

HIBBETT SPORTS INC
Form 10-Q
December 08, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended November 1, 2008
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: 000-20969

HIBBETT SPORTS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE 20-8159608
(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)
organization)

451 Industrial Lane, Birmingham, Alabama 35211
(Address of principal executive offices, including zip code)

205-942-4292
(Registrant's telephone number, including area code)

NONE

(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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer,

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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

Accelerated filer

Non-accelerated filer

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

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

Shares of common stock, par value \$.01 per share, outstanding as of December 2, 2008, were 28,528,736 shares.

HIBBETT SPORTS, INC.

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A WARNING ABOUT FORWARD-LOOKING STATEMENTS

This document contains “forward-looking statements” as that term is used in the Private Securities Litigation Reform Act of 1995. Forward-looking statements address future events, developments and results. They include statements preceded by, followed by or including words such as “believe,” “anticipate,” “expect,” “intend,” “plan,” “target” or “estimate.” For example, our forward-looking statements include statements regarding:

- our anticipated sales, including comparable store net sales changes, net sales growth and earnings;
- our growth, including our plans to add, expand or relocate stores and square footage growth, our market’s ability to support such growth and the suitability of our distribution facilities;
 - the possible effect of pending legal actions and other contingencies;
- our cash needs, including our ability to fund our future capital expenditures and working capital requirements;
 - our ability and plans to renew or increase our revolving credit facilities;
 - our seasonal sales patterns and assumptions concerning customer buying behavior;
 - our ability to renew or replace store leases satisfactorily;
- our estimates and assumptions as they relate to preferable tax and financial accounting methods, accruals, inventory valuations, dividends, carrying amount and liquidity of financial instruments and fair value of options and other stock-based compensation as well as our estimates of economic and useful lives of depreciable assets and leases;
 - our expectations concerning future stock-based award types;
 - our expectations concerning employee option exercise behavior;
- the possible effect of inflation, market decline and other economic changes on our costs and profitability, including the impact of changes in fuel costs and a downturn in the retail industry or changes in levels of store traffic;
- the possible effects of the continued volatility and further deterioration of the capital markets, the commercial and consumer credit environment and the continuation of lowered levels of consumer spending resulting from the worldwide economic downturn, lowered levels of consumer confidence and higher levels of unemployment;
 - our analyses of trends as related to earnings performance;
 - our target market presence and its expected impact on our sales growth;
 - our expectations concerning vendor level purchases and related discounts;
- our estimates and assumptions related to income tax liabilities and uncertain tax positions; and
 - the possible effect of recent accounting pronouncements.

For a discussion of the risks, uncertainties and assumptions that could affect our future events, developments or results, you should carefully consider the risk factors described from time to time in our other documents and reports, including the factors described under “Risk Factors,” “Business” and “Properties” in our Form 10-K dated April 2, 2008, our second quarter Form 10-Q dated August 2, 2008 and this Form 10-Q.

Our forward-looking statements could be wrong in light of these and other risks, uncertainties and assumptions. The future events, developments or results described in this report could turn out to be materially different. We have no obligation to publicly update or revise our forward-looking statements after the date of this report and you should not expect us to do so.

Investors should also be aware that while we do, from time to time, communicate with securities analysts and others, we do not, by policy, selectively disclose to them any material non-public information with any statement or report issued by any analyst regardless of the content of the statement or report. We do not, by policy, confirm forecasts or projections issued by others. Thus, to the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are not our responsibility.

You should assume that the information appearing in this report is accurate only as of the date it was issued. Our business, financial condition, results of operations and prospects may have changed since that date.

INVESTOR ACCESS TO COMPANY FILINGS

We make available free of charge on our website, www.hibbett.com under the heading “Investor Information,” copies of our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as well as all Forms 4 and 5 filed by our executive officers and directors, as soon as the filings are made publicly available by the Securities and Exchange Commission on its EDGAR database at www.sec.gov. In addition to accessing copies of our reports online, you may request a copy of our Annual Report on Form 10-K for the fiscal year ended February 2, 2008, at no charge, by writing to: Investor Relations, Hibbett Sports, Inc., 451 Industrial Lane, Birmingham, Alabama 35211.

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements.

HIBBETT SPORTS, INC. AND SUBSIDIARIES
 Unaudited Condensed Consolidated Balance Sheets
 (in thousands, except share and per share information)

| ASSETS | November 1, 2008 | February 2, 2008 |
|--|---------------------|---------------------|
| Current Assets: | | |
| Cash and cash equivalents | \$ 6,525 | \$ 10,742 |
| Short-term investments | 279 | 191 |
| Trade receivables, net | 2,380 | 1,899 |
| Accounts receivable, other | 3,341 | 3,676 |
| Inventories | 162,315 | 141,406 |
| Prepaid expenses and other | 6,575 | 5,348 |
| Deferred income taxes, net | 3,897 | 2,725 |
| Total current assets | 185,312 | 165,987 |
| Property and Equipment: | | |
| Land and building | 245 | 245 |
| Equipment | 43,788 | 40,338 |
| Furniture and fixtures | 22,562 | 20,991 |
| Leasehold improvements | 60,319 | 57,599 |
| Construction in progress | 1,500 | 2,564 |
| | 128,414 | 121,737 |
| Less accumulated depreciation and amortization | 83,650 | 75,232 |
| Net property and equipment | 44,764 | 46,505 |
| Deferred income taxes | 3,683 | 3,780 |
| Other assets, net | 341 | 462 |
| Total Assets | \$ 234,100 | \$ 216,734 |
| LIABILITIES AND STOCKHOLDERS' INVESTMENT | | |
| Current Liabilities: | | |
| Accounts payable | \$ 59,199 | \$ 64,125 |
| Accrued income taxes | - | 688 |
| Accrued payroll expenses | 4,362 | 4,432 |
| Deferred rent | 4,516 | 4,379 |
| Short-term debt | 14,943 | - |
| Other accrued expenses | 3,107 | 2,980 |
| Total current liabilities | 86,127 | 76,604 |
| Deferred rent | 17,123 | 18,012 |
| Deferred income taxes | 2,854 | 2,968 |
| Other liabilities, net | 272 | 95 |
| Total liabilities | 106,376 | 97,679 |
| Stockholders' Investment: | | |
| Preferred stock, \$.01 par value, 1,000,000 shares authorized, | | |

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| | | |
|---|------------|------------|
| no shares issued | - | - |
| Common stock, \$.01 par value, 80,000,000 shares authorized, 36,290,549 and 36,162,201 shares issued at November 1, 2008 and February 2, 2008, respectively | 363 | 362 |
| Paid-in capital | 90,935 | 87,142 |
| Retained earnings | 203,370 | 181,555 |
| Treasury stock, at cost; 7,761,813 and 6,723,113 shares repurchased at November 1, 2008 and February 2, 2008, respectively | (166,944) | (150,004) |
| Total stockholders' investment | 127,724 | 119,055 |
| Total Liabilities and Stockholders' Investment | \$ 234,100 | \$ 216,734 |

See notes to unaudited condensed consolidated financial statements.

HIBBETT SPORTS, INC. AND SUBSIDIARIES
Unaudited Condensed Consolidated Statements of Operations
(in thousands, except share and per share information)

| | Thirteen Weeks Ended | | Thirty-Nine Weeks Ended | |
|---|----------------------|------------|-------------------------|------------|
| | November | | November | |
| | November | 3, | 1, | 3, |
| | 1, 2008 | 2007 | 2008 | 2007 |
| Net sales | \$ 140,148 | \$ 129,628 | \$ 416,262 | \$ 377,873 |
| Cost of goods sold, including distribution center and store occupancy costs | 93,456 | 87,154 | 279,493 | 252,871 |
| Gross profit | 46,692 | 42,474 | 136,769 | 125,002 |
| Store operating, selling and administrative expenses | 31,073 | 26,898 | 91,041 | 79,512 |
| Depreciation and amortization | 3,587 | 3,023 | 10,452 | 9,038 |
| Operating income | 12,032 | 12,553 | 35,276 | 36,452 |
| Interest income | 5 | 91 | 31 | 551 |
| Interest expense | (158) | (3) | (554) | (53) |
| Interest (expense) income, net | (153) | 88 | (523) | 498 |
| Income before provision for income taxes | 11,879 | 12,641 | 34,753 | 36,950 |
| Provision for income taxes | 4,227 | 4,826 | 12,938 | 14,227 |
| Net income | \$ 7,652 | \$ 7,815 | \$ 21,815 | \$ 22,723 |
| Basic earnings per share | \$ 0.27 | \$ 0.25 | \$ 0.76 | \$ 0.73 |
| Diluted earnings per share | \$ 0.26 | \$ 0.25 | \$ 0.75 | \$ 0.71 |
| Weighted average shares outstanding: | | | | |
| Basic | 28,494,587 | 31,074,731 | 28,551,470 | 31,312,106 |
| Diluted | 28,930,306 | 31,553,636 | 28,983,303 | 31,822,506 |

See notes to unaudited condensed consolidated financial statements.

HIBBETT SPORTS, INC. AND SUBSIDIARIES
 Unaudited Condensed Consolidated Statements of Cash Flows
 (in thousands, except share information)

| | Thirty-Nine Weeks Ended | |
|---|-------------------------|---------------------|
| | November 1, 2008 | November 3, 2007 |
| Cash Flows From Operating Activities: | | |
| Net income | \$ 21,815 | \$ 22,723 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 10,452 | 9,038 |
| Deferred income tax (benefit) expense, net | (1,190) | 1,854 |
| Excess tax benefit from stock option exercises | (356) | (517) |
| Loss on disposal of assets, net | 320 | 170 |
| Stock-based compensation | 2,707 | 3,159 |
| Changes in operating assets and liabilities: | | |
| Trade receivables, net | (481) | (191) |
| Accounts receivable, other | 335 | 242 |
| Inventories | (20,909) | (23,129) |
| Prepaid expenses and other current assets | (1,229) | (1,217) |
| Accrued income taxes | (509) | (5,644) |
| Other assets, non-current | 121 | (12) |
| Accounts payable | (4,926) | 10,577 |
| Deferred rent, non-current | (889) | 824 |
| Accrued expenses and other | 372 | (2,289) |
| Net cash provided by operating activities | 5,633 | 15,588 |
| Cash Flows From Investing Activities: | | |
| Purchase of short-term investments, net | (87) | (292) |
| Capital expenditures | (9,085) | (10,165) |
| Proceeds from sale of property and equipment | 56 | 9 |
| Net cash used in investing activities | (9,116) | (10,448) |
| Cash Flows From Financing Activities: | | |
| Cash used for stock repurchases | (16,940) | (26,429) |
| Proceeds from borrowings on revolving credit facilities, net | 14,943 | - |
| Excess tax benefit from stock option exercises | 356 | 517 |
| Proceeds from options exercised and purchase of shares under the employee stock purchase plan | 907 | 1,156 |
| Net cash used in financing activities | (734) | (24,756) |
| Net Decrease in Cash and Cash Equivalents | (4,217) | (19,616) |
| Cash and Cash Equivalents, Beginning of Period | 10,742 | 30,367 |
| Cash and Cash Equivalents, End of Period | \$ 6,525 | \$ 10,751 |

See notes to unaudited condensed consolidated financial statements.

