Citi Trends Inc
Form 10-Q
May 30, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

x	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	For the quarterly period ended May 3, 2008
	OR
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File Number 000-51315

CITI TRENDS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE (State or other jurisdiction of incorporation or organization)	**52-2150697** (I.R.S. Employer Identification No.)
104 Coleman Boulevard **Savannah, Georgia** (Address of principal executive offices)	**31408** (Zip Code)

Registrant s telephone number, including area code **(912) 236-1561**

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

Large accelerated filer o	Accelerated filer x
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

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

Class	**Outstanding at May 16, 2008**
Common Stock, $.01 par value	14,268,700 shares

CITI TRENDS, INC.

FORM 10-Q

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Item 1. Financial Statements.

Citi Trends, Inc.

Condensed Balance Sheets

May 3, 2008 and February 2, 2008

(Unaudited)

(in thousands, except share data)

	May 3, 2008	February 2, 2008
Assets		
Current assets:		
Cash and cash equivalents	$ 4,697	$ 6,203
Investment securities		56,165
Inventory	83,258	82,420
Prepaid and other current assets	7,213	5,888
Deferred tax asset	3,221	2,838
Total current assets	98,389	153,514
Property and equipment, net	55,555	52,207
Investment securities	53,720	
Goodwill	1,371	1,371
Deferred tax asset	4,174	2,756
Other assets	353	329
Total assets	$ 213,562	$ 210,177
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 42,221	$ 43,566
Accrued expenses	10,311	11,864
Accrued compensation	3,938	5,225
Current portion of capital lease obligations	1,591	1,580
Income tax payable	3,228	1,155
Layaway deposits	1,460	635
Total current liabilities	62,749	64,025
Capital lease obligations, less current portion	988	1,403
Other long-term liabilities	7,168	6,602
Total liabilities	70,905	72,030
Stockholders equity:		
Common stock, $0.01 par value. Authorized 32,000,000 shares; 14,434,330 shares issued as of May 3, 2008 and 14,265,471 shares issued as of February 2, 2008; 14,268,580 shares outstanding as of May 3, 2008 and 14,099,721 outstanding as of February 2, 2008	142	142
Paid-in-capital	68,989	68,276
Retained earnings	75,062	69,894
Accumulated other comprehensive loss	(1,371)	
Treasury stock, at cost; 165,750 shares as of May 3, 2008 and February 2, 2008	(165)	(165)

Total stockholders equity		142,657		138,147
Commitments and contingencies (note 7)				
Total liabilities and stockholders equity	$	213,562	$	210,177

See accompanying notes to the condensed financial statements (unaudited).

Citi Trends, Inc.

Condensed Statements of Income

Thirteen Weeks Ended May 3, 2008 and May 5, 2007

(Unaudited)

(in thousands, except per share data)

	May 3, 2008	May 5, 2007
Net sales	$ 120,996	$ 106,576
Cost of sales	74,233	64,878
Gross profit	46,763	41,698
Selling, general and administrative expenses	36,241	30,575
Depreciation and amortization	3,703	2,821
Income from operations	6,819	8,302
Interest income	868	645
Interest expense	(87)	(144)
Income before income tax expense	7,600	8,803
Income tax expense	2,432	3,081
Net income	$ 5,168	$ 5,722
Basic net income per common share	$ 0.37	$ 0.41
Diluted net income per common share	$ 0.36	$ 0.40
Weighted average number of shares outstanding		
Basic	14,048	13,807
Diluted	14,217	14,219

See accompanying notes to the condensed financial statements (unaudited).

Citi Trends, Inc.

