DILLARDS INC
Form 10-Q
June 08, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended May 2, 2009
or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from __________ to __________.

Commission File Number: 1-6140

DILLARD'S, INC.
(Exact name of registrant as specified in its charter)

DELAWARE	71-0388071
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1600 CANTRELL ROAD, LITTLE ROCK, ARKANSAS 72201
(Address of principal executive offices)
(Zip Code)

(501) 376-5200
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

þYes ¨No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

¨Yes ¨No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

¨Yes þNo

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

CLASS A COMMON STOCK as of May 30, 2009	69,775,521
CLASS B COMMON STOCK as of May 30, 2009	4,010,929

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DILLARD'S, INC.

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PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

DILLARD'S, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In Thousands)

	May 2, 2009	January 31, 2009	May 3, 2008
Assets			
Current assets:			
Cash and cash equivalents	$102,731	$96,823	$84,043
Accounts receivable, net	70,353	87,998	9,034
Merchandise inventories	1,647,116	1,374,394	2,018,406
Federal income tax receivable	74,415	74,415	-
Other current assets	36,817	53,125	64,658
Total current assets	1,931,432	1,686,755	2,176,141
Property and equipment, net	2,918,518	2,973,151	3,182,271
Goodwill	-	-	31,912
Other assets	83,142	85,938	166,459
Total assets	$4,933,092	$4,745,844	$5,556,783
Liabilities and stockholders' equity			
Current liabilities:			
Trade accounts payable and accrued expenses	$849,343	$642,940	$957,545
Current portion of long-term debt	25,553	25,535	100,712
Current portion of capital lease obligations	1,721	1,704	2,295
Other short-term borrowings	175,000	200,000	300,000
Federal and state income taxes including current deferred taxes	55,762	43,486	39,471
Total current liabilities	1,107,379	913,665	1,400,023
Long-term debt	752,266	757,689	759,981
Capital lease obligations	23,700	24,116	25,339
Other liabilities	221,680	220,911	219,817
Deferred income taxes	370,578	378,348	435,633
Guaranteed preferred beneficial interests in the Company’s subordinated debentures	200,000	200,000	200,000
Stockholders’ equity:			
Common stock	1,209	1,206	1,206
Additional paid-in capital	782,382	781,055	780,757
Accumulated other comprehensive loss	(16,539)	(16,872)	(21,786)
Retained earnings	2,432,438	2,427,727	2,680,373
Less treasury stock, at cost	(942,001)	(942,001)	(924,560)

Total stockholders' equity	2,257,489	2,251,115	2,515,990
Total liabilities and stockholders' equity	$4,933,092	$4,745,844	$5,556,783

See notes to condensed consolidated financial statements.

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DILLARD'S, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND RETAINED EARNINGS
(Unaudited)
(In Thousands, Except Per Share Data)

	Three Months Ended	
	May 2, 2009	May 3, 2008
Net sales	$1,473,870	$1,675,554
Service charges and other income	31,426	38,044
	1,505,296	1,713,598
Cost of sales	979,579	1,118,302
Advertising, selling, administrative and general expenses	414,284	480,921
Depreciation and amortization	65,524	72,075
Rentals	14,500	15,677
Interest and debt expense, net	18,408	22,113
Gain on disposal of assets	(68)	(99)
Asset impairment and store closing charges	-	925
Income before income taxes and equity in (losses) earnings of joint ventures	13,069	3,684
Income taxes	4,650	1,610
Equity in (losses) earnings of joint ventures	(756)	619
Net income	7,663	2,693
Retained earnings at beginning of period	2,427,727	2,680,690
Cash dividends declared	(2,952)	(3,010)
Retained earnings at end of period	$2,432,438	$2,680,373
Earnings per share:		
Basic	$0.10	$0.04
Diluted	$0.10	$0.04
Cash dividends declared per common share	$0.04	$0.04

See notes to condensed consolidated financial statements.

