GUESS INC
Form 10-Q
June 10, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended May 1, 2010

OR

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

For the transition period from to

Commission file number: 1-11893

GUESS?, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**95-3679695** (I.R.S. Employer Identification No.)
1444 South Alameda Street **Los Angeles, California** (Address of principal executive offices)	**90021** (Zip Code)

(213) 765-3100

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

As of June 4, 2010, the registrant had 93,218,046 shares of Common Stock, \$.01 par value per share, outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements.

GUESS?, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

		May 1, 2010 (unaudited)		Jan. 30, 2010
ASSETS				
Current assets:				
Cash and cash equivalents	$	517,705	$	502,063
Accounts receivable, net		282,535		283,747
Inventories		245,836		253,162
Deferred tax assets		30,441		30,570
Other current assets		51,638		54,621
Total current assets		1,128,155		1,124,163
Property and equipment, net		256,962		255,308
Goodwill		29,155		29,877
Other intangible assets, net		13,474		15,974
Long-term deferred tax assets		52,743		55,504
Other assets		74,279		50,423
	$	1,554,768	$	1,531,249
LIABILITIES AND STOCKHOLDERS EQUITY				
Current liabilities:				
Current portion of capital lease obligations and borrowings	$	2,707	$	2,357
Accounts payable		175,475		195,075
Accrued expenses		136,517		145,321
Total current liabilities		314,699		342,753
Capital lease obligations		12,752		14,137
Deferred rent and lease incentives		63,809		60,642
Other long-term liabilities		77,327		73,561
		468,587		491,093
Redeemable noncontrolling interests		13,247		13,813
Commitments and contingencies (Note 11)				
Stockholders equity:				
Preferred stock, $.01 par value. Authorized 10,000,000 shares; no shares issued and outstanding				
Common stock, $.01 par value. Authorized 150,000,000 shares; issued 137,140,675 and 136,568,091 shares, outstanding 93,318,756 and 92,736,761 shares, at May 1, 2010 and January 30, 2010, respectively		933		927
Paid-in capital		335,798		319,737
Retained earnings		954,941		919,531
Accumulated other comprehensive (loss) income		(9,114)		(2,952)
Treasury stock, 43,821,919 and 43,831,330 shares at May 1, 2010 and January 30, 2010, respectively		(216,985)		(217,032)
Guess?, Inc. stockholders equity		1,065,573		1,020,211
Nonredeemable noncontrolling interests		7,361		6,132
Total stockholders equity		1,072,934		1,026,343
	$	1,554,768	$	1,531,249

See accompanying notes to condensed consolidated financial statements.

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GUESS?, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share data)
(unaudited)

	Three Months Ended May 1, 2010	Three Months Ended May 2, 2009
Net revenue:		
Product sales	$ 514,055	$ 419,127
Net royalties	25,286	22,074
	539,341	441,201
Cost of product sales	304,090	263,698
Gross profit	235,251	177,503
Selling, general and administrative expenses	158,105	129,469
Pension curtailment expense	5,819	
Earnings from operations	71,327	48,034
Other income (expense):		
Interest expense	(195)	(606)
Interest income	301	737
Other income (expense), net	3,428	1,266
	3,534	1,397
Earnings before income tax expense	74,861	49,431
Income tax expense	23,207	16,312
Net earnings	51,654	33,119
Net earnings attributable to noncontrolling interests	1,319	577
Net earnings attributable to Guess?, Inc.	$ 50,335	$ 32,542
Earnings per common share attributable to common stockholders (Note 2):		
Basic	$ 0.54	$ 0.35
Diluted	$ 0.54	$ 0.35
Weighted average common shares outstanding attributable to common stockholders (Note 2):		
Basic	91,902	90,631
Diluted	92,768	91,158
Dividends declared per common share	$ 0.16	$ 0.10

See accompanying notes to condensed consolidated financial statements.

GUESS?, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)
(unaudited)

	Three Months Ended	
	May 1, 2010	May 2, 2009
Net earnings	$ 51,654	$ 33,119
Foreign currency translation adjustment	(12,273)	10,973
Unrealized gain (loss) on hedges, net of tax effect	1,428	(3,300)
Unrealized gain on investments, net of tax effect	175	180
SERP prior service cost and actuarial valuation loss amortization, including curtailment expense, net of tax effect	4,418	284
Comprehensive income	45,402	41,256
Less comprehensive income attributable to noncontrolling interests	(1,229)	(941)
Comprehensive income attributable to Guess?, Inc.	$ 44,173	$ 40,315

See accompanying notes to condensed consolidated financial statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)
(unaudited)

