

CATO CORP
Form 10-Q
December 02, 2014

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended November 1, 2014

OR

**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
(State or other jurisdiction of incorporation or organization)

56-0484485
(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)

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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

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 X 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. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a 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 No X

As of November 1, 2014, there were 26,168,286 shares of Class A common stock and 1,743,525 shares of Class B common stock outstanding.

THE CATO CORPORATION

FORM 10-Q

Quarter Ended November 1, 2014

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PART I FINANCIAL INFORMATION**ITEM 1. FINANCIAL STATEMENTS****THE CATO CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND****COMPREHENSIVE INCOME****(UNAUDITED)**

	Three Months Ended		Nine Months Ended	
	November 1, 2014	November 2, 2013	November 1, 2014	November 2, 2013
	(Dollars in thousands, except per share data)			
REVENUES				
Retail sales	\$ 213,785	\$ 198,786	\$ 740,023	\$ 695,345
Other revenue (principally finance charges, late fees and layaway charges)	2,225	2,257	6,778	7,114
Total revenues	216,010	201,043	746,801	702,459
COSTS AND EXPENSES, NET				
Cost of goods sold (exclusive of depreciation shown below)	136,495	128,787	449,496	430,638
Selling, general and administrative (exclusive of depreciation shown below)	67,623	61,032	203,442	179,386
Depreciation	5,422	5,459	16,297	16,344
Interest and other income	(686)	(723)	(2,527)	(2,328)
Cost and expenses, net	208,854	194,555	666,708	624,040
Income before income taxes	7,156	6,488	80,093	78,419
Income tax expense	1,464	1,603	28,743	27,920
Net income	\$ 5,692	\$ 4,885	\$ 51,350	\$ 50,499

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Basic earnings per share	\$	0.20	\$	0.17	\$	1.82	\$	1.73
Diluted earnings per share	\$	0.20	\$	0.17	\$	1.82	\$	1.73
Dividends per share	\$	0.30	\$	0.05	\$	0.90	\$	0.15
Comprehensive income:								
Net income	\$	5,692	\$	4,885	\$	51,350	\$	50,499
Unrealized gain (loss) on available-for-sale securities, net of deferred income taxes of (\$21) and \$0 for the three and nine months ended November 1, 2014 and \$188 and (\$18) for the three and nine months ended November 2, 2013, respectively		(35)		312		1		(30)
Comprehensive income	\$	5,657	\$	5,197	\$	51,351	\$	50,469

See notes to condensed consolidated financial statements (unaudited).

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THE CATO CORPORATION**CONDENSED CONSOLIDATED BALANCE SHEETS****(UNAUDITED)**

	November 1, 2014	February 1, 2014	November 2, 2013
ASSETS	(Dollars in thousands)		
Current Assets:			
Cash and cash equivalents	\$ 83,749	\$ 79,427	\$ 74,055
Short-term investments	157,548	161,128	159,223
Restricted cash and investments	4,686	4,701	4,706
Accounts receivable, net of allowance for doubtful accounts of \$1,741, \$1,743 and \$2,043 at November 1, 2014, February 1, 2014 and November 2, 2013, respectively	40,555	39,224	41,156
Merchandise inventories	127,786	150,861	131,016
Deferred income taxes	4,720	4,720	4,649
Prepaid expenses	6,165	6,687	6,393
Total Current Assets	425,209	446,748	421,198
Property and equipment – net	145,962	141,129	142,991
Noncurrent deferred income taxes	1,375	1,373	-
Other assets	9,943	7,668	7,938
Total Assets	\$ 582,489	\$ 596,918	\$ 572,127
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current Liabilities:			
Accounts payable	\$ 94,135	\$ 111,514	\$ 89,468
Accrued expenses	45,300	45,763	44,534
Accrued bonus and benefits	14,541	4,999	2,598
Accrued income taxes	17,844	14,855	15,593
Total Current Liabilities	171,820	177,131	152,193
Deferred income taxes	-	-	3,330
Other noncurrent liabilities (primarily deferred rent)	32,994	28,678	28,335
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 26,168,286 shares, 27,498,216 shares and 27,515,706 shares at November 1, 2014, February 1, 2014 and November 2, 2013, respectively	872	917	917
Convertible Class B common stock, \$.033 par value per share, 15,000,000 shares authorized; issued 1,743,525 shares at November 1, 2014, February 1, 2014 and November 2, 2013, respectively	58	58	58
Additional paid-in capital	83,779	80,463	79,325
Retained earnings	292,187	308,893	307,178
Accumulated other comprehensive income	779	778	791
Total Stockholders' Equity	377,675	391,109	388,269
Total Liabilities and Stockholders' Equity	\$ 582,489	\$ 596,918	\$ 572,127