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DILLARD'S, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In Thousands)

	Three Months Ended	
	May 2, 2009	May 3, 2008
Operating activities:		
Net income	$7,663	$2,693
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and deferred financing	66,005	72,536
Gain on repurchase of debt	(1,476)	—
Gain on disposal of property and equipment	(68)	(99)
Share-based compensation	—	15
Asset impairment and store closing charges	—	925
Changes in operating assets and liabilities:		
Decrease in accounts receivable	17,645	1,846
Increase in merchandise inventories and other current assets	(256,414)	(246,925)
Decrease in other assets	2,352	3,665
Increase in trade accounts payable and accrued expenses, other liabilities and income taxes	206,714	201,877
Net cash provided by operating activities	42,421	36,533
Investing activities:		
Purchases of property and equipment	(4,828)	(46,759)
Proceeds from disposal of property and equipment	581	2
Net cash used in investing activities	(4,247)	(46,757)
Financing activities:		
Principal payments on long-term debt and capital lease obligations	(4,328)	(96,635)
Cash dividends paid	(2,938)	(3,010)
(Decrease) increase in short-term borrowings	(25,000)	105,000
Net cash (used in) provided by financing activities	(32,266)	5,355
Increase (decrease) in cash and cash equivalents	5,908	(4,869)
Cash and cash equivalents, beginning of period	96,823	88,912
Cash and cash equivalents, end of period	$102,731	$84,043
Non-cash transactions:		
Accrued capital expenditures	$5,000	$17,020
Stock awards	1,330	1,756

See notes to condensed consolidated financial statements.

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DILLARD'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements of Dillard's, Inc. (the "Company") have been prepared in accordance with the rules of the Securities and Exchange Commission (“SEC”). Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair statement have been included. Operating results for the three months ended May 2, 2009 are not necessarily indicative of the results that may be expected for the fiscal year ending January 30, 2010 due to the seasonal nature of the business. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2009 filed with the SEC on April 1, 2009.

Note 2. Business Segments

On August 29, 2008, the Company purchased the remaining interest in CDI Contractors, LLC and CDI Contractors, Inc. (collectively “CDI”), a former 50% equity method joint venture investment of the Company. Subsequent to the purchase, CDI’s results of operations have been consolidated with the Company’s results of operations.

Before the acquisition of CDI, the Company operated in one reportable segment: the operation of retail department stores. Following the acquisition, the Company operated in two reportable segments. These segments include the operation of retail department stores and a general contracting construction company.

For our retail operations reportable segment, in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, we determined our operating segments on a store by store basis. Each store’s operating performance has been aggregated into one reportable segment. Each store meets the aggregation criteria set forth in SFAS No. 131. Our operating segments are aggregated for financial reporting purposes because they are similar in each of the following areas: economic characteristics, class of consumer, nature of products, nature of production processes and distribution methods. Revenues from external customers are derived from merchandise sales and we do not rely on any major customers as a source of revenue. Across all stores, Dillard’s operates one store format under the Dillard’s name where each store offers the same general mix of merchandise with similar categories and similar customers. The Company believes that disaggregating our operating segments would not provide meaningful additional information.

The following table summarizes certain segment information, including the reconciliation of those items to the Company’s consolidated operations:

	Three Months Ended May 2, 2009		
(in thousands of dollars)	Retail Operations	Construction	Consolidated
Net sales from external customers	$ 1,414,691	$ 59,179	$ 1,473,870
Gross profit	491,706	2,585	494,291
Total assets	4,854,361	78,731	4,933,092
Income before income taxes and equity in (losses) earnings of joint ventures	11,794	1,275	13,069

Intersegment construction revenues of $8.1 million were eliminated during consolidation and have been excluded from net sales for the quarter ended May 2, 2009.

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Note 3. Stock-Based Compensation

The Company has various stock option plans that provide for the granting of options to purchase shares of Class A Common Stock to certain key employees of the Company. Exercise and vesting terms for options granted under the plans are determined at each grant date. There were no stock options granted during the quarters ended May 2, 2009 and May 3, 2008.

Stock option transactions for the three months ended May 2, 2009 are summarized as follows:

Fixed Options	Shares	Weighted-Average Exercise Price
Outstanding, beginning of period	5,261,375	$ 25.92
Granted	-	-
Exercised	-	-
Forfeited	-	-
Outstanding, end of period	5,261,375	$ 25.92
Options exercisable at period end	5,261,375	$ 25.92

At May 2, 2009, the intrinsic value of outstanding and exercisable stock options was $0.

