

Macy's, Inc.  
Form 10-Q  
December 08, 2008  
**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

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

For the quarterly period ended November 1, 2008

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: 1-13536

**Macy's, Inc.**  
Incorporated in Delaware

I.R.S. Employer Identification No.

7 West Seventh Street

13-3324058

Cincinnati, Ohio 45202

(513) 579-7000

**UNITED STATES**

and

151 West 34<sup>th</sup> Street

New York, New York 10001

(212) 494-1602

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, 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.

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

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

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

| <u>Class</u>                             | <u>Outstanding at November 28, 2008</u> |
|--|---|
| Common Stock, \$0.01 par value per share | 420,563,487 shares                      |

**PART I -- FINANCIAL INFORMATION****Item 1. Financial Statements****MACY'S, INC.****Consolidated Statements of Operations****(Unaudited)****(millions, except per share figures)**

|  | <b>13</b>           |                     | <b>39</b>           |                     |
|--|---------------------|---------------------|---------------------|---------------------|
|  | <b>Weeks</b>        |                     | <b>Weeks</b>        |                     |
|  | <b>Ended</b>        |                     | <b>Ended</b>        |                     |
|  | November 1,<br>2008 | November 3,<br>2007 | November 1,<br>2008 | November 3,<br>2007 |
| Net sales.....   | \$ 5,493            | \$ 5,906            | \$16,958            | \$17,719            |
| Cost of sales.....   | <u>(3,324)</u>      | <u>(3,585)</u>      | <u>(10,197)</u>     | <u>(10,656)</u>     |
| Gross margin.....  | 2,169               | 2,321               | 6,761               | 7,063               |
| Selling, general and administrative expenses.                        | (2,085)             | (2,121)             | (6,225)             | (6,272)             |
| Division consolidation costs.....                                    | (16)                | -                   | (129)               | -                   |
| May integration costs.....   | -                   | (17)                | -                   | (150)               |
| Asset impairment charges.....  | <u>—</u>            | <u>—</u>            | <u>(50)</u>         | <u>—</u>            |
| Operating income.....  | 68                  | 183                 | 357                 | 641                 |
| Interest expense.....  | (151)               | (149)               | (440)               | (432)               |
| Interest income.....   | <u>8</u>            | <u>4</u>            | <u>23</u>           | <u>25</u>           |
| Income (loss) from continuing operations<br>before income taxes..... | (75)                | 38                  | (60)                | 234                 |
| Federal, state and local income<br>tax benefit (expense).....        | <u>31</u>           | <u>(5)</u>          | <u>30</u>           | <u>(75)</u>         |
| Income (loss) from continuing operations.....                        | (44)                | 33                  | (30)                | 159                 |
| Discontinued operations, net of income taxes....                     | <u>—</u>            | <u>—</u>            | <u>—</u>            | <u>(16)</u>         |

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|  |                 |               |                 |               |
|--|-----------------|---------------|-----------------|---------------|
| Net income (loss).....                       | \$ <u>(44)</u>  | \$ <u>33</u>  | \$ <u>(30)</u>  | \$ <u>143</u> |
| Basic earnings (loss) per share:             |                 |               |                 |               |
| Income (loss) from continuing operations.... | \$ (.10)        | \$ .08        | \$ (.07)        | \$ .35        |
| Loss from discontinued operations.....       | <u>-</u>        | <u>-</u>      | <u>-</u>        | <u>(.03)</u>  |
| Net income (loss).....                       | \$ <u>(.10)</u> | \$ <u>.08</u> | \$ <u>(.07)</u> | \$ <u>.32</u> |
| Diluted earnings (loss) per share:           |                 |               |                 |               |
| Income (loss) from continuing operations.... | \$ (.10)        | \$ .08        | \$ (.07)        | \$ .35        |
| Loss from discontinued operations.....       | <u>-</u>        | <u>-</u>      | <u>-</u>        | <u>(.04)</u>  |
| Net income (loss).....                       | \$ <u>(.10)</u> | \$ <u>.08</u> | \$ <u>(.07)</u> | \$ <u>.31</u> |

The accompanying notes are an integral part of these unaudited Consolidated Financial Statements.

**Consolidated Balance Sheets**

**(Unaudited)**

**(millions)**

|  | November 1,<br>2008 | February 2,<br>2008 | November 3,<br>2007 |
|--|---------------------|---------------------|---------------------|
| <b>ASSETS:</b>   |                     |                     |                     |
| Current Assets:  |                     |                     |                     |
| Cash and cash equivalents.....   | \$ 300              | \$ 583              | \$ 275              |
| Receivables.....   | 367                 | 463                 | 459                 |
| Merchandise inventories.....   | 6,915               | 5,060               | 7,012               |
| Income tax receivable.....   | 43                  | -                   | -                   |
| Supplies and prepaid expenses.....   | <u>246</u>          | <u>218</u>          | <u>261</u>          |
| Total Current Assets.....  | 7,871               | 6,324               | 8,007               |
| Property and Equipment - net of accumulated<br>depreciation and amortization of<br>\$5,966, \$5,139 and \$5,438..... | 10,616              | 10,991              | 11,072              |
| Goodwill.....  | 9,123               | 9,133               | 9,139               |
| Other Intangible Assets - net.....   | 747                 | 831                 | 842                 |
| Other Assets.....  | <u>547</u>          | <u>510</u>          | <u>609</u>          |
| Total Assets.....  | <u>\$28,904</u>     | <u>\$27,789</u>     | <u>\$29,669</u>     |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY:</b>  |                     |                     |                     |
| Current Liabilities:   |                     |                     |                     |
| Short-term debt.....   | \$ 1,086            | \$ 666              | \$ 1,634            |
| Accounts payable and accrued liabilities.....  | 5,687               | 4,127               | 5,757               |
| Income taxes.....  | -                   | 344                 | 6                   |
| Deferred income taxes.....   | <u>246</u>          | <u>223</u>          | <u>253</u>          |
| Total Current Liabilities.....   | 7,019               | 5,360               | 7,650               |

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|   |                     |                     |                     |
|---|---------------------|---------------------|---------------------|
| Long-Term Debt.....                                 | 8,748               | 9,087               | 9,097               |
| Deferred Income Taxes.....                          | 1,466               | 1,446               | 1,407               |
| Other Liabilities.....                              | 1,981               | 1,989               | 2,045               |
| Shareholders' Equity.....                           | <u>9,690</u>        | <u>9,907</u>        | <u>9,470</u>        |
| <br>Total Liabilities and Shareholders' Equity..... | <br><u>\$28,904</u> | <br><u>\$27,789</u> | <br><u>\$29,669</u> |

The accompanying notes are an integral part of these unaudited Consolidated Financial Statements.

**Consolidated Statements of Cash Flows****(Unaudited)****(millions)**

|  | 39 Weeks Ended<br>November 1, 2008 | 39 Weeks Ended<br>November 3, 2007 |
|--|------------------------------------|------------------------------------|
| Cash flows from continuing operating activities:   |                                    |                                    |
| Net income (loss).....   | \$ (30)                            | \$ 143                             |
| Adjustments to reconcile net income (loss) to net cash<br>provided by continuing operating activities: |                                    |                                    |
| Loss from discontinued operations.....   | -                                  | 16                                 |
| Stock-based compensation expense.....  | 32                                 | 48                                 |
| Division consolidation costs.....  | 129                                | -                                  |
| May integration costs.....   | -                                  | 150                                |
| Asset impairment charges.....  | 50                                 | -                                  |
| Depreciation and amortization.....   | 950                                | 977                                |
| Amortization of financing costs and premium<br>on acquired debt.....                                   | (20)                               | (24)                               |
| Changes in assets and liabilities:   |                                    |                                    |
| Decrease in receivables.....   | 84                                 | 57                                 |
| Increase in merchandise inventories.....   | (1,855)                            | (1,695)                            |
| Increase in supplies and prepaid expenses.....   | (28)                               | (10)                               |
| Decrease in other assets not separately identified.....  | -                                  | 2                                  |
| Increase in accounts payable and accrued<br>liabilities not separately identified.....                 | 1,320                              | 948                                |
| Decrease in current income taxes.....  | (343)                              | (328)                              |
| Increase (decrease) in deferred income taxes.....  | 8                                  | (17)                               |
| Increase in other liabilities not separately identified.....   | <u>20</u>                          | <u>18</u>                          |
| Net cash provided by continuing operating activities.....  | <u>317</u>                         | <u>285</u>                         |
| Cash flows from continuing investing activities:   |                                    |                                    |
| Purchase of property and equipment.....  | (546)                              | (700)                              |
| Capitalized software.....  | (104)                              | (81)                               |
| Proceeds from hurricane insurance claims.....  | 19                                 | 1                                  |
| Disposition of property and equipment.....   | 25                                 | 96                                 |
| Proceeds from the disposition of After Hours Formalwear.....   | <u>-</u>                           | <u>66</u>                          |
| Net cash used by continuing investing activities.....  | <u>(606)</u>                       | <u>(618)</u>                       |
| Cash flows from continuing financing activities:   |                                    |                                    |
| Debt issued.....   |                                    | 770 2,918                          |
| Financing costs.....   |                                    | (5) (18)                           |
| Debt repaid.....   |                                    | (663) (647)                        |
| Dividends paid.....  |                                    | (166) (173)                        |
| Increase in outstanding checks.....  |                                    | 64 65                              |
| Acquisition of treasury stock.....   |                                    | (1) (3,003)                        |

|   |           |           |
|---|-----------|-----------|
| Issuance of common stock.....                                       | ___ 7     | ___ 256   |
| Net cash provided (used) by<br>continuing financing activities..... | ___ 6     | ___ (602) |
| Net cash used by continuing operations.....                         | ___ (283) | ___ (935) |
| Net cash provided by discontinued operating activities.....         | -         | 7         |
| Net cash used by discontinued investing activities.....             | -         | (7)       |
| Net cash used by discontinued financing activities.....             | ___ -     | ___ (1)   |
| Net cash used by discontinued operations.....                       | ___ -     | ___ (1)   |
| Net decrease in cash and cash equivalents.....                      | (283)     | (936)     |
| Cash and cash equivalents at beginning of period.....               | ___ 583   | ___ 1,211 |
| Cash and cash equivalents at end of period.....                     | \$ 300    | \$ 275    |
| Supplemental cash flow information:                                 |           |           |
| Interest paid.....  | \$ 461    | \$ 441    |
| Interest received.....  | 23        | 26        |
| Income taxes paid (net of refunds received).....                    | 322       | 406       |

The accompanying notes are an integral part of these unaudited Consolidated Financial Statements.

**Notes to Consolidated Financial Statements**  
**(Unaudited)**

**1. Summary of Significant Accounting Policies**

Macy's, Inc. and subsidiaries (the Company) is a retail organization operating retail stores and websites that sell a wide range of merchandise, including men's, women's and children's apparel and accessories, cosmetics, home furnishings and other consumer goods. The Company's operations include more than 850 stores in 45 states, the District of Columbia, Guam and Puerto Rico, as well as macys.com and bloomingdales.com.

