CATO CORP
Form 10-Q
June 10, 2009

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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 1-31340

THE CATO CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	56-0484485
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

8100 Denmark Road, Charlotte, North Carolina 28273-5975

(Address of principal executive offices)
(Zip Code)
(704) 554-8510

(Registrant s telephone number, including area code)
Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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.
Yes x No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes o No o

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 definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨	Accelerated filer þ	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 o No x

As of May 19, 2009, there were 27,783,568 shares of Class A common stock and 1,743,525 shares of Class B common stock outstanding.

THE CATO CORPORATION
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EX-32.2

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PART I FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

THE CATO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

	Three Months Ended	
	May 2, 2009 (Unaudited)	May 3, 2008 (Unaudited)
	(Dollars in thousands, except per share data)	
REVENUES		
Retail sales	**$ 238,055**	$ 225,791
Other income (principally finance charges, late fees and layaway charges)	**2,972**	3,037
Total revenues	**241,027**	228,828
COSTS AND EXPENSES, NET		
Cost of goods sold (exclusive of depreciation shown below)	**141,913**	141,620
Selling, general and administrative (exclusive of depreciation shown below)	**64,644**	56,317
Depreciation	**5,544**	5,610
Interest and other income	**(1,060)**	(1,901)
	211,041	201,646
Income before income taxes	**29,986**	27,182
Income tax expense	**11,173**	10,329
Net income	**$ 18,813**	$ 16,853
Basic earnings per share	**$ 0.64**	$ 0.57
Diluted earnings per share	**$ 0.64**	$ 0.57
Dividends per share	**$ .165**	$ .165
Comprehensive income:		
Net income	**$ 18,813**	$ 16,853
	(26)	(236)

Unrealized (losses) on available-for-sale securities, net of deferred income tax benefit				
Net comprehensive income	**$**	**18,787**	$	16,617

See notes to condensed consolidated financial statements.

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THE CATO CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

	May 2, 2009 (Unaudited)	May 3, 2008 (Unaudited)	January 31, 2009
		(Dollars in thousands)	
ASSETS			
Current Assets:			
Cash and cash equivalents	**$ 42,006**	$ 42,091	$ 42,262
Short-term investments	**115,696**	76,101	93,452
Restricted cash	**9,016**	9,037	9,089
Accounts receivable, net of allowance for doubtful accounts of $3,328, $3,192 and $3,723 at May 2, 2009, May 3, 2008, and January 31, 2009, respectively	**42,518**	45,570	44,136
Merchandise inventories	**114,339**	113,227	112,290
Deferred income taxes	**6,406**	6,837	6,403
Prepaid expenses	**7,530**	7,659	7,737
Total Current Assets	**337,511**	300,522	315,369
Property and equipment net	**114,096**	122,936	116,262
Other assets	**7,228**	4,548	3,722
Total Assets	**$ 458,835**	$ 428,006	$ 435,353
LIABILITIES AND STOCKHOLDERS EQUITY			
Current Liabilities:			
Accounts payable	**$ 95,644**	$ 92,041	$ 102,971
Accrued expenses	**33,901**	29,755	29,946
Accrued bonus and benefits	**8,888**	4,278	6,307
Accrued income taxes	**22,067**	17,900	11,506
Total Current Liabilities	**160,500**	143,974	150,730
Deferred income taxes	**2,528**	1,707	2,528
Other noncurrent liabilities (primarily deferred rent)	**19,325**	22,399	20,282
Commitments and contingencies			--
Stockholders Equity:			
Preferred stock, $100 par value per share, 100,000 shares authorized, none issued			
Class A common stock, $.033 par value per share, 50,000,000 shares authorized; issued 36,443,898 shares, 36,258,360 shares and 36,303,922 shares at May 2, 2009, May 3, 2008 and January 31, 2009, respectively	**1,215**	1,209	1,210
Convertible Class B common stock, $.033 par value per share, 15,000,000 shares authorized; issued 1,743,525 shares at May 2, 2009, May 3, 2008 and January 31, 2009	**58**	58	58

Additional paid-in capital	**62,325**	59,462	61,608
Retained earnings	**368,306**	352,098	354,333
Accumulated other comprehensive income	**387**	473	413
	432,291	413,300	417,622
Less Class A common stock in treasury, at cost (8,660,333 shares, 8,461,615 shares and 8,660,333 shares at May 2, 2009, May 3, 2008 and January 31, 2009, respectively)	**(155,809)**	(153,374)	(155,809)
Total Stockholders Equity	**276,482**	259,926	261,813
Total Liabilities and Stockholders Equity	**$ 458,835**	$ 428,006	$ 435,353

See notes to condensed consolidated financial statements.

