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SHOE CARNIVAL INC
Form 10-Q
September 09, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended July 31, 2010

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: 0-21360

Shoe Carnival, Inc.
(Exact name of registrant as specified in its charter)

Indiana 35-1736614
(State or other jurisdiction of (IRS Employer Identification Number)
incorporation or organization)

7500 East Columbia Street
Evansville, IN 47715
(Address of principal executive offices) (Zip code)

(812) 867-6471
(Registrant's telephone number, including area code)

NOT APPLICABLE
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes 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. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

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Yes

No

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

Number of Shares of Common Stock, \$.01 par value, outstanding at September 3, 2010 were 13,182,942.

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SHOE CARNIVAL, INC. INDEX TO FORM 10-Q

| | Page |
|--|---------|
| Part I Financial Information | |
| Item 1. Financial Statements (Unaudited) | |
| Condensed Consolidated Balance Sheets | 3 |
| Condensed Consolidated Statements of Income | 4 |
| Condensed Consolidated Statement of Shareholders' Equity | 5 |
| Condensed Consolidated Statements of Cash Flows | 6 |
| Notes to Condensed Consolidated Financial Statements | 7 - 13 |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations | 13 - 20 |
| Item 3. Quantitative and Qualitative Disclosures About Market Risk | 20 |
| Item 4. Controls and Procedures | 20 |
| Part II Other Information | |
| Item 1A. Risk Factors | 21 |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds | 21 |
| Item 6. Exhibits | 21 - 22 |
| Signature | 23 |

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SHOE CARNIVAL, INC.
PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SHOE CARNIVAL, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
Unaudited

| (In thousands, except per share data) | July 31, 2010 | January 30, 2010 | August 1, 2009 |
|---|-------------------|---------------------|-------------------|
| Assets | | | |
| Current Assets: | | | |
| Cash and cash equivalents | \$ 40,560 | \$ 44,168 | \$ 17,673 |
| Accounts receivable | 1,684 | 746 | 1,948 |
| Merchandise inventories | 238,147 | 197,452 | 216,728 |
| Deferred income tax benefit | 3,342 | 3,255 | 2,424 |
| Other | 3,403 | 2,480 | 7,540 |
| Total Current Assets | 287,136 | 248,101 | 246,313 |
| Property and equipment-net | 61,503 | 62,162 | 66,054 |
| Other | 1,205 | 1,378 | 1,627 |
| Total Assets | \$ 349,844 | \$ 311,641 | \$ 313,994 |
| Liabilities and Shareholders' Equity | | | |
| Current Liabilities: | | | |
| Accounts payable | \$ 79,016 | \$ 57,235 | \$ 73,475 |
| Accrued and other liabilities | 15,345 | 14,353 | 13,712 |
| Total Current Liabilities | 94,361 | 71,588 | 87,187 |
| Deferred lease incentives | 6,774 | 6,501 | 5,791 |
| Accrued rent | 5,164 | 5,115 | 5,155 |
| Deferred income taxes | 20 | 1,052 | 905 |
| Deferred compensation | 4,156 | 3,548 | 3,187 |
| Other | 1,374 | 2,008 | 1,858 |
| Total Liabilities | 111,849 | 89,812 | 104,083 |
| Shareholders' Equity: | | | |
| Common stock, \$.01 par value, 50,000 shares authorized, 13,655 shares issued at July 31, 2010, January 30, 2010 and August 1, 2009 | 137 | 137 | 137 |
| Additional paid-in capital | 66,243 | 66,851 | 67,428 |
| Retained earnings | 182,397 | 169,032 | 158,980 |
| Treasury stock, at cost, 472, 622 and 726 shares at July 31, 2010, January 30, 2010 and August 1, 2009, respectively | (10,782) | (14,191) | (16,634) |
| Total Shareholders' Equity | 237,995 | 221,829 | 209,911 |
| Total Liabilities and Shareholders' Equity | \$ 349,844 | \$ 311,641 | \$ 313,994 |

See notes to condensed consolidated financial statements.

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SHOE CARNIVAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
Unaudited

| (In thousands, except per share data) | Thirteen Weeks Ended July 31, 2010 | Thirteen Weeks Ended August 1, 2009 | Twenty-six Weeks Ended July 31, 2010 | Twenty-six Weeks Ended August 1, 2009 |
|---|---|--|---|--|
| Net sales | \$ 165,394 | \$ 152,840 | \$ 354,851 | \$ 320,109 |
| Cost of sales (including buying, distribution and occupancy costs) | 118,647 | 111,916 | 248,832 | 232,545 |
| Gross profit | 46,747 | 40,924 | 106,019 | 87,564 |
| Selling, general and administrative expenses | 40,758 | 39,020 | 85,039 | 79,076 |
| Operating income | 5,989 | 1,904 | 20,980 | 8,488 |
| Interest income | (28) | (1) | (51) | (4) |
| Interest expense | 63 | 42 | 132 | 84 |
| Income before income taxes | 5,954 | 1,863 | 20,899 | 8,408 |
| Income tax expense | 1,836 | 881 | 7,534 | 3,294 |
| Net income | \$ 4,118 | \$ 982 | \$ 13,365 | \$ 5,114 |
| Net income per share: | | | | |
| Basic | \$ 0.32 | \$.08 | \$ 1.05 | \$.41 |
| Diluted | \$ 0.32 | \$.08 | \$ 1.04 | \$.41 |
| Average shares outstanding: | | | | |
| Basic | 12,720 | 12,487 | 12,704 | 12,483 |
| Diluted | 12,898 | 12,569 | 12,887 | 12,543 |

See notes to condensed consolidated financial statements.

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SHOE CARNIVAL, INC.
 CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
 Unaudited

| (In thousands) | Common Stock | | Amount | Additional Paid-In Capital | Retained Earnings | Treasury Stock | Total |
|--|--------------|----------|--------|----------------------------------|----------------------|-------------------|------------|
| | Issued | Treasury | | | | | |
| Balance at January 30, 2010 | 13,655 | (622) | \$ 137 | \$ 66,851 | \$ 169,032 | \$ (14,191) | \$ 221,829 |
| Stock option exercises | | 25 | | (235) | | 560 | 325 |
| Stock-based compensation income tax benefit | | | | 482 | | | 482 |
| Employee stock purchase plan purchases | | 5 | | (20) | | 110 | 90 |
| Restricted stock awards | | 132 | | (3,018) | | 3,018 | 0 |
| Common stock repurchased | | (12) | | | | (279) | (279) |
| Stock-based compensation expense | | | | 2,183 | | | 2,183 |
| Net income | | | | | 13,365 | | 13,365 |
| Balance at July 31, 2010 | 13,655 | (472) | \$ 137 | \$ 66,243 | \$ 182,397 | \$ (10,782) | \$ 237,995 |

See notes to condensed consolidated financial statements.