A description of the Company's significant accounting policies is included in the Company's Annual Report on Form 10-K for the fiscal year ended February 2, 2008 (the 2007 10-K). The accompanying Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and notes thereto in the 2007 10-K.

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, the 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. Such estimates and assumptions are subject to inherent uncertainties, which may result in actual amounts differing from reported amounts.

The Consolidated Financial Statements for the 13 and 39 weeks ended November 1, 2008 and November 3, 2007, in the opinion of management, include all adjustments (consisting only of normal recurring adjustments) considered necessary to present fairly, in all material respects, the consolidated financial position and results of operations of the Company.

Because of the seasonal nature of the retail business, the results of operations for the 13 and 39 weeks ended November 1, 2008 and November 3, 2007 (which do not include the Christmas season) are not necessarily indicative of such results for the fiscal year.

On August 30, 2005, the Company completed the acquisition of The May Department Stores Company ( May ). The operations of the acquired Lord & Taylor division and the bridal group (consisting of David s Bridal, After Hours Formalwear and Priscilla of Boston) have been divested and were presented as discontinued operations (see Note 5, Discontinued Operations ).

Certain reclassifications were made to the prior fiscal year s amounts to conform with the classifications of such amounts for the current fiscal year.

Effective February 3, 2008, the Company adopted Statement of Financial Accounting Standards ( SFAS ) No. 157, Fair Value Measurements, ( SFAS 157 ), as it applies to financial assets and liabilities that are recognized or disclosed at fair value on a recurring basis. SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles and expands disclosures about fair value measurements. The SFAS 157 fair value hierarchy consists of three levels: Level 1 fair values are valuations based on quoted market prices in active markets for identical assets or liabilities that the Company has the ability to access; Level 2 fair values are those valuations based on quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable data for substantially the full term of the assets or liabilities; and Level 3 fair values are valuations based on inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. The adoption of SFAS 157 as it applies to financial assets and liabilities that are recognized or disclosed at fair value on a recurring basis did not have and is not expected to have an impact on the Company s consolidated financial position, results of operations or cash flows.

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In accordance with the fair value hierarchy described above, the following table shows the fair value of the Company's financial assets and liabilities that are required to be measured at fair value on a recurring basis at November 1, 2008:

|  | Total | Fair Value Measurements |         |         |
|--|-------|-------------------------|---------|---------|
|  |       | Level 1<br>(millions)   | Level 2 | Level 3 |
| Marketable equity and debt securities..... | \$ 96 | \$ 25                   | \$ 71   | \$ -    |

In February 2008, the Financial Accounting Standards Board ( FASB ) issued FASB Staff Position No. 157-2 ( FSP 157-2 ) that permits a one-year deferral for the implementation of SFAS 157 with regard to nonfinancial assets and liabilities that are not recognized or disclosed at fair value on a recurring basis (at least annually). This deferral will impact the Company's accounting for certain nonfinancial assets and liabilities accounted for under SFAS No. 142, Goodwill and Other Intangible Assets, SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, SFAS No. 143, Accounting for Asset Retirement Obligations and SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities. The Company has elected this deferral and the full adoption of SFAS 157 is not expected to have a material impact on the Company's consolidated financial position, results of operations and cash flows.

SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, ( SFAS 159 ), which provides companies with the option to report selected financial assets and liabilities at fair value, became effective for the Company beginning February 3, 2008. The adoption of this statement did not and is not expected to have an impact on the Company's consolidated financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements - an amendment of Accounting Research Bulletin ( ARB ) No. 51, ( SFAS 160 ). SFAS 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS No. 160 is effective for fiscal years beginning after December 15, 2008. The Company does not anticipate the adoption of this statement will have a material impact on the Company's consolidated financial position, results of operations or cash flows.

Also in December 2007, the FASB issued SFAS No. 141 (revised 2007), Business Combinations, ( SFAS 141R ). SFAS 141R establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. The statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141R is effective for fiscal years beginning after December 15, 2008. The adoption of this statement will affect any future acquisitions entered into by the Company, and beginning with fiscal 2009 the Company will no longer account for adjustments to acquired tax liabilities and unrecognized tax benefits as increases or decreases to goodwill. After adoption of SFAS 141R such adjustments will be accounted for in income tax expense.

In March 2008, the FASB issued SFAS No. 161, Disclosures About Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133, ( SFAS 161 ). SFAS 161 expands disclosure requirements for derivative instruments and hedging activities. SFAS 161 is effective for fiscal years beginning after November 15, 2008. The Company does not anticipate the adoption of this statement will have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles, ( SFAS 162 ). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of non-governmental entities that are presented in conformity with generally accepted accounting principles in the United States of America. SFAS 162 became effective for the Company on November 15, 2008, and the adoption of this statement did not and is not expected to have an impact on the Company's consolidated financial position, results of operations or cash flows.

## 2. Division Consolidation Costs

Division consolidation costs represent certain one-time costs related to a localization initiative, called My Macy's, and division consolidations. This initiative is to strengthen local market focus and enhance selling service to enable the Company to both accelerate same-store sales growth and reduce expenses. In combination with the localization initiative, the Company consolidated the Minneapolis-based Macy's North organization into New York-based Macy's East, the St. Louis-based Macy's Midwest organization into Atlanta-based Macy's South and the Seattle-based Macy's Northwest organization into San Francisco-based Macy's West. The Atlanta-based division was renamed Macy's Central. With My Macy's, the Company is taking action in certain markets to ensure that customers surrounding each Macy's store find merchandise assortments, size ranges, marketing programs and shopping experiences that are custom-tailored to their needs. The Company is concentrating more management talent in certain local markets, has created new positions in the field to work with division central planning and buying executives in helping to understand and act on the merchandise needs of local customers, and is empowering locally based executives to make more and better decisions. My Macy's is expected to drive sales growth by improving knowledge at the local level and then acting quickly on that knowledge.

During the 13 and 39 weeks ended November 1, 2008, the Company recorded \$16 million and \$129 million, respectively, of costs and expenses associated with the division consolidation and localization initiative, consisting primarily of severance costs and other human resource-related costs.

The following table shows the beginning and ending balance of, and the activity associated with, the severance accrual established in connection with the division consolidation and localization initiative during the 39 weeks ended November 1, 2008:

|  | February 2,<br>2008 | Charged<br>To Division<br>Consolidation<br>Costs | Payments | November 1,<br>2008 |
|--|---------------------|--|----------|---------------------|
|--|---------------------|--|----------|---------------------|

|                      |      |            |        |      |
|----------------------|------|------------|--------|------|
|                      |      | (millions) |        |      |
| Severance costs..... | \$ - | \$ 68      | \$(63) | \$ 5 |

The Company expects to pay out the accrued severance costs, which are included in accounts payable and accrued liabilities on the Consolidated Balance Sheets, prior to January 31, 2009.

### 3. May Integration Costs

May integration costs represent the costs associated with the integration of the acquired May businesses with the Company's pre-existing businesses and the consolidation of certain operations of the Company. The Company completed its review of store locations and distribution center facilities during 2007, closing certain underperforming stores, temporarily closing other stores for remodeling to optimize merchandise offering strategies, closing certain distribution center facilities, and consolidating operations in existing or newly constructed facilities. The remaining non-divested stores or facilities which have been closed, with carrying values totaling approximately \$75 million, are classified as assets held for sale and are included in other assets on the Consolidated Balance Sheets as of November 1, 2008.

During the 13 weeks ended November 3, 2007, the Company recorded \$17 million of costs and expenses associated with the integration and consolidation of May's operations into the Company's operations, including additional costs related to closed locations, severance, system conversion costs and costs related to other operational consolidations.

During the 39 weeks ended November 3, 2007, the Company recorded \$150 million of costs and expenses associated with the integration and consolidation of May's operations into the Company's operations, including \$47 million related to impairment charges in connection with distribution center facilities planned to be closed and disposed of. The remaining \$103 million of May integration costs incurred during the 39 weeks ended November 3, 2007 included additional costs related to closed locations, severance, system conversion costs, impairment charges associated with acquired indefinite lived intangible assets and costs related to other operational consolidations.

During the 39 weeks ended November 3, 2007, approximately \$80 million of property and equipment was transferred to assets held for sale upon store or facility closure. In addition, property and equipment totaling approximately \$35 million was disposed of in connection with the May integration and the Company collected approximately \$39 million of receivables from prior year dispositions.

The following tables show, for the 39 weeks ended November 1, 2008 and November 3, 2007, the beginning and ending balance of, and the activity associated with, the severance and relocation accrual established in connection with the May integration:

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|  | February 2,<br>2008 | Payments<br>(millions) | November 1,<br>2008 |
|--|---------------------|------------------------|---------------------|
| Severance and<br>relocation costs..... | \$ 30               | \$ (25)                | \$ 5                |

The Company expects to payout the accrued severance and relocation costs, which are included in accounts payable and accrued liabilities on the Consolidated Balance Sheets, prior to January 31, 2009.

|  | February 3,<br>2007 | Charged<br>To May<br>Integration<br>Costs<br>(millions) | Payments | November 3,<br>2007 |
|--|---------------------|---|----------|---------------------|
| Severance and<br>relocation costs..... | \$ 73               | \$ 21   | \$(76)   | \$ 18               |

**4. Asset Impairment Charges**

The Company reviews its goodwill and other indefinite-lived intangible assets for possible impairment on an annual basis and when events or changes in circumstances indicate that the carrying amount of the relevant assets may not be recoverable. Goodwill and other intangible assets not subject to amortization have been assigned to reporting units for purposes of impairment testing. The reporting units are the Company's retail operating divisions. The goodwill impairment test involves a two-step process. The first step is a comparison of each reporting unit's fair value to its carrying value. The Company estimates fair value based on discounted cash flows. If the carrying value of a reporting unit exceeds its estimated fair value in the first step, a second step is performed, in which a reporting unit's goodwill is written down to its implied fair value. The second step would require the Company to allocate the reporting unit fair value derived in the first step to the fair value of the reporting unit's individual assets and liabilities, with any excess of reporting unit fair value over amounts allocated to individual assets and liabilities representing the implied fair value of goodwill for that reporting unit. If the carrying value of an individual indefinite-lived intangible asset exceeds its fair value, the indefinite-lived intangible asset is written down by an amount equal to such excess.

The Company completed its annual impairment test of goodwill and indefinite-lived intangible assets during the second quarter of 2008 and concluded that no write downs or impairment charges were required at that time in relation to goodwill. However, as a result of the then current operating performance and expectations regarding future operating performance of the Karen Scott and John Ashford private brand tradenames, it was determined that the carrying values exceeded the estimated fair values and the Company recorded approximately \$50 million of asset write downs and impairment charges in relation to these indefinite-lived intangible assets.

