1% | tba | \$106.2 | tba |
| Ross Stores, Inc. | \$1,640.4 | \$1,444.6 | 13.6% | 6.0% | \$71.3 | \$50.9 | 40.1% |
| Saks Incorporated | \$669.2 | \$694.1 | -3.6% | -4.0% | (\$31.7) | (\$24.6) | -28.7% |
| Stage Stores, Inc. | \$372.7 | \$359.2 | 3.8% | -1.4% | \$9.7 | \$9.9 | -2.2% |
| Stein Mart, Inc. | \$311.6 | \$330.7 | -5.8% | -9.7% | (\$8.0) | \$2.2 | -463.6% |
| Talbots, Inc. | \$528.0 | \$572.0 | -7.7% | -12.0% | (\$25.0) | (\$13.3) | -88.0% |
| TJX Companies | \$4,621.3 | \$4,313.3 | 7.1% | 4.0% | \$200.2 | \$59.0 | 239.3% |
| Urban Outfitters, Inc. | \$454.3 | \$348.4 | 30.4% | 13.0% | tba | \$31.9 | tba |
| Wet Seal, Inc. | \$149.1 | \$143.3 | 4.0% | -4.4% | \$10.1 | \$6.8 | 50.0% |
| Mass Merchants | | | | | | | |
| Big Lots, Inc. | \$1,105.2 | \$1,084.9 | 1.9% | 2.8% | \$26.0 | \$23.4 | 11.2% |
| BJ's Wholesale Club, Inc. | \$2,651.3 | \$2,248.2 | 17.9% | 15.5% | \$36.5 | \$36.3 | 0.6% |
| Canadian Tire | \$2,949.5 | \$2,835.1 | 4.0% | -0.5% | \$97.7 | \$122.5 | -20.2% |
| Dollar General Corporation | \$2,609.4 | \$2,347.6 | 11.2% | 10.1% | \$27.7 | (\$68.8) | 140.3% |
| Dollar Tree Stores, Inc. | \$1,093.1 | \$971.2 | 12.6% | 6.5% | \$37.6 | \$32.6 | 15.3% |
| Duckwall-ALCO Stores, Inc. | \$129.6 | \$119.0 | 8.9% | -2.1% | tba | \$0.4 | tba |
| Fred's, Inc. | \$447.1 | \$424.6 | 5.3% | 4.9% | \$1.0 | \$3.1 | -66.2% |
| Overstock.com | \$188.8 | \$149.0 | 26.7% | NA | (\$6.5) | (\$13.8) | 52.9% |
| Sears Canada Inc. | \$1,420.3 | \$1,443.9 | -1.6% | 1.8% | \$61.1 | \$42.3 | 44.4% |
| Sears Holdings Corporation | \$11,762.0 | \$12,260.0 | -4.1% | -6.2% | \$65.0 | \$173.0 | -62.4% |
| Target Corporation | \$15,472.0 | \$14,620.0 | 5.8% | -0.4% | \$634.0 | \$686.0 | -7.6% |
| Wal-Mart Stores, Inc. | \$101,598 | \$91,990 | 10.4% | 4.6% | \$3,449.0 | \$2,952.0 | 16.8% |
| Sports & Footwear | | | | | | | |
| Bakers Footwear Group, Inc | \$43.6 | \$42.0 | 3.8% | 6.4% | tba | (\$8.7) | tba |
| Big 5 Sporting Goods Corp. | \$209.0 | \$217.8 | -4.0% | -7.6% | \$1.7 | \$5.9 | -71.0% |
| Broder Bros., Co. | \$257.6 | \$249.4 | 3.3% | NA | (\$0.7) | (\$4.4) | 84.1% |
| Brown Shoe Company, Inc. | \$569.2 | \$576.6 | -1.3% | -2.9% | \$2.2 | \$9.8 | -77.4% |
| Cabela's | \$526.0 | \$451.2 | 16.6% | -1.6% | \$7.3 | \$11.3 | -35.4% |
| Collective Brands (Payless St | \$911.7 | \$699.3 | 30.4% | 0.2% | \$8.1 | \$24.9 | -67.5% |
| Dick's Sporting Goods, Inc. | \$1,086.3 | \$1,013.4 | 7.2% | -3.7% | \$41.1 | \$47.9 | -14.2% |
| DSW Inc. | \$357.2 | \$348.7 | 2.4% | -6.9% | \$11.0 | \$6.5 | 68.1% |
| Foot Locker | \$1,302.0 | \$1,283.0 | 1.5% | -0.5% | \$18.0 | (\$18.0) | 200.0% |
| Footstar, Inc. | \$153.2 | \$173.4 | -11.6% | -10.3% | \$30.4 | \$21.5 | 41.4% |
| Forzani Group Ltd. (C\$) | \$295.6 | \$292.4 | 1.1% | -4.2% | \$1.5 | \$5.4 | -72.2% |
| Gander Mountain | \$252.9 | \$216.5 | 16.8% | -11.7% | (\$4.9) | (\$9.7) | 49.7% |
| Genesco Inc. | \$353.1 | \$328.0 | 7.7% | 4.0% | (\$10.3) | (\$4.2) | -145% |
| Golfsmith International | \$130.0 | \$125.0 | 4.0% | 0.5% | \$8.6 | \$6.8 | 25.8% |
| GSI Commerce | \$193.2 | \$131.3 | 47.1% | NA | (\$19.0) | (\$5.0) | -280.0% |
| Hibbett Sporting Goods, Inc. | \$130.3 | \$114.4 | 13.9% | 5.0% | \$4.8 | \$4.7 | 2.4% |
| Shoe Carnival, Inc. | \$158.5 | \$154.8 | 2.4% | -1.0% | \$1.0 | \$0.2 | 485.0% |
| Walking Company, The | \$56.0 | \$55.9 | 0.3% | -1.2% | (\$2.2) | (\$0.2) | 1059% |
| West 49 (C\$) | \$45.0 | \$42.4 | 6.1% | 3.9% | (\$1.8) | (\$0.6) | 197.3% |
| West Marine, Inc. | \$226.7 | \$247.1 | -8.3% | -7.8% | \$4.4 | \$20.8 | -78.6% |
| WinMark Corporation | \$8.7 | \$7.6 | 14.5% | NA | \$0.9 | \$0.4 | 116.3% |
| Zumiez Inc. | \$92.3 | \$82.0 | 12.5% | -1.7% | \$2.7 | \$3.1 | -12.5% |
| Specialty | | | | | | | |
| A.C. Moore Arts & Crafts | \$126.4 | \$124.4 | 1.6% | -4.8% | (\$4.3) | (\$0.6) | -663.0% |
| Advance Auto Parts, Inc. | \$1,235.8 | \$1,169.9 | 5.6% | 2.9% | \$75.4 | \$68.4 | 10.2% |

