NEIMAN MARCUS GROUP INC
Form 10-Q
June 09, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended April 30, 2005

OR

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

Commission file no. 1-9659

The Neiman Marcus Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**95-4119509**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One Marcus Square

1618 Main Street

Dallas, Texas 75201

(Address of principal executive offices)

(214) 741-6911
(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.

YES ý NO o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

YES ý NO o

As of June 3, 2005, the number of outstanding shares of each of the issuer s classes of common stock was:

Class	**Outstanding Shares**
Class A Common Stock, $.01 Par Value	29,525,199
Class B Common Stock, $.01 Par Value	19,422,379

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CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(in thousands)	April 30, 2005	July 31, 2004 (As Restated, See Note 9)	May 1, 2004
ASSETS			
Current assets:			
Cash and cash equivalents	$ 337,589	$ 368,367	$ 311,985
Restricted cash	37,500		
Accounts receivable, net of allowance of $11,956, $10,078 and $11,104	666,455	551,687	599,581
Merchandise inventories	788,915	720,277	715,539
Other current assets	49,715	65,835	46,372
Total current assets	1,880,174	1,706,166	1,673,477
Property and equipment, net	821,810	750,483	743,852
Other assets	137,822	160,999	119,442
Total assets	$ 2,839,806	$ 2,617,648	$ 2,536,771
LIABILITIES AND SHAREHOLDERS EQUITY			
Current liabilities:			
Accounts payable	$ 246,971	$ 289,282	$ 234,264
Accrued liabilities	352,526	286,833	316,305
Notes payable and current maturities of long-term liabilities	200	1,563	1,237
Current portion of borrowings under Credit Card Facility	187,500	150,000	37,500
Total current liabilities	787,197	727,678	589,306
Long-term liabilities:			
Notes and debentures	249,773	249,757	249,751
Borrowings under Credit Card Facility		75,000	187,500
Deferred real estate credits	74,429	71,898	73,208
Other long-term liabilities	133,114	112,455	97,307
Total long-term liabilities	457,316	509,110	607,766
Minority interest	13,498	10,298	12,799
Common stocks	497	492	493
Additional paid-in capital	511,338	491,849	484,151
Accumulated other comprehensive loss	(3,432)	(4,536)	(26,752)
Retained earnings	1,099,053	905,330	891,054
Treasury stock, at cost (768,731 shares, 710,227 shares and 699,777 shares)	(25,661)	(22,573)	(22,046)
Total shareholders equity	1,581,795	1,370,562	1,326,900
Total liabilities and shareholders equity	$ 2,839,806	$ 2,617,648	$ 2,536,771

See Notes to Condensed Consolidated Financial Statements.

THE NEIMAN MARCUS GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(UNAUDITED)

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
(in thousands, except per share data)	**April 30, 2005**	**May 1, 2004**	**April 30, 2005**	**May 1, 2004**
Revenues	$ 933,372	$ 873,167	$ 2,970,533	$ 2,740,303
Cost of goods sold including buying and occupancy costs	576,204	544,663	1,892,904	1,773,999
Selling, general and administrative expenses	222,516	208,909	698,054	659,420
Loss on disposition of Chef s Catalog			15,348	
Operating earnings	134,652	119,595	364,227	306,884
Interest expense, net	2,933	4,589	10,948	11,814
Earnings before income taxes and minority interest	131,719	115,006	353,279	295,070
Income taxes	50,713	44,852	136,014	107,576
Earnings before minority interest	81,006	70,154	217,265	187,494
Minority interest in net earnings of subsidiaries	(1,231)	(1,305)	(2,787)	(3,249)
Net earnings	$ 79,775	$ 68,849	$ 214,478	$ 184,245
Weighted average number of common and common equivalent shares outstanding:				
Basic	48,390	48,208	48,309	47,929
Diluted	49,695	49,124	49,427	48,806
Earnings per share:				
Basic	$ 1.65	$ 1.43	$ 4.44	$ 3.84
Diluted	$ 1.61	$ 1.40	$ 4.34	$ 3.78

See Notes to Condensed Consolidated Financial Statements.