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THE CATO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended	
	May 2, 2009 (Unaudited)	May 3, 2008 (Unaudited)
	(Dollars in thousands)	
OPERATING ACTIVITIES		
Net income	**$ 18,813**	$ 16,853
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	**5,544**	5,610
Provision for doubtful accounts	**924**	767
Share-based compensation	**426**	515
Excess tax benefits from share-based compensation	**(26)**	(13)
Loss on disposal of property and equipment	**149**	290
Changes in operating assets and liabilities which provided (used) cash:		
Accounts receivable	**694**	(1,055)
Merchandise inventories	**(2,049)**	5,452
Prepaid and other assets	**(3,299)**	100
Accrued income taxes	**10,587**	9,985
Accounts payable, accrued expenses and other liabilities	**(1,740)**	(15,213)
Net cash provided by operating activities	**30,023**	23,291
INVESTING ACTIVITIES		
Expenditures for property and equipment	**(3,533)**	(5,647)
Purchases of short-term investments	**(36,590)**	(45,536)
Sales of short-term investments	**14,316**	53,075
Change in restricted cash	**73**	
Net cash provided by (used in) investing activities	**(25,734)**	1,892
FINANCING ACTIVITIES		
Change in cash overdrafts included in accounts payable		(100)
Dividends paid	**(4,849)**	(4,849)
Proceeds from employee stock purchase plan	**178**	213
Excess tax benefits from share-based compensation	**26**	13
Proceeds from stock options exercised	**100**	48
Net cash used in financing activities	**(4,545)**	(4,675)
Net increase (decrease) in cash and cash equivalents	**(256)**	20,508
Cash and cash equivalents at beginning of period	**42,262**	21,583

Cash and cash equivalents at end of period	**$ 42,006**	$ 42,091

See notes to condensed consolidated financial statements.

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THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 2, 2009 AND MAY 3, 2008

NOTE 1 GENERAL:

The condensed consolidated financial statements have been prepared from the accounting records of The Cato Corporation and its wholly-owned subsidiaries (the Company), and all amounts shown as of and for the periods ended May 2, 2009 and May 3, 2008 are unaudited. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All such adjustments are of a normal, recurring nature unless otherwise noted. The results of the interim period may not be indicative of the results expected for the entire year.

The interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto, included in the Company s Annual Report on Form 10-K for the fiscal year ended January 31, 2009.

The year-end condensed consolidated balance sheet data presented for fiscal year ended January 31, 2009 was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

Cash equivalents consist of highly liquid investments with original maturities of three months or less. Investments with original maturities beyond three months are classified as short-term investments. The fair values of short-term investments are based on quoted market prices.

Short-term investments are classified as available-for-sale. As they are available for current operations, they are classified in the Condensed Consolidated Balance Sheets as current assets. Available-for-sale securities are carried at fair value, with unrealized gains and temporary losses, net of income taxes, reported as a component of accumulated other comprehensive income. Other than temporary declines in fair value of investments are recorded as a reduction in the cost of the investments in the accompanying Condensed Consolidated Balance Sheets and a reduction of interest and other income in the accompanying Condensed Consolidated Statements of Income and Comprehensive Income. The cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. The amortization of premiums, accretion of discounts and realized gains and losses are included in Interest and other income.

Merchandise inventories are stated at the lower of cost (first-in, first-out method) or market as determined by the retail inventory method.

On May 20, 2009, the Board of Directors maintained the quarterly dividend at $.165 per share or an annualized rate of $.66 per share.

Prior year basic and diluted weighted shares and earnings per share have been adjusted based on FASB issued FSP No. EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions are Participating Securities*. The impact to diluted and basic earnings per share for the prior year quarter due to the adoption of this FSP was $0.01.