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Second Quarter Scorecard

(continued from page 8)

| \$ in Millions. Quarter ended closest to 7/31/08 | Sales | | | Comps | Net Income | | |
|---|------------|------------|--------|--------|------------|-----------|---------|
| | 2008 | 2007 | Change | | 2008 | 2007 | Change |
| Specialty | | | | | | | |
| Amscan Holdings, Inc. | \$371.5 | \$279.2 | 33.1% | NA | \$14.7 | (\$2.5) | 688.0% |
| Barnes & Noble, Inc. | \$1,123.8 | \$1,244.2 | -9.7% | -4.7% | \$15.4 | \$18.1 | -14.7% |
| Blue Nile, Inc. | \$73.7 | \$72.1 | 2.2% | NA | \$3.2 | \$3.8 | -15.8% |
| Brookstone, Inc. | \$97.4 | \$99.9 | -2.5% | -4.3% | (\$8.7) | (\$6.5) | -34.0% |
| Cost Plus, Inc. | \$221.0 | \$209.2 | 5.6% | 1.2% | (\$26.6) | (\$18.0) | -48.1% |
| Ethan Allen | \$235.9 | \$258.5 | -8.7% | -11.1% | \$11.1 | \$20.5 | -45.9% |
| Finlay Enterprises, Inc. | \$190.6 | \$148.0 | 28.8% | -4.8% | (\$12.3) | (\$8.4) | 46.4% |
| Haverty Furniture | \$168.4 | \$187.1 | -10.0% | -12.7% | (\$2.3) | (\$1.4) | -64.3% |
| Jennifer Convertibles | \$26.8 | \$30.3 | -11.6% | -19.8% | (\$0.6) | \$1.7 | -135.3% |
| Kirkland's, Inc. | \$87.7 | \$87.4 | 0.3% | 2.8% | (\$1.7) | (\$9.2) | 81.5% |
| Leon's Furniture Limited | \$224.7 | \$190.4 | 18.0% | NA | \$11.6 | \$9.9 | 17.2% |
| Linens N Things | \$468.1 | \$593.3 | -21.1% | -18.3% | tba | tba | tba |
| Michaels Stores, Inc. | \$796.0 | \$788.0 | 1.0% | -2.6% | (\$25.0) | (\$44.0) | 43.2% |
| Movado Group, Inc. | \$129.7 | \$139.5 | -7.0% | NA | \$8.1 | \$12.3 | -34.1% |
| Pet Valu | \$44.3 | \$38.6 | 14.8% | 8.8% | \$3.6 | \$2.8 | 29.6% |
| PetSmart, Inc. | \$1,241.9 | \$1,116.7 | 11.2% | 4.0% | \$37.2 | \$47.1 | -21.0% |
| Tiffany & Co. | \$732.4 | \$662.6 | 10.5% | -1.0% | \$80.8 | \$40.5 | 99.5% |
| Williams-Sonoma, Inc. | \$819.6 | \$859.4 | -4.6% | -11.7% | \$18.4 | \$26.0 | -29.2% |
| Home Centers | | | | | | | |
| Ace Hardware | \$1,066.9 | \$1,022.6 | 4.3% | NA | \$33.4 | \$38.8 | -13.9% |
| Builders FirstSource, Inc. | \$307.3 | \$465.1 | -33.9% | NA | (\$45.9) | \$8.4 | -646.4% |
| Building Materials Holding | \$384.6 | \$656.0 | -41.4% | NA | (\$31.9) | \$19.4 | -264.4% |
| Calloway's Nursery, Inc. | \$20.3 | \$18.1 | 12.2% | 6.5% | \$1.9 | \$1.3 | 46.2% |
| Fastenal Company | \$604.2 | \$519.7 | 16.3% | 12.3% | \$76.2 | \$60.3 | 26.4% |
| Five Star Products, Inc. | \$31.4 | \$35.9 | -12.5% | NA | \$0.1 | \$0.6 | -82.7% |
| Greybar Electric | \$1,420.7 | \$1,339.5 | 6.1% | NA | \$28.4 | \$27.7 | 2.5% |