	Three Months Ended	
	May 1, 2010	May 2, 2009
Cash flows from operating activities:		
Net earnings	$ 51,654	$ 33,119
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	14,564	12,793
Amortization of intangible assets	1,187	1,754
Share-based compensation expense	8,068	6,764
Unrealized forward contract (gains) losses	(1,974)	3,066
Net loss on disposition of property and equipment	986	220
Pension curtailment expense	5,819	
Other items, net	(2,000)	759
Changes in operating assets and liabilities:		
Accounts receivable	(7,169)	(4,682)
Inventories	4,751	40,933
Prepaid expenses and other assets	(13,435)	(2,214)
Accounts payable and accrued expenses	(22,752)	(51,064)
Deferred rent and lease incentives	3,295	3,884
Other long-term liabilities	4,790	(531)
Net cash provided by operating activities	47,784	44,801
Cash flows from investing activities:		
Purchases of property and equipment	(19,405)	(18,480)
Proceeds from dispositions of long-term assets		474
Acquisition of lease interest	(2,249)	
Acquisition of businesses, net of cash acquired		(312)
Net cash settlement of forward contracts	609	3,693
Purchases of long-term investments	(2,414)	(3,640)
Net cash used in investing activities	(23,459)	(18,265)
Cash flows from financing activities:		
Certain short-term borrowings, net	442	4,623
Proceeds from borrowings		40,000
Repayment of borrowings and capital lease obligation	(390)	(40,378)
Dividends paid	(14,925)	(9,222)
Noncontrolling interest capital contributions		650
Issuance of common stock, net of nonvested award repurchases	2,606	434
Excess tax benefits from share-based compensation	5,612	60
Purchase of treasury stock		(5,309)
Net cash used in financing activities	(6,655)	(9,142)
Effect of exchange rates on cash and cash equivalents	(2,028)	1,118
Net increase in cash and cash equivalents	15,642	18,512
Cash and cash equivalents at beginning of period	502,063	294,118
Cash and cash equivalents at end of period	$ 517,705	$ 312,630
Supplemental cash flow data:		
Interest paid	$ 76	$ 690
Income taxes paid	$ 10,099	$ 12,621

See accompanying notes to condensed consolidated financial statements.

GUESS?, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

May 1, 2010

(unaudited)

(1) Basis of Presentation

In the opinion of management, the accompanying unaudited condensed consolidated financial statements of Guess?, Inc. and its subsidiaries (the Company) contain all adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation of the condensed consolidated balance sheets as of May 1, 2010 and January 30, 2010, and the condensed consolidated statements of income, condensed consolidated statements of comprehensive income and condensed consolidated statements of cash flows for the three months ended May 1, 2010 and May 2, 2009. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and the instructions to Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (the SEC). Accordingly, they have been condensed and do not include all of the information and footnotes required by GAAP for complete financial statements. The results of operations for the three months ended May 1, 2010 are not necessarily indicative of the results of operations to be expected for the full fiscal year. These financial statements should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended January 30, 2010. The Company has made certain reclassifications to the prior year s consolidated financial statements to conform to classifications in the current year. These reclassifications, none of which are material, had no impact on previously reported results of operations.

The three months ended May 1, 2010 had the same number of days as the three months ended May 2, 2009. All references herein to fiscal 2011 and fiscal 2010 represent the results of the 52-week fiscal years ended January 29, 2011 and January 30, 2010, respectively.

New Accounting Guidance

In June 2009, the Financial Accounting Standards Board (FASB) issued authoritative guidance that requires an enterprise to perform an analysis to determine whether the enterprise s variable interest or interests give it a controlling financial interest in a variable interest entity. This analysis identifies the primary beneficiary of a variable interest entity as the enterprise that has both of the following characteristics, among others: (a) the power to direct the activities of a variable interest entity that most significantly impacts the entity s economic performance, and (b) the obligation to absorb losses or the right to receive benefits from the entity, that could potentially be significant to the variable interest entity. Under this guidance, ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity are required. The Company adopted the relevant provisions of the guidance on January 31, 2010 and will apply the requirements prospectively. The adoption of this guidance did not have a material impact on the Company s consolidated financial statements.

In January 2010, the FASB issued authoritative guidance that expands the required disclosures about fair value measurements. This guidance provides for new disclosures requiring the Company to (a) disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers and (b) present separately information about purchases, sales, issuances and settlements in the reconciliation of Level 3 fair value measurements. This guidance also provides clarification of existing disclosures requiring the Company to (i) determine each class of assets and liabilities based on the nature and risks of the investments rather than by major security type and (ii) for each class of assets and liabilities, disclose the valuation techniques and inputs used to measure fair value for both Level 2 and Level 3 fair value measurements. The Company adopted the guidance effective January 31, 2010, except for the presentation of purchases, sales, issuances and settlements in the reconciliation of Level 3 fair value measurements, which will be effective for fiscal years beginning after December 15, 2010. The adoption of the first phase of this guidance did not have a material impact to the Company s consolidated financial statements.

