

MICHAELS STORES INC  
Form 10-Q  
September 07, 2006

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549**

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended July 29, 2006**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number 001-09338**

**MICHAELS STORES, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**75-1943604**

(I.R.S. employer  
identification number)

**8000 Bent Branch Drive**

**Irving, Texas 75063**

**P.O. Box 619566**

**DFW, Texas 75261-9566**

(Address of principal executive offices, including zip code)

**(972) 409-1300**

(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past

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90 days. Yes  No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

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 Registrant's classes of Common Stock, as of the latest practicable date.

<b>Title</b>	<b>Shares Outstanding as of September 5, 2006</b>
Common Stock, par value \$.10 per share	133,326,492

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**MICHAELS STORES, INC.  
FORM 10-Q**

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**MICHAELS STORES, INC.**  
**Part I FINANCIAL INFORMATION**

**Item 1. Financial Statements.**

**MICHAELS STORES, INC.**  
**CONSOLIDATED BALANCE SHEETS**

(In thousands, except share data)

(Unaudited)

	July 29, 2006	January 28, 2006	July 30, 2005
<b>ASSETS</b>			
<b>Current assets:</b>			
Cash and equivalents	\$ 379,320	\$ 452,449	\$ 182,909
Merchandise inventories	874,286	784,032	944,572
Prepaid expenses and other	46,594	44,042	39,010
Deferred and prepaid income taxes	56,863	34,125	113,936
Total current assets	1,357,063	1,314,648	1,280,427
<b>Property and equipment, at cost</b>	1,073,595	1,011,201	963,201
Less accumulated depreciation	(636,349)	(586,382)	(544,714)
	437,246	424,819	418,487
<b>Goodwill</b>	115,839	115,839	115,839
<b>Other assets</b>	22,929	20,249	18,687
	138,768	136,088	134,526
Total assets	\$ 1,933,077	\$ 1,875,555	\$ 1,833,440
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>			
<b>Current liabilities:</b>			
Accounts payable	\$ 272,886	\$ 193,595	\$ 248,645
Accrued liabilities and other	249,691	282,499	232,385
Income taxes payable		20,672	
Total current liabilities	522,577	496,766	481,030
<b>Deferred income taxes</b>		2,803	22,747
<b>Other long-term liabilities</b>	89,173	88,637	86,898

Total long-term liabilities	89,173	91,440	109,645
	611,750	588,206	590,675
<b>Commitments and contingencies</b>			
<b>Stockholders equity:</b>			
Preferred Stock, \$0.10 par value, 2,000,000 shares authorized; none issued			
Common Stock, \$0.10 par value, 350,000,000 shares authorized; 135,906,124 shares issued and 133,139,724 shares outstanding at July 29, 2006, 133,821,417 shares issued and 132,986,517 shares outstanding at January 28, 2006, and 135,827,039 shares issued and outstanding at July 30, 2005	13,591	13,382	13,583
Additional paid-in capital	442,676	386,627	435,625
Retained earnings	951,354	907,773	784,169
Treasury Stock (2,766,400 shares at July 29, 2006, 834,900 shares at January 28, 2006, and none at July 30, 2005)	(94,127)	(27,944)	
Accumulated other comprehensive income	7,833	7,511	9,388
Total stockholders equity	1,321,327	1,287,349	1,242,765
Total liabilities and stockholders equity	\$ 1,933,077	\$ 1,875,555	\$ 1,833,440

See accompanying notes to consolidated financial statements.

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## MICHAELS STORES, INC.

## CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)

(Unaudited)

	Quarter Ended		Six Months Ended	
	July 29, 2006	July 30, 2005	July 29, 2006	July 30, 2005
<b>Net sales</b>	\$ 768,264	\$ 745,493	\$ 1,600,745	\$ 1,566,509
Cost of sales and occupancy expense	495,010	481,263	1,007,051	984,467
<b>Gross profit</b>	273,254	264,230	593,694	582,042
Selling, general, and administrative expense	242,180	223,104	483,916	450,998
Store pre-opening costs	1,521	1,455	2,958	4,194
<b>Operating income</b>	29,553	39,671	106,820	126,850
Interest expense	252	15,500	424	20,589
Other (income) and expense, net	(3,329)	(2,370)	(10,491)	(5,050)
<b>Income before income taxes and cumulative effect of accounting change</b>	32,630	26,541	116,887	111,311
Provision for income taxes	12,318	10,080	44,125	42,296
<b>Income before cumulative effect of accounting change</b>	20,312	16,461	72,762	69,015
Cumulative effect of accounting change, net of income tax of \$54.2 million				88,488
<b>Net income (loss)</b>	\$ 20,312	\$ 16,461	\$ 72,762	\$ (19,473)
<b>Basic earnings (loss) per common share:</b>				
Income before cumulative effect of accounting change	\$ 0.15	\$ 0.12	\$ 0.55	\$ 0.51
Cumulative effect of accounting change, net of income tax				(0.65)
Net income (loss)	\$ 0.15	\$ 0.12	\$ 0.55	\$ (0.14)
<b>Diluted earnings (loss) per common share:</b>				
Income before cumulative effect of accounting change	\$ 0.15	\$ 0.12	\$ 0.54	\$ 0.50
Cumulative effect of accounting change, net of income tax				(0.64)