Note 4. Asset Impairment and Store Closing Charges

There were no asset impairment and store closing costs recorded during the quarter ended May 2, 2009.

During the quarter ended May 3, 2008, the Company recorded a pretax charge of $0.9 million for asset impairment and store closing costs. The charge consisted of a write-off of equipment and an accrual for future rent on a distribution center that was closed during the quarter.

Following is a summary of the activity in the reserve established for store closing charges for the quarter ended May 2, 2009:

(in thousands)	Balance, Beginning of Period	Adjustments and Charges	Cash Payments	Balance, End of Period
Rentals, property taxes and utilities	$ 5,240	$ 70	$ 550	$ 4,760

Reserve amounts are included in trade accounts payable and accrued expenses and other liabilities.

Note 5. Earnings Per Share Data

The following table sets forth the computation of basic and diluted earnings per share ("EPS") for the periods indicated (in thousands, except per share data).

	Three Months Ended	
	May 2, 2009	May 3, 2008
Basic:		
Net income	$ 7,663	$ 2,693

Weighted average shares of common stock outstanding		73,644		75,200
Basic earnings per share	$	0.10	$	0.04

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	Three Months Ended	
	May 2, 2009	May 3, 2008
Diluted:		
Net income	$ 7,663	$ 2,693
Weighted average shares of common stock outstanding	73,644	75,200
Dilutive effect of stock-based compensation	-	-
Total weighted average equivalent shares	73,644	75,200
Diluted earnings per share	$ 0.10	$ 0.04

Total stock options outstanding were 5,261,375 and 5,336,375 at May 2, 2009 and May 3, 2008, respectively. Of these, options to purchase 5,261,375 and 5,336,375 shares of Class A common stock at prices ranging from $24.01 to $30.47 per share were outstanding at May 2, 2009 and May 3, 2008, respectively, but were not included in the computation of diluted earnings per share because the effect of their inclusion would be antidilutive.

Note 6. Comprehensive Income

The following table shows the computation of comprehensive income (in thousands):

	Three Months Ended	
	May 2, 2009	May 3, 2008
Net income	$ 7,663	$ 2,693
Other comprehensive income:		
Amortization of retirement plan and other retiree benefit adjustments, net of taxes	333	425
Total comprehensive income	$ 7,996	$ 3,118

Note 7. Commitments and Contingencies

On May 27, 2009 a lawsuit was filed in the United States District Court for the Eastern District of Arkansas styled Steven Harben, Derivatively on Behalf of Nominal Defendant Dillard's Inc. v. William Dillard II et al, Case Number 4:09-IV-395. The lawsuit generally seeks return of monies and alleges that certain officers and directors of the Company have been overcompensated and/or received improper benefits at the expense of the Company and its shareholders. While it is too soon to predict the outcome of any litigation filed as recently as this suit, the named officers and directors intend to contest these allegations vigorously.

Various other legal proceedings in the form of lawsuits and claims, which occur in the normal course of business, are pending against the Company and its subsidiaries. In the opinion of management, disposition of these matters is not expected to have a material adverse effect on the Company's financial position, cash flows or results of operations.

At May 2, 2009, letters of credit totaling $91.3 million were issued under the Company's $1.2 billion revolving credit facility.

Note 8. Benefit Plans

The Company has a nonqualified defined benefit plan ("Plan") for its officers. The Plan is noncontributory and provides benefits based on years of service and compensation during employment. Pension expense is determined using various actuarial cost methods to estimate the total benefits ultimately payable to officers and allocates this cost to service periods. The Plan is unfunded. The actuarial assumptions used to calculate pension costs are reviewed annually. The Company made contributions to the Plan of $1.0 million during the quarter ended May 2, 2009. The Company expects to make contributions to the Plan of approximately $3.2 million for the remainder of fiscal 2009.