THE NEIMAN MARCUS GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(in thousands)	Thirty-Nine Weeks Ended April 30, 2005	May 1, 2004 (As Restated, See Note 9)
CASH FLOWS - OPERATING ACTIVITIES		
Net earnings	$ 214,478	$ 184,245
Adjustments to reconcile net earnings to net cash provided by (used for) operating activities:		
Depreciation	79,338	73,093
Loss on disposition of Chef s Catalog	15,348	
Minority interest	2,787	3,249
Other primarily costs related to defined benefit pension and other long-term benefit plans	27,222	24,367
	339,173	284,954
Changes in operating assets and liabilities:		
Decrease in undivided interests		242,565
Increase in accounts receivable	(114,270)	(576,986)
Increase in merchandise inventories	(78,955)	(28,477)
Decrease in other current assets	10,530	27,803
Decrease (increase) in other assets	12,276	(4,550)
Increase in accounts payable and accrued liabilities	38,763	35,347
Increase in deferred real estate credits	2,531	2,866
Funding of defined benefit pension plan	(20,000)	(30,000)
Net cash provided by (used for) operating activities	190,048	(46,478)
CASH FLOWS - INVESTING ACTIVITIES		
Capital expenditures	(150,830)	(83,152)
Increase in cash restricted for repayment of borrowings under Credit Card Facility	(37,500)	
Proceeds from sale of Chef s Catalog	14,419	
Net cash used for investing activities	(173,911)	(83,152)
CASH FLOWS - FINANCING ACTIVITIES		
Proceeds from borrowings	7,750	2,000
Repayment of debt	(9,113)	(1,500)
Borrowings under Credit Card Facility		225,000
Repayment of borrowings under Credit Card Facility	(37,500)	
Acquisitions of treasury stock	(3,088)	(7,026)
Proceeds from stock-based compensation awards	16,432	23,235
Cash dividends paid	(20,042)	(6,312)
Distributions paid	(1,354)	(732)
Net cash (used for) provided by financing activities	(46,915)	234,665
CASH AND CASH EQUIVALENTS		
(Decrease) increase during the period	(30,778)	105,035
Beginning balance	368,367	206,950
Ending balance	$ 337,589	$ 311,985
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION		
Cash paid during the period for:		
Interest	$ 12,992	$ 9,050

Income taxes	$	98,942	$	70,657

See Notes to Condensed Consolidated Financial Statements.

THE NEIMAN MARCUS GROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. Basis of Presentation

We have prepared the Condensed Consolidated Financial Statements of The Neiman Marcus Group, Inc. and its subsidiaries (Company) in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, these financial statements do not include all of the information and footnotes required by accounting principles generally accepted for complete financial statements. Therefore, these financial statements should be read in conjunction with our amendment to the Annual Report on Form 10-K/A for the fiscal year ended July 31, 2004.

Our fiscal year ends on the Saturday closest to July 31. All references to the third quarter of 2005 relate to the thirteen weeks ended April 30, 2005 and all references to the third quarter of 2004 relate to the thirteen weeks ended May 1, 2004. All references to 2005 relate to the thirty-nine weeks ended April 30, 2005 and all references to 2004 relate to the thirty-nine weeks ended May 1, 2004.

In our opinion, the accompanying unaudited Condensed Consolidated Financial Statements contain all adjustments, consisting of normal recurring adjustments, necessary to present fairly our financial position, results of operations and cash flows for the applicable interim periods. The results of operations for these periods are not necessarily comparable to, or indicative of, results of any other interim period or for the fiscal year as a whole.

We are required to make estimates and assumptions about future events in preparing financial statements in conformity with generally accepted accounting principles. These estimates and assumptions affect the amounts of assets, liabilities, revenues and expenses and the disclosure of gain and loss contingencies at the date of the Condensed Consolidated Financial Statements. While we believe that our past estimates and assumptions have been materially accurate, our current estimates are subject to change if different assumptions as to the outcome of future events were made. We evaluate our estimates and judgments on an ongoing basis and predicate those estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances. We make adjustments to our assumptions and judgments when facts and circumstances dictate. Since future events and their effects cannot be determined with absolute certainty, actual results may differ from the estimates used in preparing the accompanying Condensed Consolidated Financial Statements.

Certain prior period balances have been reclassified to conform to the current period presentation.

We believe the following critical accounting policies, among others, encompass the more significant judgments and estimates used in the preparation of our financial statements:

Revenue recognition;

Valuation of merchandise inventories, including determination of original retail values, recognition of markdowns and vendor allowances, estimation of inventory shrinkage, and determination of cost of goods sold;

Determination of impairment of long-lived assets;

Recognition of income and expenses related to our previous securitization program;

Recognition of advertising and catalog costs;

Measurement of liabilities related to our loyalty programs;

Recognition of income taxes; and

Measurement of accruals for litigation, general liability, workers compensation and health insurance, short-term disability, pension and postretirement health care benefits.

A description of our critical accounting policies is included in our amendment to the Annual Report on Form 10-K/A for the fiscal year ended July 31, 2004.

Stock-Based Compensation. We account for stock-based compensation awards to employees in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Accordingly, we have recognized compensation expense on our restricted stock and purchased restricted stock awards but have not recognized compensation expense for stock options since all options granted had an exercise price equal to the market value of our common stock on the grant date.

