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CIRCUIT CITY STORES INC
Form 10-Q
July 03, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 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 May 31, 2007
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: 1-5767

CIRCUIT CITY STORES, INC.
(Exact name of registrant as specified in its charter)

Virginia
(State of Incorporation)

54-0493875
(I.R.S. Employer Identification No.)

9950 Mayland Drive
Richmond, Virginia
(Address of principal executive offices)

23233
(Zip Code)

(804) 486 - 4000
(Registrant's telephone number, including area code)

N/A
(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 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.

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.

| Class | Outstanding at May 31, 2007 |
|--------------------------------|-----------------------------|
| Common Stock, par value \$0.50 | 168,521,667 |

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A Table of Contents is included on Page 2 and an Exhibit Index is included on Page 29.

CIRCUIT CITY STORES, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Circuit City Stores, Inc.
Consolidated Statements of Operations (Unaudited)
(Amounts in thousands except per share data)

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| | |
|---|-------|
| | 20 |
| Net sales | \$ 2, |
| Cost of sales, buying and warehousing | 1, |
| Gross profit | |
| Selling, general and administrative expenses | |
| Operating (loss) income | |
| Interest income | |
| Interest expense | |
| (Loss) earnings from continuing operations before income taxes | |
| Income tax (benefit) expense | |
| Net (loss) earnings from continuing operations | |
| Earnings (loss) from discontinued operations, net of tax | |
| Cumulative effect of change in accounting principle, net of tax | |
| Net (loss) earnings | \$ |
| Weighted average common shares: | |
| Basic | |
| Diluted | |
| (Loss) earnings per share: | |
| Basic: | |
| Continuing operations | \$ |
| Discontinued operations | \$ |
| Cumulative effect of change in accounting principle | \$ |
| Basic (loss) earnings per share | \$ |
| Diluted: | |
| Continuing operations | \$ |
| Discontinued operations | \$ |
| Cumulative effect of change in accounting principle | \$ |
| Diluted (loss) earnings per share | \$ |
| Cash dividends paid per share | \$ |

See accompanying notes to consolidated financial statements.

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Circuit City Stores, Inc.
Consolidated Balance Sheets
(Amounts in thousands except share data)

ASSETS
Current assets:

May 31,

(Unaudi

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| | |
|--|----------|
| Cash and cash equivalents | \$ 11 |
| Short-term investments | 25 |
| Accounts receivable, net of allowance for doubtful accounts | 34 |
| Merchandise inventory | 1,74 |
| Deferred income taxes | 2 |
| Income tax receivable | 10 |
| Prepaid expenses and other current assets | 8 |
| | ----- |
| Total current assets | 2,66 |
| Property and equipment, net of accumulated depreciation of \$1,351,374 and \$1,300,267 | 94 |
| Deferred income taxes | 2 |
| Goodwill | 13 |
| Other intangible assets, net of accumulated amortization of \$16,733 and \$14,179 | 1 |
| Other assets | 3 |
| | ----- |
| TOTAL ASSETS | \$ 3,82 |
| | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | |
| Current liabilities: | |
| Merchandise payable | \$ 92 |
| Expenses payable | 24 |
| Accrued expenses and other current liabilities | 35 |
| Accrued compensation | 5 |
| Accrued income taxes | 1 |
| Short-term debt | |
| Current installments of long-term debt | |
| | ----- |
| Total current liabilities | 1,59 |
| Long-term debt, excluding current installments | 4 |
| Accrued straight-line rent and deferred rent credits | 27 |
| Accrued lease termination costs | 7 |
| Other liabilities | 13 |
| | ----- |
| TOTAL LIABILITIES | 2,12 |
| | ----- |
| Commitments and contingent liabilities | |
| Stockholders' equity: | |
| Common stock, \$0.50 par value; 525,000,000 shares authorized; 168,521,667 shares issued and outstanding at May 31, 2007 (170,689,406 at February 28, 2007) | 84 |
| Additional paid-in capital | 307 |
| Retained earnings | 1,266 |
| Accumulated other comprehensive income | 42 |
| | ----- |
| TOTAL STOCKHOLDERS' EQUITY | 1,700 |
| | ----- |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 3,827 |
| | ===== |

See accompanying notes to consolidated financial statements.