Condensed Statements of Cash Flows

Thirteen Weeks Ended May 3, 2008 and May 5, 2007

(Unaudited)

(in thousands)

	May 3, 2008	May 5, 2007
Operating activities:		
Net income	$ 5,168	$ 5,722
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,703	2,821
Loss on disposal of property and equipment	7	7
Deferred income taxes	(917)	(440)
Noncash stock-based compensation expense	445	310
Excess tax benefits from stock-based payment arrangements	(209)	(332)
Changes in assets and liabilities:		
Inventory	(838)	(12,037)
Prepaid and other current assets	(429)	(86)
Other assets	(24)	(12)
Accounts payable	(1,345)	(675)
Accrued expenses and other long-term liabilities	(987)	(27)
Accrued compensation	(1,287)	(2,745)
Income tax payable	2,282	2,777
Layaway deposits	825	619
Net cash provided by (used in) operating activities	6,394	(4,098)
Investing activities:		
Purchases of investment securities	(4,222)	(2,617)
Sales of investment securities	3,516	6,974
Purchases of property and equipment	(7,058)	(4,112)
Net cash (used in) provided by investing activities	(7,764)	245
Financing activities:		
Repayments on long-term debt and capital lease obligations	(404)	(511)
Excess tax benefits from stock-based payment arrangements	209	332
Proceeds from the exercise of stock options	127	49
Cash used to settle equity instruments granted under stock-based payment arrangements	(68)	
Net cash used in financing activities	(136)	(130)
Net decrease in cash and cash equivalents	(1,506)	(3,983)
Cash and cash equivalents:		
Beginning of period	6,203	7,707
End of period	$ 4,697	$ 3,724
Supplemental disclosures of cash flow information:		
Cash paid for interest	$ 82	$ 176
Cash paid for income taxes	$ 1,303	$ 852
Supplemental disclosures of noncash financing and investing activities:		
Cumulative effect of adoption of FIN 48	$	$ 301

See accompanying notes to the condensed financial statements (unaudited).

Citi Trends, Inc.

Notes to the Condensed Financial Statements (unaudited)

May 3, 2008

1. Basis of Presentation

The condensed balance sheet as of May 3, 2008 and the condensed statements of income and cash flows for the thirteen-week periods ended May 3, 2008 and May 5, 2007 have been prepared by Citi Trends, Inc. (the Company), without audit. The condensed balance sheet as of February 2, 2008 has been derived from the audited financial statements as of that date, but does not include all required year end disclosures. In the opinion of management, such statements include all adjustments considered necessary to present fairly the Company s financial position as of May 3, 2008 and February 2, 2008, and its results of operations and cash flows for all periods presented. It is suggested that these condensed financial statements be read in conjunction with the financial statements and the notes thereto included in the Company s latest Annual Report on Form 10-K for the year ended February 2, 2008.

The accompanying unaudited condensed financial statements are also prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the interim period ended May 3, 2008 are not necessarily indicative of the results that may be expected for the fiscal year ending January 31, 2009.

The following contains references to years 2008 and 2007, which represent fiscal years ending or ended on January 31, 2009 (fiscal 2008) and February 2, 2008 (fiscal 2007), respectively. Fiscal 2008 and fiscal 2007 both have 52-week accounting periods.

2. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Earnings per Share

Basic earnings per common share amounts are calculated using the weighted average number of common shares outstanding for the period. Diluted earnings per common share amounts are calculated using the weighted average number of common shares outstanding plus the potential common shares that would have been outstanding upon the assumed exercise of all dilutive stock options and vesting of nonvested restricted stock. During loss periods, diluted earnings per share amounts are based on the weighted average number of common shares outstanding.

The following table provides a reconciliation of the average number of common shares outstanding used to calculate basic earnings per share to the number of common shares and common stock equivalents outstanding used in calculating diluted earnings per share for the thirteen weeks ended May 3, 2008 and May 5, 2007:

	Thirteen Weeks Ended	
	May 3, 2008	**May 5, 2007**
Average number of common shares outstanding	14,047,841	13,807,134
Incremental shares from assumed exercises of stock options	168,739	411,500
Average number of common shares and common stock equivalents outstanding	14,216,580	14,218,634

In accordance with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 128, *Earnings per Share*, the Company calculates the dilutive effect of stock-based compensation arrangements using the treasury stock method. This method assumes that the proceeds the Company receives from the exercise of stock options are used to repurchase common shares in the market. In accordance with SFAS No. 123R, *Share-Based Payment,* the Company includes as assumed proceeds the amount of compensation cost attributed to future services and not yet recognized, and the amount of tax benefits, if any, that would be credited to additional paid-in capital assuming exercise of outstanding options and vesting of nonvested restricted stock. For the thirteen weeks ended May 3, 2008 and May 5, 2007, there were 81,000 and 2,000 options outstanding, respectively, to purchase shares of common stock excluded from the calculation of diluted earnings per share because of antidilution. For the thirteen weeks ended May 3, 2008 and May 5, 2007, there were no shares of nonvested restricted stock included in the calculation of diluted earnings per share because of antidilution.