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SHOE CARNIVAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
Unaudited

| (In thousands) | Twenty-six Weeks Ended July 31, 2010 | Twenty-six Weeks Ended August 1, 2009 |
|---|---|--|
| Cash Flows From Operating Activities | | |
| Net income | \$ 13,365 | \$ 5,114 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 6,815 | 7,590 |
| Stock-based compensation | 2,398 | 220 |
| Loss on retirement and impairment of assets | 1,223 | 57 |
| Deferred income taxes | (1,119) | (358) |
| Lease incentives | 981 | 715 |
| Other | (899) | (320) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (938) | (241) |
| Merchandise inventories | (40,695) | (27,234) |
| Accounts payable and accrued liabilities | 22,196 | 15,045 |
| Other | (1,336) | (2,538) |
| Net cash provided by (used in) operating activities | 1,991 | (1,950) |
| Cash Flows From Investing Activities | | |
| Purchases of property and equipment | (6,565) | (5,474) |
| Proceeds from sale of property and equipment | 311 | 8 |
| Proceeds from note receivable | 100 | 100 |
| Net cash used in investing activities | (6,154) | (5,366) |
| Cash Flows From Financing Activities | | |
| Proceeds from issuance of stock | 415 | 106 |
| Excess tax benefits from stock-based compensation | 419 | 66 |
| Purchase of treasury stock | (279) | 0 |
| Net cash provided by financing activities | 555 | 172 |
| Net decrease in cash and cash equivalents | (3,608) | (7,144) |
| Cash and cash equivalents at beginning of period | 44,168 | 24,817 |
| Cash and Cash Equivalents at End of Period | \$ 40,560 | \$ 17,673 |
| Supplemental disclosures of cash flow information: | | |
| Cash paid during period for interest | \$ 125 | \$ 83 |
| Cash paid during period for income taxes | \$ 9,826 | \$ 180 |
| Capital expenditures incurred but not yet paid | \$ 1,387 | \$ 912 |
| Supplemental disclosures of non-cash operating and investing activities: | | |
| Forgiveness of accounts payable from litigation settlement (1) | \$ 0 | \$ 1,160 |
| Recording of note receivable from litigation settlement (1) | \$ 0 | \$ 1,200 |

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- (1) On May 30, 2009 a settlement with SDI Industries, Inc. was reached. SDI agreed to forego the collection of the unpaid retainage and to pay \$1.2 million towards remediation of the distribution center's material handling system.

See notes to condensed consolidated financial statements.

SHOE CARNIVAL, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
Unaudited

Note 1 - Basis of Presentation

In our opinion, the accompanying unaudited condensed consolidated financial statements contain all normal recurring adjustments necessary to present fairly our financial position and the results of our operations and our cash flows for the periods presented. Certain information and disclosures normally included in the notes to consolidated financial statements have been condensed or omitted according to the rules and regulations of the Securities and Exchange Commission (the "SEC"), although we believe that the disclosures are adequate to make the information presented not misleading. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year. The condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto contained in our Annual Report on Form 10-K for the fiscal year ended January 30, 2010.

Note 2 - Net Income Per Share

The computation of basic earnings per share of common stock is based on the weighted average number of common shares outstanding during the period. The computation of diluted earnings per share of common stock is based on the weighted average number of shares outstanding plus the incremental shares that would be outstanding assuming the exercise of dilutive stock options and the vesting of restricted stock. The number of incremental shares is calculated by applying the treasury stock method. The following table presents a reconciliation of our basic and diluted weighted average common shares outstanding in accordance with current authoritative guidance:

| (In thousands) | Thirteen Weeks Ended July 31, 2010 | Thirteen Weeks Ended August 1, 2009 | Twenty-six Weeks Ended July 31, 2010 | Twenty-six Weeks Ended August 1, 2009 |
|---------------------------------------|---|--|---|--|
| Basic shares | 12,720 | 12,487 | 12,704 | 12,483 |
| Dilutive effect of stock-based awards | 178 | 82 | 183 | 60 |
| Diluted shares | 12,898 | 12,569 | 12,887 | 12,543 |

No options to purchase shares of common stock were excluded in the computation of diluted shares for the second quarter or for the first six months of fiscal 2010. Options to purchase 410,400 shares of common stock for the second quarter of fiscal 2009 and options to purchase 413,200 shares of common stock for the first six months of fiscal 2009 were not included in the computation of diluted shares because the options' exercise prices were greater than the average market price of our common stock for the period.

Note 3 – Recently Issued Accounting Pronouncements

During January 2010, the Financial Accounting Standards Board ("FASB") issued guidance which provides amendments that require separate disclosure of significant transfers in and out of Level 1 and Level 2 fair value measurements and the presentation of separate information regarding purchases, sales, issuances and settlements for Level 3 fair value measurements. Additionally, the guidance provides amendments that clarify existing disclosures about the level of disaggregation and inputs and valuation techniques. The guidance is effective for financial statements issued for interim and annual periods ending after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements, which are effective for interim and annual periods ending after December 15, 2010. We adopted the guidance on January 31, 2010. This adoption did not have a material impact on our consolidated financial position, results of operations, or cash flows.

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Note 4 - Fair Value Measurements

The FASB has established guidance for using fair value to measure assets and liabilities. This guidance only applies when other standards require or permit the fair value measurement of assets and liabilities. It does not expand the use of fair value measurements. A fair value hierarchy was established, which prioritizes the inputs used in measuring fair value into three broad levels.

- Level 1 – Quoted prices in active markets that are unadjusted and accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2 – Quoted prices for identical assets and liabilities in markets that are not active, quoted prices for similar assets and liabilities in active markets or financial instruments for which significant inputs are observable, either directly or indirectly; and
- Level 3 – Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

Our financial assets as of July 31, 2010, January 30, 2010, and August 1, 2009 included cash and cash equivalents, which are valued using the market approach. The carrying value of cash and cash equivalents approximates fair value due to its short-term nature and is considered a Level 1 fair value measurement. We did not have any financial liabilities measured at fair value for these periods.