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Circuit City Stores, Inc.
 Consolidated Statements of Cash Flows (Unaudited)
 (Amounts in thousands)

| | |
|---|---------|
| | 200 |
| | ----- |
| Operating Activities: | |
| Net (loss) earnings | \$ (54) |
| Adjustments to reconcile net (loss) earnings to net cash used in operating activities of continuing operations: | |
| Net (earnings) loss from discontinued operations | |
| Depreciation expense | 48 |
| Amortization expense | 1 |
| Stock-based compensation expense | 4 |
| Loss on dispositions of property and equipment | |
| Provision for deferred income taxes | 6 |
| Cumulative effect of change in accounting principle | |
| Other | |
| Changes in operating assets and liabilities: | |
| Accounts receivable, net | 19 |
| Merchandise inventory | (99) |
| Prepaid expenses and other current assets | (33) |
| Other assets | |
| Merchandise payable | (2) |
| Expenses payable | (10) |
| Accrued expenses, other current liabilities and income taxes | (159) |
| Other long-term liabilities | 24 |
| | ----- |
| Net cash used in operating activities of continuing operations | (254) |
| | ----- |
| Investing Activities: | |
| Purchases of property and equipment | (65) |
| Proceeds from sales of property and equipment | 10 |
| Purchases of investment securities | (238) |
| Sales and maturities of investment securities | 585 |
| Other investing activities | (1) |
| | ----- |
| Net cash provided by investing activities of continuing operations | 290 |
| | ----- |
| Financing Activities: | |
| Proceeds from short-term borrowings | 4 |
| Principal payments on short-term borrowings | |
| Principal payments on long-term debt | (2) |
| Change in overdraft balances | (28) |
| Excess tax benefit from stock-based payments | |
| Repurchases of common stock | (46) |
| Issuances of common stock | 3 |
| Dividends paid | (6) |
| Other financing activities | |
| | ----- |
| Net cash used in financing activities of continuing operations | (76) |
| | ----- |
| Discontinued Operations: | |

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| | |
|--|--------|
| Operating cash flows | 1 |
| Investing cash flows | |
| Financing cash flows | |
| Net cash provided by (used in) discontinued operations | 11 |
| Effect of exchange rate changes on cash | |
| (Decrease) increase in cash and cash equivalents | (28) |
| Cash and cash equivalents at beginning of year | 141 |
| Cash and cash equivalents at end of period | \$ 112 |

See accompanying notes to consolidated financial statements.

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CIRCUIT CITY STORES, INC.
Notes to Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

Description of Business: Circuit City Stores, Inc. is a leading specialty retailer of consumer electronics, home office products, entertainment software, and related services. The company has two reportable segments: its domestic segment and its international segment.

The domestic segment is engaged in the business of selling brand-name consumer electronics, personal computers, entertainment software, and related services in Circuit City stores in the United States and via the Web at www.circuitcity.com and www.firedog.com. At May 31, 2007, the company's domestic segment operated 643 Superstores and 13 other stores in 158 U.S. media markets.

The international segment, which is comprised of the operations of InterTAN, Inc., is engaged in the business of selling private-label and brand-name consumer electronics in Canada. The international segment's headquarters are located in Barrie, Ontario, Canada, and it operates through retail stores and dealer outlets in Canada primarily under the trade name The Source By Circuit CitySM. At May 31, 2007, the international segment conducted business through 800 retail stores and dealer outlets, which consisted of 505 company-owned stores, 294 dealer outlets, and 1 Battery Plus(R) store. The international segment also operates a Web site at www.thesource.ca.

Effective January 28, 2007, the company returned the management of 92 Rogers Plus(R) stores to Rogers Wireless Inc. in accordance with the Amending Agreement dated March 27, 2004, between Rogers Wireless Inc. and InterTAN Canada Ltd. Results from the Rogers Plus(R) stores are presented as results from discontinued operations in all periods presented.

In February 2007, the board of directors authorized management to explore strategic alternatives for InterTAN, Inc., which could include the sale of the operation.

The company closed a domestic segment operation in fiscal 2007 that previously had been held for sale. Results from this operation are presented as results from discontinued operations in all periods presented.

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The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. Actual results may differ from those estimates. The accompanying unaudited financial statements contain all adjustments of a normal, recurring nature, except as otherwise disclosed herein, which are, in the opinion of management, necessary for a fair presentation. Due to the seasonal nature of the company's business, interim results are not necessarily indicative of results for the entire fiscal year. The company's consolidated financial statements included in this report should be read in conjunction with the notes to the audited financial statements in the company's fiscal 2007 Annual Report on Form 10-K.

2. Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" (FIN 48). FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The company adopted FIN 48 on March 1, 2007.

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Additional discussion and the impact of adopting this Interpretation are included in Note 4, Income Taxes.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements." SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires additional disclosures about fair value measurements. The provisions of SFAS No. 157 are effective for the company beginning with the first quarter of fiscal 2009. The company has not yet determined the impact of adopting this standard.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities." SFAS No. 159 permits entities to choose to measure many financial instruments and certain assets and liabilities at fair value. SFAS No. 159 will be effective for the company beginning with the first quarter of 2009. The company has not yet determined the impact of adopting this standard.

3. (Loss) Earnings Per Share

The following table presents a reconciliation of the denominators used in the (loss) earnings per share calculations.

| (Shares in millions) | Three Months Ended May 31 | |
|--|------------------------------|-------|
| | 2007 | 2006 |
| Weighted average common shares..... | 165.8 | 171.1 |
| Potentially dilutive common equivalent shares: | | |
| Options..... | - | 3.8 |
| Nonvested stock..... | - | 1.4 |
| Weighted average common shares and potentially dilutive common equivalent shares..... | 165.8 | 176.3 |

=====

For the three months ended May 31, 2007, no options or nonvested stock were included in the computation of diluted loss per share because the company reported a net loss from continuing operations. For the three months ended May 31, 2006, the computation of potentially dilutive common equivalent shares excluded certain options to purchase shares of common stock because the exercise prices were greater than the average market price of the common shares and, therefore, the effect would be anti-dilutive. Shares excluded were as follows:

| (Shares in millions) | Three Months Ended May 31 | |
|----------------------|------------------------------|------|
| | 2007 | 2006 |
| Options..... | 8.6 | 1.1 |
| Nonvested stock..... | 4.0 | - |

4. Income Taxes

On March 1, 2007, the company adopted the provisions of FIN 48. As a result, the company decreased retained earnings by \$8.4 million. At March 1, 2007, the company had unrecognized tax benefits of \$38.4 million, of which \$17.6 million would reduce the effective tax rate if recognized in future periods. At March 1, 2007, the company anticipated that total unrecognized tax benefits would decrease by approximately \$6 million by February 29, 2008, as a result of the settlement of state tax uncertainties and the expiration of the statute of limitations in several jurisdictions.

In conjunction with the adoption of FIN 48, the company has classified unrecognized tax benefits not expected to be settled in one year as other liabilities on the consolidated balance sheet. It is the company's policy to account for interest and penalties as a component of income tax expense. The total amount of accrued interest at March 1, 2007, was \$15.3 million. There were no accrued penalties.

The Internal Revenue Service ("IRS") is completing its examination of the company's federal income tax returns for fiscal years 2001, 2002 and 2003. All issues relating to these years have been resolved, but the statute of limitations remains open for these years as a result of waivers. The IRS is currently examining the company's fiscal 2004, 2005 and 2006 income tax returns. With limited exceptions, the company is no longer subject to federal, state, or local income tax examinations for fiscal years before 2001. The statute of limitations for the Canadian tax returns is open for fiscal 2002 to the present.

During the three months ended May 31, 2007, the company decreased its unrecognized tax benefits by \$2.1 million as a result of the resolution of the IRS audit of fiscal year 2003. In addition, the company accrued interest of \$0.1 million associated with its uncertain tax positions.

5. Exit and Other Activities

At a location's cease-use date, estimated lease termination costs to close a store, distribution center or repair center are recorded in selling, general and administrative expenses on the consolidated statements of operations. The calculation of accrued lease termination costs includes future minimum lease payments, taxes, insurance and maintenance costs from the date of closure to the end of the remaining lease term. The calculation also includes estimated sublease income, net of tenant improvement

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allowances and broker fees. The liability for lease termination costs is discounted using a credit-adjusted risk-free rate of interest. The company evaluates these assumptions each quarter and adjusts the liability accordingly.