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The components of net periodic benefit costs are as follows (in thousands):

	Three Months Ended	
	May 2, 2009	May 3, 2008
Components of net periodic benefit costs:		
Service cost	$ 771	$ 626
Interest cost	1,826	1,764
Net actuarial loss	368	513
Amortization of prior service cost	157	157
Net periodic benefit costs	$ 3,122	$ 3,060

Note 9. Recently Issued Accounting Standards

In March 2008, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 161, Disclosures about Derivative Instruments and Hedging Activities—an Amendment of FASB Statement No. 133 ("SFAS 161"). SFAS 161 requires entities to provide enhanced disclosures related to how an entity uses derivative instruments, how derivatives are accounted for under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities and how derivative instruments and the related hedged items impact an entity's financial statements. The provisions of SFAS 161 were adopted February 1, 2009 and did not have a material impact on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interest in Consolidated Financial Statements ("SFAS 160"). SFAS 160's objective is to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 was adopted February 1, 2009 and did not have a material impact on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements ("SFAS 157"). This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having concluded in those other accounting pronouncements that fair value is the relevant measurement attribute. This statement was effective for financial assets and liabilities in financial statements issued for fiscal years beginning after November 15, 2007. The adoption of this portion of the statement did not have a material impact on our consolidated financial statements.

In February 2008, the FASB issued FASB Staff Position ("FSP") FAS No. 157-2, Effective Date for FASB Statement No. 157. This FSP permitted the delayed application of SFAS 157 for all nonrecurring fair value measurements of nonfinancial assets and nonfinancial liabilities until fiscal years beginning after November 15, 2008. We adopted this portion of the statement on February 1, 2009, and the adoption did not have a material impact on our consolidated financial statements.

In April 2009, the FASB issued FSP No. FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments ("FSP FAS 107-1 and APB 28-1"). This FSP amends SFAS No. 107, Disclosures about Fair Value of Financial Instruments, to require disclosures about fair value of financial instruments in interim as well as in annual financial statements. This FSP also amends Accounting Principles Board ("APB") Opinion No. 28, Interim Financial Reporting, to require those disclosures in all interim financial statements. FSP FAS 107-1 and APB 28-1 will be effective for interim and annual periods ending after June 15, 2009. We expect that the adoption of FSP FAS 107-1 and APB 28-1 will not have a material impact on our consolidated financial statements.

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Note 10. Revolving Credit Agreement

At May 2, 2009, the Company maintained a $1.2 billion revolving credit facility (“credit agreement”) with JPMorgan Chase Bank (“JPMorgan”) as the lead agent for various banks, secured by the inventory of Dillard’s, Inc. operating subsidiaries. The credit agreement expires December 12, 2012. Borrowings under the credit agreement accrue interest starting at either JPMorgan’s Base Rate minus 0.5% or LIBOR plus 1.0% subject to certain availability thresholds as defined in the credit agreement. Due to lower average availability (which is analyzed each calendar quarter), effective April 1, 2009, interest on borrowings under the credit agreement began accruing interest at either JPMorgan’s Base Rate minus 0.25% or LIBOR plus 1.25% (1.66% at May 2, 2009).

Limited to 85% of the inventory of certain Company subsidiaries, availability for borrowings and letter of credit obligations under the credit agreement was $1,023.1 million at May 2, 2009. Borrowings of $175.0 million were outstanding and letters of credit totaling $91.3 million were issued under this credit agreement leaving unutilized availability under the facility of approximately $757 million at May 2, 2009. There are no financial covenant requirements under the credit agreement provided availability exceeds $100 million. The Company pays an annual commitment fee to the banks of 0.25% of the committed amount less outstanding borrowings and letters of credit.

Note 11. Share Repurchase Program

The Company was authorized by its board of directors in November 2007 to repurchase up to $200 million of its Class A Common Stock under an open-ended plan (“Plan”). No shares were repurchased under the Plan during the quarters ended May 2, 2009 and May 3, 2008. Share repurchase authorization remaining under the Plan at May 2, 2009 was $182.6 million.

Note 12. Income Taxes

FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (“FIN 48”) clarifies the accounting for uncertainty in income tax recognized in an entity’s financial statements in accordance with SFAS No. 109. The total amount of unrecognized tax benefits as of May 2, 2009 and May 3, 2008 was $27.3 million and $25.4 million, respectively, of which $19.6 million and $17.0 million, respectively would, if recognized, affect the effective tax rate. The total amount of accrued interest and penalties as of May 2, 2009 and May 3, 2008 was $9.7 million and $9.1 million, respectively. The Company classifies accrued interest and penalties relating to income tax in the financial statements as income tax expense.