(2) Earnings Per Share

Basic earnings per share represents net earnings attributable to common stockholders divided by the weighted-average number of common shares outstanding for the period. Diluted earnings per share represent net earnings attributable to common stockholders divided by the weighted-average number of common shares outstanding, inclusive of the dilutive impact of common equivalent shares outstanding during the period. However, nonvested restricted stock awards (referred to as participating securities) are excluded from the dilutive impact of common equivalent shares outstanding in accordance with FASB issued authoritative guidance under the two-class method since the nonvested restricted stockholders are entitled to participate in dividends declared on common stock as if the shares were fully vested and hence are deemed to be participating securities. Under the two-class method, earnings attributable to nonvested restricted stockholders are excluded from net earnings attributable to common stockholders for purposes of calculating basic and diluted earnings per common share.

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The computation of basic and diluted net earnings per common share attributable to common stockholders is as follows (in thousands):

	Three Months Ended	
	May 1, 2010	May 2, 2009
Net earnings attributable to Guess?, Inc.	$ 50,335	$ 32,542
Net earnings attributable to nonvested restricted stockholders	553	532
Net earnings attributable to common stockholders	$ 49,782	$ 32,010
Weighted average shares used in basic computations	91,902	90,631
Effect of dilutive securities:		
Stock options and restricted stock units	866	527
Weighted average shares used in diluted computations	92,768	91,158
Net earnings per common share attributable to common stockholders:		
Basic	$ 0.54	$ 0.35
Diluted	$ 0.54	$ 0.35

For the three months ended May 1, 2010 and May 2, 2009, equity awards granted for 320,500 and 1,537,394, respectively, of the Company s common shares were outstanding but were excluded from the computation of diluted weighted average common shares and common share equivalents outstanding because their effect would have been anti-dilutive.

In addition to the participating securities discussed above, the Company also excluded 563,400 nonvested stock options granted to certain employees from the computation of diluted weighted average common shares and common share equivalents outstanding for the three months ended May 2, 2009, because they were subject to a performance-based annual vesting condition.

In March 2008, the Company s Board of Directors terminated the previously authorized 2001 share repurchase program and authorized a new program to repurchase, from time to time and as market and business conditions warrant, up to $200 million of the Company s common stock (the 2008 Share Repurchase Program). Repurchases may be made on the open market or in privately negotiated transactions, pursuant to Rule 10b5-1 trading plans or other available means. There is no minimum or maximum number of shares to be repurchased under the program and the program may be discontinued at any time, without prior notice. During the three months ended May 2, 2009, the Company repurchased 407,600 shares under the 2008 Share Repurchase Program at an aggregate cost of $5.3 million. There were no share repurchases under the 2008 Share Repurchase Program during the three months ended May 1, 2010. At May 1, 2010, the Company had remaining authority under the 2008 Share Repurchase Program to purchase an additional $134.2 million of its common stock.

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(3) Stockholders Equity and Redeemable Noncontrolling Interests

A reconciliation of the total carrying amount of total stockholders equity, Guess?, Inc. stockholders equity and stockholders equity attributable to nonredeemable and redeemable noncontrolling interests for the fiscal year ended January 30, 2010 and three months ended May 1, 2010 is as follows (in thousands):

	Guess?, Inc. Stockholders Equity	Stockholders Equity Nonredeemable Noncontrolling Interests	Total	Redeemable Noncontrolling Interests
Balances at January 31, 2009	$ 773,001	$ 2,453	$ 775,454	$ 10,050
Issuance of common stock under stock compensation plans, net of tax effect	9,408		9,408	
Issuance of stock under ESPP	1,249		1,249	
Share-based compensation	27,339		27,339	
Dividends	(41,598)		(41,598)	
Share repurchases	(5,309)		(5,309)	
Acquisition of subsidiary with redeemable put feature				2,815
Noncontrolling interest capital contribution		1,001	1,001	
Noncontrolling interest capital distribution	(109)	(1,202)	(1,311)	
Comprehensive income (loss) (a):				
Net earnings	242,761	3,569	246,330	
Foreign currency translation adjustment	22,684	311	22,995	948
Unrealized loss on hedges, net of income tax of $2,690	(6,918)		(6,918)	
Unrealized gain on investments, net of income tax of $58	94		94	
SERP prior service cost and actuarial valuation loss amortization, net of income tax of $1,435	(2,391)		(2,391)	
Balances at January 30, 2010	$ 1,020,211	$ 6,132	$ 1,026,343	$ 13,813
Issuance of common stock under stock compensation plans, net of tax effect	7,703		7,703	
Issuance of stock under ESPP	343		343	
Share-based compensation	8,068		8,068	
Dividends	(14,925)		(14,925)	
Comprehensive income (loss) (a):				
Net earnings	50,335	1,319	51,654	
Foreign currency translation adjustment	(12,183)	(90)	(12,273)	(566)
Unrealized gain on hedges, net of income tax of $130	1,428		1,428	
Unrealized gain on investments, net of income tax of $13	175		175	
SERP prior service cost and actuarial valuation loss amortization, including curtailment expense, net of income tax of $2,832	4,418		4,418	
Balances at May 1, 2010	$ 1,065,573	$ 7,361	$ 1,072,934	$ 13,247