HIBBETT SPORTS, INC. AND SUBSIDIARIES
 Unaudited Condensed Consolidated Statements of Stockholders' Investment
 (in thousands, except share information)

| | Common Stock | | | Treasury Stock | | Total Stockholders' Investment | |
|--|---------------------|--------|--------------------|----------------------|---------------------|--------------------------------------|------------|
| | Number of Shares | Amount | Paid-In Capital | Retained Earnings | Number of Shares | | Amount |
| Balance-February 3, 2007 | 36,047,732 | \$ 360 | \$ 81,916 | \$ 151,697 | 4,306,413 | \$ (97,332) | \$ 136,641 |
| Net income | | | | 30,329 | | | 30,329 |
| Cumulative effect of adopting FIN No. 48 | | | | (554) | | | (554) |
| Cumulative effect of change in accounting principle, net | | | | 83 | | | 83 |
| Issuance of shares from the employee stock purchase plan and the exercise of stock options, including tax benefit of \$275 | 114,469 | 2 | 1,549 | | | | 1,551 |
| Purchase of shares under the stock repurchase program | | | | | 2,416,700 | (52,672) | (52,672) |
| Stock-based compensation | | | 3,677 | | | | 3,677 |
| Balance-February 2, 2008 | 36,162,201 | 362 | 87,142 | 181,555 | 6,723,113 | (150,004) | 119,055 |
| Net income | | | | 21,815 | | | 21,815 |
| Issuance of shares from the employee stock purchase plan and the exercise of stock options, including tax | 128,348 | 1 | 1,262 | | | | 1,263 |

benefit of \$356

| | | |
|--|-------|-------|
| Tax shortfall on release of restricted stock | (176) | (176) |
|--|-------|-------|

| | | | |
|---|-----------|----------|----------|
| Purchase of shares under the stock repurchase program | 1,038,700 | (16,940) | (16,940) |
|---|-----------|----------|----------|

| | | |
|--------------------------|-------|-------|
| Stock-based compensation | 2,707 | 2,707 |
|--------------------------|-------|-------|

| | | | | | | | | | | | | |
|--------------------------|------------|----|-----|----|--------|----|---------|-----------|----|-----------|----|---------|
| Balance-November 1, 2008 | 36,290,549 | \$ | 363 | \$ | 90,935 | \$ | 203,370 | 7,761,813 | \$ | (166,944) | \$ | 127,724 |
|--------------------------|------------|----|-----|----|--------|----|---------|-----------|----|-----------|----|---------|

See notes to unaudited condensed consolidated financial statements.

HIBBETT SPORTS, INC. AND SUBSIDIARIES
Notes to Unaudited Condensed Consolidated Financial Statements

1. Basis of Presentation and Accounting Policies

The accompanying unaudited condensed consolidated financial statements of Hibbett Sports, Inc. and its wholly-owned subsidiaries have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and are presented in accordance with the requirements of Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the fiscal year ended February 2, 2008. In our opinion, the unaudited condensed consolidated financial statements included herein contain all adjustments considered necessary for a fair presentation of our financial position as of November 1, 2008 and February 2, 2008 and the results of our operations and cash flows for the periods presented.

Seasonality and Inflation

We have historically experienced and expect to continue to experience seasonal fluctuations in our net sales and operating income. Our net sales and operating income are typically higher in the fourth quarter due to the holiday selling season. However, the seasonal fluctuations are mitigated by the strong product demand in the spring and back-to-school sales periods. Our quarterly results of operations may also fluctuate significantly as a result of a variety of factors, including the timing of new store openings, the amount and timing of net sales contributed by new stores, the level of pre-opening expenses associated with new stores, the relative proportion of new stores to mature stores, merchandise mix and demand for apparel and accessories driven by local interest in sporting events.

Although our operations are influenced by general economic conditions, we do not believe that, historically, inflation has had a material impact on our results of operations as we are generally able to pass along inflationary increases in costs to our customers.

Business

We operate sporting goods retail stores in small and mid-sized markets predominately in the Southeast, Southwest, Mid-Atlantic and the lower Midwest regions of the United States. Our fiscal year ends on the Saturday closest to January 31 of each year. Our merchandise assortment features a core selection of brand name merchandise emphasizing team sports equipment, athletic and fashion apparel and footwear. We complement this core assortment with a selection of localized apparel and accessories designed to appeal to a wide range of customers within each market.

Principles of Consolidation

The unaudited condensed consolidated financial statements of our Company include its accounts and the accounts of all wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation. Occasionally, certain reclassifications are made to conform previously reported data to the current presentation. Such reclassifications had no impact on total assets, net income or stockholders' investment.

Reportable Segments

Given the economic characteristics of our store formats, the similar nature of products offered for sale, the type of customers, the methods of distribution and how our Company is managed, our operations constitute only one

reportable segment.

Revenues from external customers by product category are impractical for us to report.

Use of Estimates in the Preparation of Unaudited Condensed Consolidated Financial Statements

The preparation of unaudited condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles requires our management to make estimates and assumptions that affect:

- the reported amounts of certain assets and liabilities;
- the disclosure of certain contingent assets and liabilities at the date of the unaudited condensed consolidated financial statements; and
- the reported amounts of certain revenues and expenses during the reporting period.

Actual results could differ from those estimates.

Vendor Arrangements

We enter into arrangements with some of our vendors that entitle us to a partial refund of the cost of merchandise purchased during the year or reimbursement of certain costs we incur to advertise or otherwise promote their product. The volume based rebates, supported by vendor agreements, are estimated throughout the year and reduce the cost of inventory and cost of goods sold during the year. This estimate is regularly monitored and adjusted for current or anticipated changes in purchase levels and for sales activity.

We also receive consideration from vendors through a variety of other programs, including markdown reimbursements, vendor compliance charges and defective merchandise credits. If the payment is a reimbursement for costs incurred, it is offset against those related costs; otherwise, it is treated as a reduction to the cost of merchandise. Markdown reimbursements related to merchandise that has been sold are negotiated by our merchandising teams and are credited directly to cost of goods sold in the period received. If vendor funds are received prior to merchandise being sold, they are recorded as a reduction of merchandise cost.

Cash and Cash Equivalents

We consider all short-term, highly liquid investments with original maturities of 90 days or less, including commercial paper and money market funds, to be cash equivalents. We place our cash equivalents in high credit quality financial institutions. We are exposed to credit risk in the event of default by these institutions to the extent the amount recorded on the balance sheet exceeds the FDIC insurance limits per institution. Amounts due from third party credit card processors for the settlement of debit and credit card transactions are included as cash equivalents as they are generally collected within three business days. Cash equivalents related to credit and debit card transactions at November 1, 2008 and February 2, 2008 were \$1.9 million and \$2.4 million, respectively.

Short-Term Investments

All investments with original maturities of greater than 90 days are accounted for in accordance with Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities." We determine the appropriate classification at the time of purchase. We held approximately \$0.3 million and \$0.2 million of investments in securities at November 1, 2008 and February 2, 2008, respectively. Our investments in securities primarily consisted of municipal bonds classified as available-for-sale. Investments in these securities are recorded at cost, which approximates fair value. As a result, there are no cumulative gross unrealized holding gains (losses) or gross realized gains (losses) from our securities. All income generated from these securities is recorded as interest income. We continually evaluate our short-term investments for other than temporary impairment.

Trade and Other Accounts Receivable

Trade accounts receivable consists primarily of amounts due to us from sales to educational institutions and youth associations. We do not require collateral and we maintain an allowance for potential uncollectible accounts based on an analysis of the aging of accounts receivable at the date of the financial statements, historical losses and existing economic conditions, when relevant. The allowance for doubtful accounts at November 1, 2008 and February 2, 2008 was \$60,000 and \$46,000, respectively.

Other accounts receivable consists primarily of tenant allowances due from landlords and cooperative advertising due from vendors, all of which are deemed to be collectible.

Inventory Valuation

Lower of Cost or Market: Inventories are valued using the lower of weighted-average cost or market method. Market is determined based on estimated net realizable value. We regularly review inventories to determine if the carrying value exceeds realizable value, and we record an accrual to reduce the carrying value to net realizable value as necessary. We account for obsolescence as part of our lower of cost or market accrual based on historical trends and specific identification. As of November 1, 2008 and February 2, 2008, the accrual was \$1.9 million and \$1.5 million, respectively. A determination of net realizable value requires significant judgment and estimates.

Shrinkage: We accrue for inventory shrinkage based on the actual historical results of our most recent physical inventories. These estimates are compared to actual results as physical inventory counts are performed and reconciled to the general ledger. Store counts are typically performed on a cyclical basis and the distribution center's counts have historically been performed mid-year and in late December or early January every year. In Fiscal 2009, the distribution center's counts are being performed quarterly. As of November 1, 2008 and February 2, 2008, the accrual was \$0.9 million for both periods.

Inventory Purchase Concentration: Our business is dependent to a significant degree upon close relationships with our vendors. Our largest vendor, Nike, represented approximately 46.4% and 46.3% of our purchases for the thirteen weeks ended November 1, 2008 and November 3, 2007, respectively. Our second largest vendor represented approximately 11.4% and 8.9% of our purchases while our third largest vendor represented approximately 10.1% and 10.4% of our purchases for the thirteen weeks ended November 1, 2008 and November 3, 2007, respectively.

For the thirty-nine weeks ended November 1, 2008 and November 3, 2007, Nike, our largest vendor, represented approximately 50.3% and 48.4% of our purchases, respectively. Our second largest vendor represented approximately 8.3% and 9.4% of our purchases while our third largest vendor represented approximately 8.3% and 6.8% of our purchases for the thirty-nine weeks ended November 1, 2008 and November 3, 2007, respectively.

Property and Equipment

Property and equipment are recorded at cost. Depreciation on assets is principally provided using the straight-line method over their estimated service lives (3 to 5 years for equipment, 7 years for furniture and fixtures and 39 years for buildings) or, in the case of leasehold improvements, the shorter of the initial term of the underlying leases or the estimated economic lives of the improvements (typically 3 to 10 years). We continually reassess the remaining useful life of leasehold improvements in light of store closing plans.

Construction in progress is comprised primarily of property and equipment related to unopened stores and costs associated with technology upgrades at period end. At November 1, 2008, construction in progress was comprised mostly of a conveyor project in our distribution center and expenses related to unopened stores.

Maintenance and repairs are charged to expense as incurred. The cost and accumulated depreciation of assets sold, retired or otherwise disposed of are removed from property and equipment and the related gain or loss is credited or charged to income.