The following table summarizes our cash and cash equivalents that are measured at fair value on a recurring basis:

| (In thousands) | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value |
|---------------------------------------|--|--|--|---------------------|
| As of July 31, 2010 | | | | |
| Cash and short-term investments (1) | \$ 32,363 | \$ 0 | \$ 0 | \$ 32,363 |
| Credit and debit card receivables (2) | 8,197 | 0 | 0 | 8,197 |
| | \$ 40,560 | \$ 0 | \$ 0 | \$ 40,560 |
| As of January 30, 2010 | | | | |
| Cash and short-term investments (1) | \$ 40,148 | \$ 0 | \$ 0 | \$ 40,148 |
| Credit and debit card receivables (2) | 4,020 | 0 | 0 | 4,020 |
| | \$ 44,168 | \$ 0 | \$ 0 | \$ 44,168 |
| As of August 1, 2009 | | | | |
| Cash (1) | \$ 9,530 | \$ 0 | \$ 0 | \$ 9,530 |
| Credit and debit card receivables (2) | 8,143 | 0 | 0 | 8,143 |
| | \$ 17,673 | \$ 0 | \$ 0 | \$ 17,673 |

(1) Cash and short-term investments represent cash deposits and short-term investments held with financial institutions, such as commercial paper and money market funds. To date, we have experienced no loss or lack of access to either invested cash or cash held in our bank accounts.

(2) Our credit and debit card receivables are highly liquid financial assets that typically settle in less than three days.

From time to time, we measure certain assets at fair value on a non-recurring basis, specifically long-lived assets evaluated for impairment. Long-lived assets are reviewed for impairment in accordance with current authoritative literature whenever events or changes in circumstances indicate that full recoverability is questionable. If the expected future cash flows related to the long-lived assets are less than the assets' carrying value, an impairment loss would be recognized for the difference between estimated fair value and carrying value. Assets subject to impairment are adjusted to estimated fair value and, if applicable, an impairment loss is recorded in selling, general and administrative expenses.

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The fair value of impaired long-lived assets were measured at fair value on a nonrecurring basis using Level 3 inputs as defined in the fair value hierarchy. During the thirteen-weeks ended July 31, 2010, there were no impairments recorded on long-lived assets held and used. During the thirteen-weeks ended May 1, 2010, long-lived assets held and used with a gross carrying amount of \$7.2 million were written down to their fair value of \$6.1 million, resulting in an impairment charge of \$1.1 million, which was included in earnings for the period. Subsequent to this impairment, these long-lived assets had a remaining unamortized basis of \$375,000. During the fifty-two weeks ended January 30, 2010, long-lived assets held and used with a carrying amount of \$1.4 million were written down to their fair value of \$1.3 million, resulting in an impairment charge of \$90,000, which was included in earnings for the period. Subsequent to this impairment, these long-lived assets had a remaining unamortized basis of \$11,000. We did not have any non-financial liabilities measured at fair value for these periods.

Note 5 - Stock-Based Compensation

Stock Options

The following table summarizes the stock option transactions pursuant to the stock-based compensation plans:

| | Number of Shares | Weighted- Average Exercise Price | Weighted- Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value (in thousands) |
|---|---------------------|---|--|--|
| Outstanding at January 30, 2010 | 393,632 | \$ 14.29 | | |
| Grants | 0 | 0.00 | | |
| Forfeited or expired | (750) | | | |
| Exercised | (24,500) | | | |
| Outstanding July 31, 2010 | 368,382 | \$ 14.36 | 2.79 | \$ 2,463 |
| Options outstanding at July 31, 2010, net of estimated forfeitures | 367,690 | \$ 14.37 | 2.78 | \$ 2,457 |
| Exercisable at July 31, 2010 | 350,047 | \$ 14.46 | 2.54 | \$ 2,308 |

The total fair value at grant date of previously non-vested stock options that vested during each of the twenty-six week periods ended July 31, 2010 and August 1, 2009 was \$32,000. No stock options were granted during the first half of fiscal 2010 or fiscal 2009.

The following table summarizes information regarding options exercised:

| (In thousands) | Thirteen Weeks Ended July 31, 2010 | Thirteen Weeks Ended August 1, 2009 | Twenty-six Weeks Ended July 31, 2010 | Twenty-six Weeks Ended August 1, 2009 |
|---|--|---|--|---|
| Total intrinsic value (1) | \$ 32 | \$ 38 | \$ 230 | \$ 38 |
| Total cash received | \$ 12 | \$ 22 | \$ 325 | \$ 22 |
| Associated excess income tax benefits recorded | \$ 12 | \$ 66 | \$ 79 | \$ 66 |

(1) Defined as the difference between the market value at exercise and the grant price of stock options exercised.

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The following table summarizes information regarding outstanding and exercisable options at July 31, 2010:

| Range of Exercise Price | Options Outstanding | | | Options Exercisable | | |
|-------------------------|-------------------------------|---------------------------------|---------------------------------|-------------------------------|---------------------------------|--|
| | Number of Options Outstanding | Weighted Average Remaining Life | Weighted Average Exercise Price | Number of Options Exercisable | Weighted Average Exercise Price | |
| \$ 4.38 – 12.67 | 186,712 | 3.20 | \$ 12.05 | 175,044 | \$ 12.09 | |
| \$ 13.68 – 17.12 | 181,670 | 2.37 | \$ 16.74 | 175,003 | \$ 16.83 | |

The following table summarizes information regarding stock-based compensation expense recognized for non-vested options:

| (In thousands) | Thirteen Weeks Ended | Thirteen Weeks Ended | Twenty-six Weeks Ended | Twenty-six Weeks Ended |
|---|----------------------|----------------------|------------------------|------------------------|
| | July 31, 2010 (1) | August 1, 2009 | July 31, 2010 (1) | August 1, 2009 |
| Stock-based compensation expense before the recognized income tax benefit | \$ 18 | \$ 19 | \$ 39 | \$ 40 |
| Income tax benefit | \$ 7 | \$ 9 | \$ 15 | \$ 16 |

- (1) Income tax benefit was calculated using an adjusted effective tax rate. The adjusted rate removes the tax effect from a favorable resolution of a state tax position.

As of July 31, 2010, there was approximately \$50,000 of unrecognized compensation expense, net of estimated forfeitures, remaining related to non-vested stock options. This expense is expected to be recognized over a weighted-average period of approximately 0.8 years.

Restricted Stock Awards

The following table summarizes the share transactions for restricted stock awards:

| | Number of Shares | Weighted-Average Grant Date Fair Value |
|--------------------------------|------------------|--|
| Non-vested at January 30, 2010 | 366,334 | \$ 16.89 |
| Granted | 132,181 | 21.63 |
| Vested | (38,922) | 12.50 |
| Forfeited | 0 | 0 |
| Non-vested at July 31, 2010 | 459,593 | \$ 18.63 |

The total fair value at grant date of previously non-vested stock awards that vested during the first half of fiscal 2010 and the first half of fiscal 2009 was \$487,000 and \$12,900, respectively. The weighted-average grant date fair value of stock awards granted during the twenty-six week period ended July 31, 2010 was \$21.63. The weighted-average grant date fair value of stock awards granted during the twenty-six week period ended August 1, 2009 was \$12.26.