(a) Total comprehensive income consists of net earnings, Supplemental Executive Retirement Plan (SERP) related prior service cost and actuarial valuation loss amortization, unrealized gains or losses on investments available for sale, foreign currency translation adjustments and the effective portion of the change in the fair value of cash flow hedges.

Redeemable Noncontrolling Interests

In connection with the acquisition of two majority-owned subsidiaries, the Company is party to put arrangements with respect to the common securities that represent the remaining noncontrolling interests of the acquired companies. Each put arrangement is exercisable by the counter-party outside the control of the Company by requiring the Company to redeem the counterparty s entire equity stake in the subsidiary at a put price based on a multiple of earnings formula. Each put arrangement is recorded on the balance sheet at its redemption value and classified as a redeemable noncontrolling interest outside of permanent equity. As of May 1, 2010, the redeemable noncontrolling interests of $13.2 million was composed of redemption values related to the Focus Europe S.r.l. (Focus) and Guess Sud SAS (Guess Sud) put arrangements of $10.4 million and $2.8 million, respectively. As of January 30, 2010, the redeemable noncontrolling interests of $13.8 million was composed of redemption values related to the Focus and Guess Sud put arrangements of $10.9 million and $2.9 million, respectively.

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The put arrangement for Focus, representing 25% of the total outstanding equity interest of that subsidiary, may be exercised at the discretion of the minority owner by providing written notice to the Company no later than June 27, 2012. The redemption value of the Focus put arrangement is based on a multiple of Focus s net earnings.

The put arrangement for Guess Sud, representing 40% of the total outstanding equity interest of that subsidiary, may be exercised at the discretion of the minority owners by providing written notice to the Company anytime after January 30, 2012 or sooner in certain limited circumstances. The redemption value of the Guess Sud put arrangement is based on a multiple of Guess Sud s earnings before interest, taxes, depreciation and amortization.

(4) Accounts Receivable

Accounts receivable consists of trade receivables primarily relating to the Company s wholesale businesses in Europe, North America and Asia. The Company provided for allowances relating to these receivables of $29.4 million and $29.9 million at May 1, 2010 and January 30, 2010, respectively. In addition, accounts receivable includes royalty receivables relating to licensing operations of $22.1 million and $23.0 million at May 1, 2010 and January 30, 2010, respectively, for which the Company recorded an allowance for doubtful accounts of $0.7 million at both May 1, 2010 and January 30, 2010. The accounts receivable allowance includes allowances for doubtful accounts, wholesale sales returns and wholesale markdowns. Retail sales returns allowances are included in accrued expenses.

(5) Inventories

Inventories consist of the following (in thousands):

		May 1, 2010		**Jan. 30, 2010**
Raw materials	$	12,387	$	9,405
Work in progress		3,017		2,689
Finished goods		230,432		241,068
	$	245,836	$	253,162

As of May 1, 2010 and January 30, 2010, inventories had been written down to the lower of cost or market by $18.0 million and $16.8 million, respectively.

(6) Income Taxes

Income tax expense for the interim periods was computed using the effective tax rate estimated to be applicable for the full fiscal year. The Company s effective income tax rate decreased to 31.0% for the three months ended May 1, 2010 from 33.0% in the three months ended May 2, 2009 primarily due to a higher estimated proportion of annual earnings in lower tax jurisdictions.

(7) Segment Information

In the first quarter of fiscal 2011, the Company revised its segment reporting whereby the North American wholesale and Asia segments are now separate segments for reporting purposes. The Company s businesses are now grouped into five reportable segments for management and internal financial reporting purposes: North American retail, North American wholesale, Europe, Asia and licensing. Management evaluates segment performance based primarily on revenues and earnings from operations. The Company believes this segment reporting better reflects how its five business segments are managed and each segment s performance is evaluated. The North American retail segment includes the Company s retail operations in North America. The North American wholesale segment includes the Company s wholesale operations in North America. The Europe segment includes both wholesale and retail operations in Europe and the Middle East. The Asia segment includes the Company s wholesale and retail operations in Asia. The licensing segment includes the worldwide licensing operations of the Company. Corporate overhead, interest income, interest expense and other income and expense are evaluated on a consolidated basis and not allocated to the Company s business segments.