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 2, 2009 AND MAY 3, 2008

NOTE 2 EARNINGS PER SHARE:

FASB No. 128, *Earnings Per Share,* requires dual presentation of basic EPS and diluted EPS on the face of all income statements for all entities with complex capital structures. The Company has presented one basic EPS and one diluted EPS amount for all common shares in the accompanying Condensed Consolidated Statement of Income. While the Company s articles of incorporation provide the right for the Board of Directors to declare dividends on Class A shares without declaration of commensurate dividends on Class B shares, the Company has historically paid the same dividends to both Class A and Class B shareholders and the Board of Directors has resolved to continue this practice. Accordingly, the Company s allocation of income for purposes of EPS computation is the same for Class A and Class B shares and the EPS amounts reported herein are applicable to both Class A and Class B shares.

Basic EPS is computed as net income less earnings allocated to non-vested equity awards divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock options and the Employee Stock Purchase Plan.

	Three Months Ended	
	May 2, 2009	May 3, 2008
	(Dollars in thousands, except per share data)	
Basic earnings per share:		
Net earnings	**$ 18,813**	$ 16,853
Earnings allocated to non-vested equity awards	**(271)**	(168)
Net earnings available to common stockholders	**$ 18,542**	$ 16,685
Basic weighted-average common shares outstanding	**28,954,367**	29,095,913
Basic earnings per share	**$ 0.64**	$ 0.57
Diluted earnings per share:		
Net earnings	**$ 18,813**	$ 16,853
Earnings allocated to non-vested equity awards	**(271)**	(168)
Net earnings available to common stockholders	**$ 18,542**	$ 16,685
Basic weighted-average common shares outstanding	**28,954,367**	29,095,913
Dilutive effect of stock options	**17,085**	17,310
Diluted weighted avg. shares outstanding	**28,971,452**	29,113,223
Diluted earnings per share	**$ 0.64**	**$ 0.57**

NOTE 3 SUPPLEMENTAL CASH FLOW INFORMATION:

Income tax payments, net of refunds received, for the three months ended May 2, 2009 and May 3, 2008 were $136,000 and $339,000, respectively.

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THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 2, 2009 AND MAY 3, 2008

NOTE 4 FINANCING ARRANGEMENTS:

As of May 2, 2009, the Company had an unsecured revolving credit agreement of $35 million. Net of the Company s standby letter of credit for payments to the current general liability and worker s compensation insurance processor, the revolving credit agreement provided for borrowings of up to $34.3 million. The revolving credit agreement is committed until August 2010. The credit agreement contains various financial covenants and limitations, including the maintenance of specific financial ratios with which the Company was in compliance as of May 2, 2009. There were no borrowings outstanding under this credit facility during the first three months ended May 2, 2009 or May 3, 2008, or the fiscal year ended January 31, 2009. Interest on any borrowings is based on LIBOR which was 0.41% at May 2, 2009.

At May 2, 2009 and May 3, 2008, the Company had approximately $4,045,000 and $4,968,000, respectively, of outstanding irrevocable letters of credit relating to purchase commitments.

NOTE 5 REPORTABLE SEGMENT INFORMATION:

The Company has two reportable segments: retail and credit. The Company operated its women s fashion specialty retail stores in 31 states at May 2, 2009, principally in the southeastern United States. The Company offers its own credit card to its customers and all related credit authorizations, payment processing, and collection efforts are performed by a separate subsidiary of the Company.

The following schedule summarizes certain segment information (in thousands):

Three Months Ended May 2, 2009	Retail	Credit	Total
Revenues	$ 238,608	$ 2,419	$ 241,027
Depreciation	5,544		5,544
Interest and other income	(1,060)		(1,060)
Income before taxes	29,370	616	29,986
Total assets	384,459	74,376	458,835
Capital expenditures	3,533		3,533

Three Months Ended May 3, 2008	Retail	Credit	Total
Revenues	$ 226,310	$ 2,518	$ 228,828
Depreciation	5,600	10	5,610
Interest and other income	(1,901)		(1,901)
Income before taxes	26,319	863	27,182
Total assets	357,696	70,310	428,006
Capital expenditures	5,647		5,647

The Company evaluates performance based on income before taxes. The Company does not allocate certain corporate expenses or income taxes to the credit segment.