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The following table summarizes information regarding stock-based compensation expense (income) recognized for restricted stock awards:

| (In thousands) | Thirteen Weeks Ended July 31, 2010 (1) | Thirteen Weeks Ended August 1, 2009 | Twenty-six Weeks Ended July 31, 2010 (1) | Twenty-six Weeks Ended August 1, 2009 |
|--|--|---|--|---|
| Stock-based compensation expense before the recognized income tax benefit | \$ 1,054 | \$ 305 | \$ 2,127 | \$ (57) |
| Income tax benefit (expense) | \$ 407 | \$ 144 | \$ 812 | \$ (22) |

(1) Income tax benefit was calculated using an adjusted effective tax rate. The adjusted rate removes the tax effect from a favorable resolution of a state tax position.

The \$57,000 of income recorded during the first half of fiscal 2009 was comprised of compensation expense of \$596,000 offset by income of \$653,000. The income was attributable to the first quarter reversal of the cumulative prior period expense for performance-based awards which were deemed by management as not probable of vesting. However, based on our improved financial outlook, a cumulative catch-up of \$279,000 was recorded during the first quarter of fiscal 2010 for a portion of these awards now deemed probable of vesting.

As of July 31, 2010, there was approximately \$3.8 million of unrecognized compensation expense remaining related to both our performance-based and service-based non-vested stock awards. The cost is expected to be recognized over a weighted average period of approximately 0.9 years. This incorporates the current assumptions of the estimated requisite service period required to achieve the designated performance conditions for performance-based stock awards.

Cash-Settled Stock Appreciation Rights (SARs)

Cash-settled stock appreciation rights (SARs) were granted to certain non-executive employees in fiscal 2008 such that one-third of the shares underlying the SARs granted would vest and become fully exercisable on each of the first three anniversaries of the date of the grant and were assigned a five-year term from the date of grant. Each SAR entitles the holder, upon exercise, to receive cash in the amount equal to the closing price of our stock on the date of exercise less the exercise price. The maximum amount paid, however, cannot exceed 100% of the exercise price. In accordance with current authoritative guidance, cash-settled SARs are classified as Other liabilities on the Condensed Consolidated Balance Sheets.

The following table summarizes the SARs activity:

| | Number of Shares | Weighted- Average Exercise Price | Weighted- Average Remaining Contractual Term (Years) |
|---------------------------------|---------------------|---|--|
| Outstanding at January 30, 2010 | 103,364 | \$ 9.72 | |
| Granted | 0 | 0.00 | |
| Forfeited or expired | (2,001) | 9.72 | |
| Exercised | 0 | 0.00 | |
| Outstanding at July 31, 2010 | 101,363 | \$ 9.72 | 3.38 |
| Exercisable at July 31, 2010 | 0 | \$ 0.00 | 0.00 |

The fair value of these liability awards is remeasured at each reporting period until the date of settlement. Increases or decreases in stock-based compensation expense are recognized over the vesting period, or immediately for vested awards. The weighted-average fair value of outstanding, non-vested SAR awards was \$7.19 as of July 31, 2010.

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The fair value was estimated using a trinomial lattice model with the following assumptions:

| | July 31, 2010 |
|-------------------------------------|---------------|
| Risk free interest rate yield curve | 0.14% -1.60% |
| Expected dividend yield | 0.0% |
| Expected volatility | 60.68% |
| Maximum life | 3.38 Years |
| Exercise multiple | 1.71 – 1.74 |
| Maximum payout | \$9.72 |
| Employee exit rate | 2.2% - 9.0% |

The risk free interest rate was based on the U.S. Treasury yield curve in effect at the end of the reporting period. We had not paid and did not anticipate paying cash dividends; therefore, the expected dividend yield was assumed to be zero. Expected volatility was based on the historical volatility of our stock. The exercise multiple and employee exit rate are based on historical option data.

The following table summarizes information regarding stock-based compensation expense recognized for SARs:

| | Thirteen Weeks Ended July 31, 2010 (1) | Thirteen Weeks Ended August 1, 2009 | Twenty-six Weeks Ended July 31, 2010 (1) | Twenty-six Weeks Ended August 1, 2009 |
|--|--|---|--|---|
| (In thousands) | | | | |
| Stock-based compensation expense before the recognized income tax benefit | \$ 36 | \$ 119 | \$ 215 | \$ 222 |
| Income tax benefit | \$ 14 | \$ 56 | \$ 82 | \$ 87 |

- (1) Income tax benefit was calculated using an adjusted effective tax rate. The adjusted rate removes the tax effect from a favorable resolution of a state tax position.

As of July 31, 2010, there was approximately \$235,000 in unrecognized compensation expense related to non-vested SARs. The cost is expected to be recognized over a weighted-average period of approximately 0.9 years.

Employee Stock Purchase Plan

The following table summarizes information regarding stock-based compensation expense recognized for the employee stock purchase plan:

| | Thirteen Weeks Ended July 31, 2010 (1) | Thirteen Weeks Ended August 1, 2009 | Twenty-six Weeks Ended July 31, 2010 (1) | Twenty-six Weeks Ended August 1, 2009 |
|--|--|---|--|---|
| (In thousands) | | | | |
| Stock-based compensation expense before the recognized income tax benefit (2) | \$ 5 | \$ 6 | \$ 16 | \$ 15 |
| Income tax benefit | \$ 2 | \$ 3 | \$ 6 | \$ 6 |

- (1) Income tax benefit was calculated using an adjusted effective tax rate. The adjusted rate removes the tax effect from a favorable resolution of a state tax position.

- (2) Amounts are representative of the 15% discount employees are provided for purchases under the employee stock purchase plan.