In connection with the preparation of the Company's third quarter financial statements, management conducted a sensitivity analysis relating to the fair value of its reporting units, and concluded that no impairment of goodwill was

indicated.

This sensitivity analysis will be repeated in the Company's fourth fiscal quarter which ends January 31, 2009. It is possible that changes in circumstances, existing at that time or at other times in the future, or in the numerous variables associated with the judgments, assumptions and estimates made by the Company in assessing the appropriate valuation of its goodwill, could in the future require the Company to write down a portion of its goodwill and record related non-cash impairment charges. If the Company were required to write down a portion of its goodwill and record related non-cash impairment charges, the Company's financial position and results of operations would be adversely affected and the Company's leverage ratio for purposes of its credit agreement would increase. If such leverage ratio were to exceed the maximum permitted under its credit agreement, the Company would be in default under its credit agreement. At November 1, 2008, a write down of goodwill in excess of approximately \$3.9 billion after income tax benefit, or approximately 43% of the Company's goodwill, would have been required to cause the Company's leverage ratio to exceed the permitted maximum. Due to the seasonal nature of the Company's business, the Company's leverage ratio as determined on a quarterly basis generally is at its highest point as of the end of the Company's third fiscal quarter. Accordingly, it is expected that an even greater write down of goodwill would be required to cause the Company's leverage ratio to exceed the permitted maximum as calculated as of the end of the Company's fourth fiscal quarter.

## **5. Discontinued Operations**

In April 2007, the Company completed the sale of its After Hours Formalwear business for approximately \$66 million in cash, net of \$1 million of transaction costs. The After Hours Formalwear business represented approximately \$73 million of net assets. The Company recorded the loss on disposal of the After Hours Formalwear business of \$7 million on a pre-tax and after-tax basis, or \$.01 per diluted share.

Discontinued operations included net sales of approximately \$27 million for the 39 weeks ended November 3, 2007. No consolidated interest expense had been allocated to discontinued operations. For the 39 weeks ended November 3, 2007, the loss from discontinued operations, including the loss on disposal of the Company's After Hours Formalwear business, totaled \$22 million before income taxes, with a related income tax benefit of \$6 million.

In connection with the sale of the David's Bridal and Priscilla of Boston businesses, the Company agreed to indemnify the buyer and related parties of the buyer for certain losses or liabilities incurred by the buyer or such related parties with respect to (1) certain representations and warranties made to the buyer by the Company in connection with the sale, (2) liabilities relating to the After Hours Formalwear Business under certain circumstances, and (3) certain pre-closing tax obligations. The representations and warranties in respect of which the Company is subject to indemnification are generally limited to representations and warranties relating to the capitalization of the entities that were sold, the Company's ownership of the equity interests that were sold, the enforceability of the agreement and certain employee benefits and tax matters. The indemnity for breaches of most of these representations expired on March 31, 2008, with the exception of certain representations relating to capitalization and the Company's ownership interest, in respect of which the indemnity does not expire and is not subject to a cap or deductible.

Indemnity obligations created in connection with the sales of businesses generally do not represent added liabilities for the Company, but simply serve to protect the buyer from potential liabilities associated with particular conditions. The Company records accruals for those pre-closing obligations that are considered probable and estimable. Under FASB Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, the Company is required to record a liability for the fair value of the guarantees that are entered into subsequent to December 15, 2002. The Company has not accrued any additional amounts as a result of the indemnity arrangements summarized above as the Company believes the fair value of these arrangements is not material.

## 6. Earnings (Loss) Per Share

The following tables set forth the computation of basic and diluted earnings (loss) per share based on income (loss) from continuing operations:

|  | 13 Weeks Ended                       |            |                  |            |
|--|--------------------------------------|------------|------------------|------------|
|  | November 1, 2008                     |            | November 3, 2007 |            |
|  | Loss                                 | Shares     | Income           | Shares     |
|  | (millions, except per share figures) |            |                  |            |
| Income (loss) from continuing operations and average number of shares outstanding..... | \$ (44)                              | 420.1      | \$ 33            | 433.2      |
| Shares to be issued under deferred compensation plans.....                             | <u>      </u>                        | <u>1.2</u> | <u>      </u>    | <u>1.0</u> |
|  | \$ (44)                              | 421.3      | \$ 33            | 434.2      |
| Basic earnings (loss) per share.....   | <u>\$(.10)</u>                       |            | <u>\$.08</u>     |            |
| Effect of dilutive securities - stock options and restricted stock....                 | <u>      </u>                        | <u>-</u>   | <u>      </u>    | <u>3.9</u> |
|  | \$ (44)                              | 421.3      | \$ 33            | 438.1      |
| Diluted earnings (loss) per share.....   | <u>\$(.10)</u>                       |            | <u>\$.08</u>     |            |

|  | 39 Weeks Ended   |        |                  |        |
|--|------------------|--------|------------------|--------|
|  | November 1, 2008 |        | November 3, 2007 |        |
|  | Loss             | Shares | Income           | Shares |

**Loss**

(millions, except per share figures)

|  |                   |                |                   |              |
|--|-------------------|----------------|-------------------|--------------|
| Income (loss) from continuing operations and average number of shares outstanding..... | \$ (30)           | 420.0          | \$ 159            | 450.5        |
| Shares to be issued under deferred compensation plans.....                             | <u>          </u> | <u>1.1</u>     | <u>          </u> | <u>0.9</u>   |
|  | \$ (30)           | 421.1          | \$ 159            | 451.4        |
| Basic earnings (loss) per share.....   |                   | <u>\$(.07)</u> |                   | <u>\$.35</u> |
| Effect of dilutive securities - stock options and restricted stock.....                | <u>          </u> | <u>-</u>       | <u>          </u> | <u>6.0</u>   |
|  | \$ (30)           | 421.1          | \$ 159            | 457.4        |
| Diluted earnings (loss) per share.....   |                   | <u>\$(.07)</u> |                   | <u>\$.35</u> |

Stock options to purchase 39.0 million shares of common stock at prices ranging from \$12.79 to \$46.15 per share and 483,000 shares of restricted stock were outstanding at November 1, 2008, but were not included in the computation of diluted loss per share for the 13 or 39 weeks ended November 1, 2008 because, as a result of the Company's net loss during these periods, their inclusion would have been antidilutive.

In addition to the stock options and restricted stock reflected in the foregoing tables, stock options to purchase 18.7 million shares of common stock at prices ranging from \$27.40 to \$46.15 per share and 274,000 shares of restricted stock were outstanding at November 3, 2007, but were not included in the computation of diluted earnings per share for the 13 or 39 weeks ended November 3, 2007 because their inclusion would have been antidilutive.

**7. Benefit Plans**

The Company has a funded defined benefit plan ( Pension Plan ) and a defined contribution plan, which cover substantially all employees who work 1,000 hours or more in a year. The Company also has an unfunded defined benefit supplementary retirement plan ( SERP ), which provides benefits, for certain employees, in excess of qualified plan limitations.

In addition, certain retired employees currently are provided with specified health care and life insurance benefits ( Postretirement Obligations ). Eligibility requirements for such benefits vary by division and subsidiary, but generally state that benefits are available to eligible employees who were hired prior to a certain date and retire after a certain age with specified years of service. Certain employees are subject to having such benefits modified or terminated.

The actuarially determined components of the net periodic benefit cost are as follows:

|   | 13 Weeks Ended   |                  | 39 Weeks Ended   |                  |
|---|------------------|------------------|------------------|------------------|
|   | November 1, 2008 | November 3, 2007 | November 1, 2008 | November 3, 2007 |
|   | (millions)       |                  |                  |                  |
| <b>Pension Plan</b>                           |                  |                  |                  |                  |
| Service cost.....                             | \$ 20            | \$ 20            | \$ 73            | \$ 78            |
| Interest cost.....                            | 39               | 37               | 119              | 118              |
| Expected return on assets.....                | (49)             | (45)             | (144)            | (147)            |
| Recognition of net actuarial loss.....        | 1                | 8                | 4                | 17               |
| Amortization of prior service cost.....       | <u>-</u>         | <u>-</u>         | <u>-</u>         | <u>(1)</u>       |
|   | <u>\$ 11</u>     | <u>\$ 20</u>     | <u>\$ 52</u>     | <u>\$ 65</u>     |
| <b>Supplementary Retirement Plan</b>          |                  |                  |                  |                  |
| Service cost.....                             | \$ 3             | \$ 1             | \$ 6             | \$ 6             |
| Interest cost.....                            | 9                | 8                | 29               | 28               |
| Recognition of net actuarial loss.....        | -                | -                | -                | -                |
| Amortization of prior service cost.....       | <u>-</u>         | <u>-</u>         | <u>(1)</u>       | <u>(1)</u>       |
|   | <u>\$ 12</u>     | <u>\$ 9</u>      | <u>\$ 34</u>     | <u>\$ 33</u>     |
| <b>Postretirement Obligations</b>             |                  |                  |                  |                  |
| Service cost.....                             | \$ -             | \$ -             | \$ -             | \$ -             |
| Interest cost.....                            | 3                | 5                | 14               | 15               |
| Recognition of net actuarial (gain) loss..... | (3)              | 1                | (2)              | 1                |
| Amortization of prior service cost.....       | <u>-</u>         | <u>-</u>         | <u>-</u>         | <u>-</u>         |
|   | <u>\$ -</u>      | <u>\$ 6</u>      | <u>\$ 12</u>     | <u>\$ 16</u>     |

The Company is considering making a voluntary funding contribution to the Pension Plan for the 2008 plan year of approximately \$175 million at some date prior to September 15, 2009.

## 8. Accumulated Other Comprehensive Loss

The following table shows the beginning and ending balance of, and the activity associated with, accumulated other comprehensive loss, net of income tax effects, for the 39 weeks ended November 1, 2008 and November 3, 2007:

|  | November 1, 2008 | November 3, 2007 |
|--|------------------|------------------|
|  | (millions)       |                  |
| Accumulated other comprehensive loss, at beginning of period.....                                | \$ (182)         | \$ (182)         |
| Adjustment to adopt new accounting pronouncements, net of income tax effect of \$14 million..... | -                | 29               |

|  |                 |                 |
|--|-----------------|-----------------|
| Unrealized loss on marketable securities, net of income tax effect of \$11 million and \$16 million..... | (17)            | (25)            |
| Post employment and postretirement benefit plans:  |                 |                 |
| Recognition of net actuarial loss, net of income tax effect of \$1 million and \$7 million.....          | 1               | 11              |
| Prior service cost, net of income tax effect of less than \$1 million and \$1 million.....               | <u>(1)</u>      | <u>(1)</u>      |
| Accumulated other comprehensive loss, at end of period.....  | <u>\$ (199)</u> | <u>\$ (168)</u> |

## 9. Legal Settlement

The Company is subject to a wage and hour class action in California. The Company concluded that it is probable that a loss of approximately \$25 million will be incurred to settle this legal matter and has recorded this estimated amount as part of selling, general and administrative expenses during the 39 weeks ended November 1, 2008, including an additional amount of \$2 million during the 13 weeks ended November 1, 2008. However, because this settlement is subject to court approval, there can be no assurance that the outcome of the legal matter will not result in an additional loss.