The accrual for lease termination costs for the domestic segment includes the following activity:

| (Amounts in millions) | Three Months Ended May 31, 2007 |
|---|------------------------------------|
| ----- | ----- |
| Accrued lease termination costs at beginning of period..... | \$ 105.6 |
| Provisions for closed locations..... | - |
| Changes in assumptions about future sublease income and terminations..... | 2.4 |
| Interest accretion..... | 2.0 |
| Cash payments, net of cash received on subleased locations..... | (8.6) |
| ----- | ----- |
| Accrued lease termination costs at end of period..... | 101.4 |
| Less current portion of accrued lease termination costs..... | 29.7 |
| ----- | ----- |
| Non-current portion of accrued lease termination costs..... | \$ 71.7 |
| ===== | ===== |

The current portion of accrued lease termination costs is included in accrued expenses and other current liabilities, and the non-current portion is presented separately on the consolidated balance sheets.

During the first quarter of fiscal 2008, the company made cash payments of \$14.0 million and recorded an additional accrual of \$5.2 million related to severance arrangements. At May 31, 2007, accrued severance totaled \$14.7 million and is included in accrued compensation on the consolidated balance sheet.

6. Stock-Based Compensation

Under the company's stock-based incentive plans, nonqualified stock options, nonvested stock, nonvested stock units and other equity-based awards may be granted to management, key employees and non-employee directors. At May 31, 2007, 4.5 million shares of common stock were available for future grants of options, nonvested stock or nonvested stock units. Upon the exercise of stock options, the grant of nonvested stock, or the vesting of or lapse of deferral restrictions on nonvested stock units, common shares are issued from authorized and unissued shares.

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Compensation expense for stock-based incentive plans is summarized in the table below.

| (Amounts in millions) | Three Months Ended May 31 | |
|--|------------------------------|--------|
| ----- | 2007 | 2006 |
| ----- | ----- | ----- |
| Compensation expense recognized: | | |
| Stock options..... | \$ 2.6 | \$ 4.4 |
| Nonvested stock and nonvested stock units..... | 2.3 | 4.2 |
| Phantom stock units..... | (0.1) | 1.1 |
| Employee stock purchase plan..... | 0.2 | 0.2 |
| Other..... | 0.1 | 0.1 |
| ----- | ----- | ----- |

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| | | |
|--|--------|--------|
| Total compensation expense recognized..... | \$ 5.1 | \$10.0 |
| | ===== | |
| Tax benefit recognized..... | \$ 1.8 | \$ 3.3 |

Stock-based compensation expense is recorded in cost of sales, buying and warehousing or in selling, general and administrative expenses depending on the classification of the related employee's payroll cost. Of the \$5.1 million of stock-based compensation expense recorded in the three months ended May 31, 2007, \$0.6 million was recorded in cost of sales, buying and warehousing and \$4.5 million was recorded in selling, general and administrative expenses. Of the \$10.0 million of stock-based compensation expense recorded in the three months ended May 31, 2006, \$1.3 million was recorded in cost of sales, buying and warehousing and \$8.7 million was recorded in selling, general and administrative expenses.

The company recognizes stock-based compensation expense net of an estimated forfeiture rate based on historical forfeiture activity. During the three months ended May 31, 2007, the company increased the estimated forfeiture rate on certain nonvested stock awards to reflect changes in expectations regarding the number of instruments that will vest. These changes were the result of higher than anticipated actual forfeitures, due in part to restructuring activities.

The value of each phantom stock unit is based on the market value of one share of common stock on the vesting date. The units, which will be settled in cash upon vesting, are remeasured at each reporting date. Due to the decrease in the market value of the company's common stock, the company recorded a benefit of \$0.1 million related to phantom stock units in the three months ended May 31, 2007.

7. Comprehensive (Loss) Income

The components of the company's comprehensive (loss) income consist of net (loss) earnings and other comprehensive income. Other comprehensive income is comprised primarily of foreign currency translation adjustments related to the international segment but also includes unrealized gains and losses on available-for-sale securities and pension adjustments. Other comprehensive income is recorded net of deferred income taxes directly as a component of stockholders' equity.

The components of comprehensive (loss) income, net of taxes, were as follows:

| (Amounts in millions) | Three Months Ended May 31 | |
|-----------------------------------|------------------------------|--------|
| | 2007 | 2006 |
| Net (loss) earnings..... | \$(54.6) | \$ 6.4 |
| Foreign currency translation..... | 16.6 | 7.7 |
| Other..... | 0.1 | - |
| | ----- | |
| Comprehensive (loss) income..... | \$(37.9) | \$14.1 |
| | ===== | |

8. Common Stock Repurchased

The company's board of directors has authorized the repurchase of up to \$1.2 billion of common stock, of which \$233.7 million remained available at May 31, 2007. As of May 31, 2007, the company had repurchased 60.4 million shares of common stock at a cost of \$966.3 million, excluding commission

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fees, cumulatively since inception of the stock repurchase program.