See notes to condensed consolidated financial statements (unaudited).

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THE CATO CORPORATION**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(UNAUDITED)**

	Nine Months Ended	
	November 1, 2014	November 2, 2013
	(Dollars in thousands)	
Operating Activities:		
Net income	\$ 51,350	\$ 50,499
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	16,297	16,344
Provision for doubtful accounts	805	975
Amortization (purchase) of investment premiums	258	(1,338)
Share-based compensation	2,678	2,264
Excess tax benefits from share-based compensation	(181)	(38)
Loss on disposal and write-offs of property and equipment	618	1,532
Changes in operating assets and liabilities which provided (used) cash:		
Accounts receivable	(2,136)	(2,115)
Merchandise inventories	23,075	9,722
Prepaid and other assets	(1,696)	3,181
Accrued income taxes	3,170	1,339
Accounts payable, accrued expenses and other liabilities	(4,358)	(6,706)
Net cash provided by operating activities	89,880	75,659
Investing Activities:		
Expenditures for property and equipment	(21,380)	(23,781)
Purchase of short-term investments	(33,050)	(52,358)
Sales of short-term investments	36,320	51,871
Change in restricted cash and investments	15	1,293
Net cash used in investing activities	(18,095)	(22,975)
Financing Activities:		
Dividends paid	(25,508)	(4,390)
Repurchase of common stock	(42,615)	(5,783)
Proceeds from employee stock purchase plan	468	387
Excess tax benefits from share-based compensation	181	38
Proceeds from stock options exercised	11	50
Net cash used in financing activities	(67,463)	(9,698)
Net increase in cash and cash equivalents	4,322	42,986

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Cash and cash equivalents at beginning of period		79,427		31,069
Cash and cash equivalents at end of period	\$	83,749	\$	74,055
Non-cash investing activity:				
Accrued plant and equipment	\$	(3,681)	\$	(5,678)

See notes to condensed consolidated financial statements (unaudited).

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**THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS AND NINE MONTHS ENDED NOVEMBER 1, 2014 AND NOVEMBER 2,
2013**

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 three and nine month periods ended November 1, 2014 and November 2, 2013 are unaudited. In the opinion of management, all adjustments considered necessary for a fair statement 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/A for the fiscal year ended February 1, 2014. Amounts as of February 1, 2014 have been derived from the audited balance sheet, but do not include all disclosures required by accounting principles generally accepted in the United States of America.

During the fourth quarter of 2013, the Company discovered that it had improperly netted purchases and sales activity for investments within cash flows related to investing activities in prior periods. In addition, the Company had also improperly classified the premiums and amortization of premiums on those investments in cash flows related to investing activities when it should have been in cash flows related to operating activities. The Condensed Consolidated Statement of Cash Flows for the nine months ended November 2, 2013 has been revised to correct the presentation of the amounts, which resulted in a decrease to Net cash provided by operating activities and a corresponding decrease to Net cash provided (used) in investing activities of \$1.3 million dollars. The revision is not deemed material to the prior period consolidated financial statements.

The decrease in Stockholders’ Equity for the first nine months ended November 1, 2014 compared to the fiscal year ended February 1, 2014 is primarily due to a stock repurchase of \$42.6 million and dividends paid of \$25.5 million, partially offset by net income of \$51.4 million.

On November 25, 2014, the Board of Directors maintained the quarterly dividend at \$0.30 per share.