## 10. Condensed Consolidating Financial Information

Macy's, Inc. ( Parent ) has fully and unconditionally guaranteed certain long-term debt obligations of its wholly-owned subsidiary, Macy's Retail Holdings, Inc. ( Subsidiary Issuer ). Other Subsidiaries includes all other direct subsidiaries of Parent, including FDS Bank, Leadville Insurance Company and Snowdin Insurance Company and, prior to the date of disposition, After Hours Formalwear, Inc. Subsidiary Issuer includes operating divisions and non-guarantor subsidiaries of the Subsidiary Issuer on an equity basis. The assets and liabilities and results of operations of the non-guarantor subsidiaries of the Subsidiary Issuer, including Macy's Merchandising Group International, LLC, are also reflected in Other Subsidiaries.

Condensed Consolidating Balance Sheets as of November 1, 2008, November 3, 2007 and February 2, 2008, the related Condensed Consolidating Statements of Operations for the 13 and 39 weeks ended November 1, 2008 and November 3, 2007, and the related Condensed Consolidating Statements of Cash Flows for the 39 weeks ended November 1, 2008 and November 3, 2007 are presented on the following pages.

### Condensed Consolidating Balance Sheet As of November 1, 2008

(millions)

Pension Plan

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|                                    | Parent         | Subsidiary Issuer | Other Subsidiaries | Consolidating Adjustments | Consolidated    |
|------------------------------------|----------------|-------------------|--------------------|---------------------------|-----------------|
| <b>ASSETS:</b>                     |                |                   |                    |                           |                 |
| Current Assets:                    |                |                   |                    |                           |                 |
| Cash and cash equivalents.....     | \$ 59          | \$ 63             | \$ 178             | \$ -                      | \$ 300          |
| Receivables.....                   | -              | 22                | 345                | -                         | 367             |
| Merchandise inventories.....       | -              | 3,688             | 3,227              | -                         | 6,915           |
| Supplies and prepaid expenses..... | -              | 121               | 125                | -                         | 246             |
| Income tax receivable.....         | <u>147</u>     | <u>-</u>          | <u>-</u>           | <u>(104)</u>              | <u>43</u>       |
| Total Current Assets.....          | 206            | 3,894             | 3,875              | (104)                     | 7,871           |
| Property and Equipment - net.....  | -              | 6,041             | 4,575              | -                         | 10,616          |
| Goodwill.....                      | -              | 6,556             | 2,567              | -                         | 9,123           |
| Other Intangible Assets - net..... | -              | 263               | 484                | -                         | 747             |
| Other Assets.....                  | 4              | 128               | 415                | -                         | 547             |
| Deferred Income Tax Assets.....    | 105            | -                 | -                  | (105)                     | -               |
| Intercompany Receivable.....       | 1,375          | -                 | 1,681              | (3,056)                   | -               |
| Investment in Subsidiaries.....    | <u>8,277</u>   | <u>4,950</u>      | <u>-</u>           | <u>(13,227)</u>           | <u>-</u>        |
| Total Assets.....                  | <u>\$9,967</u> | <u>\$21,832</u>   | <u>\$13,597</u>    | <u>\$(16,492)</u>         | <u>\$28,904</u> |

**LIABILITIES AND SHAREHOLDERS**

**EQUITY:**

Current Liabilities:

|   |          |            |           |          |            |
|---|----------|------------|-----------|----------|------------|
| Short-term debt.....                          | \$ -     | \$ 1,084   | \$ 2      | \$ -     | \$ 1,086   |
| Accounts payable and accrued liabilities..... | 214      | 2,474      | 2,999     | -        | 5,687      |
| Income taxes.....                             | -        | 23         | 81        | (104)    | -          |
| Deferred income taxes.....                    | <u>9</u> | <u>219</u> | <u>18</u> | <u>-</u> | <u>246</u> |
| Total Current Liabilities.....                | 223      | 3,800      | 3,100     | (104)    | 7,019      |

|  |                |                 |                 |                   |                 |
|--|----------------|-----------------|-----------------|-------------------|-----------------|
| Long-Term Debt.....                            | -              | 8,720           | 28              | -                 | 8,748           |
| Intercompany Payable.....                      | -              | 3,056           | -               | (3,056)           | -               |
| Deferred Income Taxes.....                     | -              | 841             | 730             | (105)             | 1,466           |
| Other Liabilities.....                         | 54             | 863             | 1,064           | -                 | 1,981           |
| Shareholders Equity.....                       | <u>9,690</u>   | <u>4,552</u>    | <u>8,675</u>    | <u>(13,227)</u>   | <u>9,690</u>    |
| Total Liabilities and Shareholders Equity..... | <u>\$9,967</u> | <u>\$21,832</u> | <u>\$13,597</u> | <u>\$(16,492)</u> | <u>\$28,904</u> |

**Condensed Consolidating Statement of Operations  
For the 13 Weeks Ended November 1, 2008**

(millions)

|   | Parent   | Subsidiary Issuer | Other Subsidiaries | Consolidating Adjustments | Consolidated   |
|---|----------|-------------------|--------------------|---------------------------|----------------|
| Net sales.....                                    | \$ -     | \$ 2,978          | \$ 3,130           | \$ (615)                  | \$ 5,493       |
| Cost of sales.....                                | <u>-</u> | <u>(1,973)</u>    | <u>(1,948)</u>     | <u>597</u>                | <u>(3,324)</u> |
| Gross margin.....                                 | -        | 1,005             | 1,182              | (18)                      | 2,169          |
| Selling, general and administrative expenses..... | (1)      | (1,190)           | (912)              | 18                        | (2,085)        |

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|  |                |                 |               |             |                |
|--|----------------|-----------------|---------------|-------------|----------------|
| Division consolidation costs.....                          | <u>—</u>       | <u>(13)</u>     | <u>(3)</u>    | <u>—</u>    | <u>(16)</u>    |
| Operating income (loss).....                               | (1)            | (198)           | 267           | -           | 68             |
| Interest (expense) income, net                             |                |                 |               |             |                |
| External.....  | 7              | (150)           | -             | -           | (143)          |
| Intercompany.....  | 7              | (41)            | 34            | -           | -              |
| Equity in earnings of subsidiaries.....                    | <u>(45)</u>    | <u>45</u>       | <u>—</u>      | <u>—</u>    | <u>—</u>       |
| Income (loss) before income taxes.....                     | (32)           | (344)           | 301           | -           | (75)           |
| Federal, state and local income tax benefit (expense)..... | <u>(12)</u>    | <u>129</u>      | <u>(86)</u>   | <u>—</u>    | <u>31</u>      |
| Net income (loss).....                                     | <u>\$ (44)</u> | <u>\$ (215)</u> | <u>\$ 215</u> | <u>\$ —</u> | <u>\$ (44)</u> |

**Condensed Consolidating Statement of Operations  
For the 39 Weeks Ended November 1, 2008**

(millions)

|  | Parent         | Subsidiary<br>Issuer | Other<br>Subsidiaries | Consolidating<br>Adjustments | Consolidated    |
|--|----------------|----------------------|-----------------------|------------------------------|-----------------|
| Net sales.....   | \$ -           | \$ 9,110             | \$ 9,451              | \$(1,603)                    | \$16,958        |
| Cost of sales.....   | <u>—</u>       | <u>(5,834)</u>       | <u>(5,913)</u>        | <u>1,550</u>                 | <u>(10,197)</u> |
| Gross margin.....  | -              | 3,276                | 3,538                 | (53)                         | 6,761           |
| Selling, general and administrative expenses.....          | (4)            | (3,500)              | (2,774)               | 53                           | (6,225)         |
| Division consolidation costs.....                          | -              | (93)                 | (36)                  | -                            | (129)           |
| Asset impairment charges.....                              | <u>—</u>       | <u>—</u>             | <u>(50)</u>           | <u>—</u>                     | <u>(50)</u>     |
| Operating income (loss).....                               | (4)            | (317)                | 678                   | -                            | 357             |
| Interest (expense) income, net                             |                |                      |                       |                              |                 |
| External.....  | 17             | (437)                | 3                     | -                            | (417)           |
| Intercompany.....  | 22             | (124)                | 102                   | -                            | -               |
| Equity in earnings of subsidiaries.....                    | <u>(54)</u>    | <u>147</u>           | <u>—</u>              | <u>(93)</u>                  | <u>—</u>        |
| Income (loss) before income taxes.....                     | (19)           | (731)                | 783                   | (93)                         | (60)            |
| Federal, state and local income tax benefit (expense)..... | <u>(11)</u>    | <u>288</u>           | <u>(247)</u>          | <u>—</u>                     | <u>30</u>       |
| Net income (loss).....                                     | <u>\$ (30)</u> | <u>\$ (443)</u>      | <u>\$ 536</u>         | <u>\$ (93)</u>               | <u>\$ (30)</u>  |

Pension Plan

**Condensed Consolidating Statement of Cash Flows**  
**For the 39 Weeks Ended November 1, 2008**

(millions)

|  | Parent       | Subsidiary<br>Issuer | Other<br>Subsidiaries | Consolidating<br>Adjustments | Consolidated  |
|--|--------------|----------------------|-----------------------|------------------------------|---------------|
| Cash flows from continuing operating activities:                         |              |                      |                       |                              |               |
| Net income (loss).....   | \$ (30)      | \$ (443)             | \$ 536                | \$ (93)                      | \$ (30)       |
| Division consolidation costs.....  | -            | 93                   | 36                    | -                            | 129           |
| Asset impairment charges.....  | -            | -                    | 50                    | -                            | 50            |
| Equity in earnings of subsidiaries.....                                  | 54           | (147)                | -                     | 93                           | -             |
| Dividends received from subsidiaries.....                                | 353          | -                    | -                     | (353)                        | -             |
| Depreciation and amortization.....                                       | -            | 511                  | 439                   | -                            | 950           |
| Decrease in working capital.....   | (183)        | (428)                | (211)                 | -                            | (822)         |
| Other, net.....  | <u>(92)</u>  | <u>(47)</u>          | <u>179</u>            | <u>-</u>                     | <u>40</u>     |
| Net cash provided (used) by continuing<br>operating activities.....      | <u>102</u>   | <u>(461)</u>         | <u>1,029</u>          | <u>(353)</u>                 | <u>317</u>    |
| Cash flows from continuing investing activities:                         |              |                      |                       |                              |               |
| Purchase of property and equipment<br>and capitalized software, net..... | <u>-</u>     | <u>(186)</u>         | <u>(420)</u>          | <u>-</u>                     | <u>(606)</u>  |
| Net cash used by continuing<br>investing activities.....                 | <u>-</u>     | <u>(186)</u>         | <u>(420)</u>          | <u>-</u>                     | <u>(606)</u>  |
| Cash flows from continuing financing activities:                         |              |                      |                       |                              |               |
| Debt issued, net of debt repaid.....                                     | -            | 109                  | (2)                   | -                            | 107           |
| Dividends paid.....  | (166)        | -                    | (353)                 | 353                          | (166)         |
| Issuance of common stock, net of<br>common stock acquired.....           | 6            | -                    | -                     | -                            | 6             |
| Intercompany activity, net.....  | (276)        | 533                  | (257)                 | -                            | -             |
| Other, net.....  | <u>58</u>    | <u>(7)</u>           | <u>8</u>              | <u>-</u>                     | <u>59</u>     |
| Net cash provided (used) by<br>continuing financing activities.....      | <u>(378)</u> | <u>635</u>           | <u>(604)</u>          | <u>353</u>                   | <u>6</u>      |
| Net increase (decrease) in cash<br>and cash equivalents.....             | (276)        | (12)                 | 5                     | -                            | (283)         |
| Cash and cash equivalents at beginning<br>of period.....                 | <u>335</u>   | <u>75</u>            | <u>173</u>            | <u>-</u>                     | <u>583</u>    |
| Cash and cash equivalents at end of period.....                          | <u>\$ 59</u> | <u>\$ 63</u>         | <u>\$ 178</u>         | <u>\$ -</u>                  | <u>\$ 300</u> |