Self-Insurance Accrual

We are self-insured for a significant portion of our health insurance. Liabilities associated with the risks that are retained by us are estimated, in part, by considering our historical claims. The estimated accruals for these liabilities could be affected if future occurrences and claims differ from our assumptions. To minimize our potential exposure, we carry stop-loss insurance which reimburses us for losses over \$0.1 million per covered person per year or \$2.0 million per year in the aggregate. As of November 1, 2008 and February 2, 2008, the accrual for these liabilities was \$0.6 million and \$0.5 million, respectively, and was included in accrued expenses in the unaudited condensed consolidated balance sheets.

We are also self-insured for our workers' compensation and general liability insurance up to an established deductible with a cumulative stop loss. As of November 1, 2008 and February 2, 2008, the accrual for these liabilities (which is not discounted) was \$0.3 million for both periods and was included in accrued expenses in the unaudited condensed consolidated balance sheets.

Deferred Rent

Deferred rent primarily consists of step rent and allowances from landlords related to our leased properties. Step rent represents the difference between actual operating lease payments due and straight-line rent expense, which is recorded by the Company over the term of the lease, including the build-out period. This amount is recorded as deferred rent in the early years of the lease, when cash payments are generally lower than straight-line rent expense, and reduced in the later years of the lease when payments begin to exceed the straight-line expense. Landlord allowances are generally comprised of amounts received and/or promised to us by landlords and may be received in the form of cash or free rent. We record a receivable from the landlord and a deferred rent liability when the allowances are earned. This deferred rent is amortized into income (through lower rent expense) over the term (including the pre-opening build-out period) of the applicable lease, and the receivable is reduced as amounts are received from the landlord.

On our unaudited condensed consolidated statements of cash flows, the current and long-term portions of landlord allowances are included as changes in cash flows from operations. The current portion is included as a change in accrued expenses and the long-term portion is included as a change in deferred rent, non-current. The liability for the current portion of unamortized landlord allowances was \$4.0 million and \$3.9 million at November 1, 2008 and February 2, 2008, respectively. The liability for the long-term portion of unamortized landlord allowances was \$13.7 million and \$14.6 million at November 1, 2008 and February 2, 2008, respectively. The non-cash portion of landlord allowances received is immaterial.

Revenue Recognition

We recognize revenue, including gift card and layaway sales, in accordance with the Securities and Exchange Commission (SEC) Staff Accounting Bulletin (SAB) No. 101, "Revenue Recognition in Financial Statements," as amended by SAB No. 104, "Revenue Recognition."

Retail merchandise sales occur on-site in our retail stores. Customers have the option of paying the full purchase price of the merchandise upon sale or paying a down payment and placing the merchandise on layaway. The customer may make further payments in installments, but the entire purchase price for merchandise placed on layaway must be received by the Company within 30 days. The down payment and any installments are recorded by us as short-term deferred revenue until the customer pays the entire purchase price for the merchandise. We recognize revenue at the time the customer takes possession of the merchandise. Retail sales are recorded net of returns and discounts and exclude sales taxes.

The cost of coupon sales incentives is recognized at the time the related revenue is recognized by the Company. Proceeds received from the issuance of gift cards are initially recorded as deferred revenue. Revenue is subsequently recognized at the time the customer redeems the gift cards and takes possession of the merchandise. Unredeemed gift cards are recorded as a current liability.

It is not our policy to take unclaimed layaway deposits and unredeemed gift cards into income. As of November 1, 2008 and November 3, 2007, there was no breakage revenue recorded in income. The deferred revenue liability for layaway deposits and unredeemed gift cards was \$1.9 million and \$2.1 million at November 1, 2008 and February 2, 2008, respectively. Any unrecognized breakage revenue is immaterial. We escheat unredeemed gift cards to the extent required by law.

Cost of Goods Sold

We include inbound freight charges, merchandise purchases, store occupancy costs and a portion of our distribution costs related to our retail business in cost of goods sold. Outbound freight charges associated with moving merchandise to and between stores are included in store operating, selling and administrative expenses.

Store Opening and Closing Costs

New store opening costs, including pre-opening costs, are charged to expense as incurred. Store opening costs primarily include payroll expenses, training costs and straight-line rent expenses. All pre-opening costs are included in store operating, selling and administrative expenses as a part of operating expenses.

We consider individual store closings to be a normal part of operations and regularly review store performance against expectations. Costs associated with store closings are recognized at the time of closing or when a liability has been incurred.

Impairment of Long-Lived Assets

We continually evaluate whether events and circumstances have occurred that indicate the remaining balance of long-lived assets may be impaired and not recoverable. Our policy is to recognize any impairment loss on long-lived assets as a charge to current income when events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. Impairment is assessed considering the estimated undiscounted cash flows over the asset's remaining life. If estimated cash flows are insufficient to recover the investment, an impairment loss is recognized based on a comparison of the cost of the asset to fair value less any costs of disposition. Evaluation of asset impairment requires significant judgment and estimates.

Advertising

We expense advertising costs when incurred. We participate in various advertising and marketing cooperative programs with our vendors, who, under these programs, reimburse us for certain costs incurred. A receivable for cooperative advertising to be reimbursed is recorded as a decrease to expense as advertisements are run.

The following table presents the components of our advertising expense (in thousands):

| Thirteen Weeks Ended | | Thirty-Nine Weeks Ended | |
|----------------------|----------|-------------------------|----------|
| November | November | November | November |
| 1, | 3, | 1, | 3, |
| 2008 | 2007 | 2008 | 2007 |

| | | | | | | | | |
|----------------------------|----|-------|----|-------|----|---------|----|---------|
| Gross advertising costs | \$ | 1,118 | \$ | 1,220 | \$ | 5,052 | \$ | 5,113 |
| Advertising reimbursements | | (456) | | (571) | | (2,936) | | (3,249) |
| Net advertising costs | \$ | 662 | \$ | 649 | \$ | 2,116 | \$ | 1,864 |

Fair Value of Financial Instruments

Effective February 3, 2008, we adopted SFAS No. 157, "Fair Value Measurements," which defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. The adoption of SFAS No. 157 did not have a material impact on our consolidated financial statements.

SFAS No. 157 establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- Level I – Quoted prices in active markets for identical assets or liabilities.
- Level II – Observable inputs other than quoted prices included in Level I, such as quoted prices for markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

- Level III – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The table below segregates all financial assets and liabilities that are measured at fair value on a recurring basis (at least annually) into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value as of November 1, 2008 (in thousands).

| | Level I | Level II | Level III | Total |
|------------------------|---------|----------|-----------|--------|
| Short-term investments | \$ 279 | \$ - | \$ - | \$ 279 |

Financial Accounting Standard Board (FASB) Staff Position (FSP) Financial Accounting Standard (FAS) No. 157-2, “Effective Date of FASB Statement No. 157,” delayed the effective date for all nonfinancial assets and liabilities until January 1, 2009, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (see Note 2 below).

In October 2008, the FASB issued FSP FAS No. 157-3, “Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active,” which clarifies the application of SFAS No. 157 in determining the fair value of assets and liabilities for which there is no active market or the principal market for such asset or liability is not active. This FSP was effective upon issuance and did not have a material impact on our consolidated financial statements.

2. Recent Accounting Pronouncements

In May 2008, the FASB issued SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles.” This statement identifies the sources for U.S. generally accepted accounting principles (GAAP) and lists the categories in descending order. An entity should follow the highest category of GAAP applicable for each of its accounting transactions. SFAS No. 162 is effective 60 days following SEC approval of the Public Company Accounting Oversight Board (PCAOB) amendments to remove the hierarchy of generally accepted accounting principles from auditing standards. The SEC approved the PCAOB amendments on September 16, 2008, making SFAS No. 162 effective on November 15, 2008. The adoption of SFAS No. 162 did not have a material impact on our consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities.” This statement requires companies to provide enhanced disclosures about (a) how and why they use derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations and (c) how derivative instruments and related hedged items affect a company’s financial position, financial performance and cash flows. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. We do not expect the adoption of SFAS No. 161 to have a material impact on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141(R), “Business Combinations.” SFAS No. 141(R) requires an acquirer to recognize the assets acquired, the liabilities assumed and any noncontrolling interest in purchased entities, measured at their fair values at the date of acquisition based upon the definition of fair value outlined in SFAS No. 157. For us, SFAS No. 141(R) is effective for acquisitions beginning on and after February 1, 2010. We do not expect the adoption of SFAS No. 141(R) to have a material impact on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities – Including an Amendment of FASB Statement 115.” This statement permits companies to elect to measure

certain assets and liabilities at fair value. At each reporting date subsequent to adoption, unrealized gains and losses on items for which the fair value option has been elected must be reported in earnings. On February 3, 2008, we adopted SFAS No. 159 and elected not to use fair value measurement on any assets or liabilities under this statement.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements." SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of their financial instruments according to a fair value hierarchy, as defined. SFAS No. 157 may require companies to provide additional disclosures based on that hierarchy. This statement was to be effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. In February 2008, the FASB issued FSP No. 157-2 which delayed for one year the applicability of SFAS No. 157's fair-value measurements to certain nonfinancial assets and liabilities. We adopted SFAS No. 157 as of February 3, 2008, except as it applies to those nonfinancial assets and liabilities affected by the one-year delay. The partial adoption of SFAS No. 157 did not have a material impact on our consolidated financial statements. We do not expect the adoption of the remaining provisions of SFAS No. 157 to have a material impact on our consolidated financial statements.

3. Debt

At November 1, 2008, we had two unsecured revolving credit facilities, which are renewable in December 2008 and August 2009. The facilities allow for borrowings up to \$50.0 million and \$30.0 million, respectively, at a fixed rate, a rate based on prime or LIBOR plus 0.375%, at our election. Under the provisions of both facilities, we do not pay commitment fees and are not subject to covenant requirements. As of November 1, 2008, we had \$14.9 million of debt outstanding under these facilities all of which is short-term in nature. At February 2, 2008, we only had one credit facility that allowed borrowings up to \$30.0 million. As of February 2, 2008, we had no debt outstanding under this facility.

Subsequent to November 1, 2008, we renewed our existing \$50.0 million facility at a rate equal to prime plus 2%. The renewal was effective November 20, 2008 and will expire on November 20, 2009. The facility is unsecured and does not require a commitment or agency fee nor are there any covenant restrictions.