4. Fair Value Measurement

Effective February 3, 2008, the Company adopted the methods of fair value as described in SFAS No. 157, *Fair Value Measurements,* to value its financial assets and liabilities. SFAS No. 157 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 in the principal or most advantageous market at the measurement date. This statement also establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable prices that are based on inputs not quoted on active markets, but corroborated by market data.

Level 3: Unobservable inputs are used when little or no market data is available. Level 3 inputs are given the lowest priority in the fair value hierarchy.

The Company s assets carried at fair value on a recurring basis are as follows at May 3, 2008 (in thousands):

	Level 3
Auction rate securities	$ 53,720

Investment securities on the condensed balance sheets consist exclusively of municipal auction rate securities (ARS) issued by student loan funding organizations. These securities are high-grade (AAA rated with at least one rating agency) and approximately 84% of them are either guaranteed by the Department of Education under the Federal Family Education Loan Program (40%) or backed by insurance companies, AMBAC Assurance Corporation (35%) and MBIA Insurance Corporation (9%). Historically, the ARS provided liquidity via an auction process that reset the interest rate every 35 days, allowing investors to either roll over their investments or sell them at par. Beginning in February 2008, there was insufficient demand for these types of investments during the auctions and, as a result, these securities are not currently liquid. The Company may not be able to access cash by selling these securities without incurring a loss of principal until either, liquidity returns to the auction process, a secondary market emerges, they are redeemed by the issuer, or they mature in years ranging from 2010 to 2040.

The Company classifies its ARS as available-for-sale and, therefore, they are carried at estimated fair value. As of May 3, 2008, there was insufficient observable market information available to determine the fair value of the Company s ARS. Accordingly, the Company estimated Level 3 fair values for these securities based on assumptions that market participants would use in their estimates of fair value. These assumptions included, among other things, discounted cash flow projections, the timing of expected future successful auctions, collateralization of the underlying securities and the credit worthiness of the issuer. Through February 2, 2008, the ARS were valued at par value due to the frequent resets that historically occurred through the auction process.

As a result of the temporary declines in fair value for the Company s ARS, which the Company attributes to current liquidity issues rather than credit issues, it has recorded an unrealized loss of $1,371,000 (net of tax) to accumulated other comprehensive loss in the condensed balance sheet as of May 3, 2008. The Company believes the current illiquid conditions are temporary in nature and that it has the ability to hold the ARS until liquidity returns to the market. If it is later determined that the fair value of these securities is other-than-temporarily impaired, the Company will record a loss in the statement of income. Due to the Company s belief that the market for these investments may take in excess of twelve months to fully recover, the Company has classified them as noncurrent assets on the accompanying condensed balance sheet as of May 3, 2008.

5. Comprehensive Income

The components of comprehensive income for the thirteen weeks ended May 3, 2008 are as follows (in thousands):

Net income, as reported reported	$	5,168
Other comprehensive loss: loss:		
Unrealized loss on available-for-sale securities, net of tax of $884		(1,371)
Comprehensive income	$	3,797

6. Revolving Line of Credit

In March 2008, the Company obtained a $35 million unsecured revolving credit facility with Bank of America, replacing a $3 million facility that had been scheduled to expire on June 30, 2008. The $35 million facility has a term of 364 days, has an unused commitment fee equal to 0.15%, and has one restrictive financial covenant (adjusted leverage ratio). Loans under the facility bear interest at either (a) a rate equal to the higher of (i) the Federal Funds Rate plus 0.50% and (ii) Bank of America s prime rate, plus an applicable margin; or (b) a rate equal to LIBOR plus an applicable margin. The applicable margin is dependent on the Company s adjusted leverage ratio and ranges from 1.00% to 1.50% for LIBOR-based loans, and from 0.00% to 0.50% for prime rate-based loans. The Company has had no borrowings under this facility.