**Condensed Consolidating Balance Sheet**  
**As of November 3, 2007**

(millions)

|   | Parent         | Subsidiary<br>Issuer | Other<br>Subsidiaries | Consolidating<br>Adjustments | Consolidated    |
|---|----------------|----------------------|-----------------------|------------------------------|-----------------|
| <b>ASSETS:</b>                                    |                |                      |                       |                              |                 |
| Current Assets:                                   |                |                      |                       |                              |                 |
| Cash and cash equivalents.....                    | \$ 17          | \$ 73                | \$ 185                | \$ -                         | \$ 275          |
| Receivables.....                                  | -              | 38                   | 421                   | -                            | 459             |
| Merchandise inventories.....                      | -              | 3,881                | 3,131                 | -                            | 7,012           |
| Supplies and prepaid expenses.....                | -              | 173                  | 88                    | -                            | 261             |
| Income tax receivable.....                        | <u>120</u>     | <u>-</u>             | <u>-</u>              | <u>(120)</u>                 | <u>-</u>        |
| Total Current Assets.....                         | 137            | 4,165                | 3,825                 | (120)                        | 8,007           |
| Property and Equipment - net.....                 | 3              | 6,382                | 4,687                 | -                            | 11,072          |
| Goodwill.....                                     | -              | 6,568                | 2,571                 | -                            | 9,139           |
| Other Intangible Assets - net.....                | -              | 299                  | 543                   | -                            | 842             |
| Other Assets.....                                 | 4              | 208                  | 397                   | -                            | 609             |
| Deferred Income Tax Assets.....                   | 21             | -                    | -                     | (21)                         | -               |
| Intercompany Receivable.....                      | 384            | -                    | 2,081                 | (2,465)                      | -               |
| Investment in Subsidiaries.....                   | <u>9,236</u>   | <u>5,684</u>         | <u>-</u>              | <u>(14,920)</u>              | <u>-</u>        |
| Total Assets.....                                 | <u>\$9,785</u> | <u>\$23,306</u>      | <u>\$14,104</u>       | <u>\$(17,526)</u>            | <u>\$29,669</u> |
| <b>LIABILITIES AND SHAREHOLDERS</b>               |                |                      |                       |                              |                 |
| <b>EQUITY:</b>                                    |                |                      |                       |                              |                 |
| Current Liabilities:                              |                |                      |                       |                              |                 |
| Short-term debt.....                              | \$ -           | \$ 1,632             | \$ 2                  | \$ -                         | \$ 1,634        |
| Accounts payable and accrued<br>liabilities.....  | 180            | 2,460                | 3,117                 | -                            | 5,757           |
| Income taxes.....                                 | -              | 19                   | 107                   | (120)                        | 6               |
| Deferred income taxes.....                        | <u>-</u>       | <u>238</u>           | <u>15</u>             | <u>-</u>                     | <u>253</u>      |
| Total Current Liabilities.....                    | 180            | 4,349                | 3,241                 | (120)                        | 7,650           |
| Long-Term Debt.....                               | -              | 9,067                | 30                    | -                            | 9,097           |
| Intercompany Payable.....                         | -              | 2,465                | -                     | (2,465)                      | -               |
| Deferred Income Taxes.....                        | -              | 985                  | 443                   | (21)                         | 1,407           |
| Other Liabilities.....                            | 135            | 973                  | 937                   | -                            | 2,045           |
| Shareholders Equity.....                          | <u>9,470</u>   | <u>5,467</u>         | <u>9,453</u>          | <u>(14,920)</u>              | <u>9,470</u>    |
| Total Liabilities and<br>Shareholders Equity..... | <u>\$9,785</u> | <u>\$23,306</u>      | <u>\$14,104</u>       | <u>\$(17,526)</u>            | <u>\$29,669</u> |

**Condensed Consolidating Statement of Operations**  
**For the 13 Weeks Ended November 3, 2007**

**(millions)**

|   | Parent       | Subsidiary<br>Issuer | Other<br>Subsidiaries | Consolidating<br>Adjustments | Consolidated   |
|---|--------------|----------------------|-----------------------|------------------------------|----------------|
| Net sales.....  | \$ -         | \$ 3,154             | \$ 3,412              | \$ (660)                     | \$ 5,906       |
| Cost of sales.....                                    | <u>-</u>     | <u>(2,098)</u>       | <u>(2,128)</u>        | <u>641</u>                   | <u>(3,585)</u> |
| Gross margin.....                                     | -            | 1,056                | 1,284                 | (19)                         | 2,321          |
| Selling, general and administrative expenses.....     | (2)          | (1,240)              | (898)                 | 19                           | (2,121)        |
| May integration costs.....                            | <u>-</u>     | <u>(9)</u>           | <u>(8)</u>            | <u>-</u>                     | <u>(17)</u>    |
| Operating income (loss).....                          | (2)          | (193)                | 378                   | -                            | 183            |
| Interest (expense) income, net                        |              |                      |                       |                              |                |
| External.....   | -            | (147)                | 2                     | -                            | (145)          |
| Intercompany.....                                     | 9            | (35)                 | 26                    | -                            | -              |
| Equity in earnings of subsidiaries.....               | <u>24</u>    | <u>116</u>           | <u>-</u>              | <u>(140)</u>                 | <u>-</u>       |
| Income (loss) before income taxes.....                | 31           | (259)                | 406                   | (140)                        | 38             |
| Federal, state and local income tax benefit (expense) | <u>2</u>     | <u>100</u>           | <u>(107)</u>          | <u>-</u>                     | <u>(5)</u>     |
| Net income (loss).....                                | <u>\$ 33</u> | <u>\$ (159)</u>      | <u>\$ 299</u>         | <u>\$ (140)</u>              | <u>\$ 33</u>   |

**Condensed Consolidating Statement of Operations  
For the 39 Weeks Ended November 3, 2007**

**(millions)**

|   | Parent   | Subsidiary<br>Issuer | Other<br>Subsidiaries | Consolidating<br>Adjustments | Consolidated    |
|---|----------|----------------------|-----------------------|------------------------------|-----------------|
| Net sales.....                                    | \$ -     | \$ 8,962             | \$10,490              | \$ (1,733)                   | \$17,719        |
| Cost of sales.....                                | <u>-</u> | <u>(5,774)</u>       | <u>(6,542)</u>        | <u>1,660</u>                 | <u>(10,656)</u> |
| Gross margin.....                                 | -        | 3,188                | 3,948                 | (73)                         | 7,063           |
| Selling, general and administrative expenses..... | (8)      | (3,407)              | (2,945)               | 88                           | (6,272)         |

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|  |               |                 |                |                 |                |
|--|---------------|-----------------|----------------|-----------------|----------------|
| May integration costs.....   | <u>    -</u>  | <u>  (94)</u>   | <u>  (63)</u>  | <u>    7</u>    | <u>  (150)</u> |
| Operating income (loss).....   | (8)           | (313)           | 940            | 22              | 641            |
| Interest (expense) income, net                                       |               |                 |                |                 |                |
| External.....  | 16            | (429)           | 6              | -               | (407)          |
| Intercompany.....  | 40            | (106)           | 66             | -               | -              |
| Equity in earnings of subsidiaries.....                              | <u>  110</u>  | <u>  258</u>    | <u>    -</u>   | <u>  (368)</u>  | <u>    -</u>   |
| Income (loss) from continuing operations<br>before income taxes..... | 158           | (590)           | 1,012          | (346)           | 234            |
| Federal, state and local income tax benefit (expense)                | <u>  (15)</u> | <u>  280</u>    | <u>  (334)</u> | <u>    (6)</u>  | <u>  (75)</u>  |
| Income (loss) from continuing operations.....                        | 143           | (310)           | 678            | (352)           | 159            |
| Discontinued operations, net of income taxes.....                    | <u>    -</u>  | <u>    -</u>    | <u>    -</u>   | <u>  (16)</u>   | <u>  (16)</u>  |
| Net income (loss).....   | <u>\$ 143</u> | <u>\$ (310)</u> | <u>\$ 678</u>  | <u>\$ (368)</u> | <u>\$ 143</u>  |

**Condensed Consolidating Statement of Cash Flows  
For the 39 Weeks Ended November 3, 2007**

(millions)

|  | Parent       | Subsidiary<br>Issuer | Other<br>Subsidiaries | Consolidating<br>Adjustments | Consolidated  |
|--|--------------|----------------------|-----------------------|------------------------------|---------------|
| Cash flows from continuing operating activities:                         |              |                      |                       |                              |               |
| Net income (loss).....   | \$ 143       | \$ (310)             | \$ 678                | \$ (368)                     | \$ 143        |
| Loss from discontinued operations.....                                   | -            | -                    | -                     | 16                           | 16            |
| May integration costs.....   | -            | 94                   | 63                    | (7)                          | 150           |
| Equity in earnings of subsidiaries.....                                  | (110)        | (258)                | -                     | 368                          | -             |
| Dividends received from subsidiaries.....                                | 351          | -                    | -                     | (351)                        | -             |
| Depreciation and amortization.....                                       | 1            | 505                  | 471                   | -                            | 977           |
| (Increase) decrease in working capital.....                              | (241)        | (907)                | 136                   | (16)                         | (1,028)       |
| Other, net.....  | <u>  109</u> | <u>  1,110</u>       | <u>  (1,192)</u>      | <u>    -</u>                 | <u>    27</u> |
| Net cash provided by continuing<br>operating activities.....             | <u>  253</u> | <u>  234</u>         | <u>  156</u>          | <u>  (358)</u>               | <u>  285</u>  |
| Cash flows from continuing investing activities:                         |              |                      |                       |                              |               |
| Purchase of property and equipment<br>and capitalized software, net..... | -            | (170)                | (521)                 | 7                            | (684)         |
| Proceeds from the disposition of<br>After Hours Formalwear.....          | <u>  66</u>  | <u>    -</u>         | <u>    -</u>          | <u>    -</u>                 | <u>  66</u>   |