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THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 2, 2009 AND MAY 3, 2008

NOTE 5 REPORTABLE SEGMENT INFORMATION (CONTINUED):

The following schedule summarizes the direct expenses of the credit segment which are reflected in selling, general and administrative expenses (in thousands):

	Three Months Ended	
	May 2, 2009	May 3, 2008
Bad debt expense	**$ 924**	$ 767
Payroll	**249**	253
Postage	**245**	273
Other expenses	**375**	352
Total expenses	**$ 1,793**	$ 1,645

NOTE 6 STOCK BASED COMPENSATION:

As of May 2, 2009, the Company had three long-term compensation plans pursuant to which stock-based compensation was outstanding or could be granted. The Company s 1987 Non-Qualified Stock Option Plan authorized 5,850,000 shares for the granting of options to officers and key employees. The 1999 Incentive Compensation Plan and 2004 Amended and Restated Incentive Compensation Plan authorized 1,500,000 and 1,350,000 shares, respectively, for the granting of various forms of equity-based awards, including restricted stock and stock options to officers and key employees. The 1999 Plan has expired as to the ability to grant new awards.

The following table presents the number of options and shares of restricted stock initially authorized and available for grant under each of the plans:

	1987 Plan	1999 Plan	2004 Plan	Total
Options and/or restricted stock initially authorized	5,850,000	1,500,000	1,350,000	8,700,000
Options and/or restricted stock available for grant:				
January 31, 2009	18,627		868,078	886,705
May 2, 2009	18,627		749,490	768,117

Stock option awards outstanding under the Company s current plans were granted at exercise prices which were equal to the market value of the Company s stock on the date of grant, vest over five years and expire no later than ten years after the grant date.

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NOTE 6 STOCK BASED COMPENSATION (CONTINUED):

The following is a summary of the changes in stock options outstanding during the three months ended May 2, 2009:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (a)
Options outstanding at January 31, 2009	107,950	$ 12.72	4.07 years	$ 124,527
Granted				
Forfeited or expired				
Exercised	9,275			
Outstanding at May 2, 2009	98,675	$ 12.90	3.92 years	$ 346,618
Vested and exercisable at May 2, 2009	87,425	$ 12.61	3.56 years	$ 332,333

(a) The intrinsic value of a stock option is the amount by which the market value of the underlying stock exceeds the exercise price of the option.

No options were granted in fiscal 2008 or the first quarter of fiscal 2009.

As of May 2, 2009, there was approximately $38,876 of total unrecognized compensation cost related to nonvested options, which is expected to be recognized over a remaining weighted-average vesting period of 0.34 years. The total intrinsic value of options exercised during the first quarter ended May 2, 2009 was approximately $72,646.

The Company recognized share-based compensation expense for nonvested options of $40,000 and $23,000 for the first quarter ended May 2, 2009 and May 3, 2008, respectively. These expenses are classified as a component of selling, general and administrative expenses.

SFAS No. 123R requires the benefits of tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. For the three months ended May 2, 2009 and May 3, 2008, the Company reported $26,000 and $13,000 of excess tax benefits as a financing cash inflow in addition to $279,000 and $261,000 in cash proceeds received from the exercise of stock options and Employee Stock Purchase Plan purchases, respectively.

The Company s Employee Stock Purchase Plan allows eligible full-time employees to purchase a limited number of shares of the Company s Class A Common Stock during each semi-annual offering period at a 15% discount through payroll deductions. During the three months ended May 2, 2009 and May 3, 2008, the Company sold 12,113 shares and 16,628 shares to employees at an average discount of $2.60 and $2.13 per share, respectively, under the Employee Stock Purchase Plan. The compensation expense recognized for the 15% discount given under the Employee Stock Purchase Plan was approximately $31,000 and $35,000 for the three months ended May 2, 2009 and May 3, 2008, respectively.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 2, 2009 AND MAY 3, 2008

NOTE 6 STOCK BASED COMPENSATION (CONTINUED):

In accordance with SFAS No. 123R, the fair value of current restricted stock awards is estimated on the date of grant based on the market price of the Company s stock and is amortized to compensation expense on a straight-line basis over the related vesting periods. As of May 2, 2009 and May 3, 2008, there was $4,703,272 and $6,721,625 of total unrecognized compensation cost related to nonvested restricted stock awards, which have a remaining weighted-average vesting period of 2.7 years and 3.7 years, respectively. The total fair value of the shares recognized as compensation expense during the first quarter ended May 2, 2009 and May 3, 2008 was $329,000 and $438,000, respectively.

The following summary shows the changes in the shares of restricted stock outstanding during the three months ended May 2, 2009:

	Number of	Weighted Average Grant Date F