| Home Depot, Inc. | \$20,990.0 | \$22,184.0 | -5.4% | -7.9% | \$2,042.0 | \$2,557.0 | -20.1% |
| Huttig Building Products | \$195.4 | \$239.5 | -18.4% | NA | (\$2.5) | \$1.1 | -327.3% |
| Interline Brands, Inc. | \$311.4 | \$313.2 | -0.6% | NA | \$11.2 | \$12.0 | -6.7% |
| Lowe's Companies | \$14,509.0 | \$14,167.0 | 2.4% | -5.3% | \$938.0 | \$1,019.0 | -7.9% |
| Lumber Liquidators | \$128.0 | \$105.7 | 21.1% | 2.7% | \$5.9 | \$2.3 | 156.5% |
| Rona, Inc. (C\$) | \$1,473.3 | \$1,469.1 | 0.3% | -4.4% | \$80.1 | \$86.2 | -7.1% |
| Sherwin-Williams Company | \$2,229.5 | \$2,198.2 | 1.4% | -4.5% | \$171.7 | \$202.6 | -15.3% |
| Tractor Supply Company | \$898.3 | \$790.9 | 13.6% | 3.4% | \$47.0 | \$43.8 | 7.3% |
| United Rentals, Inc. | \$831.0 | \$962.0 | -13.6% | NA | \$37.0 | \$67.0 | -44.8% |
| W.W. Grainger | \$1,756.9 | \$1,601.0 | 9.7% | 8.8% | \$113.2 | \$104.8 | 8.0% |
| Wesco International | \$1,587.8 | \$1,518.1 | 4.6% | NA | \$60.1 | \$59.6 | 0.8% |
| Food | | | | | | | |
| Arden Group | \$116.6 | \$119.8 | -2.7% | -2.7% | \$6.6 | \$6.5 | 1.7% |
| Casey's General Stores | \$1,565.7 | \$1,279.3 | 22.4% | 4.7% | \$28.8 | \$29.8 | -3.4% |
| Great Atlantic & Pacific Tea | \$2,922.7 | \$1,679.2 | 74.1% | 3.2% | \$2.2 | (\$65.1) | 103.4% |
| Loblaw Companies Limited | \$7,037.0 | \$6,933.0 | 1.5% | 0.7% | \$140.0 | \$119.0 | 17.6% |
| Nash Finch Company | \$1,042.0 | \$1,064.0 | -2.1% | -3.9% | \$10.1 | \$9.6 | 5.2% |
| Publix Super Markets | \$5,894.8 | \$5,699.0 | 3.4% | 1.3% | \$295.8 | \$306.4 | -3.5% |
| Safeway, Inc. | \$10,120.0 | \$9,823.3 | 3.0% | -0.3% | \$234.3 | \$218.2 | 7.4% |
| Supervalu Inc. | \$13,347.0 | \$13,292.0 | 0.4% | -0.9% | \$162.0 | \$148.0 | 9.5% |
| Weis Markets, Inc. | \$603.4 | \$578.8 | 4.3% | 4.3% | \$12.8 | \$18.2 | -29.7% |
| Drug | | | | | | | |
| Abbott | \$7,314.0 | \$6,370.6 | 14.8% | NA | \$1,322.0 | \$988.7 | 33.7% |
| AmerisourceBergen Corp | \$17,507.5 | \$15,289.7 | 14.5% | NA | (\$108.0) | \$129.9 | -183.1% |
| CVS Caremark Corporation | \$21,140.3 | \$20,703.3 | 2.1% | 3.1% | \$774.8 | \$723.6 | 7.1% |
| Drugstore.com, Inc. | \$122.8 | \$110.4 | 11.2% | NA | (\$2.3) | (\$3.0) | -23.3% |
| Duane Reade Holdings | \$451.4 | \$431.9 | 4.5% | 4.7% | (\$12.1) | (\$20.1) | -39.8% |
| Express Scripts, Inc. | \$4,706.5 | \$4,574.8 | 2.9% | NA | \$190.2 | \$152.7 | 24.6% |
| Longs Drug Stores | \$1,332.7 | \$1,274.5 | 4.6% | -1.1% | \$27.5 | \$26.6 | 3.3% |
| McKesson Corp. | \$26,704.0 | \$24,528.0 | 8.9% | NA | \$235.0 | \$235.0 | 0.0% |