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Net income (loss)	\$	0.15	\$	0.12	\$	0.54	\$	(0.14)
Dividends declared per common share	\$	0.12	\$	0.10	\$	0.22	\$	0.17

See accompanying notes to consolidated financial statements.



**Table of Contents****MICHAELS STORES, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

	<b>Six Months Ended</b>	
	<b>July 29, 2006</b>	<b>July 30, 2005</b>
<b>Operating activities:</b>		
Net income (loss)	\$ 72,762	\$ (19,473)
Adjustments:		
Depreciation	56,433	48,085
Amortization	187	194
Share-based compensation	10,867	10,646
Tax benefits from stock options exercised	(16,065)	(16,794)
Non-cash charge for the cumulative effect of accounting change		142,723
Loss from early extinguishment of debt		12,133
Other	168	325
Changes in assets and liabilities:		
Merchandise inventories	(90,027)	(151,050)
Prepaid expenses and other	(2,991)	(12,397)
Deferred income taxes and other	(6,190)	(8,899)
Accounts payable	50,560	(7,621)
Accrued liabilities and other	(8,707)	4,125
Income taxes payable	(27,329)	(88,035)
Other long-term liabilities	1,845	11,584
Net cash provided by (used in) operating activities	41,513	(74,454)
<b>Investing activities:</b>		
Additions to property and equipment	(69,549)	(60,510)
Purchases of short-term investments		(226)
Sales of short-term investments		50,605
Net proceeds from sales of property and equipment	8	
Net cash used in investing activities	(69,541)	(10,131)
<b>Financing activities:</b>		
Repayment of Senior Notes		(209,250)
Cash dividends paid to stockholders	(26,625)	(32,670)
Repurchase of Common Stock	(66,182)	(71,197)
Proceeds from stock options exercised	27,870	25,787
Tax benefits from stock options exercised	16,065	16,794
Proceeds from issuance of Common Stock and other	1,791	2,178

Change in cash overdraft	1,980	
Net cash used in financing activities	(45,101)	(268,358)
<b>Net decrease in cash and equivalents</b>	<b>(73,129)</b>	<b>(352,943)</b>
<b>Cash and equivalents at beginning of period</b>	<b>452,449</b>	<b>535,852</b>
<b>Cash and equivalents at end of period</b>	<b>\$ 379,320</b>	<b>\$ 182,909</b>

See accompanying notes to consolidated financial statements.

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**MICHAELS STORES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**For the Six Months Ended July 29, 2006**

**(Unaudited)**

**Note 1. Basis of Presentation**

The consolidated financial statements include the accounts of Michaels Stores, Inc. and our wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated. All expressions of us, we, our, and all similar expressions are references to Michaels Stores, Inc. and our consolidated, wholly-owned subsidiaries, unless otherwise expressly stated or the context otherwise requires.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals and other items, as disclosed) considered necessary for a fair presentation have been included. Because of the seasonal nature of our business, the results of operations for the quarter ended July 29, 2006 are not indicative of the results to be expected for the entire year.

The balance sheet at January 28, 2006 has been derived from the audited financial statements at that date, but does not include all of the information and notes required by generally accepted accounting principles for complete financial statements. For further information, refer to the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended January 28, 2006.

All references herein to fiscal 2006 relate to the 53 weeks ending February 3, 2007 and all references to fiscal 2005 relate to the 52 weeks ended January 28, 2006. In addition, all references herein to the second quarter of fiscal 2006 and the first six months of 2006 relate to the 13 weeks and 26 weeks ended July 29, 2006, respectively, and all references to the second quarter of fiscal 2005 and the first six months of 2005 relate to the 13 weeks and 26 weeks ended July 30, 2005, respectively.

Amounts as of and for the three and six months ended July 30, 2005 were restated to reflect weighted average cost accounting for inventory and the impact of expensing stock options under Statement of Financial Accounting Standards No. 123(R). The changes to our accounting policies are more fully described in Note 2 to these financial statements.

Certain prior period amounts were reclassified to conform to current year presentation.

**Note 2. Changes in Accounting**

As more fully described in our fiscal 2005 Annual Report on Form 10-K, we changed o