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|  |                |              |               |             |               |
|--|----------------|--------------|---------------|-------------|---------------|
| Net cash provided (used) by continuing investing activities..... | <u>66</u>      | <u>(170)</u> | <u>(521)</u>  | <u>7</u>    | <u>(618)</u>  |
| Cash flows from continuing financing activities:                 |                |              |               |             |               |
| Debt issued, net of debt repaid.....                             | -              | 2,273        | (2)           | -           | 2,271         |
| Dividends paid.....  | (173)          | -            | (351)         | 351         | (173)         |
| Acquisition of common stock, net of common stock issued.....     | (2,747)        | -            | -             | -           | (2,747)       |
| Intercompany activity, net.....                                  | 1,570          | (2,291)      | 719           | 2           | -             |
| Other, net.....  | <u>80</u>      | <u>(46)</u>  | <u>13</u>     | <u>-</u>    | <u>47</u>     |
| Net cash provided (used) by continuing financing activities..... | <u>(1,270)</u> | <u>(64)</u>  | <u>379</u>    | <u>353</u>  | <u>(602)</u>  |
| Net cash provided (used) by continuing operations.....           | (951)          | -            | 14            | 2           | (935)         |
| Net cash used by discontinued operations.....                    | <u>-</u>       | <u>-</u>     | <u>-</u>      | <u>(1)</u>  | <u>(1)</u>    |
| Net increase (decrease) in cash and cash equivalents.....        | (951)          | -            | 14            | 1           | (936)         |
| Cash and cash equivalents at beginning of period.....            | <u>968</u>     | <u>73</u>    | <u>171</u>    | <u>(1)</u>  | <u>1,211</u>  |
| Cash and cash equivalents at end of period.....                  | <u>\$ 17</u>   | <u>\$ 73</u> | <u>\$ 185</u> | <u>\$ -</u> | <u>\$ 275</u> |

**Condensed Consolidating Balance Sheet  
As of February 2, 2008**

(millions)

|                                    | Parent   | Subsidiary<br>Issuer | Other<br>Subsidiaries | Consolidating<br>Adjustments | Consolidated |
|------------------------------------|----------|----------------------|-----------------------|------------------------------|--------------|
| <b>ASSETS:</b>                     |          |                      |                       |                              |              |
| Current Assets:                    |          |                      |                       |                              |              |
| Cash and cash equivalents.....     | \$ 335   | \$ 75                | \$ 173                | \$ -                         | \$ 583       |
| Receivables.....                   | -        | 68                   | 395                   | -                            | 463          |
| Merchandise inventories.....       | -        | 2,704                | 2,356                 | -                            | 5,060        |
| Supplies and prepaid expenses..... | -        | 118                  | 100                   | -                            | 218          |
| Income taxes.....                  | 21       | -                    | -                     | (21)                         | -            |
| Deferred income tax assets.....    | -        | -                    | -                     | -                            | -            |
| .....                              | <u>-</u> | <u>-</u>             | <u>7</u>              | <u>(7)</u>                   | <u>-</u>     |
| Total Current Assets.....          | 356      | 2,965                | 3,031                 | (28)                         | 6,324        |
| Property and Equipment - net.....  | 3        | 6,292                | 4,696                 | -                            | 10,991       |
| Goodwill.....                      | -        | 6,564                | 2,569                 | -                            | 9,133        |
| Other Intangible Assets - net..... | -        | 290                  | 541                   | -                            | 831          |
| Other Assets.....                  | 4        | 155                  | 351                   | -                            | 510          |
| Deferred Income Tax Assets.....    | 22       | -                    | -                     | (22)                         | -            |

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|                                 |                 |                 |                 |                   |                 |
|---------------------------------|-----------------|-----------------|-----------------|-------------------|-----------------|
| Intercompany Receivable.....    | 1,045           | -               | 1,412           | (2,457)           | -               |
| Investment in Subsidiaries..... | <u>8,707</u>    | <u>4,805</u>    | <u>-</u>        | <u>(13,512)</u>   | <u>-</u>        |
| Total Assets.....               | <u>\$10,137</u> | <u>\$21,071</u> | <u>\$12,600</u> | <u>\$(16,019)</u> | <u>\$27,789</u> |

LIABILITIES AND SHAREHOLDERS

EQUITY:

Current Liabilities:

|   |          |            |          |            |            |
|---|----------|------------|----------|------------|------------|
| Short-term debt.....                          | \$ -     | \$ 664     | \$ 2     | \$ -       | \$ 666     |
| Accounts payable and accrued liabilities..... | 159      | 1,880      | 2,088    | -          | 4,127      |
| Income taxes.....                             | -        | 11         | 354      | (21)       | 344        |
| Deferred income taxes.....                    | <u>-</u> | <u>230</u> | <u>-</u> | <u>(7)</u> | <u>223</u> |
| Total Current Liabilities.....                | 159      | 2,785      | 2,444    | (28)       | 5,360      |

|  |                 |                 |                 |                   |                 |
|--|-----------------|-----------------|-----------------|-------------------|-----------------|
| Long-Term Debt.....                            | -               | 9,058           | 29              | -                 | 9,087           |
| Intercompany Payable.....                      | -               | 2,457           | -               | (2,457)           | -               |
| Deferred Income Taxes.....                     | -               | 882             | 586             | (22)              | 1,446           |
| Other Liabilities.....                         | 71              | 877             | 1,041           | -                 | 1,989           |
| Shareholders Equity.....                       | <u>9,907</u>    | <u>5,012</u>    | <u>8,500</u>    | <u>(13,512)</u>   | <u>9,907</u>    |
| Total Liabilities and Shareholders Equity..... | <u>\$10,137</u> | <u>\$21,071</u> | <u>\$12,600</u> | <u>\$(16,019)</u> | <u>\$27,789</u> |

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

For purposes of the following discussion, all references to third quarter of 2008 and third quarter of 2007 are to the Company's 13-week fiscal periods ended November 1, 2008 and November 3, 2007, respectively, and all references to 2008 and 2007 are to the Company's 39-week fiscal periods ended November 1, 2008 and November 3, 2007, respectively.

The Company is a retail organization operating retail stores and websites that sell a wide range of merchandise, including men's, women's and children's apparel and accessories, cosmetics, home furnishings and other consumer goods. The Company's operations include more than 850 stores in 45 states, the District of Columbia, Guam and Puerto Rico as well as macys.com and bloomingdales.com. The Company operates under two retail brands - Macy's and Bloomingdale's.

In 2003, the Company commenced the implementation of a strategy to more fully utilize its Macy's brand, converting all of the Company's regional store nameplates to the Macy's nameplate. This strategy allowed the Company to magnify the impact of its marketing efforts on a nationwide basis, as well as to leverage major events such as the Macy's Thanksgiving Day Parade and Macy's 4th of July fireworks.

In early 2004, the Company announced a further step in reinventing its department stores - the creation of a centralized organization to be responsible for the overall strategy, merchandising and marketing of home-related categories of business in all of its Macy's-branded stores. While its benefits have taken longer to be realized, the centralized operation is still expected to accelerate future sales in these categories largely by improving and further differentiating the Company's home-related merchandise assortments.

For the past several years, the Company has been focused on four key priorities for improving the business over the longer term: (i) differentiating and editing merchandise assortments; (ii) simplifying pricing; (iii) improving the overall shopping experience; and (iv) communicating better with customers through more brand focused and effective marketing.

In 2005, the Company launched a new nationwide Macy's customer loyalty program, called Star Rewards, in coordination with the launch of the Macy's nameplate in cities across the country. The program provides an enhanced level of benefits to Macy's best credit card customers.

On August 30, 2005, the Company completed its merger with The May Department Stores Company (May) (the Merger). The Company added about 400 Macy's locations nationwide in 2006 as it converted the regional department store nameplates acquired through the Merger. In conjunction with the conversion process, the Company identified certain store locations and distribution center facilities to be divested.

Following the Merger, the Company announced its intention to sell the acquired Lord & Taylor division and the acquired bridal group business (which included David's Bridal, After Hours Formalwear and Priscilla of Boston). The sale of the Lord & Taylor division was completed in October 2006, the sale of David's Bridal and Priscilla of Boston was completed in January 2007 and the sale of After Hours Formalwear was completed in April 2007. As a result of the Company's disposition of the Lord & Taylor division and bridal group business, these businesses were reported as discontinued operations. Unless otherwise indicated, the following discussion relates to the Company's continuing operations.

In February 2008, the Company announced a new initiative to strengthen local market focus and enhance selling service expected to enable the Company to both accelerate same-store sales growth and reduce expense. The localization initiative, called My Macy's, was developed with the goal to accelerate sales growth in existing locations by ensuring that core customers surrounding each Macy's store find merchandise assortments, size ranges, marketing programs and shopping experiences that are custom-tailored to their needs. To maximize the results from My Macy's, the Company is taking action in certain markets that will: concentrate more management talent in local markets, effectively reducing the span of control over local stores; create new positions in the field to work with division central planning and buying executives in helping to understand and act on the merchandise needs of local customers; and empower locally based executives to make more and better decisions. In combination with the localization initiative, the Company consolidated the Minneapolis-based Macy's North organization into New York-based Macy's East, the St. Louis-based Macy's Midwest organization into Atlanta-based Macy's South and the Seattle-based Macy's

Northwest organization into San Francisco-based Macy's West. The Atlanta-based division was renamed Macy's Central. The savings from the division consolidation process, net of the amount invested in the localization initiative and increased store staffing levels, are expected to reduce selling, general and administrative (SG&A) expenses by approximately \$100 million per year, beginning in 2009. The partial-year reduction in SG&A expenses for 2008 is estimated at approximately \$60 million. The Company anticipates incurring approximately \$150 million of one-time costs related to the division consolidations and the localization initiative in fiscal 2008, consisting primarily of human resource-related costs.

The Company's operations are impacted by competitive pressures from department stores, specialty stores, mass merchandisers and all other retail channels. The Company's operations are also impacted by general consumer spending levels, which are affected by general economic conditions, consumer confidence and employment levels, the availability and cost of consumer credit, the level of consumer debt, the costs of basic necessities and other goods, weather conditions and other factors over which the Company has little or no control.