7. Commitments and Contingencies

The Company from time to time is involved in various legal proceedings incidental to the conduct of its business, including claims by customers, employees or former employees. While litigation is subject to uncertainties and the outcome of any litigated matter is not predictable, the Company is not aware of any legal proceedings pending or threatened against it that it expects to have a material adverse effect on its financial condition, results of operations or liquidity.

8. Recent Accounting Pronouncements

Effective February 3, 2008, the Company adopted SFAS No. 157, *Fair Value Measurements.* SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and requires additional disclosures about fair value measurements. SFAS No. 157 applies to fair value measurements that are already required or permitted by other accounting standards, except for measurements of share-based payments and measurements that are similar to, but not intended to be, fair value and does not change existing guidance as to whether or not an instrument is carried at fair value. In February 2008, the FASB issued FASB Staff Position No. 157-2, *Partial Deferral of the Effective Date of Statement No. 157,* which provides a one year deferral of the effective date of SFAS No. 157 for non-financial assets and non-financial liabilities, except those that are recognized or disclosed in the financial statements at fair value at least annually. Therefore, the Company has adopted the provisions of SFAS No. 157 with respect to its financial assets and financial liabilities only. The adoption of this statement did not have a material impact on the Company s financial statements. See related disclosures in Note 4.

Effective February 3, 2008, the Company adopted SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*.   SFAS No. 159 permits entities to choose to measure specified financial assets and financial liabilities at fair value. Election of the fair value option is irrevocable and is applied on a contract-by-contract basis. The Company has elected not to apply the fair value option to the specified financial assets and financial liabilities, and accordingly, the adoption of SFAS No. 159 had no financial statement impact.

9. Reclassifications

Certain prior year amounts have been reclassified to conform to current year presentation. The decrease of cash and accounts payable through a reclassification of outstanding checks for all prior periods caused net cash used in operating activities shown in the statements of cash flows to increase by $1,012,000 from that previously reported for the thirteen weeks ended May 5, 2007.

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

Forward-Looking Statements

Except for specific historical information, many of the matters discussed in this Form 10-Q may express or imply projections of revenues or expenditures, statements of plans and objectives for future operations, growth or initiatives, statements of future economic performance, or statements regarding the outcome or impact of pending or threatened litigation. These, and similar statements, are forward-looking statements concerning matters that involve risks, uncertainties and other factors that may cause the actual performance of the Company to differ materially from those expressed or implied by these statements. All forward-looking information should be evaluated in the context of these risks, uncertainties and other factors. The words believe, anticipate, project, plan, expect, estimate, objective, forecast, goal, intend, or will continue and similar words and expressions generally identify forward-looking statements. The Company believes the assumptions underlying these forward-looking statements are reasonable; however, any of the assumptions could be inaccurate, and therefore, actual results may differ materially from those projected in the forward-looking statements.

The factors that may result in actual results differing from such forward-looking information include, but are not limited to: transportation and distribution delays or interruptions; changes in freight rates; the Company s ability to negotiate effectively the cost and purchase of merchandise; inventory risks due to shifts in market demand; the Company s ability to gauge fashion trends and changing consumer preferences; changes in consumer spending on apparel; changes in product mix; interruptions in suppliers businesses; interest rate fluctuations; a deterioration in general economic conditions caused by acts of war or terrorism or other factors; temporary changes in demand due to weather patterns; seasonality of the Company s business; delays associated with building, opening and operating new stores; delays associated with building, opening, expanding or converting new or existing distribution centers; and other factors described in the section titled Item 1A. Risk Factors and elsewhere in the Company s Annual Report on Form 10-K for the fiscal year ended February 2, 2008 and in Part II, Item 1A. Risk Factors and elsewhere in the Company s Quarterly Reports on Form 10-Q and in the other documents the Company files with the Securities and Exchange Commission (SEC), including other reports on Form 8-K and 10-Q, and any amendments thereto.

Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this Form 10-Q. Except as may be required by law, the Company undertakes no obligation to update or revise publicly any forward-looking statements contained herein to reflect events or circumstances occurring after the date of this Form 10-Q or to reflect the occurrence