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Net revenue and earnings from operations are summarized as follows for the three months ended May 1, 2010 and May 2, 2009 (in thousands):

	Three Months Ended	
	May 1, 2010	May 2, 2009
Net revenue:		
North American retail	$ 235,773	$ 207,560
North American wholesale	42,728	33,573
Europe	186,968	145,698
Asia	48,586	32,296
Licensing	25,286	22,074
	$ 539,341	$ 441,201
Earnings (loss) from operations:		
North American retail	$ 24,372	$ 18,007
North American wholesale	10,211	4,926
Europe	34,482	23,139
Asia	7,137	2,496
Licensing	21,860	19,015
Corporate overhead	(26,735)	(19,549)
	$ 71,327	$ 48,034

Due to the seasonal nature of the Company s business segments, the above net revenue and operating results are not necessarily indicative of the results that may be expected for the full fiscal year.

All amounts for the years ended January 30, 2010 and January 31, 2009 have been revised as follows to conform to the new segment reporting described above (in thousands):

	First Quarter Ended May 2, 2009	Second Quarter Ended Aug. 1, 2009	Third Quarter Ended Oct. 31, 2009	Fourth Quarter Ended Jan. 30, 2010	Year Ended Jan. 30, 2010	Year Ended Jan. 31, 2009
Net revenue:						
North American retail	$ 207,560	$ 227,460	$ 239,518	$ 309,365	$ 983,903	$ 977,980
North American wholesale	33,573	33,213	46,124	39,772	152,682	176,303
Europe	145,698	210,159	168,829	222,556	747,242	718,964
Asia	32,296	29,532	40,527	44,932	147,287	119,878
Licensing	22,074	22,059	27,814	25,405	97,352	100,265
	$ 441,201	$ 522,423	$ 522,812	$ 642,030	$ 2,128,466	$ 2,093,390
Earnings (loss) from operations:						
North American retail	$ 18,007	$ 30,208	$ 33,110	$ 50,962	$ 132,287	$ 93,156
North American wholesale	4,926	8,328	12,245	9,667	35,166	39,786
Europe	23,139	52,293	40,801	57,002	173,235	168,630
Asia	2,496	1,564	5,472	6,293	15,825	5,715
Licensing	19,015	18,672	24,176	24,777	86,640	86,422
Corporate overhead	(19,549)	(19,951)	(16,830)	(28,007)	(84,337)	(64,922)

$	48,034	$	91,114	$	98,974	$	120,694	$	358,816	$	328,787

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(8) Borrowings and Capital Lease Obligations

Borrowings and capital lease obligations are summarized as follows (in thousands):

	May 1, 2010	Jan. 30, 2010
European capital lease, maturing quarterly through 2016	$ 14,799	$ 15,756
Other	660	738
	15,459	16,494
Less current installments	2,707	2,357
Long-term capital lease obligations	$ 12,752	$ 14,137

The Company entered into a capital lease in December 2005 for a new building in Florence, Italy. At May 1, 2010, the capital lease obligation was $14.8 million. The Company has entered into a separate interest rate swap agreement designated as a non-hedging instrument that resulted in a swap fixed rate of 3.55%. This interest rate swap agreement matures in 2016 and converts the nature of the capital lease obligation from Euribor floating rate debt to fixed rate debt. The fair value of the interest rate swap liability as of May 1, 2010 was approximately $1.0 million.

On September 19, 2006, the Company and certain of its subsidiaries entered into a credit facility led by Bank of America, N.A., as administrative agent for the lenders (the Credit Facility). The Credit Facility provides for an $85 million revolving multicurrency line of credit and is available for direct borrowings and the issuance of letters of credit, subject to certain letters of credit sublimits. The Credit Facility is scheduled to mature on September 30, 2011. At May 1, 2010, the Company had $12.5 million in outstanding standby letters of credit, no outstanding documentary letters of credit and no outstanding borrowings under the Credit Facility.

The Company, through its European subsidiaries, maintains short-term borrowing agreements, primarily for working capital purposes, with various banks in Europe. Under these agreements, which are generally secured by specific accounts receivable balances, the Company can borrow up to $218.7 million, limited primarily by accounts receivable balances at the time of borrowing. Based on the applicable accounts receivable balances at May 1, 2010, the Company could have borrowed up to approximately $210.9 million under these agreements. However, the Company s ability to borrow through foreign subsidiaries is generally limited to $185.0 million under the terms of the Credit Facility. At May 1, 2010, the Company had no outstanding borrowings and $11.8 million in outstanding documentary letters of credit under these credit agreements. The agreements are primarily denominated in euros and provide for annual interest rates ranging from 0.7% to 3.5%. The maturities of the short-term borrowings are generally linked to the credit terms of the underlying accounts receivable that secure the borrowings. With the exception of one facility for $19.9 million that has a minimum net equity requirement, there are no other financial ratio covenants.