In recent periods, consumer spending levels have been adversely affected by a number of factors, including substantial declines in the level of general economic activity and real estate and investment values, substantial increases in consumer pessimism, unemployment and the costs of basic necessities, and a significant tightening of consumer credit. These conditions have reduced the amount of funds that consumers are willing and able to spend for discretionary purchases, including purchases of some of the merchandise offered by the Company. Based on its assessment of market conditions and its recent performance, the Company is assuming that its comparable store sales in the fourth quarter of 2008 will be down in the range of 1% to 6% from levels in the fourth quarter of 2007. If the sales trend in the fourth quarter of 2008 does not improve from that experienced in the third quarter of 2008, the Company expects that its fourth quarter of 2008 comparable store sales will be at the low end of this range.

The Company cannot predict whether, when or the manner in which the economic conditions described above will change.

The following discussion should be read in conjunction with our Consolidated Financial Statements and the related notes included elsewhere in this report, as well as the financial and other information included in the 2007 10-K. The following discussion contains forward-looking statements that reflect the Company's plans, estimates and beliefs. The Company's actual results could materially differ from those discussed in these forward-looking statements. Factors that could cause or contribute to those differences include, but are not limited to, those discussed below and elsewhere in this report (particularly in Forward-Looking Statements) and in the 2007 10-K (particularly in Risk Factors).

## **Results of Operations**

### **Comparison of the 13 Weeks Ended November 1, 2008 and November 3, 2007**

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The net loss for the third quarter of 2008 was \$44 million, compared to net income of \$33 million in the third quarter of 2007. The net loss for the third quarter of 2008 reflects the lower sales trend and includes the impact of \$16 million of division consolidation costs. Net income in the third quarter of 2007 included the impact of \$17 million of May integration costs.

Net sales for the third quarter of 2008 totaled \$5,493 million, compared to net sales of \$5,906 million for the third quarter of 2007, a decrease of \$413 million or 7.0%. On a comparable store basis, net sales for the third quarter of 2008 were down 6.0% compared to the third quarter of 2007. Sales from the Company's Internet businesses in the third quarter of 2008 increased 22.7% compared to the third quarter of 2007. By family of business, sales in the third quarter of 2008 were strongest in cold weather categories, including outerwear, boots and cold weather accessories. The weaker businesses during the quarter were furniture and mattresses. The Company calculates comparable store sales as sales from stores in operation throughout 2007 and 2008 and all Internet sales. Stores undergoing remodeling, expansion or relocation remain in the comparable store sales calculation unless the store is closed for a significant period of time. Definitions and calculations of comparable store sales differ among companies in the retail industry.

Cost of sales was \$3,324 million or 60.5% of net sales for the third quarter of 2008, compared to \$3,585 million or 60.7% of net sales for the third quarter of 2007, a decrease of \$261 million. The valuation of merchandise inventories on the last-in, first-out basis did not impact cost of sales in either period.

SG&A expenses were \$2,085 million or 38.0% of net sales for the third quarter of 2008, compared to \$2,121 million or 35.9% of net sales for the third quarter of 2007, a decrease of \$36 million. The SG&A rate as a percent to sales was higher in the third quarter of 2008, compared to the third quarter of 2007, primarily because of weaker sales. SG&A expenses in the third quarter of 2008 reflected lower pension and supplementary retirement plan expenses, lower stock-based compensation expense and consolidation-related expense savings, partially offset by lower income from credit and higher logistics related costs in support of the Company's multi-channel operations.

Division consolidation costs for the third quarter of 2008 amounted to \$16 million and consisted primarily of human resource-related costs.

May integration costs for the third quarter of 2007 amounted to \$17 million and consisted primarily of additional costs related to closed locations, severance, system conversion costs and costs related to other operational consolidations.

Net interest expense was \$143 million for the third quarter of 2008 compared to \$145 million for the third quarter of 2007, a decrease of \$2 million.

The Company's effective income tax rate of 42.0% for the third quarter of 2008 and 13.1% for the third quarter of 2007 differ from the federal income tax statutory rate of 35.0%, and on a comparative basis, principally because of the

effect of state and local income taxes, including the settlement of various tax issues and tax examinations.

**Comparison of the 39 Weeks Ended November 1, 2008 and November 3, 2007**

The net loss for 2008 was \$30 million, compared to net income of \$143 million in 2007. The net loss for 2008 reflects the lower sales trend and includes the impact of \$129 million of division consolidation costs and \$50 million of asset impairment charges. Net income for 2007 included income from continuing operations of \$159 million and a loss from discontinued operations of \$16 million. Income from continuing operations in 2007 included the impact of \$150 million of May integration costs. The loss from discontinued operations in 2007 included the loss on disposal of the After Hours Formalwear business of \$7 million on a pre-tax and after-tax basis.

Net sales for 2008 totaled \$16,958 million, compared to net sales of \$17,719 million for 2007, a decrease of \$761 million or 4.3%. On a comparable store basis, net sales for 2008 were down 3.5% compared to 2007. Sales from the Company's Internet businesses in 2008 increased 32.1% compared to 2007. By family of business, sales in 2008 were strongest in young men's, mattresses and housewares. The weaker business in 2008 was women's ready to wear. The Company calculates comparable store sales as sales from stores in operation throughout 2007 and 2008 and all Internet sales. Stores undergoing remodeling, expansion or relocation remain in the comparable store sales calculation unless the store is closed for a significant period of time. Definitions and calculations of comparable store sales differ among companies in the retail industry.

Cost of sales was \$10,197 million or 60.1% of net sales for 2008, compared to \$10,656 million or 60.1% of net sales for 2007, a decrease of \$459 million. The valuation of merchandise inventories on the last-in, first-out basis did not impact cost of sales in either period.

SG&A expenses were \$6,225 million or 36.7% of net sales for 2008, compared to \$6,272 million or 35.4% of net sales for 2007, a decrease of \$47 million. The SG&A rate as a percent to sales was higher in 2008, compared to 2007, primarily because of weaker sales. SG&A expenses in 2008 benefited from lower depreciation and amortization expenses, lower stock-based compensation expenses and lower pension and supplementary retirement plan expenses, partially offset by lower income from credit and higher logistics related costs in support of the Company's multi-channel operations.

Division consolidation costs for 2008 amounted to \$129 million and consisted primarily of severance costs and other human resource-related costs.

Asset impairment charges for 2008 amounted to \$50 million and related to indefinite lived private brand tradenames acquired in the May acquisition.

May integration costs for 2007 amounted to \$150 million, including \$47 million related to impairment charges in connection with distribution center facilities planned to be closed and disposed of. The remaining \$103 million of May integration costs for 2007 included additional costs related to closed locations, severance, system conversion costs, impairment charges associated with acquired indefinite lived intangible assets and costs related to other operational consolidations.

Net interest expense was \$417 million for 2008 compared to \$407 million for 2007, an increase of \$10 million. The increase in net interest expense for 2008, as compared to 2007, resulted primarily from higher average outstanding borrowings.

The Company's effective income tax rate of 51.3% for 2008 and 31.9% for 2007 differ from the federal income tax statutory rate of 35.0%, and on a comparative basis, principally because of the effect of state and local income taxes, including the settlement of various tax issues and tax examinations.

For 2007, the loss from the discontinued operations of the acquired After Hours Formalwear business, net of income taxes, was \$16 million on sales of approximately \$27 million. The loss from discontinued operations included the loss on disposal of the After Hours Formalwear business of \$7 million on a pre-tax and after-tax basis.

### **Liquidity and Capital Resources**

The Company's principal sources of liquidity are cash from operations, cash on hand and the available credit facilities described below.

Net cash provided by continuing operating activities in 2008 was \$317 million, compared to net cash provided by continuing operating activities of \$285 million in 2007. The increase in net cash provided by continuing operating activities reflects a larger increase in accounts payable and accrued liabilities not separately identified, partially offset by a larger increase in merchandise inventories and a net loss in 2008 as compared to net income in 2007.

Net cash used by continuing investing activities was \$606 million for 2008, compared to net cash used by continuing investing activities of \$618 million for 2007. Continuing investing activities for 2008 include purchases of property and equipment totaling \$546 million and capitalized software of \$104 million, compared to purchases of property and equipment totaling \$700 million and capitalized software of \$81 million for 2007. During 2008, the Company opened four new Macy's department stores and one new Macy's furniture gallery, and reopened one Macy's store that was previously closed from hurricane damage. During 2007, the Company opened eight Macy's department stores, one Macy's furniture gallery and two Bloomingdale's department stores. Cash flows from continuing investing activities

included \$25 million and \$96 million from the disposition of property and equipment for 2008 and 2007, respectively. Continuing investing activities for 2007 also included \$66 million of proceeds from the disposition of the discontinued operations of After Hours Formalwear.

Net cash provided by continuing financing activities was \$6 million for 2008, including the issuance of \$770 million of debt, the issuance of \$7 million of common stock, primarily related to the exercise of stock options, and an increase in outstanding checks of \$64 million, partially offset by the repayment of \$663 million of debt and the payment of \$166 million of cash dividends. During 2008, the Company repurchased no shares of its common stock under its share repurchase program and anticipates no share repurchases under its share repurchase program for the remainder of fiscal 2008 or fiscal 2009. Net cash used by the Company from continuing financing activities was \$602 million for 2007, including the repayment of \$647 million of debt, the acquisition of 72.3 million shares of its common stock at an approximate cost of \$3,003 million and the payment of \$173 million of cash dividends, partially offset by the issuance of \$2,918 million of debt, the issuance of \$256 million of common stock, primarily related to the exercise of stock options, and an increase in outstanding checks of \$65 million. The debt issued during 2008 included \$650 million of 7.875% senior notes due 2015 and \$120 million of outstanding borrowings under the Company's credit agreement at November 1, 2008. The debt repaid in 2008 included \$500 million of 6.625% senior notes due September 1, 2008 and \$150 million of 5.95% notes due November 1, 2008. The debt issued during 2007 included \$1,100 million of 5.35% senior notes due 2012, \$500 million of 6.375% senior notes due 2037, \$350 million of 5.875% senior notes due 2013 and \$968 million of commercial paper outstanding at November 3, 2007. The debt repaid in 2007 included \$400 million of 3.95% senior notes due July 15, 2007, \$6 million of 9.93% medium term notes due August 1, 2007 and \$225 million of 7.9% senior debentures due October 15, 2007.

The Company is a party to a credit agreement with certain financial institutions providing for revolving credit borrowings and letters of credit in an aggregate amount not to exceed \$2,000 million (which may be increased to \$2,500 million at the option of the Company, subject to the willingness of existing or new lenders to provide commitments for such additional financing) outstanding at any particular time. This agreement is set to expire August 30, 2012. As of November 1, 2008, the Company had \$120 million of borrowings outstanding under this agreement. As of December 8, 2008, all borrowings under this agreement had been repaid.

The credit agreement requires the Company to maintain a specified interest coverage ratio of no less than 3.25 and a specified leverage ratio, which approximates the ratio of debt to debt and equity, of no more than .62. At November 1, 2008, the Company's interest coverage ratio was 5.07 and the Company's leverage ratio was .49.