During fiscal 2008, the IRS completed its examination of the Company’s federal income tax returns for the fiscal tax years 2003 through 2005. Certain issues relating to this examination are currently under appeal. The Company is also under examination by various state and local taxing jurisdictions for various fiscal years. The tax years that remain subject to examination for major tax jurisdictions are fiscal tax years 2003 and forward, with the exception of fiscal 1997 through 2002 amended state and local tax returns related to the reporting of federal audit adjustments. At this time, the Company does not expect the results from any income tax audit to have a material impact on the Company’s financial statements.

The Company has taken positions in certain taxing jurisdictions for which it is reasonably possible that the total amounts of unrecognized tax benefits may decrease within the next twelve months. The possible decrease could result from the finalization of the Company’s federal and various state income tax audits. The Company’s federal income tax audit uncertainties primarily relate to research and development credits, while various state income tax audit uncertainties primarily relate to income from intangibles. The estimated range of the reasonably possible uncertain tax benefit decrease in the next twelve months is between $1 million and $4 million. Changes in the Company’s assumptions and judgments can materially affect amounts recognized in the consolidated balance sheets and statements of operations.

The Company's estimated federal and state income tax rate, inclusive of equity in (losses) earnings of joint ventures, was approximately 37.8% for the three months ended May 2, 2009 and 37.4% for the three months ended May 3, 2008. During the three months ended May 2, 2009, the Company recorded an income tax expense relating to a net increase in FIN 48 liabilities and other tax reserves of approximately $0.4 million and recognized tax benefits of approximately $0.3 million due to federal tax credits. During the three months ended May 3, 2008, the Company recorded an income tax expense relating to a net increase in FIN 48 liabilities and other tax reserves of approximately $0.2 million and recognized tax benefits of approximately $0.2 million due to federal tax credits.

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Note 13. Note Repurchase

During the quarter ended May 2, 2009, the Company repurchased $5.0 million face amount of 9.125% notes with an original maturity on August 1, 2011. This repurchase resulted in a pretax gain of approximately $1.5 million and was recorded in net interest and debt expense.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

EXECUTIVE OVERVIEW

The sustained economic decline throughout the first quarter of fiscal 2009 continued to have a significant impact on Dillard's, Inc.'s (the "Company", "we", "us" or "our") operations. Net sales from retail operations were $1,414.7 milli during the quarter ended May 2, 2009, a decrease of $260.9 million or 16% from the quarter ended May 3, 2008. The continued slowdown in consumer spending had a negative impact on net sales. Despite the significant decrease in sales, gross profit from retail operations increased 150 basis points of sales, primarily due to our inventory management efforts as evidenced by lower inventory levels (down 17% in comparable stores), decreased purchases and decreased markdown activity. Our extensive cost reduction measures that began in fiscal 2008 reduced advertising, selling, administrative and general expenses for the first quarter of 2009 by $66.6 million compared to the first quarter of fiscal 2008. We also repurchased $5.0 million face amount of debt prior to its maturity, resulting in a pretax gain of $1.5 million. The Company recorded net income for the first quarter of 2009 of $7.7 million, or $0.10 per share, compared to net income of $2.7 million or $0.04 per share for the first quarter of 2008.

As of May 2, 2009, we had working capital of $824 million, cash and cash equivalents of $102.7 million and $1,152.8 million of total debt outstanding. Cash flows from operating activities were $42.4 million for the first quarter of fiscal 2009. We operated 315 total stores as of May 2, 2009, a decrease of 4.8% from the same period last year as a result of the store closures that occurred during fiscal 2008. At May 2, 2009, we had unutilized availability of approximately $757 million under our $1.2 billion revolving credit facility that expires December 12, 2012.

Key Performance Indicators

We use a number of key indicators of financial condition and operating performance to evaluate our business, including the following:

	Three Months Ended	
	May 2, 2009*	May 3, 2008
Net sales (in millions)	$ 1,414.7	$ 1,675.6
Sales per square foot	$ 26	