Note 6 – Stock Repurchase Program

On August 23, 2010, our Board of Directors authorized a \$25 million share repurchase program, which will terminate upon the earlier of the repurchase of the maximum amount or December 31, 2011. The purchases may be made in the open market or privately negotiated transactions from time-to-time and in accordance with applicable laws, rules and regulations. The program may be amended, suspended or discontinued at any time and does not commit us to repurchase shares of our common stock. We intend to fund the share repurchase program from cash on hand and any shares acquired will be available for stock-based compensation awards and other corporate purposes. The actual number and value of the shares to be purchased will depend on the performance of our stock price and other market conditions. As required by our credit agreement, consent was obtained from the Agent and the Majority Banks, each as defined in the credit agreement. No shares have been repurchased under this program as of September 6, 2010.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Factors That May Effect Future Results

This quarterly report on Form 10-Q contains forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995, that involve a number of risks and uncertainties. A number of factors could cause our actual results, performance, achievements or industry results to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. These factors include, but are not limited to: general economic conditions in the areas of the United States in which our stores are located; the effects and duration of the current economic downturn and unemployment rates; changes in the overall retail environment and more specifically in the apparel and footwear retail sectors; our ability to generate increased sales at our stores; the potential impact of national and international security concerns on the retail environment; changes in our relationships with key suppliers; the impact of competition and pricing; changes in weather patterns, consumer buying trends and our ability to identify and respond to emerging fashion trends; the impact of disruptions in our distribution or information technology operations; the effectiveness of our inventory management; the impact of hurricanes or other natural disasters on our stores, as well as on consumer confidence and purchasing in general; risks associated with the seasonality of the retail industry; our ability to successfully execute our growth strategy, including the availability of desirable store locations at acceptable lease terms, our ability to open new stores in a timely and profitable manner and the availability of sufficient funds to implement our growth plans; higher than anticipated costs associated with the closing of underperforming stores; the inability of manufacturers to deliver products in a timely manner; changes in the political and economic environments in the People's Republic of China, Brazil, Spain and East Asia, where the primary manufacturers of footwear are located; the impact of regulatory changes in the United States and the countries where our manufacturers are located; and the continued favorable trade relations between the United States and China and the other countries which are the major manufacturers of footwear. For a more detailed discussion of certain risk factors see the "Risk Factors" section of our Annual Report on Form 10-K for the fiscal year ended January 30, 2010.

General

Management's Discussion and Analysis of Financial Condition and Results of Operations is intended to provide information to assist the reader in better understanding and evaluating our financial condition and results of operations. We encourage you to read this in conjunction with our condensed consolidated financial statements and the notes to those statements included in PART I, ITEM 1. FINANCIAL STATEMENTS of this Quarterly Report on Form 10-Q, as well as our Annual Report on Form 10-K for the fiscal year ended January 30, 2010 as filed with the SEC.

Overview of Our Business

Shoe Carnival, Inc. is one of the nation's largest family footwear retailers. As of July 31, 2010, we operated 313 stores in 30 states primarily in the Midwest, South and Southeast regions of the United States. We offer a distinctive shopping experience, a broad merchandise assortment and value to our customers while maintaining an efficient store level cost structure.

Our stores combine competitive pricing with a highly promotional, in-store marketing effort that encourages customer participation and creates a fun and exciting shopping experience. We believe this highly promotional atmosphere results in various competitive advantages, including increased multiple unit sales; the building of a loyal, repeat customer base; the creation of word-of-mouth advertising; and enhanced sell through of in-season goods. Our objective is to be the destination store-of-choice for a wide range of consumers seeking moderately priced, current season name brand and private label footwear. Our product assortment includes dress and casual shoes, sandals, boots and a wide assortment of athletic shoes for the entire family. We believe that by offering a wide selection of both athletic and non-athletic footwear, we are able to reduce our exposure to shifts in fashion preferences between those categories.

Our marketing effort targets moderate income, value-conscious consumers seeking name brand footwear for all age groups. We believe that by offering a wide selection of popular styles of name brand merchandise at competitive prices, we generate broad customer appeal. Our cost-efficient store operations and real estate strategy enable us to price products competitively. Low labor costs are achieved by housing merchandise directly on the selling floor in an open-stock format, enabling customers to serve themselves, if they choose. This reduces the staffing required to assist customers and reduces store level labor costs as a percentage of sales. We locate stores predominantly in strip shopping centers in order to take advantage of lower occupancy costs and maximize our exposure to value-oriented shoppers.

Critical Accounting Policies

It is necessary for us to include certain judgments in our reported financial results. These judgments involve estimates that are inherently uncertain and actual results could differ materially from these estimates. The accounting policies that require the more significant judgments are:

Merchandise Inventories - Merchandise inventories are stated at the lower of cost or market using the first-in, first-out (FIFO) method. In determining market value, we estimate the future sales price of items of merchandise contained in the inventory as of the balance sheet date. Factors considered in this determination include, among others, current and recently recorded sales prices, the length of time product has been held in inventory and quantities of various product styles contained in inventory. The ultimate amount realized from the sale of certain product could differ materially from our estimates. We also estimate a shrinkage reserve for the period between the last physical count and the balance sheet date. The estimate for the shrinkage reserve can be affected by changes in merchandise mix and changes in actual shrinkage trends.

Valuation of Long-Lived Assets - We review long-lived assets whenever events or circumstances indicate the carrying value of an asset may not be recoverable. We evaluate the ongoing value of assets associated with each retail store that has been open longer than one year. If the expected future cash flows related to the long-lived assets are less than the assets' carrying value, an impairment loss would be recognized for the difference between estimated fair value and carrying value. Assets subject to impairment are adjusted to estimated fair value and, if applicable, an impairment loss is recorded in selling, general and administrative expenses. Our assumptions and estimates used in the evaluation of impairment, including current and future economic trends for stores, are subject to a high degree of judgment and if actual results or market conditions differ from those anticipated, additional losses may be recorded.

Income Taxes - We calculate income taxes and account for uncertain tax positions in accordance with current authoritative guidance. Deferred tax assets and liabilities are recognized based on the difference between the consolidated financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the estimated tax rates in effect in the years when those temporary differences are expected to reverse. We are also required to make many subjective assumptions and judgments regarding our income tax exposures. Interpretations of and guidance surrounding income tax laws and regulations are often complex, ambiguous and change over time. As such, changes in our subjective assumptions and judgments can materially affect amounts recognized in the consolidated financial statements.

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Insurance Reserves - We use a combination of self-insurance and third-party insurance for workers' compensation, employee medical and general liability insurance. These plans have stop-loss provisions that protect us from individual and aggregate losses over specified dollar values. When estimating our self-insured liabilities, we consider a number of factors, including historical claims experience, severity factors, statistical trends and, in certain instances, valuation assistance provided by independent third-parties. We will continue to evaluate our self-insured liabilities and the underlying assumptions on a quarterly basis and make adjustments as needed. The ultimate cost of these claims may be greater than or less than the established accruals. While we believe that the recorded amounts are adequate, there can be no assurance that changes to management's estimates will not occur due to limitations inherent in the estimating process. In the event we determine an accrual should be increased or reduced, we will record such adjustments in the period in which such determination is made.