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Second Quarter Scorecard

(continued from page 9)

| \$ in Millions. Quarter ended closest to 7/31/08 | Sales | | | Comps | Net Income | | |
|---|-----------|-----------|--------|--------|------------|----------|---------|
| | 2008 | 2007 | Change | | 2008 | 2007 | Change |
| Drug | | | | | | | |
| Omnicare, Inc. | \$1,550.2 | \$1,549.2 | 0.1% | NA | \$36.8 | \$49.2 | -25.2% |
| PharMerica Corporation | \$486.3 | \$173.4 | 180.4% | NA | \$2.9 | (\$0.4) | 825.0% |
| Shoppers Drug Mart | \$2,109.3 | \$1,928.1 | 9.4% | 4.6% | \$128.3 | \$112.2 | 14.3% |
| Ulta | \$249.1 | \$200.4 | 24.3% | 3.7% | \$3.7 | \$2.2 | 68.2% |
| High-Tech & Electronics | | | | | | | |
| Aaron Rents, Inc. | \$411.2 | \$359.0 | 14.5% | 4.1% | \$23.3 | \$19.7 | 18.3% |
| Amazon.com, Inc. | \$4,063.0 | \$2,886.0 | 40.8% | NA | \$158.0 | \$78.0 | 102.6% |
| BMTC Group Inc. | \$225.5 | \$216.1 | 4.3% | NA | \$17.1 | \$14.9 | 14.8% |
| Conn's, Inc. | \$179.0 | \$190.6 | -6.1% | -1.4% | \$9.7 | \$10.2 | -4.9% |
| GameStop Corp. | \$1,804.4 | \$1,338.2 | 34.8% | 20.0% | \$57.2 | \$21.8 | 162.4% |
| Ingram Micro Inc. | \$8,816.6 | \$8,186.1 | 7.7% | NA | \$58.9 | \$52.4 | 12.4% |
| Office Depot, Inc. | \$3,605.1 | \$3,631.6 | -0.7% | -10.0% | (\$2.0) | \$105.6 | -101.9% |
| OfficeMax Incorporated | \$1,984.6 | \$2,132.4 | -6.9% | -10.0% | (\$894.2) | \$27.4 | -3364% |
| PC Connection, Inc. | \$449.4 | \$441.0 | 1.9% | NA | \$5.1 | \$5.8 | -12.1% |
| PC Mall, Inc. | \$331.2 | \$263.0 | 25.9% | NA | \$3.0 | \$3.0 | 1.1% |
| RadioShack Corporation | \$994.6 | \$934.8 | 6.4% | 6.9% | \$41.4 | \$47.0 | -11.9% |
| Rent-A-Center, Inc. | \$719.0 | \$724.2 | -0.7% | 0.9% | \$37.7 | \$41.3 | -8.7% |
| Staples, Inc. | \$5,074.7 | \$4,290.4 | 18.3% | -7.0% | \$150.2 | \$178.8 | -16.0% |
| Tech Data Corporation | \$6,166.0 | \$5,613.3 | 9.8% | NA | \$23.7 | \$7.2 | 229.2% |
| Trans World Entertainment | \$215.2 | \$267.3 | -19.5% | -7.0% | (\$19.2) | (\$10.1) | -90.1% |
| Zones, Inc. | \$158.3 | \$192.2 | -17.6% | NA | \$3.6 | \$4.4 | -17.8% |