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NOTE 2 - EARNINGS PER SHARE:

Accounting Standard Codification (“ASC”) 260 – *Earnings Per Share* requires dual presentation of basic and diluted Earnings Per Share (“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 Statements of Income and Comprehensive Income. While the Company’s certificate of incorporation provides 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 the 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		Nine Months Ended	
	November	November	November	November
	1, 2014	2, 2013	1, 2014	2, 2013
	(Dollars in thousands)			
Numerator				
Net earnings	\$ 5,692	\$ 4,885	\$ 51,350	\$ 50,499
Earnings allocated to non-vested equity awards	(113)	(81)	(1,001)	(818)
Net earnings available to common stockholders	\$ 5,579	\$ 4,804	\$ 50,349	\$ 49,681
Denominator				
Basic weighted average common shares outstanding	27,359,660	28,746,459	27,673,293	28,772,006
Dilutive effect of stock options	4,493	7,860	2,640	5,309
Diluted weighted average common shares outstanding	27,364,153	28,754,319	27,675,933	28,777,315
Net income per common share				

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Basic earnings per share (Class A and B Shares)	\$	0.20	\$	0.17	\$	1.82	\$	1.73
Diluted earnings per share (Class A and B Shares)	\$	0.20	\$	0.17	\$	1.82	\$	1.73

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2013

NOTE 3 – ACCUMULATED OTHER COMPREHENSIVE INCOME:

The following table sets forth information regarding the reclassification out of Accumulated other comprehensive income (in thousands) for the three months ended November 1, 2014:

		Changes in Accumulated Other Comprehensive Income (a) Unrealized Gains and (Losses) on Available-for-Sale Securities
Beginning Balance at August 2, 2014	\$	814
Other comprehensive income before reclassifications		(40)
Amounts reclassified from accumulated other comprehensive income (b)		5
Net current-period other comprehensive income		(35)
Ending Balance at November 1, 2014	\$	779

(a) All amounts are net-of-tax. Amounts in parentheses indicate a debit/reduction to Other Comprehensive Income.

(b) Includes \$8 impact of Accumulated other comprehensive income reclassifications into Interest and other

income for net gains on available-for-sale securities. The tax impact of this reclassification was \$3.

The following table sets forth information regarding the reclassification out of Accumulated other comprehensive income (in thousands) for the nine months ended November 1, 2014:

**Changes in Accumulated Other
Comprehensive Income (a)
Unrealized Gains
and (Losses) on**

		Available-for-Sale Securities
Beginning Balance at February 1, 2014	\$	778
Other comprehensive income before reclassifications		141
Amounts reclassified from accumulated other comprehensive income (b)		(140)
Net current-period other comprehensive income		1
Ending Balance at November 1, 2014	\$	779

(a) All amounts are net-of-tax. Amounts in parentheses indicate a debit/reduction to Other Comprehensive Income.

(b) Includes \$224 impact of Accumulated other comprehensive income reclassifications into Interest and other

income for net gains on available-for-sale securities. The tax impact of this reclassification was \$84.

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FOR THE THREE MONTHS AND NINE MONTHS ENDED NOVEMBER 1, 2014 AND NOVEMBER 2, 2013

NOTE 3 – ACCUMULATED OTHER COMPREHENSIVE INCOME (CONTINUED):

The following table sets forth information regarding the reclassification out of Accumulated other comprehensive income (in thousands) for the three months ended November 2, 2013:

	Changes in Accumulated Other Comprehensive Income (a) Unrealized Gains and (Losses) on Available-for-Sale Securities	
Beginning Balance at August 3, 2013	\$	479
Other comprehensive income before reclassifications		294
Amounts reclassified from accumulated other comprehensive income (b)		18
Net current-period other comprehensive income		312
Ending Balance at November 2, 2013	\$	791

(a) All amounts are net-of-tax. Amounts in parentheses indicate a debit/reduction to Other Comprehensive Income.

(b) Includes \$29 impact of Accumulated other comprehensive income reclassifications into Interest and other

income for net gains on available-for-sale securities. The tax impact of this reclassification was \$11.