Results of Operations Summary Information

| Quarter Ended | Number of Stores | | | End of Period | Store Square Footage | | Comparable Store Sales |
|-------------------|---------------------|--------|--------|---------------|----------------------|---------------|------------------------|
| | Beginning Of Period | Opened | Closed | | Net Change | End of Period | |
| May 1, 2010 | 311 | 3 | 3 | 311 | 2,000 | 3,374,000 | 13.1% |
| July 31, 2010 | 311 | 3 | 1 | 313 | 23,000 | 3,397,000 | 8.3% |
| Year-to-date 2010 | 311 | 6 | 4 | 313 | 25,000 | 3,397,000 | 10.8% |
| May 2, 2009 | 304 | 10 | 1 | 313 | 78,000 | 3,413,000 | (0.3)% |
| August 1, 2009 | 313 | 2 | 1 | 314 | 6,000 | 3,419,000 | (6.4)% |
| Year-to-date 2009 | 304 | 12 | 2 | 314 | 84,000 | 3,419,000 | (3.3)% |

Comparable store sales for the periods indicated include stores that have been open for 13 full months prior to the beginning of the period, including those stores that have been relocated or remodeled. Therefore, stores opened or closed during the periods indicated are not included in comparable store sales.

The following table sets forth our results of operations expressed as a percentage of net sales for the periods indicated:

| | Thirteen Weeks Ended July 31, 2010 | Thirteen Weeks Ended August 1, 2009 | Twenty-six Weeks Ended July 31, 2010 | Twenty-six Weeks Ended August 1, 2009 |
|--|------------------------------------|-------------------------------------|--------------------------------------|---------------------------------------|
| Net sales | 100.0% | 100.0% | 100.0% | 100.0% |
| Cost of sales (including buying, distribution and occupancy costs) | 71.7 | 73.2 | 70.1 | 72.6 |
| Gross profit | 28.3 | 26.8 | 29.9 | 27.4 |
| Selling, general and administrative expenses | 24.7 | 25.6 | 24.0 | 24.7 |
| Operating income | 3.6 | 1.2 | 5.9 | 2.7 |
| Interest income | 0.0 | 0.0 | 0.0 | 0.0 |
| Interest expense | 0.0 | 0.0 | 0.0 | 0.1 |
| Income before income taxes | 3.6 | 1.2 | 5.9 | 2.6 |
| Income tax expense | 1.1 | 0.6 | 2.1 | 1.0 |
| Net income | 2.5% | 0.6% | 3.8% | 1.6% |

Executive Summary for Second Quarter Ended July 31, 2010

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In second quarter of fiscal 2010, we were able to take advantage of increased consumer demand for footwear and consequently, our strong quarterly sales performance, which, when combined with a higher gross profit margin and controlled expenses, produced record second quarter earnings.

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During the second quarter of fiscal 2010:

- Net sales increased \$12.6 million to \$165.4 million, an 8.2% increase over the prior year comparative period.
- Our comparable store sales increased 8.3%. Our sales gains were largely driven by an increase in the number of footwear units sold as the consumer responded favorably to our assortment of footwear.
- Our gross profit margin increased to 28.3% from 26.8% in the second quarter of fiscal 2009. The merchandise margin increased 1.0%. Buying, distribution and occupancy costs decreased 0.5%, as a percentage of sales, due to the leverage associated with comparable store sales increases.
- Selling, general and administrative expenditures decreased 0.9% as a percentage of sales when compared to the second quarter of fiscal 2009.
- We ended the quarter with \$40.6 million in cash and cash equivalents and no interest bearing debt.
- Inventories at July 31, 2010, when compared to levels at the end of the second quarter of fiscal 2009, were up 10.2% on a per store basis. This was in line with our plan to increase inventory in categories where we have an expectation of strong consumer demand.

Results of Operations for the Second Quarter Ended July 31, 2010

Net Sales

Net sales increased \$12.6 million to \$165.4 million during the second quarter ended July 31, 2010, an 8.2% increase over the prior year's second quarter net sales of \$152.8 million. This increase was primarily due to an increase of 8.3% in comparable store sales and a \$3.6 million increase in sales generated by new stores opened since the first quarter of fiscal 2009. These increases were partially offset by a \$3.4 million loss in sales from the 13 stores closed since the first quarter of fiscal 2009.

Gross Profit

Gross profit increased \$5.8 million to \$46.7 million in the second quarter of fiscal 2010 from gross profit of \$40.9 million in the comparable prior year period. The gross margin in the second quarter of fiscal 2010 increased 1.5% to 28.3% from 26.8% in the second quarter of last year. The merchandise margin increased 1.0%. Buying, distribution and occupancy costs decreased 0.5%, as a percentage of sales, primarily due to the leverage associated with comparable store sales increases.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$1.8 million in the second quarter of fiscal 2010 to \$40.8 million from \$39.0 million in the second quarter of last year; however, our sales gain enabled us to leverage these costs as a percentage of sales by 0.9%. Incentive compensation increased \$1.0 million during the second quarter of fiscal 2010, as compared to the prior year period, due to our improved financial performance. Also during the second quarter of fiscal 2010, we spent an additional \$732,000 on advertising and incurred an additional \$1.0 million in store operating expenses as compared to the same period last year. These increases were partially offset by a \$900,000 decrease in our self-insured health care costs, as compared to the second quarter of fiscal 2009 when we experienced unusually high claim activity. The costs related to our self-insured health care programs are subject to a certain degree of volatility and can vary materially between reporting periods.

We opened three stores in the second quarter of fiscal 2010 as compared to two stores in the second quarter of fiscal 2009. Pre-opening costs, such as advertising, payroll and supplies, incurred prior to the opening of a new store are charged in the period they are incurred. The total amount of pre-opening expense incurred will vary by store depending on the specific market and the promotional activities involved. Pre-opening costs included in selling, general and administrative expenses were \$162,000, or 0.1% as a percentage of sales, for the second quarter of fiscal 2010 as compared to \$153,000, or 0.1% as a percentage of sales, for the second quarter of fiscal 2009.

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Interest (Income) Expense, Net

We recorded net interest expense of \$35,000 in the second quarter of fiscal 2010 as compared to net interest expense of \$41,000 in the second quarter of the prior year.

Income Taxes

The effective income tax rate for the second quarter of fiscal 2010 was 30.8% as compared to 47.3% for the second quarter of fiscal 2009. Our provision for income tax expense is based on the current estimate of our annual effective tax rate and is adjusted as necessary for quarterly events. Included in income tax expense for the second quarter of fiscal 2010 was a \$466,000 benefit related to the favorable resolution of a state tax position. This benefit significantly lowered our effective income tax rate for the quarter. Our effective income tax rate for the second quarter of fiscal 2009 increased due to certain discrete quarterly increases in income tax expense. While the value of these discrete adjustments was not materially significant to our financial statements, our lower earnings for the second quarter of fiscal 2009 resulted in a disproportionately higher tax rate.