From time to time the Company will obtain other short term financing in foreign countries for working capital to finance its local operations.

(9) Share-Based Compensation

The following table summarizes the share-based compensation expense recognized under all of the Company s stock plans during the three months ended May 1, 2010 and May 2, 2009 (in thousands):

	Three Months Ended	
	May 1, 2010	May 2, 2009
Stock options	$ 1,859	$ 1,547
Nonvested stock awards/units	6,115	5,062
Employee Stock Purchase Plan	94	155
Total share-based compensation expense	$ 8,068	$ 6,764

Unrecognized compensation cost related to nonvested stock options and nonvested stock awards/units totaled approximately $16.7 million and $38.9 million, respectively, as of May 1, 2010. This unrecognized expense assumes the performance-based equity awards vest in the future. This cost is expected to be recognized over a weighted-average period of 1.7 years. The weighted average fair values of stock options granted during the three months ended May 1, 2010 and May 2, 2009 were $15.38 and $8.88, respectively.

On April 29, 2010, the Company made an annual grant of 237,400 stock options and 230,300 nonvested stock awards/units to its employees. On April 14, 2009, the Company made an annual grant of 1,105,400 stock options and 106,400 nonvested stock awards/units to its employees.

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On May 1, 2008, the Company granted an aggregate of 167,000 nonvested stock awards to certain employees which are subject to certain annual performance-based vesting conditions over a five-year period. On October 30, 2008, the Company granted an aggregate of 563,400 nonvested stock options to certain employees scheduled to vest over a four-year period, subject to the achievement of performance-based vesting conditions for fiscal 2010. During the first quarter of fiscal 2010, the Compensation Committee determined that the performance goals established in the prior year were no longer set at an appropriate level to incentivize and help retain employees given the greater than previously anticipated deterioration of the economy that had occurred since the goals were established. Therefore, in April 2009, the Compensation Committee modified the performance goals of that year s tranche of the outstanding performance-based stock awards and options to address the challenges associated with the economic environment. During the first quarter of fiscal 2011, the Compensation Committee modified the performance goals of the current year tranche of the outstanding performance based stock awards to address the continuing challenges associated with the economic environment. None of the modifications had a material impact on the consolidated financial statements of the Company.

(10) Related Party Transactions

The Company and its subsidiaries periodically enter into transactions with other entities or individuals that are considered related parties, including certain transactions with entities affiliated with trusts for the respective benefit of Maurice and Paul Marciano, who are executives of the Company, Armand Marciano, their brother and former executive of the Company, and certain of their children (the Marciano Trusts).

Leases

The Company leases warehouse and administrative facilities, including the Company s corporate headquarters in Los Angeles, California, from partnerships affiliated with the Marciano Trusts and certain of their affiliates. There were three of these leases in effect at May 1, 2010 with expiration dates in February 2011, December 2015 and July 2018.

Aggregate rent expense under these related party leases for both of the three months ended May 1, 2010 and May 2, 2009 was $1.0 million. The Company believes the related party lease terms have not been significantly affected by the fact that the Company and the lessors are related.

Aircraft Arrangements

The Company periodically charters aircraft owned by MPM Financial, LLC (MPM Financial), an entity affiliated with the Marciano Trusts, through an independent third party management company contracted by MPM Financial to manage its aircraft. Under an informal arrangement with MPM Financial and the third party management company, the Company has chartered and may from time to time continue to charter aircraft owned by MPM Financial at a discount from the third party management company s preferred customer hourly charter rates. The total fees paid under these arrangements for the three months ended May 1, 2010 and May 2, 2009 were approximately $0.2 million and $0.1 million, respectively.

These related party disclosures should be read in conjunction with the disclosure concerning related party transactions in the Company s Annual Report on Form 10-K for the year ended January 30, 2010.

(11) Commitments and Contingencies

Leases

The Company leases its showrooms and retail store locations under operating lease agreements expiring on various dates through September 2027. Some of these leases require the Company to make periodic payments for property taxes, utilities and common area operating expenses. Certain retail store leases provide for rents based upon the minimum annual rental amount and a percentage of annual sales volume, generally ranging from 3% to 6%, when specific sales volumes are exceeded. Some leases include lease incentives, rent abatements and fixed rent escalations, which are amortized and recorded over the initial lease term on a straight-line basis. The Company also leases some of its equipment under operating lease agreements expiring at various dates through January 2016.