Retailer of the Week: Pacific Sunwear

(continued from page 1)

second quarter profits were light, and if PacSun has a future it needs to solve the problems at its namesake banner.

| \$ FIGURES IN MILLIONS | 08/02/2008 (Q2 YTD FY09) | 08/04/2007 (Q2 YTD FY08) | Year-over-Year Change |
|---|-----------------------------|-----------------------------|--------------------------|
| Liquidity Ratios | | | |
| Cash and Equivalents | \$1.6 | \$42.3 | -96.3% |
| Cash and Equivalents % Current Liabilities | 0.74% | 21.72% | -2,098 bps |
| Working Capital | \$103.0 | \$160.7 | -35.91% |
| Current Ratio | 1.49x | 1.83x | -34 bps |
| Leverage Ratios | | | |
| Total Debt | \$10.8 | \$0.0 | n/a |
| Total Debt / Equity | 2.7% | 0.0% | 270 bps |
| Total Liabilities / Total Assets | 45.1% | 40.9% | 419 bps |

OPERATING PERFORMANCE

Revenues for the second quarter ended August 2, 2008 were \$312.7 million, a 0.3% increase from the same quarter a year ago. Additional PacSun locations contributed an extra \$9 million to the top line, while store closures brought the revenue stream down \$5 million. For the quarter, comp store sales fell 1%, responsible for about \$3 million in revenue declines. Gross margin for the quarter was down 220 basis points, mainly due to a drop in merchandise margins and the de-leveraging of occupancy expenses from a drop in comp store sales. SG&A as a percentage of revenues was up 90 basis points, further harming the results. The largest change was from an

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Retailer of the Week: Pacific Sunwear

(continued from page 10)

accelerated depreciation charge associated with store closures. For the quarter, operating income was just \$5.1 million, down sharply from \$15.5 million last year. The EBITDA remained firmly positive, however. The net income was \$2.8 million for the three months. The absence of the demo and One Thousand Steps locations places these subpar results firmly on the shoulders of PacSun. The future is now for this firm, and there isn't anymore fat to trim.

Revenues for the first half ended August 2, 2008 were \$579.6 million, a marginal decrease from the first half a year ago. Additional PacSun locations contributed an extra \$17 million to the top line, while store closures brought the revenue stream down \$12 million. For the semester, comp store sales fell 1%, responsible for about \$5 million in revenue declines. Gross margin for the period fell 100 basis points. The drop in gross margin was mainly due to a de-leveraging expense from the drop in comps in the first half. The negative effects of the Demo closure start with the SG&A expenses. SG&A as a percentage of revenues was up 390 basis points. The largest change was from an asset impairment charge associated with the closure of a distribution center, while legal and severance expenses from Demo put the final hurt on the operating line. For the semester, operating loss was \$15.3 million. The store closures also forced Pacific Sunwear to take a \$26 million loss from discontinued operations, pulling the firm well into the red for the first half. The net loss was \$34.3 million for the six months. It is clear that PacSun was struggling with the other two banners, and the decision to close them down was a correct one. However, now is the time for the firm to improve its namesake banner.

CAPITAL STRUCTURE

In the past, we have had no problems for PacSun from a credit standpoint. During the second quarter, however, PacSun couldn't resist the urge to buy back stock. During the quarter, the company used \$52.9 million for this purpose. The absence of the cash creates a huge hole on the firm's liquidity side of the sheet.

Cash on hand was a measly \$1.6 million at the end of the quarter. This was enough to cover up a pathetic 0.74% of current liabilities. There was a lot of cash used in the first quarter for various costs associated with Demo, while the cash was used in the second quarter to buy back stock. PacSun was able to bring inventory down nicely. While this affected its profits for the year, it was a necessary step as the company digs itself out of the hole created by its subsidiaries. The working capital was still in decent shape at the end of the quarter, but the absurdly low cash position has us very worried.

To fund the stock buybacks, PacSun was forced to partially borrow on its revolver. There was \$10.8 million outstanding on the facility at the end of the quarter. There was still \$139 million available at that time.

PacSun still has a decent equity position of \$399.2 million.

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