Net Income

Net income for the second quarter of fiscal 2010 increased to \$4.1 million, or \$0.32 per diluted share, compared to \$982,000, or \$0.08 per diluted share, for the second quarter of fiscal 2009. Included in the \$0.32 per diluted share was a \$0.04 benefit resulting from the favorable resolution of a state tax position.

Results of Operations for the Six Months Ended July 31, 2010

Net Sales

Net sales increased \$34.8 million to \$354.9 million during the six months ended July 31, 2010, a 10.9% increase over net sales of \$320.1 million for the first six months of fiscal 2009. This increase was primarily due to a 10.8% gain in comparable store sales along with an \$8.8 million increase in sales from new stores opened since the beginning of fiscal 2009. These increases were partially offset by a \$7.2 million loss from the 13 stores that were closed since the beginning of fiscal 2009. Increased consumer demand for footwear, combined with our business model of providing a broad product assortment for the entire family at a compelling value, resulted in a significant year-over-year increase in the number of footwear units sold as well as a moderate increase in average unit price.

Gross Profit

Gross profit increased \$18.4 million to \$106.0 million in the first six months of fiscal 2010 from gross profit of \$87.6 million in the comparable prior year period. The gross margin for the first six months of fiscal 2010 increased 2.5% to 29.9% from 27.4% in the comparable prior year period. The merchandise margin increased 1.6%. Buying, distribution and occupancy costs decreased 0.9%, as a percentage of sales, primarily due to the leverage associated with comparable store sales increases.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$5.9 million in the first six months of fiscal 2010 to \$85.0 million from \$79.1 million in the prior year comparable period; however, our sales gain enabled us to leverage these costs as a percentage of sales by 0.7%. Incentive compensation increased \$4.6 million during the first six months of fiscal 2010, as compared to the same period in the prior year, due to our improved financial performance. Also, during the first quarter of fiscal 2010 we recorded a non-cash asset impairment of \$1.1 million related to certain underperforming stores. We increased advertising \$1.0 million year-over-year. These increases were partially offset by a \$1.8 million decrease in our self-insured health care costs, as compared to the first six months of fiscal 2009 when we experienced unusually high claim activity. The costs related to our self-insured health care programs are subject to a certain degree of volatility and can vary materially between reporting periods. Depreciation decreased \$784,000.

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Pre-opening costs included in selling, general and administrative expenses were \$337,000, or 0.1% as a percentage of sales, for the first six months of fiscal 2010 as compared to \$634,000, or 0.2% as a percentage of sales, for the first six months of fiscal 2009. We opened six stores in the first six months of fiscal 2010 as compared to 12 stores in the first six months of fiscal 2009.

The portion of store closing costs and non-cash asset impairment charges included in selling, general and administrative expenses for the first six months of fiscal 2010 was \$1.3 million, or 0.4% as a percentage of sales. In the first six months of fiscal 2009, we incurred \$262,000, or 0.1% as a percentage of sales.

Interest (Income) Expense, Net

We recorded net interest expense of \$81,000 in the first six months of fiscal 2010 as compared to net interest expense of \$80,000 in the first six months of the prior year.

Income Taxes

The effective income tax rate for the first six months of fiscal 2010 was 36.0% as compared to 39.2% for first six months of fiscal 2009. Included in income tax expense for the first six months of fiscal 2010 was a \$466,000 benefit related to the favorable resolution of a state tax position. This benefit significantly lowered our effective income tax rate for the first six months of fiscal 2010 as compared to the same period last year. The annual effective income tax rate for fiscal 2010 is expected to be approximately 37.0%.

Liquidity and Capital Resources

Our primary sources of funds are cash flows from operations and borrowings under our revolving credit facility. Our net cash provided by operating activities was \$2.0 million in the first six months of fiscal 2010 as compared to cash used in operations of \$2.0 million in the first six months of 2009. The change in operating cash flow, when comparing the two periods of each year, was primarily driven by increased earnings and the timing of payments for accounts payable and accrued liabilities, partially offset by an increase in merchandise inventories.

Working capital increased to \$192.8 million at July 31, 2010 from \$159.1 million at August 1, 2009. This \$33.7 million increase resulted primarily from a \$44.3 million increase in cash and cash equivalents and inventories, partially offset by a \$7.2 million increase in accounts payable and accrued and other liabilities. The current ratio at July 31, 2010 was 3.0 as compared to 2.8 at August 1, 2009. We had no outstanding interest bearing debt as of the end of either period.

We expended \$6.6 million in cash during the first six months of fiscal 2010 for the purchase of property and equipment, of which \$3.5 million was for new stores, remodeling and store relocation activities. Additional capital expenditures of approximately \$8 million to \$9 million are expected to be made over the remainder of fiscal 2010 and include four new stores at a projected cost of approximately \$1.5 million and up to \$3.4 million in store remodeling and relocation costs. Additional lease incentives to be received from landlords are expected to approximate \$2.1 million. As part of our long-term strategy to grow our store base and increase our distribution capabilities, we are in the process of redesigning certain elements of the material handling system in our distribution center. We anticipate capital expenditures for the distribution center to total \$1.5 million in fiscal 2010, of which \$1.1 million was expended through the first six months of this year. The remaining capital expenditures are expected to be incurred for various other store improvements, along with continued investments in technology and normal asset replacement activities. The actual amount of cash required for capital expenditures for store operations depends in part on the number of new stores opened, the amount of lease incentives, if any, received from landlords and the number of stores remodeled. The opening of new stores will be dependent upon, among other things, the availability of desirable locations, the negotiation of acceptable lease terms and general economic and business conditions affecting consumer spending in areas we target for expansion.

Our current store prototype uses between 8,000 and 12,000 square feet depending upon, among other factors, the location of the store and the population base the store is expected to service. Capital expenditures for a new store in fiscal 2010 are expected to average approximately \$366,000 with landlord incentives expected to average approximately \$139,000. The average inventory investment in a new store is expected to range from \$325,000 to \$500,000 depending on the size and sales expectation of the store and the timing of the new store opening. Pre-opening expenses, such as advertising, salaries and supplies, are expected to average approximately \$59,000 per store in fiscal 2010. Pre-opening costs, such as advertising, payroll and supplies, incurred prior to the opening of a new store are charged to expense in the period they are incurred. The total amount of pre-opening expense incurred will vary on a store-by-store basis depending on the specific market and the promotional activities involved.