Incentive Bonuses

Certain officers and key employees of the Company are eligible to receive annual cash incentive bonuses based on the achievement of certain performance criteria. These bonuses are based on performance measures such as earnings per share and earnings from operations of the Company or particular segments thereof, as well as other objective and subjective criteria as determined by the Compensation Committee of the Board of Directors. In addition to such annual incentive opportunities, Paul Marciano, Chief Executive Officer and Vice Chairman of the Company, is entitled to receive a $3.5 million special cash bonus in December 2012, subject to the receipt by the Company of a fixed cash rights payment of $35.0 million that is due in January 2012 from one of its licensees. In connection with this special bonus, the Company will accrue an expense of $3.5 million, plus applicable payroll taxes, through December 2012.

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Litigation

On May 6, 2009, Gucci America, Inc. filed a complaint in the U.S. District Court for the Southern District of New York against Guess?, Inc. and Guess Italia, S.r.l. asserting, among other things, trademark and trade dress law violations and unfair competition. The complaint seeks injunctive relief, unspecified compensatory damages, including treble damages, and certain other relief. A similar complaint has also been filed in the Court of Milan, Italy. The Company plans to defend the allegations vigorously. The Company believes that it is too early to predict the outcome of this action or whether the outcome will have a material impact on the Company s financial position or results of operations.

The Company is also involved in various other claims and other matters incidental to the Company s business, the resolution of which is not expected to have a material adverse effect on the Company s financial position or results of operations. No material amounts were accrued as of May 1, 2010 related to any of the Company s legal proceedings.

(12) Supplemental Executive Retirement Plan

The components of net periodic pension cost for the three months ended May 1, 2010 and May 2, 2009 were as follows (in thousands):

	Three Months Ended	
	May 1, 2010	May 2, 2009
Service cost	$ 69	$ 53
Interest cost	558	513
Net amortization of unrecognized prior service cost	436	436
Net amortization of actuarial losses	140	
Curtailment expense	5,819	
Net periodic defined benefit pension cost	$ 7,022	$ 1,002

As a non-qualified pension plan, no funding of the SERP is required. However, the Company expects to make periodic payments into insurance policies held in a rabbi trust to fund the expected obligations arising under the non-qualified SERP. The cash surrender values of the insurance policies were $25.8 and $22.1 million as of May 1, 2010 and January 30, 2010, respectively, and were included in other assets. The amount of future payments may vary, depending on the future years of service, future annual compensation of the participants and investment performance of the trust. As a result of an increase in value of the insurance policy investments, the Company recorded gains of $1.3 million and $1.2 million in other income and expense during the three months ended May 1, 2010 and May 2, 2009, respectively.

During the three months ended May 1, 2010, the Company recorded a plan curtailment expense of $5.8 million before taxes related to the accelerated amortization of prior service cost resulting from the departure of Carlos Alberini, the Company s former President and Chief Operating Officer. Mr. Alberini s departure resulted in a significant reduction in the total expected remaining years of future service of all participants combined, triggering the pension curtailment.

(13) Fair Value Measurements

Authoritative guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The guidance establishes a fair value hierarchy, which prioritizes the inputs used in measuring fair value into three broad levels as follows:

Level 1 - Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that can be accessed at the measurement date.

Level 2 - Inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (i.e. interest rates, yield curves, etc.), and inputs that are derived principally from or corroborated by observable market data by correlation or other means (market corroborated inputs).

Level 3 - Unobservable inputs that reflect assumptions about what market participants would use in pricing the asset or liability. These inputs would be based on the best information available, including the Company s own data.

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The following table presents the fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of May 1, 2010 and January 30, 2010 (in thousands):

	Fair Value Measurements at May 1, 2010				Fair Value Measurements at Jan. 30, 2010			
Recurring Fair Value Measures	**Level 1**	**Level 2**	**Level 3**	**Total**	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets:								
Foreign exchange forward contracts	$	$ 12,183	$	$ 12,183	$	$ 8,075	$	$ 8,075
Securities available for sale	590			590	399			399
Total	$ 590	$ 12,183	$	$ 12,773	$ 399	$ 8,075	$	$ 8,474
Liabilities:								
Foreign exchange forward contracts	$	$ 2,584	$	$ 2,584	$	$ 922	$	$ 922
Interest rate swaps		1,352		1,352		1,231		1,231
Deferred compensation obligations		7,970		7,970		6,677		6,677
Total	$	$ 11,906	$	$ 11,906	$	$ 8,830	$	$ 8,830

The fair values of the Company s available-for-sale securities are based on quoted prices. Fair value of the interest rate swaps are based upon inputs corroborated by observable market data. The foreign exchange forward contracts are entered into by the Company principally to hedge the future payment of inventory and intercompany transactions by non-U.S. subsidiaries. The fair values of the Company s foreign exchange forward contracts are based on quoted forward foreign exchange prices at the reporting date. Deferred compensation obligations to employees are adjusted based on changes in the fair value of the underlying employee-directed investments. Fair value of these obligations is based upon inputs corroborated by observable market data.