4. Stock-Based Compensation Plans

At November 1, 2008, we had four stock-based compensation plans:

- (a) The 2005 Equity Incentive Plan (Incentive Plan) provides that the Board of Directors (Board) may grant equity awards to certain employees of the Company at its discretion. The Incentive Plan was adopted effective July 1, 2005 and authorizes grants of equity awards of up to 1,233,159 authorized but unissued shares of common stock. At November 1, 2008, there were 761,047 shares available for grant under the Incentive Plan.
- (b) The 2005 Employee Stock Purchase Plan (ESPP) allows for qualified employees to participate in the purchase of up to 204,794 shares of our common stock at a price equal to 85% of the lower of the closing price at the beginning or end of each quarterly stock purchase period. The ESPP was adopted effective July 1, 2005. At November 1, 2008, there were 140,730 shares available for purchase under the ESPP.
- (c) The 2005 Director Deferred Compensation Plan (Deferred Plan) allows non-employee directors an election to defer all or a portion of their fees into stock units or stock options. The Deferred Plan was adopted effective July 1, 2005 and authorizes grants of stock up to 112,500 authorized but unissued shares of common stock. At November 1, 2008, there were 84,583 shares available for grant under the Deferred Plan.
- (d) The 2006 Non-Employee Director Equity Plan (DEP) provides for grants of equity awards to non-employee directors. The DEP was adopted effective June 1, 2006 and authorizes grants of equity awards of up to 679,891 authorized but unissued shares of common stock. At November 1, 2008, there were 609,891 shares available for grant under the DEP.

Our plans allow for a variety of equity awards including stock options, restricted stock awards, stock appreciation rights and performance awards. As of November 1, 2008, the Company had only granted awards in the form of stock options, restricted stock units (RSUs) and performance-based awards (PSAs). RSUs and options to purchase our common stock have been granted to officers, directors and key employees. Beginning with the adoption of the Incentive Plan, a greater proportion of the awards granted to employees, including executive employees, have been RSUs as opposed to stock options when compared to grants made in prior years. The annual grant made for Fiscal 2009 and Fiscal 2008 to employees consisted solely of RSUs. We also have awarded PSAs to our named executive officers and expect the Board will continue to grant PSAs to key employees in the future. The terms and vesting

schedules for stock-based awards vary by type of grant and generally vest upon time-based conditions. Upon exercise, stock-based compensation awards are settled with authorized but unissued Company stock. On May 30, 2008, the Compensation Committee of the Board awarded a grant of 19,900 non-qualified stock options to our Chief Executive Officer that vest equally over four years and have an eight year life.

The compensation costs that have been charged against income for these plans were as follows for the thirteen and thirty-nine weeks ended November 1, 2008 and November 3, 2007 (in thousands):

| | Thirteen Weeks Ended | | Thirty-Nine Weeks Ended | |
|--|----------------------|----------|-------------------------|----------|
| | November | November | November | November |
| | 1, | 3, | 1, | 3, |
| | 2008 | 2007 | 2008 | 2007 |
| Stock-based compensation expense by type: | | | | |
| Stock options | \$ 315 | \$ 389 | \$ 1,658 | \$ 1,682 |
| Restricted stock awards | 255 | 294 | 967 | 1,377 |
| Employee stock purchase | 28 | 22 | 72 | 75 |
| Director deferred compensation | - | 7 | 10 | 25 |
| Total stock-based compensation expense | 598 | 712 | 2,707 | 3,159 |
| Tax benefit recognized | 138 | 166 | 704 | 819 |
| Stock-based compensation expense, net of tax | \$ 460 | \$ 546 | \$ 2,003 | \$ 2,340 |

Share-based and deferred stock compensation expenses have been included in store operating, selling and administrative expenses. There is no capitalized stock-based compensation cost.

The tax benefit recognized in our consolidated financial statements, as disclosed above, is based on the amount of compensation expense recorded for book purposes. The actual tax benefit realized in our tax return is based on the intrinsic value, or the excess of the market value over the exercise or purchase price, of stock options exercised and restricted stock awards vested during the period. The actual tax benefit realized for the deductions considered on our tax returns through November 1, 2008 and November 3, 2007 was from option exercises and totaled \$0.6 million for both periods.

Stock Options

Stock options are granted with an exercise price equal to the closing market price of our common stock on the date of grant. During the period between July 2005 and December 2006, stock options were granted with an exercise price equal to the closing market price of our common stock on the last trading day preceding the date of grant. Vesting and expiration provisions vary between equity plans. Grants awarded to employees under the 1996 Plan, as amended, vest over a five-year period in equal installments beginning on the first anniversary of the grant date and expire on the tenth anniversary of the date of grant. Grants awarded to employees under the Incentive Plan vest over a four-year period in equal installments beginning on the first anniversary of the grant date and expire on the eighth anniversary of the date of grant with the exception of a grant made on August 18, 2005, whose provisions provided for the five-year vesting schedule and ten-year term described in the 1996 Plan. Grants awarded to outside directors under both the DEP and Deferred Plan, vest immediately upon grant and expire on the tenth anniversary of the date of grant.

Following is the weighted average fair value of each option granted during the thirty-nine weeks ended November 1, 2008. The fair value was estimated on the date of grant using the Black-Scholes pricing model with the following weighted average assumptions for each period:

| Grant date | Thirty-Nine Weeks Ended November 1, 2008 | | | | | |
|--|--|---------|---------|---------|---------|---------|
| | 3/14/08 | 3/18/08 | 3/31/08 | 5/30/08 | 6/30/08 | 9/30/08 |
| Weighted average fair value at date of grant | \$5.92 | \$6.36 | \$6.67 | \$10.03 | \$9.18 | \$9.24 |
| Expected option life (years) | 4.20 | 4.20 | 4.20 | 5.07 | 4.20 | 4.76 |
| Expected volatility | 50.61% | 50.89% | 51.68% | 50.18% | 50.38% | 51.54 |
| Risk-free interest rate | 2.12% | 2.19% | 2.27% | 3.39% | 3.14% | 2.60% |
| Dividend yield | None | None | None | None | None | None |

We calculate the expected term for our stock options based on historical employee exercise behavior. Historically, an increase in our stock price has led to a pattern of earlier exercise by employees. We also expected the reduction of the contractual term from 10 years to 8 years to facilitate a pattern of earlier exercise by employees and to contribute to a gradual decline in the average expected term in future periods. For the last two years, the Compensation Committee has primarily awarded RSUs rather than options to our employees. With the absence of substantial new grants, the expected term may increase slightly because it will be affected to a greater extent by director options which have a longer contractual life.

The volatility used to value stock options is based on historical volatility. We calculate historical volatility using an average calculation methodology based on daily price intervals as measured over the expected term of the option. We have consistently applied this methodology since our adoption of the original disclosure provisions of SFAS No. 123, "Accounting for Share-Based Compensation."

Beginning with awards granted in the second quarter of Fiscal 2008, we base the risk-free interest rate on the annual continuously compounded risk-free rate with a term equal to the option's expected term. Previously, we used the market yield on U.S. Treasury securities. While the difference between the two rates is minimal and has only a slight effect on the fair value calculation, we believe using the annual continuously compounded risk-free rate is more compliant with SFAS No. 123R, "Share-Based Payments." The dividend yield is assumed to be zero since we have no current plan to declare dividends.

Activity for our option plans during the thirty-nine weeks ended November 1, 2008 was as follows:

| | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value (\$000's) |
|---|---------------------|--|--|--|
| Options outstanding at February 2, 2008 | 1,283,758 | \$ 15.89 | | \$ 7,559 |
| Granted | 69,963 | 16.65 | | |
| Exercised | (81,320) | 7.91 | | |
| Forfeited, cancelled or expired | (3,725) | 24.98 | | |
| Options outstanding at November 1, 2008 | 1,268,676 | \$ 16.41 | 5.29 | \$ 5,728 |
| Exercisable at November 1, 2008 | 1,015,299 | \$ 14.68 | 5.11 | \$ 5,566 |

The weighted average grant fair value of options granted during the thirteen weeks ended November 1, 2008 and November 3, 2007 was \$9.24 and \$9.56, respectively. The compensation expense included in store operating, selling and administrative expenses and recognized during the thirteen weeks ended November 1, 2008 and November 3, 2007 was \$0.3 million and \$0.4 million, respectively, before the recognized income tax benefit of \$42,000 and \$50,000, respectively.

The weighted average grant fair value of options granted during the thirty-nine weeks ended November 1, 2008 and November 3, 2007 was \$7.42 and \$10.50, respectively. The compensation expense included in store operating, selling and administrative expenses and recognized during the thirty-nine weeks ended November 1, 2008 and November 3, 2007 was \$1.7 million for both periods, before the recognized income tax benefit of \$0.3 million for both periods.

The total intrinsic value of stock options exercised during the thirteen weeks ended November 1, 2008 and November 3, 2007 was \$0.9 million and \$0.1 million, respectively. The intrinsic value of stock options is defined as the difference between the current market value and the grant price. The total cash received from these stock option exercises during the thirteen weeks ended November 1, 2008 and November 3, 2007 was \$0.5 million and \$0.1 million, respectively.

The total intrinsic value of stock options exercised during the thirty-nine weeks ended November 1, 2008 and November 3, 2007 was \$1.2 million and \$1.8 million, respectively. The total cash received from these stock option exercises during the thirty-nine weeks ended November 1, 2008 and November 3, 2007 was \$0.6 million and \$0.9 million, respectively. Excess tax benefits from stock option exercises are included in cash flows from financing activities as required by SFAS No. 123R. As of November 1, 2008, there was \$1.6 million of unrecognized compensation cost related to nonvested stock options. This cost is expected to be recognized over a weighted-average period of 1.36 years.

Restricted Stock Awards

Restricted stock awards are granted with a fair value equal to the closing market price of our common stock on the date of grant with the exception of those granted between August 2005 and December 2006 which were granted with a fair value equal to the closing market price of our common stock on the last trading day preceding the date of grant. Compensation expense is recorded straight-line over the vesting period. Restricted stock awards cliff vest in four to five years from the date of grant for those awards that are not performance-based. Performance-based

restricted stock awards cliff vest in one to five years from the date of grant after achievement of stated performance criterion and upon meeting service conditions.

The following table summarizes the restricted stock awards activity under all of our plans during the thirty-nine weeks ended November 1, 2008:

| | Number of Awards | Weighted-Average Grant Date Fair Value |
|---|---------------------|--|
| Restricted stock awards outstanding at February 2, 2008 | 143,046 | \$ 29.28 |
| Granted | 230,255 | 15.11 |
| Vested | (24,900) | 32.37 |
| Forfeited, cancelled or expired | (34,199) | 17.19 |
| Restricted stock awards outstanding at November 1, 2008 | 314,202 | \$ 19.96 |

There were no restricted stock awards granted during the thirteen weeks ended November 1, 2008 and November 3, 2007. The weighted-average grant date fair value of our RSUs granted was \$15.11 and \$28.30 for the thirty-nine weeks ended November 1, 2008 and November 3, 2007, respectively. The compensation expense included in store operating, selling and administrative expenses and recognized during the comparable thirteen week periods was \$0.3 million for both periods, before the recognized income tax benefit of \$0.1 million for both periods. The compensation expense included in store operating, selling and administrative expenses and recognized during the comparable thirty-nine week periods was \$1.0 million and \$1.4 million, respectively, before the recognized income tax benefit of \$0.4 million and \$0.5 million, respectively.