We closed four stores in the first six months of fiscal 2010 and expect to close three additional stores during the remainder of the fiscal 2010. We have identified six stores for closure in fiscal 2011. Depending upon the results of lease re-negotiations with certain landlords of underperforming stores, we may increase or decrease the number of store closures in future periods. The timing and actual amount of expense recorded in closing a store can vary significantly depending, in part, on the period in which management commits to a closing plan, the remaining basis in the fixed assets to be disposed of at closing and the amount of any lease buyout.

We will continue to review our annual store growth rate based on our view of the internal and external opportunities and challenges in the marketplace. At this time, we anticipate opening approximately 20 new stores during fiscal 2011. This will lead to a net store square footage growth of approximately 5%. We continue to believe our strong, unleveraged financial position provides a solid platform for additional square footage growth, as the retail real estate market continues to improve over the next several months and coming years.

Our unsecured credit agreement provides for up to \$50.0 million in cash advances and commercial and standby letters of credit with borrowing limits based on eligible inventory. It contains covenants which stipulate: (1) Total Shareholders' Equity, adjusted for the effect of any share repurchases, will not fall below that of the prior fiscal year-end; (2) the ratio of funded debt plus rent to EBITDA plus rent will not exceed 2.5 to 1.0; and (3) cash dividends for a fiscal year will not exceed 30% of consolidated net income for the immediately preceding fiscal year. We were in compliance with these covenants as of July 31, 2010. Should a default condition be reported, the lenders may preclude additional borrowings and call all loans and accrued interest at their discretion. As of July 31, 2010, there was \$11.1 million in letters of credit outstanding and \$38.9 million available to us for additional borrowings under the credit facility.

On August 23, 2010, our Board of Directors authorized a \$25 million share repurchase program, which will terminate upon the earlier of the repurchase of the maximum amount or December 31, 2011. The purchases may be made in the open market or privately negotiated transactions from time-to-time and in accordance with applicable laws, rules and regulations. The program may be amended, suspended or discontinued at any time and does not commit us to repurchase shares of our common stock. We intend to fund the share repurchase program from cash on hand and any shares acquired will be available for stock-based compensation awards and other corporate purposes. The actual number and value of the shares to be purchased will depend on the performance of our stock price and other market conditions. As required by our credit agreement, consent was obtained from the Agent and the Majority Banks, each as defined in the credit agreement. No shares have been repurchased under this program as of September 6, 2010.

We anticipate that our existing cash and cash flow from operations, supplemented by borrowings under our revolving credit line, will be sufficient to fund our planned store expansion along with other capital expenditures and other operating cash requirements for at least the next 12 months.

Seasonality

Our quarterly results of operations have fluctuated and are expected to continue to fluctuate in the future primarily as a result of seasonal variances and the timing of sales and costs associated with opening new stores. Non-capital expenditures, such as advertising and payroll, incurred prior to opening a new store are charged to expense as incurred. Therefore, our results of operations may be adversely affected in any quarter in which we incur pre-opening expenses related to the opening of new stores.

We have three distinct peak selling periods: Easter, back-to-school and Christmas.

New Accounting Pronouncements

Recent accounting pronouncements applicable to our operations are contained in Note 3 – "Recently Issued Accounting Pronouncements" contained in the Notes to Condensed Consolidated Financial Statements included in PART I, ITEM 1. FINANCIAL STATEMENTS of this Quarterly Report on Form 10-Q.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk in that the interest payable under our credit facility is based on variable interest rates and therefore is affected by changes in market rates. We do not use interest rate derivative instruments to manage exposure to changes in market interest rates. We had no borrowings under our credit facility during the first six months of fiscal 2010.

ITEM 4. CONTROLS AND PROCEDURES

Our Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of July 31, 2010, that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports filed or submitted by us under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and include controls and procedures designed to ensure that information required to be disclosed by us in such reports is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There has been no change in our internal control over financial reporting that occurred during the quarter ended July 31, 2010 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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SHOE CARNIVAL, INC.
PART II - OTHER INFORMATION

ITEM 1A. RISK FACTORS

You should carefully consider the risks and uncertainties we describe both in this Quarterly Report on Form 10-Q and in the "Risk Factors" section of our Annual Report on Form 10-K for the fiscal year ended January 30, 2010 before deciding to invest in, or retain, shares of our common stock. These are not the only risks and uncertainties that we face. Additional risks and uncertainties that we do not currently know about, we currently believe are immaterial or we have not predicted may also harm our business operations or adversely affect us. If any of these risks or uncertainties actually occur, our business, financial condition, results of operations or cash flows could be materially adversely affected. There have been no material changes to the risk factors set forth in our Annual Report on Form 10-K for the fiscal year ended January 30, 2010.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Issuer Purchases of Equity Securities

| Period | Total Number of Shares Purchased ¹ | Average Price Paid per Share | Total Number | Approximate |
|-------------------------------|---|---------------------------------------|---|---|
| | | | of Publicly Announced Programs ² | Dollar Value of Shares that May Yet Be Purchased Under Programs |
| May 2, 2010 to May 29, 2010 | 0 | \$ 0.00 | 0 | \$ 0 |
| May 30, 2010 to July 3, 2010 | 0 | \$ 0.00 | 0 | \$ 0 |
| July 4, 2010 to July 31, 2010 | 220 | \$ 18.18 | 0 | \$ 0 |
| | 220 | | 0 | |

1 Delivered to or withheld by us in connection with employee payroll tax withholding upon the vesting of certain restricted stock awards.

2 On August 23, 2010, our Board of Directors authorized a \$25 million share repurchase program, which will terminate upon the earlier of the repurchase of the maximum amount or December 31, 2011. See Note 6 – "Stock Repurchase Program" for the details of this program.

ITEM 6. EXHIBITS

| Exhibit No. | Description | Incorporated by Reference To | | | Filed Herewith |
|----------------|--|------------------------------|---------|----------------|-------------------|
| | | Form | Exhibit | Filing Date | |
| 3-A | Restated Articles of Incorporation of Registrant | 10-K | 3-A | 4/25/2002 | |
| 3-B | By-laws of Registrant, as amended to date | 8-K | 3-B | 6/12/2009 | |
| 31.1 | Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | | | | X |

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EXHIBITS - Continued

| Exhibit No. | Description | Incorporated by Reference To | | Filing Date | Filed Herewith |
|----------------|--|------------------------------|---------|----------------|-------------------|
| | | Form | Exhibit | | |
| 31.2 | Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | | | | X |
| 32.1 | Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | | | | X |
| 32.2 | Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | | | | X |

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SHOE CARNIVAL, INC.
SIGNATURE

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

Date: September 9, 2010

SHOE CARNIVAL, INC.
(Registrant)

By: /s/ W. Kerry Jackson
W. Kerry Jackson
Executive Vice President and
Chief Financial Officer
(Duly Authorized Officer and Principal Financial Officer)