The company's stock repurchase activity for the three months ended May 31, 2007, was as follows:

| (Amounts in millions) | Three Months Ended May 31, 2007 |
|---|------------------------------------|
| Total number of shares repurchased..... | 2.5 |
| Cost, excluding commission fees..... | \$46.7 |

9. Pension Plans

The company's domestic segment has a noncontributory defined benefit pension plan that was frozen as of February 28, 2005, except for employees who (i) were within three years of their early retirement date or normal retirement date; (ii) had reached their early or normal retirement date; or (iii) were permanently disabled before March 1, 2005. As a result, all employees affected by the plan freeze retain any benefits accumulated to the effective date, but are no longer eligible to increase their benefit.

The company also has an unfunded nonqualified benefit restoration plan that restored retirement benefits for domestic segment senior executives who were affected by Internal Revenue Code limitations on benefits provided under the company's pension plan. The benefit restoration plan was frozen as of February 28, 2005, and will provide benefits for participants who, as of that date, were within 10 years of attaining their early retirement date or normal retirement date.

On December 22, 2005, the benefit restoration plan was amended to permit W. Alan McCollough to elect to receive a lump-sum payment following his retirement, allowing him to receive the maximum benefit payable under the plan. This lump-sum payment resulted in a loss due to settlement of \$0.2 million for the first quarter of fiscal 2007.

The components of the net pension (income) expense for the plans were as follows:

| (Amounts in thousands) | Three Months Ended May 31 | |
|-------------------------------------|------------------------------|---------|
| | 2007 | 2006 |
| Service cost..... | \$ 589 | \$ 778 |
| Interest cost..... | 4,020 | 3,794 |
| Expected return on plan assets..... | (5,182) | (4,782) |
| Recognized prior service cost..... | 53 | 54 |
| Recognized actuarial loss..... | 372 | 609 |
| Loss due to settlement..... | - | 191 |
| Net pension (income) expense..... | \$ (148) | \$ 644 |
| | ===== | |

The company did not make a contribution to the defined benefit pension plan during the three months ended May 31, 2007. No contributions are required during fiscal 2008 under applicable law for this pension plan. The company intends to make any contributions necessary to meet ERISA minimum funding standards and intends to make additional contributions as needed to ensure that the fair value of plan assets at February 29, 2008 exceeds the accumulated benefit obligation.

A contribution of \$0.7 million, which is equal to the expected benefit payments for fiscal 2008, is expected to be made to the restoration plan

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during fiscal 2008. Benefit payments during the three months ended May 31, 2007, were \$0.2 million.

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10. Discontinued Operations

For the quarter ended May 31, 2007, earnings from discontinued operations totaled \$0.2 million, which is net of \$0.2 million of income taxes, and primarily related to the operations of the Rogers Plus(R) stores, of which the management was returned to Rogers Wireless Inc. in January 2007.

For the quarter ended May 31, 2006, the loss from discontinued operations totaled \$0.7 million, which is net of \$0.4 million of income taxes, and related to the operations of the Rogers Plus(R) stores and a domestic segment operation that was closed in fiscal 2007.

11. Segment Information

The company has two reportable segments: its domestic segment and its international segment. The company identified these segments based on its management reporting structure and the nature of the products and services offered by each segment. The domestic segment is engaged in the business of selling brand-name consumer electronics, personal computers, entertainment software, and related services in the United States. The international segment is engaged in the business of selling private-label and brand-name consumer electronics in Canada.

Net sales by reportable segment were as follows:

| (Amounts in millions) | Three Months Ended May 31 | |
|----------------------------|------------------------------|-----------|
| | 2007 | 2006 |
| Domestic segment..... | \$2,376.9 | \$2,485.5 |
| International segment..... | 108.6 | 111.1 |
| Net sales..... | \$2,485.5 | \$2,596.6 |

Net (loss) earnings from continuing operations by reportable segment were as follows:

| (Amounts in millions) | Three Months Ended May 31 | |
|---|------------------------------|--------|
| | 2007 | 2006 |
| Domestic segment..... | \$(57.4) | \$ 9.3 |
| International segment..... | 2.6 | (4.0) |
| Net (loss) earnings from continuing operations..... | \$(54.8) | \$ 5.3 |

The international segment's net earnings from continuing operations for the first quarter of fiscal 2008 include \$5.0 million, after-tax, of additional sales proceeds related to a former subsidiary.