There were no restricted stock awards that vested during the current thirteen week period. There was one restricted stock award of 24,900 units that vested during the current thirty-nine week period with an intrinsic value of \$0.4 million. No restricted stock awards vested during the comparable period in the prior year. The total intrinsic value of our restricted stock awards outstanding and unvested at November 1, 2008 and November 3, 2007 was \$5.6 million and \$4.3 million, respectively. As of November 1, 2008, there was approximately \$4.1 million of total unrecognized compensation cost related to restricted stock awards. This cost is expected to be recognized over a weighted-average period of 2.94 years.

Employee Stock Purchase Plan

The Company's ESPP allows eligible employees the right to purchase shares of our common stock, subject to certain limitations, at 85% of the lesser of the fair market value at the end of each calendar quarter (purchase date) or the beginning of each calendar quarter. Our employees purchased 4,857 shares of common stock at \$17.02 per share through the ESPP during the thirteen weeks ended November 1, 2008. Our employees purchased 18,798 shares of common stock at an average price of \$14.37 during the thirty-nine weeks ended November 1, 2008. During the thirteen weeks ended November 3, 2007, our employees purchased 4,304 shares of common stock at \$21.08 per share through the ESPP. Our employees purchased 13,221 shares of common stock at an average price of \$22.95 during the thirty-nine weeks ended November 3, 2007.

The assumptions used in the option pricing model for the thirteen and thirty-nine weeks ended November 1, 2008 and November 3, 2007 were as follows:

| | Thirteen Weeks Ended | | Thirty-Nine Weeks Ended | |
|--|----------------------|------------------|-------------------------|------------------|
| | November 1, 2008 | November 3, 2007 | November 1, 2008 | November 3, 2007 |
| Weighted average fair value at date of grant | \$4.82 | \$5.57 | \$4.26 | \$6.07 |
| Expected life (years) | 0.25 | 0.25 | 0.25 | 0.25 |
| Expected volatility | 50.3% | 36.3% | 48.0%-50.8% | 36.3%-41.8% |
| Risk-free interest rate | 1.88% | 4.75% | 1.28%-3.06% | 4.75%-5.08% |
| Dividend yield | None | None | None | None |

The expense related to the ESPP was determined using the Black-Scholes option pricing model and the provisions of FASB Technical Bulletin (FTB) No. 97-1, "Accounting under Statement 123 for Certain Employee Stock Purchase Plans with a Look-Back Option," as amended by SFAS No. 123R. The compensation expense included in store operating, selling and administrative expenses and recognized during the thirteen weeks ended November 1, 2008 and November 3, 2007 was approximately \$28,000 and \$22,000, respectively. The compensation expense included in store operating, selling and administrative expenses and recognized during the thirty-nine weeks ended November 1, 2008 and November 3, 2007 was approximately \$72,000 and \$75,000, respectively.

Director Deferred Compensation

Under the Deferred Plan, outside non-employee directors can elect to defer all or a portion of their Board and Board committee fees into cash, stock options or deferred stock units. Those fees deferred into stock options are subject to the same provisions as provided for in the DEP and are expensed and accounted for accordingly. Director fees deferred into our common stock are calculated and expensed each calendar quarter by taking total fees earned during the calendar quarter and dividing by the closing price on the last day of the calendar quarter, rounded to the nearest whole share. The total annual retainer, Board and Board committee fees for non-employee directors that are not deferred into stock options, but which includes amounts deferred into stock units under the Deferred Plan, are expensed as incurred in all periods presented. No stock units were deferred during the third quarter of Fiscal 2009 and 292 stock units were deferred during the third quarter of Fiscal 2008. A total of 664 and 918 stock units were deferred under this plan through the third quarter of Fiscal 2009 and Fiscal 2008, respectively. As of June 2, 2008, all stock units deferred under this plan have been released to the participant upon retirement from the Board of Directors.

No compensation expense was recognized during the thirteen weeks ended November 1, 2008. The compensation expense included in store operating, selling and administrative expenses and recognized during the thirteen weeks ended November 3, 2007 was approximately \$7,000 before the recognized income tax benefit of \$3,000. The compensation expense included in store operating, selling and administrative expenses and recognized during the thirty-nine weeks ended November 1, 2008 and November 3, 2007 was approximately \$10,000 and \$25,000, respectively, before the recognized income tax benefit of \$4,000 and \$10,000, respectively.

5. Defined Contribution Plans

We maintain a 401(k) plan for the benefit of our employees. In addition to the Hibbett Sports, Inc. 401(k) Plan (Existing Plan), in November 2007, our Board adopted the Hibbett Sports, Inc. Supplemental 401(k) Plan (Supplemental Plan) for the purpose of supplementing the employer matching contribution and salary deferral opportunity available to highly compensated employees of the Company who are selected to participate in the Supplemental Plan. The non-qualified deferred compensation Supplemental Plan allows participants to defer up to 40% of their compensation and receive an employer matching contribution equal to \$0.75 for each dollar of compensation deferred, subject to a maximum of 4.5% of compensation. The employer matching contribution under the Existing Plan is equal to \$0.75 for each dollar of compensation deferred, subject to a maximum of 6.0% of compensation. The employer matching contribution is determined each year and credited annually to participant accounts who are currently employed by the Company. We expensed \$0.1 million for the Existing Plan during each of the thirteen weeks ended November 1, 2008 and November 3, 2007. We expensed \$0.3 million and \$0.4 million during the thirty-nine weeks ended November 1, 2008 and November 3, 2007, respectively. We expensed \$15,000 and \$59,000 for the Supplemental Plan during the thirteen and thirty-nine weeks ended November 1, 2008. No expense was incurred for the Supplemental Plan during the thirteen or thirty-nine weeks ended November 3, 2007.

6. Earnings Per Share

The computation of basic earnings per share (EPS) is based on the number of weighted-average common shares outstanding during the period. The computation of diluted EPS is based on the weighted-average number of shares outstanding plus the incremental shares that would be outstanding assuming exercise of dilutive stock options and issuance of restricted stock. The number of incremental shares is calculated by applying the treasury stock method. The following table sets forth the computation of basic and diluted earnings per share:

| | Thirteen Weeks Ended | | Thirty-Nine Weeks Ended | |
|--|----------------------|------------|-------------------------|------------|
| | November | November | November | November |
| | 1, | 3, | 1, | 3, |
| | 2008 | 2007 | 2008 | 2007 |
| Net income, in thousands | \$ 7,652 | \$ 7,815 | \$ 21,815 | \$ 22,723 |
| Weighted average number of common shares outstanding | 28,494,587 | 31,074,731 | 28,551,470 | 31,312,106 |
| Stock options | 365,109 | 416,542 | 361,833 | 443,936 |
| Restricted stock | 70,610 | 62,363 | 70,000 | 66,464 |
| Weighted average number of common shares outstanding and dilutive shares | 28,930,306 | 31,553,636 | 28,983,303 | 31,822,506 |
| Basic earnings per common share | \$ 0.27 | \$ 0.25 | \$ 0.76 | \$ 0.73 |
| Diluted earnings per common share | \$ 0.26 | \$ 0.25 | \$ 0.75 | \$ 0.71 |

In calculating diluted earnings per share for the thirteen and thirty-nine weeks ended November 1, 2008 and November 3, 2007, options to purchase 309,496 and 279,681 shares of common stock, respectively, were outstanding as of the end of the period, but were not included in the computation of diluted earnings per share due to their anti-dilutive effect.

7. Stock Repurchase Plan

In August 2004, our Board authorized a plan to repurchase our common stock. The Board has subsequently authorized increases to this plan with a current authorization effective November 2007 of \$250.0 million. Stock repurchases may be made in the open market or in negotiated transactions until January 30, 2010, with the amount and timing of repurchases dependent on market conditions and at the discretion of our management.

We did not repurchase any shares of our common stock during the thirteen weeks ended November 1, 2008. We repurchased 1,038,700 shares of our common stock during the thirty-nine weeks ended November 1, 2008 at a cost of \$16.9 million bringing the total shares repurchased to 7,761,813 shares at a cost of \$166.9 million. After considering past stock repurchases, approximately \$83.1 million of the total authorization remained for future stock repurchases at November 1, 2008.

8. Properties

We currently lease all of our existing store locations and expect that our policy of leasing rather than owning will continue as we continue to expand. Our leases typically provide for terms of five to ten years with options on our part to extend. Most leases also contain a kick-out clause if projected sales levels are not met and an early termination/remedy option if co-tenancy and exclusivity provisions are violated. We believe this leasing strategy enhances our flexibility to pursue various expansion opportunities resulting from changing market conditions and to periodically re-evaluate store locations. Our ability to open new stores is contingent upon locating satisfactory sites, negotiating favorable leases, recruiting and training qualified management personnel and the availability of market relevant inventory.

As current leases expire, we believe we will either be able to obtain lease renewals for present store locations or to obtain leases for equivalent or better locations in the same general area. For the most part, we have not experienced any significant difficulty in either renewing leases for existing locations or securing leases for suitable locations for new stores. Based primarily on our belief that we maintain good relations with our landlords, that most of our leases are at approximate market rents and that generally we have been able to secure leases for suitable locations, we believe our lease strategy will not be detrimental to our business, financial condition or results of operations.

Our corporate offices and our retail distribution center are leased under an operating lease. We own the Team Sales' facility located in Birmingham, Alabama that warehouses inventory for educational institutions and youth associations. We believe our current distribution center is suitable and adequate to support our current needs as well as our expected needs over the next few years.

We currently operate 726 stores in 24 contiguous states, opening our first store in Wisconsin in the third quarter of Fiscal 2009. Of these stores, 219 are located in malls and 507 are located in strip centers which are generally the centers of commerce and which are usually influenced by a Wal-Mart store. Over the last several years, we have concentrated our store base growth in strip centers within the markets we target.

9. Commitments and Contingencies

Lease Commitments.

We lease the premises for our retail sporting goods stores under non-cancelable operating leases having initial or remaining terms of more than one year. The leases typically provide for terms of five to ten years with options on our part to extend. Many of our leases contain scheduled increases in annual rent payments and the majority of our leases also require us to pay maintenance, insurance and real estate taxes. Additionally, many of the lease agreements contain tenant improvement allowances, rent holidays and/or rent escalation clauses (contingent rentals). For purposes of recognizing incentives and minimum rental expenses on a straight-line basis over the terms of the leases, we use the date of initial possession to begin amortization, which is generally when we enter the space and begin to make improvements in preparation of our intended use.

We also lease certain computer hardware, office equipment and transportation equipment under non-cancelable operating leases having initial or remaining terms of more than one year.

In February 1996, we entered into a sale-leaseback transaction to finance our distribution center and office facilities. In December 1999, the related operating lease was amended to include the Fiscal 2000 expansion of these facilities. The amended lease rate is \$877,000 per year and can increase annually with the Consumer Price Index. This lease will expire in December 2014.