The following table sets forth information regarding the reclassification out of Accumulated other comprehensive income (in thousands) for the nine months ended November 2, 2013:

**Changes in Accumulated Other
Comprehensive Income (a)**

**Unrealized Gains
and (Losses) on
Available-for-Sale
Securities**

Beginning Balance at February 2, 2013	\$	821
Other comprehensive income before reclassifications		11
Amounts reclassified from accumulated other comprehensive income (b)		(41)
Net current-period other comprehensive income		(30)
Ending Balance at November 2, 2013	\$	791

(a) All amounts are net-of-tax. Amounts in parentheses indicate a debit/reduction to Other Comprehensive Income.

(b) Includes \$47 impact of Accumulated other comprehensive income reclassifications into Interest and other

income for net gains on available-for-sale securities. The tax impact of this reclassification was \$25.

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2013

NOTE 4 – FINANCING ARRANGEMENTS:

As of November 1, 2014, the Company had an unsecured revolving credit agreement to borrow \$35.0 million, less the value of revocable letters of credit discussed below. During 2013, the revolving credit agreement was amended and extended to August 2015. 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 November 1, 2014. There were no borrowings outstanding under this credit facility during the periods ended November 1, 2014, February 1, 2014 or November 2, 2013. The weighted average interest rate under the credit facility was zero at November 1, 2014 due to no borrowings during the year.

At November 1, 2014, February 1, 2014 and November 2, 2013, the Company had approximately \$0.4 million, \$0.4 million and \$0.6 million, respectively, of outstanding revocable letters of credit related to purchase commitments.

NOTE 5 – REPORTABLE SEGMENT INFORMATION:

The Company has determined that it has four operating segments, as defined under ASC 280-10, including Cato, It's Fashion, Versona and Credit. As outlined in ASC 280-10, the Company has two reportable segments: Retail and Credit. The Company has aggregated its retail operating segments based on the aggregation criteria outlined in ASC 280-10, which states that two or more operating segments may be aggregated into a single reportable segment if aggregation is consistent with the objective and basic principles of ASC 280-10, if the segments have similar economic characteristics, similar product, similar production processes, similar clients and similar methods of distribution.

The Company's retail operating segments have similar economic characteristics and similar operating, financial and competitive risks. They are similar in nature of product, as they all offer women's apparel, shoes and accessories. Merchandise inventory of the Company's operating segments is sourced from the same countries and some of the same vendors, using similar production processes. Customers of the Company's operating segments have similar characteristics. Merchandise for the Company's operating segments is distributed to retail stores in a similar manner through the Company's single distribution center and is subsequently distributed to customers in a similar manner, through its retail stores.

The Company operates its women's fashion specialty retail stores in 32 states as of November 1, 2014, principally in the southeastern United States. The Company offers its own credit card to its customers and all credit authorizations, payment processing and collection efforts are performed by a separate subsidiary of the Company.

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NOTE 5 – REPORTABLE SEGMENT INFORMATION (CONTINUED):

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

Three Months Ended				Nine Months Ended			
November 1, 2014	Retail	Credit	Total	November 1, 2014	Retail	Credit	Total
Revenues	\$ 214,569	\$ 1,441	\$ 216,010	Revenues	\$ 742,448	\$ 4,353	\$ 746,801
Depreciation	5,412	10	5,422	Depreciation	16,262	35	16,297
Interest and other income	(686)	-	(686)	Interest and other income	(2,527)	-	(2,527)
Income before taxes	6,630	526	7,156	Income before taxes	78,509	1,584	80,093
Total assets	514,727	67,762	582,489	Total assets	514,727	67,762	582,489
Capital expenditures	7,414	-	7,414	Capital expenditures	21,380	-	21,380
Three Months Ended				Nine Months Ended			
November 2, 2013	Retail	Credit	Total	November 2, 2013	Retail	Credit	Total
Revenues	\$ 199,540	\$ 1,503	\$ 201,043	Revenues	\$ 697,782	\$ 4,677	\$ 702,459
Depreciation	5,451	8	5,459	Depreciation	16,314	30	16,344
Interest and other income	(723)	-	(723)	Interest and other income	(2,328)	-	(2,328)
Income before taxes	5,948	540	6,488	Income before taxes	76,756	1,663	78,419
Total assets	505,595	66,532	572,127	Total assets	505,595	66,532	572,127
Capital expenditures	13,087	88	13,175	Capital expenditures	23,693	88	23,781

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

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**Nine Months Ended**