The following table illustrates the effect on net earnings and earnings per share as if we had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation using the Black-Scholes option-pricing model for 2005 and 2004:

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
(in thousands, except per share data)	**April 30, 2005**	**May 1, 2004**	**April 30, 2005**	**May 1, 2004**
Net earnings:				
As reported	$ 79,775	$ 68,849	$ 214,478	$ 184,245
Add: stock-based employee compensation recorded under intrinsic value method, net of related taxes	1,343	866	3,646	2,233
Less: stock-based employee compensation expense determined under fair value based method, net of related taxes	(3,434)	(3,076)	(9,846)	(8,644)
Pro forma	$ 77,684	$ 66,639	$ 208,278	$ 177,834
Basic earnings per share:				
As reported	$ 1.65	$ 1.43	$ 4.44	$ 3.84
Pro forma	$ 1.61	$ 1.38	$ 4.31	$ 3.71
Diluted earnings per share:				
As reported	$ 1.61	$ 1.40	$ 4.34	$ 3.78
Pro forma	$ 1.56	$ 1.36	$ 4.21	$ 3.64

The effects on pro forma net earnings and earnings per share of expensing the estimated fair value of stock options are not necessarily representative of the effects on reported net earnings for future periods due to such factors as the vesting periods of stock options and the potential issuance of additional stock options in future years. In addition, the Black-Scholes option-pricing model has inherent limitations in calculating the fair value of stock options for which no active market exists since the model does not consider the inability to sell or transfer options, vesting requirements and a reduced exercise period upon termination of employment - all of which would reduce the fair value of the options.

***Reclassification Loyalty Programs*.** A substantial portion of the points earned by customers in connection with our loyalty programs are redeemed for gift cards. At the time the qualifying sales giving rise to the loyalty program points are made, we defer the portion of the revenues on the qualifying sales transactions equal to our estimate of the retail value of the gift cards to be issued upon conversion of the points to gift cards. Beginning in the first quarter of 2005, we began to record the deferral of revenues related to gift card awards under our loyalty programs as a reduction of revenues. Previously, we charged such amounts to selling, general and administrative expenses (SG&A). In addition, we now charge the cost of all other awards under our loyalty programs to cost of goods sold (COGS) rather than SG&A. These changes in classification do not impact the previously reported operating earnings, net income or earnings per share amounts.

The following table presents quarterly and annual information giving recognition to the changes in classification related to our loyalty programs:

(in thousands)	**Revenues**	**COGS**	**SG&A**
Fiscal Year 2004:			
First quarter	$ 818,769	$ 510,350	$ 211,130
Second quarter	1,048,367	718,985	239,381
Third quarter	873,167	544,663	208,909
Fourth quarter	784,468	553,231	189,033
Total	$ 3,524,771	$ 2,327,229	$ 848,453
Fiscal Year 2003:			
First quarter	$ 727,832	$ 455,307	$ 197,281
Second quarter	934,844	655,459	220,981
Third quarter	718,557	465,160	181,565
Fourth quarter	699,120	502,510	179,981
Total	$ 3,080,353	$ 2,078,436	$ 779,808

Recent Accounting Pronouncements. In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123R, Share-Based Payment. This standard is a revision of SFAS No. 123, Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS No. 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values and is effective for the first interim period or annual reporting period beginning after June 15, 2005. We expect to adopt SFAS No. 123R in the first quarter of our fiscal year 2006. We are in the process of evaluating the impact of the adoption of SFAS No. 123R. The adoption of SFAS No. 123R will reduce reported net income and earnings per share because we will be required to recognize compensation expense for our stock options.

2. Loss on Disposition of Chef s Catalog

In November 2004, we sold our Chef s Catalog direct marketing business to a private equity firm. Chef s Catalog is a multi-channel retailer of professional-quality kitchenware with revenues of approximately $73 million in fiscal year 2004. At October 30, 2004, Chef s Catalog had net tangible assets, primarily inventory, of $12.5 million and net intangible assets of $17.2 million. We received proceeds, net of selling costs, of $14.4 million from the sale. As the carrying value of the Chef s Catalog assets exceeded the net proceeds from the sale, we incurred a pre-tax loss of $15.3 million in the first quarter of 2005 related to the disposition of Chef s Catalog.

3. Operating Segments

We have identified two reportable segments: Specialty Retail Stores and Direct Marketing. Our Specialty Retail Stores segment includes all of our Neiman Marcus and Bergdorf Goodman retail stores, including Neiman Marcus clearance stores. Our Direct Marketing segment conducts both print catalog and online operations under the Neiman Marcus, Horchow and Bergdorf Goodman brand names and, until its disposition in November 2004, the Chef s Catalog brand name. Other includes the operations of Kate Spade LLC and Gurwitch Products, LLC (the Brand Development Companies).

Both the Specialty Retail Stores and Direct Marketing segments, as well as Kate Spade LLC and Gurwitch Products, LLC, derive their revenues from the sales of high-end fashion apparel, accessories, cosmetics and fragrances from leading designers, precious and fashion jewelry and decorative home accessories.

The following table sets forth the information for our reportable segments:

	Thirteen Weeks Ended		**Thirty-Nine Weeks Ended**	
(in thousands)	**April 30, 2005**	**May 1, 2004**	**April 30, 2005**	**May 1, 2004**
REVENUES:				