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During the thirteen weeks ended November 1, 2008, we increased our lease commitments by a net of 14 retail stores and various office and transportation equipment. The retail stores opened in the third quarter of Fiscal 2009 have initial lease termination dates between October 2013 and January 2019. At November 1, 2008, the future minimum lease payments, excluding maintenance, insurance and real estate taxes, for our current operating leases and including the net 14 store operating leases added during the thirteen weeks ended November 1, 2008, were as follows (in thousands):

| | |
|-----------------------|------------|
| Remaining Fiscal 2009 | \$ 10,807 |
| Fiscal 2010 | 42,139 |
| Fiscal 2011 | 35,769 |
| Fiscal 2012 | 29,251 |
| Fiscal 2013 | 23,365 |
| Fiscal 2014 | 16,394 |
| Thereafter | 26,934 |
| TOTAL | \$ 184,659 |

Incentive Bonuses.

Specified officers and employees of our Company are entitled to incentive bonuses, primarily based on operating income of our Company or particular operations thereof. At November 1, 2008 and February 2, 2008, there was \$1.8 million and \$0.6 million of bonus related expense included in accrued expenses.

In addition, starting in March 2006, the Compensation Committee (Committee) of the Board of Directors of our Company began placing performance criteria on awards of RSUs to our named executive officers under the Incentive Plan. The performance criteria are primarily tied to performance targets with respect to future sales and operating income over a specified period of time. These PSAs are being expensed under the provisions of SFAS No. 123R and are evaluated each quarter to determine the probability that the performance conditions set within will be met. We expect the Committee to continue to place performance criteria on awards of RSUs to our named executive officers.

Legal Proceedings and Other Contingencies.

We are a party to various legal proceedings incidental to our business. We do not believe that any of these matters will, individually or in the aggregate, have a material adverse effect on our business or financial condition. We cannot give assurance, however, that one or more of these lawsuits will not have a material adverse effect on our results of operations for the period in which they are resolved. At November 1, 2008, we estimate that the liability related to these matters is approximately \$30,000 and accordingly, have accrued \$30,000 as a current liability on our unaudited condensed consolidated balance sheet. As of February 2, 2008, we had accrued \$0.8 million as it related to our estimated liability for legal proceedings which primarily consisted of an amount accrued for a pending lawsuit that has since been settled.

The estimates of our liability for pending and unasserted potential claims do not include litigation costs. It is our policy to accrue legal fees when it is probable that we will have to defend against known claims or allegations and we can reasonably estimate the amount of the anticipated expense. Although we have accrued legal fees associated with litigation currently pending against us, we have not made any accruals for potential liability for settlements or judgments because the potential liability is neither probable nor estimable.

From time to time, we enter into certain types of agreements that require us to indemnify parties against third party claims under certain circumstances. Generally these agreements relate to: (a) agreements with vendors and suppliers under which we may provide customary indemnification to our vendors and suppliers in respect of actions they take at our request or otherwise on our behalf; (b) agreements to indemnify vendors against trademark and copyright infringement claims concerning merchandise manufactured specifically for or on behalf of the Company; (c) real estate leases, under which we may agree to indemnify the lessors from claims arising from our use of the property; and (d) agreements with our directors, officers and employees, under which we may agree to indemnify such persons for liabilities arising out of their relationship with us. The Company has director and officer liability insurance, which, subject to the policy's conditions, provides coverage for indemnification amounts payable by us with respect to our directors and officers up to specified limits and subject to certain deductibles.

10. Income Taxes

Our effective tax rate is based on expected income, statutory tax rates and tax planning opportunities available in the various jurisdictions in which we operate. For interim financial reporting, we estimate the annual tax rate based on projected taxable income for the full year and record a quarterly income tax provision in accordance with the anticipated annual rate. We refine the estimates of the taxable income throughout the year as new information becomes available, including year-to-date financial results. This process often results in a change to our expected effective tax rate for the year. When this occurs, we adjust the income tax provision during the quarter in which the

change in estimate occurs so that the year-to-date provision reflects the expected annual tax rate. Significant judgment is required in determining our effective tax rate and in evaluating our tax positions.

In accordance with SFAS No. 109, "Accounting for Income Taxes," we recognize deferred tax assets and liabilities based on the difference between the financial statement carrying amounts and the tax basis of assets and liabilities. Deferred tax assets represent items to be used as a tax deduction or credit in future tax returns for which we have already properly recorded the tax benefit in the income statement. At least quarterly, we assess the likelihood that the deferred tax assets balance will be recovered. We take into account such factors as prior earnings history, expected future earnings, carryback and carryforward periods and tax strategies that could potentially enhance the likelihood of a realization of a deferred tax asset. To the extent recovery is not more likely than not, a valuation allowance is established against the deferred tax asset, increasing our income tax expense in the year such determination is made.

On February 4, 2007, we adopted the provisions of FASB Interpretation No. 48 (FIN No. 48), "Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109." FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes," by prescribing the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Under FIN No. 48, the financial statement effects of a tax position should initially be recognized when it is more-likely-than-not, based on the technical merits, that the position will be sustained upon examination. A tax position that meets the more-likely-than-not recognition threshold should initially and subsequently be measured as the largest amount of tax benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with a taxing authority.

As a result of implementing FIN No. 48, we increased the liability for unrecognized tax benefits by \$3.8 million, increased deferred tax assets by \$3.2 million and reduced retained earnings as of February 4, 2007 by \$0.6 million. Our total liability for unrecognized tax benefits as of February 4, 2007 amounted to \$5.7 million.

Beginning with the adoption of FIN No. 48, we classify gross interest and penalties and unrecognized tax benefits that are not expected to result in payment or receipt of cash within one year as non-current liabilities. As of November 1, 2008 and February 2, 2008, our total liability for unrecognized tax benefits amounted to \$2.9 million and \$3.0 million, respectively, of which \$1.1 million and \$1.0 million, if recognized, would affect our effective tax rate, respectively. Our liability for unrecognized tax benefits is generally presented as non-current. However, if we anticipate paying cash within one year to settle an uncertain tax position, the liability is presented as current.

We classify interest and penalties recognized on the liability for unrecognized tax benefits as income tax expense. As of November 1, 2008 and February 2, 2008, we had accrued \$0.4 million and \$0.3 million, respectively, for gross interest and penalties, which is generally classified as a non-current liability.

We file income tax returns in the U.S. federal and various state jurisdictions. Generally, we are not subject to changes in income taxes by the U.S. federal taxing jurisdiction for years prior to Fiscal 2006 or by most state taxing jurisdictions for years prior to Fiscal 2003. We do not anticipate a material change in our FIN No. 48 liability in the next 12 months.

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

Overview

Hibbett Sports, Inc. operates sporting goods stores in small and mid-sized markets, predominantly in the Southeast, Southwest, Mid-Atlantic and the lower Midwest. Our stores offer a broad assortment of quality athletic equipment, footwear and apparel with a high level of customer service. As of November 1, 2008, we operated a total of 726 retail stores composed of 704 Hibbett Sports stores, 18 Sports Additions athletic shoe stores and 4 Sports & Co. superstores in 24 states, opening our first store in Wisconsin in the third quarter of Fiscal 2009.

Our primary retail format and growth vehicle is Hibbett Sports, a 5,000-square-foot store located primarily in strip centers which are usually influenced by a Wal-Mart store and in enclosed malls. Over the last several years, we have concentrated and expect to continue our store base growth in strip centers versus enclosed malls. We believe Hibbett Sports stores are typically the primary sporting goods retailers in their markets due to the extensive selection of quality branded merchandise and a high level of customer service. We do not expect that the average size of our stores opening in Fiscal 2009 will vary significantly from the average size of stores opened in Fiscal 2008.

We historically have comparable store sales in the low to mid-single digit range. We plan to increase total company-wide square footage by approximately 9% in Fiscal 2009, which is below our increases over the last several years. We believe total sales percentage growth will be mid to high single digits in Fiscal 2009. Over the past several years, we have increased our gross profit due to improved vendor discounts, fewer retail reductions, increased efficiencies in logistics and systems and favorable leveraging of store occupancy costs. We expect this trend to continue with a slight improvement in gross profit rate in Fiscal 2009.

Due to our increased sales, we have historically leveraged our store operating, selling and administrative expenses. Based on projected sales, we expect store operating, selling and administrative rates to increase in Fiscal 2009 primarily due to lower than normal historical sales growth and increases in statutory minimum wage and bonus and sales related expenses. We expect to continue to generate sufficient cash to enable us to expand and remodel our store base and to provide capital expenditures for both distribution center and technology upgrade projects.

We maintain a merchandise management system that allows us to identify and monitor trends. However, this system does not produce U.S. generally accepted accounting principles (GAAP) financial information by product category. Therefore, it is impracticable to provide GAAP net sales by product category.

We operate on a 52- or 53-week fiscal year ending on the Saturday nearest to January 31 of each year. The consolidated statement of operations for fiscal years ended January 31, 2009 and February 2, 2008 will include 52 weeks of operations. We have operated as a public company and have been incorporated under the laws of the State of Delaware since October 6, 1996.

Significant Accounting Estimates

The unaudited condensed consolidated financial statements are prepared in conformity with GAAP. The preparation of these financial statements requires the use of estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the periods presented. Actual results could differ from those estimates and assumptions. Our significant accounting policies and estimates are described in Note 1 to the unaudited condensed consolidated financial statements and more fully in the Fiscal 2008 Annual Report on Form 10-K filed on April 2, 2008. There have been no changes in our accounting policies in the current period that had a material impact on our unaudited condensed consolidated financial statements.

Recent Accounting Pronouncements

See Note 2 of our unaudited condensed consolidated financial statements for information regarding recent accounting pronouncements.

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Results of Operations

The following table sets forth unaudited condensed consolidated statements of operations items expressed as a percentage of net sales for the periods indicated:

| | Thirteen Weeks Ended | | Thirty-Nine Weeks Ended | |
|---|----------------------|------------------|-------------------------|------------------|
| | November 1, 2008 | November 3, 2007 | November 1, 2008 | November 3, 2007 |
| Net sales | 100.0% | 100.0% | 100.0% | 100.0% |
| Costs of goods sold, including distribution and store occupancy costs | 66.7 | 67.2 | 67.1 | 66.9 |
| Gross profit | 33.3 | 32.8 | 32.9 | 33.1 |
| Store operating, selling and administrative expenses | 22.2 | 20.8 | 21.9 | 21.0 |
| Depreciation and amortization | 2.6 | 2.3 | 2.5 | 2.4 |
| Operating income | 8.6 | 9.7 | 8.5 | 9.7 |
| Interest income | - | 0.1 | - | 0.1 |
| Interest expense | (0.1) | - | (0.1) | - |
| Interest (expense) income, net | (0.1) | 0.1 | (0.1) | 0.1 |
| Income before provision for income taxes | 8.5 | 9.8 | 8.4 | 9.8 |
| Provision for income taxes | 3.0 | 3.7 | 3.1 | 3.8 |
| Net income | 5.5% | 6.0% | 5.2% | 6.0% |

Note: Columns may not sum due to rounding.