The Company has \$350 million of 6.3% senior notes due April 1, 2009 and \$600 million of 4.8% senior notes due July 15, 2009. As of the date of this report, the Company intends to fund these debt maturities with cash on hand and funds from operations, but would also have the ability to fund these debt maturities with borrowings under its credit agreement.

On October 24, 2008, the Company's board of directors declared a regular quarterly dividend of 13.25 cents per share on its common stock, payable January 2, 2009, to shareholders of record at the close of business on December 15, 2008.

Management believes that, with respect to the Company's current operations, cash on hand and funds from operations, together with its credit facility and other capital resources, will be sufficient to cover the Company's reasonably foreseeable working capital, capital expenditure and debt service requirements and other cash requirements in both the near term and over the longer term. The Company's ability to generate funds from operations may be affected by numerous factors, including general economic conditions and levels of consumer confidence and demand; however, the Company expects to be able to manage its working capital levels and capital expenditure amounts so as to maintain sufficient levels of liquidity. Depending upon conditions in the capital markets and other factors, the Company will from time to time consider the issuance of debt or other securities, or other possible capital markets transactions, the proceeds of which could be used to refinance current indebtedness or for other corporate purposes.

Management believes the department store business and other retail businesses will continue to consolidate. The Company intends from time to time to consider additional acquisitions of, and investments in, department stores and other complementary assets and companies. Acquisition transactions, if any, are expected to be financed from one or more of the following sources: cash on hand, cash from operations, borrowings under existing or new credit facilities and the issuance of long-term debt, commercial paper or other securities, including common stock.

#### **Item 4. Controls and Procedures**

The Company's Chief Executive Officer and Chief Financial Officer have carried out, as of November 1, 2008, with the participation of the Company's management, an evaluation of the effectiveness of the Company's disclosure controls and procedures, as defined in Rule 13a-15(e) under the Exchange Act. Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by the Company in reports the Company files under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission (SEC) rules and forms, and that information required to be disclosed by the Company in the reports the Company files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in the Company's internal control over financial reporting that occurred during the Company's most recently completed fiscal quarter that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II -- OTHER INFORMATION**

### **MACY'S, INC.**

#### **Item 1. Legal Proceedings.**

On January 11, 2006, Edward Decristofaro, an alleged former May stockholder, filed a purported class action lawsuit in the Circuit Court of St. Louis, Missouri on behalf of all former May stockholders against May and the former members of the board of directors of May. The complaint generally alleges that the directors of May breached their fiduciary duties of loyalty, due care, good faith and candor to May stockholders in connection with the Merger. The plaintiffs seek rescission of the Merger or an unspecified amount of rescissory damages and costs including attorneys fees and experts fees. In July 2007, the court denied the defendants motion to dismiss the case. The Company believes the lawsuit is without merit and intends to contest it vigorously.

On June 20, 2007, the Pirelli Armstrong Tire Corp. Retiree Medical Benefits Trust, an alleged stockholder of the Company, filed a stockholder derivative action in the United States District Court for the Southern District of New York. The derivative complaint charges the members of the Company s board of directors and certain members of senior management with breach of fiduciary duty and violations of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, alleging that the defendants made false and misleading statements regarding the Company s business, operations and prospects in relation to the integration of the acquired May operations, resulting in supposed artificial inflation of the Company s stock price between August 30, 2005 and May 15, 2007. The plaintiff seeks various forms of relief from the defendants for the benefit of the Company, including unspecified money damages and disgorgement of profits from allegedly improper trading of Company stock. On September 30, 2008, the court dismissed the plaintiff s complaint without prejudice, and gave the plaintiff until November 1, 2008 to file a further amended complaint. The plaintiff did not file a further amended complaint before that date and, on November 10, 2008, the court dismissed the action with prejudice.

On October 3, 2007, Ebrahim Shanehchian, an alleged participant in the Macy s, Inc. Profit Sharing 401(k) Investment Plan (the 401(k) Plan ), filed a purported class action lawsuit in the United States District Court for the Southern District of Ohio on behalf of persons who participated in the 401(k) Plan and The May Department Stores Company Profit Sharing Plan (the May Plan ) between February 27, 2005 and the present. The complaint charges the Company, as well as certain current and former members of the Company s board of directors and certain current and former members of management, with breach of fiduciary duties owed under the Employee Retirement Income Security Act ( ERISA ) to participants in the 401(k) Plan and the May Plan, alleging that the defendants made false and misleading statements regarding the Company s business, operations and prospects in relation to the integration of the acquired May operations, resulting in supposed artificial inflation of the Company s stock price between August 30, 2005 and May 15, 2007. The plaintiff seeks an unspecified amount of compensatory damages and costs. The Company

believes the lawsuit is without merit and intends to contest it vigorously.

## **Item 1A. Risk Factors.**

Except as set forth below, there have been no material changes to the Risk Factors described in Part I Item 1A. Risk Factors in the Company's Annual Report on Form 10-K for the fiscal year ended February 2, 2008 as filed with the SEC.

*The Company periodically reviews the carrying value of its goodwill for possible impairment; if future circumstances indicate that goodwill is impaired, the Company could be required to write down amounts of goodwill and record impairment charges.*

The Company monitors relevant circumstances, including consumer spending levels, general economic conditions and the market prices for the Company's common stock, and the potential impact that such circumstances might have on the valuation of the Company's goodwill. It is possible that changes in such circumstances, or in the numerous variables associated with the judgments, assumptions and estimates made by the Company in assessing the appropriate valuation of its goodwill, could in the future require the Company to write down a portion of its goodwill and record related non-cash impairment charges. If the Company were required to write down a portion of its goodwill and record related non-cash impairment charges, the Company's financial position and results of operations would be adversely affected and the Company's leverage ratio for purposes of its credit agreement would increase. If such leverage ratio were to exceed the maximum permitted under its credit agreement, the Company would be in default under its credit agreement. At November 1, 2008, a write down of goodwill in excess of approximately \$3.9 billion after income tax benefit, or approximately 43% of the Company's goodwill, would have been required to cause the Company's leverage ratio to exceed the permitted maximum. Due to the seasonal nature of the Company's business, the Company's leverage ratio as determined on a quarterly basis generally is at its highest point as of the end of the Company's third fiscal quarter. Accordingly, it is expected that an even greater write down of goodwill would be required to cause the Company's leverage ratio to exceed the permitted maximum as calculated as of the end of the Company's fourth fiscal quarter.

## **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

The following table provides information regarding the Company's purchases of common stock during the third quarter of 2008:

Pension Plan

|                   | Total Number<br>of Shares<br>Purchased<br>(thousands) | Average<br>Price per<br>Share (\$) | Total Number of<br>Shares Purchased<br>Under Program (1)<br>(thousands) | Open<br>Authorization<br>Remaining (1) (\$)<br>(millions) |
|-------------------|---|------------------------------------|---|---|
| August 3, 2008 -  |   |                                    |   |   |
| August 30, 2008   | -   | -                                  | -   | 852   |
| August 31, 2008 - |   |                                    |   |   |
| October 4, 2008   | -   | -                                  | -   | 852   |
| October 5, 2008 - |   |                                    |   |   |
| November 1, 2008  | =   | =                                  | =   | 852   |
| Total             | =   | =                                  | =   |   |

(1) The Company's board of directors initially approved a \$500 million authorization to purchase common stock on January 27, 2000 and approved additional \$500 million authorizations on each of August 25, 2000, May 18, 2001 and April 16, 2003, additional \$750 million authorizations on each of February 27, 2004 and July 20, 2004, an additional authorization of \$2,000 million on August 25, 2006 and an additional authorization of \$4,000 million on February 26, 2007. All authorizations are cumulative and do not have an expiration date.

## Item 5. Other Information

### Forward-Looking Statements

This report and other reports, statements and information previously or subsequently filed by the Company with the SEC contain or may contain forward-looking statements. Such statements are based upon the beliefs and assumptions of, and on information available to, the management of the Company at the time such statements are made. The following are or may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995: (i) statements preceded by, followed by or that include the words may, will, could, should, believe, expect, future, potential, anticipate, intend, plan, think, estimate or continue or the negative thereof, and (ii) statements regarding matters that are not historical facts. Such forward-looking statements are subject to various risks and uncertainties, including:

risks and uncertainties relating to the possible invalidity of the underlying beliefs and assumptions;

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competitive pressures from department and specialty stores, general merchandise stores, manufacturers' outlets, off-price and discount stores, and all other retail channels, including the Internet, mail-order catalogs and television;

general consumer-spending levels, including the impact of the availability, cost and level of consumer debt, levels of unemployment and consumer confidence, the costs of basic necessities and other goods and the effects of the weather or natural disasters;

possible changes or developments in social, economic, business, industry, market, legal and regulatory circumstances and conditions;

actions taken or omitted to be taken by third parties, including customers, suppliers, business partners, competitors and legislative, regulatory, judicial and other governmental authorities and officials;

adverse changes in relationships with vendors and other product and service providers;

risks related to currency and exchange rates and other capital market, economic and geo-political conditions;

risks associated with severe weather and changes in weather patterns;

risks associated with an outbreak of an epidemic or pandemic disease;

the potential impact of national and international security concerns on the retail environment, including any possible military action, terrorist attacks or other hostilities;

risks associated with the possible inability of the Company's manufacturers to deliver products in a timely manner or meet quality standards;

risks associated with the Company's reliance on foreign sources of production, including risks related to the disruption of imports by labor disputes;

risks related to duties, taxes, and other charges and quotas on imports; and

system failures and/or security breaches, including any security breach that results in the theft, transfer or unauthorized disclosure of customer, employee or company information, or the failure to comply with various laws applicable to the Company in the event of such a breach.

In addition to any risks and uncertainties specifically identified in the text surrounding such forward-looking statements, the statements in the immediately preceding sentence and the statements under captions such as Risk Factors and Special Considerations in reports, statements and information filed by the Company with the SEC from time to time constitute cautionary statements identifying important factors that could cause actual amounts, results, events and circumstances to differ materially from those reflected in such forward-looking statements.

Item 6. Exhibits

- 10.1 Form of Amendment No. 3 to Severance Agreement (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated November 3, 2008).
- 10.2 Fourth Amendment to Credit Card Program Agreement.
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a).
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a).
- 32.1 Certification of Chief Executive Officer under Section 906 of the Sarbanes-Oxley Act.
- 32.2 Certification of Chief Financial Officer under Section 906 of the Sarbanes-Oxley Act.

SIGNATURES

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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.

MACY'S, INC.

Dated: December 8, 2008

By: /s/ Dennis J. Broderick

Name: Dennis J. Broderick

Title: Senior Vice President, General Counsel  
and Secretary

By: /s/ Joel A. Belsky

Name: Joel A. Belsky

Title: Vice President and Controller  
(Principal Accounting Officer)