Long-term investments are recorded at fair value and consist of certain marketable equity securities of $0.6 million and $0.4 million at May 1, 2010 and January 30, 2010, respectively, and are included in other assets in the accompanying condensed consolidated balance sheets. Unrealized gains (losses), net of taxes, are included as a component of stockholders equity and comprehensive income. The accumulated unrealized gains (losses), net of taxes, included in accumulated other comprehensive income relating to marketable equity securities owned by the Company at May 1, 2010 and January 30, 2010, were $0.1 million and ($0.1) million, respectively.

The carrying amount of the Company s remaining financial instruments, which principally include cash and cash equivalents, trade receivables, accounts payable and accrued expenses, approximates fair value due to the relatively short maturity of such instruments. The fair values of the Company s debt instruments (see Note 8) are based on the amount of future cash flows associated with each instrument discounted using the Company s incremental borrowing rate. At May 1, 2010, the carrying value of all financial instruments was not materially different from fair value, as the interest rates on variable rate debt including the capital lease obligation approximated rates currently available to the Company.

Long-lived assets, such as property, plant, and equipment, and purchased intangibles that are subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The recoverability of assets that are to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by such asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of such asset exceeds the estimated discounted future cash flows. The impairment loss calculations require management to apply judgment in estimating future cash flows and the discount rates that reflect the risk inherent in the future cash flows. The estimated cash flows used for this nonrecurring fair value measurement is considered a Level 3 input as defined above.

(14) Derivative Financial Instruments

Hedging Strategy

The Company operates in foreign countries, which exposes it to market risk associated with foreign currency exchange rate fluctuations. The Company has entered into certain forward contracts to hedge the risk of foreign currency rate fluctuations. The Company has elected to apply the hedge accounting rules in accordance with authoritative guidance for certain of these hedges.

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The Company s objective is to hedge the variability in forecasted cash flows due to the foreign currency risk. Various transactions that occur in Canada, Europe and South Korea are denominated in U.S. dollars, British pounds or Swiss francs and thus are exposed to earnings risk as a result of exchange rate fluctuations when converted to their local functional currencies. These types of transactions include U.S. dollar denominated purchases of merchandise and U.S. dollar and British pound intercompany liabilities. In addition, certain sales and operating expenses are denominated in Swiss francs and are exposed to earnings risk as a result of exchange rate fluctuations when converted to the functional currency. The Company enters into derivative financial instruments, including forward exchange contracts to manage exchange risk on certain anticipated foreign currency transactions. The Company does not hedge all transactions denominated in foreign currency.

The impact of the credit risk of the counterparties to the derivative contracts is considered in determining the fair value of the foreign currency forward contracts. As of May 1, 2010, credit risk has not had a significant effect on the fair value of the Company s foreign currency contracts.

The Company also has interest rate swap agreements, which are not designated as hedges for accounting purposes, to effectively convert its floating-rate capital lease obligation to a fixed-rate basis. The principal objective of these contracts is to eliminate or reduce the variability of the cash flows in interest payments associated with the Company s variable rate capital lease obligation, thus reducing the impact of interest rate changes on future interest cash flows. Refer to Note 8 for further information.

Hedge Accounting Policy

U.S. dollar forward contracts are used to hedge forecasted merchandise purchases over specific months. Changes in the fair value of these U.S. dollar forward contracts, designated as cash flow hedges, are recorded as a component of accumulated other comprehensive income within stockholders equity, and are recognized in cost of product sales in the period which approximates the time the hedged merchandise inventory is sold. The Company also hedges forecasted intercompany royalties over specific months. Changes in the fair value of these U.S. dollar forward contracts designated as cash flow hedges are recorded as a component of accumulated other comprehensive income within stockholders equity, and are recognized in other income/expense in the period in which the royalty expense is incurred.

From time to time, Swiss franc forward contracts are used to hedge certain anticipated Swiss operating expenses over specific months. Changes in the fair value of Swiss franc forward contracts designated as cash flow hedges are recorded as a component of accumulated other comprehensive income within stockholders equity, and are recognized in SG&A in the period which approximates the time the expenses are incurred.

The Company also has foreign currency contracts that are not designated as hedges for accounting purposes. Changes in fair value of foreign currency contracts not qualifying as cash flow hedges are reported in net earnings as part of other income and expense.

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Summary of Derivative Instruments

The fair value of derivative instruments in the condensed consolidated balance sheet as of May 1, 2010 and January 30, 2010 was as follows (in thousands):

	Derivative Balance Sheet Location	Fair Value at May 1, 2010	Fair Value at January 30, 2010
ASSETS:			
Derivatives designated as hedging instruments:			
Foreign exchange currency contracts	Other current assets	$ 4,759	$ 3,351