Thirteen Weeks Ended November 1, 2008 Compared to Thirteen Weeks Ended November 3, 2007

Net sales. Net sales increased \$10.5 million, or 8.1%, to \$140.1 million for the thirteen weeks ended November 1, 2008 from \$129.6 million for the comparable period in the prior year. The following factors helped define this quarter:

- We opened 22 Hibbett Sports stores and closed 8 in the thirteen weeks ended November 1, 2008. New stores and stores not in the comparable store net sales calculation increased \$10.0 million during the thirteen week period.
- We experienced a 0.4% increase in comparable store net sales for the thirteen weeks ended November 1, 2008. Higher comparable store net sales contributed \$0.5 million to the increase in net sales.

The increase in comparable store sales was primarily attributable to a slight increase in the number of items per transaction and improved efficiencies in systems that enhanced our ability to offer the right product in the right store. We also believe that the close proximity of our stores, coupled with branded merchandise selection and fuel costs, encouraged the customer in our smaller markets to shop closer to home. Our sales were negatively impacted by severe weather events in the Sunbelt during the quarter.

We experienced the following performance trends in the thirteen week period ended November 1, 2008:

-

Branded activewear performance increased slightly in women's and children's and led by Under Armour and Nike technical products. Urban lifestyle apparel consisting primarily of men's lifestyle was negative continuing a trend from previous periods.

- Licensed business was negative mid-single-digits, while Mixed Martial Arts apparel performed very well. We also saw strong improvements in accessories led by Nike, Under Armour, Shock Doctor, Wilson and Oakley.
- Footwear was positive single-digits overall although women's footwear underperformed. Key performers included Nike Shox, Air Force One, Air Jordan, Adidas Bounce, Asics Performance Running, DC Skate and Under Armour Training shoes.
 - Equipment was negative low-single-digits.
- Strip center locations continue to outperform enclosed mall stores and non-urban stores continue to outperform urban locations.

Comparable store net sales data for the period reflects sales for our traditional format Hibbett Sports and Sports Additions stores open throughout the period and the corresponding period of the prior fiscal year. If a store remodel or relocation results in the store being closed for a significant period of time, its sales are removed from the comparable store base until it has been open a full 12 months. During the thirteen weeks ended November 1, 2008, 614 stores were included in the comparable store sales comparison. Our four Sports & Co. stores are not and have never been included in the comparable store net sales comparison because we have not opened a superstore since September 1996 nor do we have plans to open additional superstores in the future.

Gross profit. Cost of goods sold includes the cost of inventory, occupancy costs for stores and occupancy and operating costs for the distribution center. Gross profit was \$46.7 million, or 33.3% of net sales, in the thirteen weeks ended November 1, 2008, compared with \$42.5 million, or 32.8% of net sales, in the same period of the prior fiscal year. Our increase in gross profit percent was due primarily to improvement in inbound freight and inventory shrinkage rates and the leveraging of occupancy and warehouse costs. Distribution expense experienced decreases in data processing costs while fuel costs increased. Occupancy expense decreased and saw its largest decrease in rent expense as a percent to net sales due primarily to favorable rent negotiations in new and existing locations. Product margin increased due to improved shrinkage results and a lower sales return accrual.

Store operating, selling and administrative expenses. Store operating, selling and administrative expenses were \$31.1 million, or 22.2% of net sales, for the thirteen weeks ended November 1, 2008, compared to \$26.9 million, or 20.8% of net sales, for the comparable period a year ago. We attribute this increase to the following factors:

- Salary and benefit costs increased in our stores by 55 basis points, resulting primarily from increased incentive sales pay and increases in minimum wage. These costs increased 70 basis points at the administrative level as the result of an increase in our bonus accrual based on our financial performance expectations for the year.
- Health insurance expenses increased as a result of higher claims. Also increasing during the quarter were outbound freight and shipping expenses due to increased fuel costs and higher store count.
- Somewhat offsetting the increases above were decreases in store training expenses and in stock-based compensation expenses, primarily resulting from forfeited awards.

Depreciation and amortization. Depreciation and amortization as a percentage of net sales was 2.6% in the thirteen weeks ended November 1, 2008 compared to 2.3% for the comparable period a year ago. The weighted-average lease term of new store leases added during the thirteen weeks ended November 1, 2008 decreased to 6.57 years compared to those added during the thirteen weeks ended November 3, 2007 of 6.80 years. We attribute the increase in depreciation expense as a percent to sales primarily due to a change in estimate of the economic useful life of leasehold improvements in certain underperforming stores.

Provision for income taxes. Provision for income taxes as a percentage of net sales was 3.0% in the thirteen weeks ended November 1, 2008, compared to 3.7% for the thirteen weeks ended November 3, 2007. The combined federal, state and local effective income tax rate as a percentage of pre-tax income was 35.6% and 38.2% for the thirteen weeks ended November 1, 2008 and November 3, 2007, respectively. The decrease in rate over last year is primarily the result of employment-related tax credits and a lesser impact of discrete items as compared to last year.

Thirty-Nine Weeks Ended November 1, 2008 Compared to Thirty-Nine Weeks Ended November 3, 2007

Net sales. Net sales increased \$38.4 million, or 10.2%, to \$416.3 million for the thirty-nine weeks ended November 1, 2008 from \$377.9 million for the comparable period in the prior year. The following factors helped define this period:

- We opened 50 Hibbett Sports stores and closed 12 in the thirty-nine weeks ended November 1, 2008. New stores and stores not in the comparable store net sales calculation increased \$32.3 million during the thirty-nine week

period.

- We experienced a 1.7% increase in comparable store net sales for the thirty-nine weeks ended November 1, 2008. Higher comparable store net sales contributed \$6.1 million to the increase in net sales.

The increase in comparable store sales was primarily attributable to an increase in the number of items per transaction and improved efficiencies in systems that enhanced our ability to offer the right product in the right store. We also believe that the close proximity of our stores, coupled with branded merchandise selection and rising fuel costs, encouraged the customer in our smaller markets to shop closer to home.

We experienced the following performance trends in the thirty-nine week period ended November 1, 2008:

- Children's footwear performed well, while women's footwear weakened. Men's marquee product performed well.
 - The decline in the urban apparel business was offset by double-digit increases in Mixed Martial Arts.
 - Our strip center and non-urban stores outperformed our mall-based and urban stores.

Comparable store net sales data for the period reflects sales for our traditional format Hibbett Sports and Sports Additions stores open throughout the period and the corresponding period of the prior fiscal year. If a store remodel or relocation results in the store being closed for a significant period of time, its sales are removed from the comparable store base until it has been open a full 12 months. During the thirty-nine weeks ended November 1, 2008, 587 stores were included in the comparable store sales comparison. Our four Sports & Co. stores are not and have never been included in the comparable store net sales comparison because we have not opened a superstore since September 1996 nor do we have plans to open additional superstores in the future.

Gross profit. Cost of goods sold includes the cost of inventory, occupancy costs for stores and occupancy and operating costs for the distribution center. Gross profit was \$136.8 million, or 32.9% of net sales, in the thirty-nine weeks ended November 1, 2008, compared with \$125.0 million, or 33.1% of net sales, in the same period of the prior fiscal year. Our decrease in gross profit percent was due primarily to increased markdowns and promotions in the early part of this year. We also experienced an unfavorable comparison resulting from a favorable gross profit adjustment in prior year as we took all store inventories in the second quarter and the actual shrinkage was better than the accrued estimates. Distribution expense experienced decreases in data processing and salary and benefit expenses while fuel costs increased. Occupancy expense decreases were primarily due to decreases in rent expense as a percent to sales offset somewhat by an increase in utility expenses. Product margin decreased due to increased markdowns and a shift in product mix towards footwear which tends to have a lower overall product margin.

Store operating, selling and administrative expenses. Store operating, selling and administrative expenses were \$91.0 million, or 21.9% of net sales, for the thirty-nine weeks ended November 1, 2008, compared to \$79.5 million, or 21.0% of net sales, for the comparable period a year ago. We attribute this increase to the following factors:

- Salary and benefit costs increased in our stores by 63 basis points, resulting primarily from increased incentive sales pay and increases in minimum wage. These costs increased 38 basis points at the administrative level, partly as the result of an increase in corporate employee headcount and an increase in the bonus accrual based on our financial performance expectations for the year.
- Health insurance expenses increased as a result of higher claims and an increase in our accrual. Store training expenses increased somewhat as the result of higher attendance and travel costs to Hibbett U held at our corporate offices.
- Somewhat offsetting the increases above was a decrease in stock-based compensation expense as the result of lower fair values, the timing of the expensing of certain executive grants and forfeited awards. Other decreases were experienced in data processing and inventory counting expenses as compared against higher costs in the prior period when all stores were inventoried in the second quarter.

Depreciation and amortization. Depreciation and amortization as a percentage of net sales was 2.5% in the thirty-nine weeks ended November 1, 2008 compared to 2.4% for the comparable period a year ago. The weighted-average lease term of new store leases added during the thirty-nine weeks ended November 1, 2008 decreased slightly to 6.85 years compared to those added during the thirty-nine weeks ended November 3, 2007 of 6.88 years. We attribute the slight increase in depreciation expense as a percent to sales primarily due to a change in estimate of the economic useful life of leasehold improvements in certain underperforming stores.

Provision for income taxes. Provision for income taxes as a percentage of net sales was 3.1% in the thirty-nine weeks ended November 1, 2008, compared to 3.8% for the thirty-nine weeks ended November 3, 2007. The combined federal, state and local effective income tax rate as a percentage of pre-tax income was 37.2% and 38.5% for the thirty-nine weeks ended November 1, 2008 and November 3, 2007, respectively. The decrease in rate over last year is primarily the result of employment-related tax credits and a lesser impact of discrete items as compared to last year.

Liquidity and Capital Resources

Our capital requirements relate primarily to new store openings, stock repurchases and working capital requirements. Our working capital requirements are somewhat seasonal in nature and typically reach their peak near the end of the third and the beginning of the fourth quarters of our fiscal year. Historically, we have funded our cash requirements primarily through our cash flow from operations and occasionally from borrowings under our revolving credit facilities.

Our unaudited condensed consolidated statements of cash flows are summarized as follows (in thousands):

| | Thirty-Nine Weeks Ended | |
|--|-------------------------|------------------|
| | November 1, 2008 | November 3, 2007 |
| Net cash provided by operating activities: | \$ 5,633 | \$ 15,588 |
| Net cash used in investing activities: | (9,116) | (10,448) |
| Net cash used in financing activities: | (734) | (24,756) |
| Net decrease in cash and cash equivalents | \$ (4,217) | \$ (19,616) |

Operating Activities.

Cash flow from operations is seasonal in our business. Typically, we use cash flow from operations to increase inventory in advance of peak selling seasons, such as pre-Christmas and back-to-school. Inventory levels are reduced in connection with higher sales during the peak selling seasons and this inventory reduction, combined with proportionately higher net income, typically produces a positive cash flow.

Net cash provided by operating activities was \$5.6 million for the thirty-nine weeks ended November 1, 2008 compared with net cash provided by operating activities of \$15.6 million for the thirty-nine weeks ended November 3, 2007. The largest use of cash during the period resulted from an increase in inventory of \$20.9 million due in part by a higher store count and by cost inflation. The inventory level on a per store basis decreased by 2.0%. Other uses of cash during the period included a decrease in accounts payable of \$4.9 million and an increase of \$1.2 million in prepaid expenses and other current assets. Net income of \$21.8 million and non-cash charges, including depreciation and amortization expense of \$10.5 million and stock-based compensation expense of \$2.7 million also helped offset uses of cash in operating activities.

The largest uses of cash during the thirty-nine weeks ended November 3, 2007 resulted from an increase in inventory of \$23.1 million, accrued income taxes of \$5.6 million and prepaid expenses and other current assets of \$1.2 million. Offsetting this use of cash was an increase in accounts payable of \$10.6 million, net income of \$22.7 million and non-cash charges, including depreciation and amortization expense of \$9.0 million and stock-based compensation expense of \$3.2 million.

Investing Activities.

Cash used in investing activities in the thirty-nine weeks ended November 1, 2008 totaled \$9.1 million. Net purchases of short-term investments were approximately \$0.1 million compared to net purchases of short-term investments of \$0.3 million as of November 3, 2007. Capital expenditures used \$9.1 million of cash in the thirty-nine weeks ended November 1, 2008 compared to \$10.2 million for the comparable period last year. We use cash in investing activities to build new stores and remodel or relocate existing stores. Furthermore, net cash used in investing activities includes purchases of information technology assets and expenditures for our distribution facility and corporate headquarters.

We opened 50 new stores and relocated or remodeled 7 existing store during the thirty-nine weeks ended November 1, 2008 as compared to opening 44 new stores and relocating or remodeling 11 existing stores during the thirty-nine weeks ended November 3, 2007.

We estimate the cash outlay for capital expenditures in Fiscal 2009 will be approximately \$15.0 million, which relates to the opening of 75 to 79 new stores, remodeling of selected existing stores, information technology upgrades and enhancements and various improvements at our headquarters and distribution center. Of the total budgeted dollars for

capital expenditures for Fiscal 2009, we anticipate that approximately 80% will be related to the opening of new stores and remodeling or relocating existing stores. Approximately 10% will be related to improvements in information technology and distribution with the remaining 10% related primarily to loss prevention tools, office space improvements, equipment and automobiles.

Financing Activities.

Net cash used in financing activities was \$0.7 million in the thirty-nine weeks ended November 1, 2008 compared to net cash used in financing activities of \$24.8 million in the prior year period. The cash fluctuation as compared to the same period last fiscal year was primarily due to the borrowings against our credit facilities to repurchase shares of our common stock and to finance our inventory position in preparation for the back-to-school and holiday selling seasons. In the thirty-nine weeks ended November 1, 2008, we expended \$16.9 million on repurchases of our common stock compared to \$26.4 million for the thirty-nine weeks ended November 3, 2007. Financing activities also consisted of proceeds from transactions in our common stock and the excess tax benefit from the exercise of incentive stock options. As stock options are exercised, we will continue to receive proceeds and expect a tax deduction; however, the amounts and timing cannot be predicted.

At November 1, 2008, we had two unsecured revolving credit facilities that allow borrowings up to \$50.0 million and \$30.0 million, respectively, and which renew in December 2008 and August 2009, respectively. The facilities do not require a commitment or agency fee nor are there any covenant restrictions. We plan to renew these facilities as they expire and do not anticipate any problems in doing so; however, no assurance can be given that we will be granted a renewal or terms which are acceptable to us. As of November 1, 2008, we had \$14.9 million of debt outstanding under these facilities.

Subsequent to November 1, 2008, we renewed our existing \$50.0 million facility at a rate equal to prime plus 2%. The renewal was effective November 20, 2008 and will expire on November 20, 2009. The facility is unsecured and does not require a commitment or agency fee nor are there any covenant restrictions.

At November 3, 2007, we had one unsecured revolving credit facility that allowed borrowings up to \$30.0 million and which renewed annually in August. Under the provisions of this facility, we could draw down funds when our main operating account fell below \$100,000. The facility did not require a commitment or agency fee nor are there any covenant restrictions. As of November 3, 2007, we did not have any debt outstanding under this facility.

Based on our current operating and store opening plans and management's plans for the repurchase of our common stock, we believe that we can fund our cash needs for the foreseeable future through cash generated from operations and, if necessary, through periodic future borrowings against our credit facilities.

Off-Balance Sheet Arrangements

We have not provided any financial guarantees as of November 1, 2008. All purchase obligations are cancelable.

We have not created, and are not party to, any special-purpose or off-balance sheet entities for the purpose of raising capital, incurring debt or operating our business. We do not have any arrangements or relationships with entities that are not consolidated into the financial statements.

Quarterly and Seasonal Fluctuations

We have historically experienced and expect to continue to experience seasonal fluctuations in our net sales and operating income. Our net sales and operating income are typically higher in the fourth quarter due to sales increases during the holiday selling season. However, the seasonal fluctuations are mitigated by the strong product demand in the spring and back-to-school sales periods. Our quarterly results of operations may also fluctuate significantly as a result of a variety of factors, including the timing of new store openings, the amount and timing of net sales contributed by new stores, the level of pre-opening expenses associated with new stores, the relative proportion of new stores to mature stores, merchandise mix and demand for apparel and accessories driven by local interest in sporting events.

Although our operations are influenced by general economic conditions, we do not believe that, historically, inflation has had a material impact on our results of operations as we are generally able to pass along inflationary increases in costs to our customers. However, in recent periods, we have experienced an impact on overall sales due to a consumer spending slowdown spawned by the commercial and consumer credit environment, fuel prices, a slump in the housing market and cost inflation from foreign suppliers.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk.

Our financial condition, results of operations and cash flows are subject to market risk from interest rate fluctuations on our credit facilities which bear an interest rate that varies with LIBOR, prime or fixed rates. We have cash and

cash equivalents at financial institutions that are in excess of federally insured limits per institution. With the current financial environment and the instability of financial institutions, we cannot be assured that we will not experience losses on our deposits.

At November 1, 2008, we had \$14.9 million outstanding under our credit facilities. There were 91 days and 263 days during the thirteen and thirty-nine weeks ended November 1, 2008, respectively, where we incurred borrowings against our credit facilities for an average borrowing of \$19.5 million and \$24.4 million, respectively. The maximum borrowing was \$29.5 million and \$47.1 million for the thirteen and thirty-nine weeks ended November 1, 2008, respectively, with a weighted-average interest rate of 3.05% and 3.09%, respectively.

At February 2, 2008, we had no borrowings outstanding under any credit facility. There were 106 days during the fifty-two weeks ended February 2, 2008, where we incurred borrowings against our credit facility for an average borrowing of \$7.8 million. During Fiscal 2008, the maximum amount outstanding against these agreements was \$18.4 million and the weighted average interest rate was 5.64%.

A 10% increase or decrease in market interest rates would not have a material impact on our financial condition, results of operations or cash flows.

ITEM 4.

Controls and Procedures.

Evaluation of Disclosure Controls and Procedures.

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act) as of November 1, 2008. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of November 1, 2008, our disclosure controls and procedures were effective.

Changes in Internal Control Over Financial Reporting.

We have not identified any changes in our internal control over financial reporting that occurred during the period ended November 1, 2008, that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings.

We are a party to various legal proceedings incidental to our business. We do not believe that any of these matters will, individually or in the aggregate, have a material adverse effect on our business or financial condition. We cannot give assurance, however, that one or more of these lawsuits will not have a material adverse effect on our results of operations for the period in which they are resolved. At November 1, 2008, we estimate that the liability related to these matters is approximately \$30,000 and accordingly, have accrued \$30,000 as a current liability on our unaudited condensed consolidated balance sheet. As of February 2, 2008, we had accrued \$0.8 million as it related to our estimated liability for legal proceedings which primarily consisted of an amount accrued for a pending lawsuit that has since been settled.

The estimates of our liability for pending and unasserted potential claims do not include litigation costs. It is our policy to accrue legal fees when it is probable that we will have to defend against known claims or allegations and we can reasonably estimate the amount of the anticipated expense. Although we have accrued legal fees associated with litigation currently pending against us, we have not made any accruals for potential liability for settlements or judgments because the potential liability is neither probable nor estimable.

If the Company believes that a loss is both probable and estimable for a particular matter, the loss is accrued in accordance with the requirements of SFAS No. 5, "Accounting for Contingencies." With respect to any matter, we could change our belief as to whether a loss is probable or estimable, or our estimate of loss, at any time. Even though we may not believe a loss is probable or estimable, it is reasonably possible that we could suffer a loss with respect to that matter in the future.

ITEM 1A. Risk Factors.

In addition to the "Warning About Forward-Looking Statements" in the introduction and other information set forth in this report, you should carefully consider the disclosure in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended February 2, 2008, as filed on April 2, 2008 and in our Quarterly Report on Form 10-Q for the period ended August 2, 2008, as filed on September 9, 2008 with the SEC, discussing factors which could materially affect our business, financial condition or future results.

Disruptions in the capital and credit markets related to the current national and worldwide financial crisis, which may continue indefinitely or intensify, could adversely affect our results of operations, cash flows and financial condition, or those of our customers and vendors.

The current disruptions in the capital and credit markets may continue indefinitely or intensify, and adversely impact our results of operations, cash flows and financial condition, or those of our customers and vendors. Disruptions in the capital and credit markets as a result of uncertainty, changing or increased regulation, reduced alternatives or failures of significant financial institutions could adversely affect our access to liquidity. Such disruptions may also adversely impact the capital needs of our customers and vendors, which, in turn, could adversely affect our results of operations, cash flows and financial condition.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

ITEM 3. Defaults Upon Senior Securities.

None.

ITEM 4. Submission of Matters to a Vote of Security Holders.

None.

ITEM 5. Other Information.

None.

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ITEM 6.

Exhibits.

Exhibit No.

- 10.1 Sub-Sub-Sublease Agreement between Hibbett Sporting Goods, Inc. and Books-A-Million, dated April 23, 1996; incorporated by reference as Exhibit 10.3 to the Registrant's Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on September 7, 2006.
- 10.2 Credit Agreement between the Company and Regions Bank, effective August 28, 2008; incorporated by reference as Exhibit 10.1 to the Registrant's Form 8-K filed with the Securities and Exchange Commission on August 20, 2008.
- 31.1 * Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
- 31.2 * Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
- 32.1 * Section 1350 Certification of Chief Executive Officer and Chief Financial Officer
- * Filed Within

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HIBBETT SPORTS, INC.

By: /s/ Gary A. Smith
Gary A. Smith
Vice President & Chief Financial Officer
(Principal Financial Officer and Chief
Accounting Officer)

Date: December 8, 2008

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