Total assets by reportable segment were as follows:

| (Amounts in millions) | At May 31 2007 | At February 2007 |
|-----------------------|-------------------|---------------------|
| ----- | | |

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| | | |
|----------------------------|-----------|----------|
| Domestic segment..... | \$3,483.1 | \$3,657. |
| International segment..... | 344.8 | 349. |
| <hr/> | | |
| Total assets..... | \$3,827.9 | \$4,007. |
| <hr/> | | |

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The domestic segment net sales by category were as follows:

| (Dollar amounts in millions) | Three Months Ended May 31 | | | |
|--------------------------------------|---------------------------|------------|-----------|------------|
| | 2007 | | 2006 (a) | |
| | \$ | % of Sales | \$ | % of Sales |
| Video..... | \$ 934.0 | 39.3% | \$1,031.9 | 41.5% |
| Information technology..... | 628.6 | 26.4 | 618.8 | 24.9 |
| Audio..... | 334.9 | 14.1 | 380.6 | 15.3 |
| Entertainment..... | 272.5 | 11.5 | 258.8 | 10.4 |
| Warranty, services and other(b)..... | 206.9 | 8.7 | 195.5 | 7.9 |
| <hr/> | | | | |
| Net sales..... | \$2,376.9 | 100.0% | \$2,485.5 | 100.0% |
| <hr/> | | | | |

(a) Reclassifications have been made to conform with the current year presentation. These include reclassifying sales from video and information technology to warranty, services and other.

(b) Warranty, services and other includes extended warranty net sales; revenues from computer-related services, mobile installations, home theater installations and product repairs; net financing; and revenues from third parties for services subscriptions.

The international segment net sales by category were as follows:

| (Dollar amounts in millions) | Three Months Ended May 31 | | | |
|--------------------------------------|---------------------------|------------|---------|------------|
| | 2007 | | 2006 | |
| | \$ | % of Sales | \$ | % of Sales |
| Video..... | \$ 20.0 | 18.5% | \$ 20.5 | 18.5% |
| Information technology..... | 39.8 | 36.6 | 44.6 | 40.1 |
| Audio..... | 36.5 | 33.6 | 35.8 | 32.2 |
| Entertainment..... | 5.0 | 4.6 | 3.2 | 2.9 |
| Warranty, services and other(a)..... | 7.3 | 6.7 | 7.0 | 6.3 |
| <hr/> | | | | |
| Net sales..... | \$108.6 | 100.0% | \$111.1 | 100.0% |
| <hr/> | | | | |

(a) Warranty, services and other includes extended warranty sales and product repair revenue.

12. Supplemental Consolidated Statements of Cash Flows Information

The following table summarizes supplemental cash flow information.

(Amounts in millions)

Supplemental schedule of non-cash investing and financing activities:

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| | |
|--|--------|
| Increase in capital expenditure accrual..... | \$ 0. |
| Capital lease obligation..... | \$ 0. |
| (Decrease) increase in sale-leaseback receivables..... | \$ (8. |

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

We are a leading specialty retailer of consumer electronics, home office products, entertainment software, and related services. We have two reportable segments: our domestic segment and our international segment.

Our domestic segment is engaged in the business of selling brand-name consumer electronics, personal computers, entertainment software, and related services in our stores in the United States and via the Web at www.circuitcity.com and www.firedog.com. At May 31, 2007, the domestic segment operated 643 Superstores and 13 other stores in 158 U.S. media markets.

Our international segment, which is comprised of the operations of InterTAN, Inc., is engaged in the business of selling private-label and brand-name consumer electronics in Canada. The international segment's headquarters are located in Barrie, Ontario, Canada, and it operates through retail stores and dealer outlets in Canada primarily under the trade name The Source By Circuit CitySM. At May 31, 2007, the international segment conducted business through 800 retail stores and dealer outlets, which consisted of 505 company-owned stores, 294 dealer outlets and 1 Battery Plus(R) store. The international segment also operates a Web site at www.thesource.ca.

Effective January 28, 2007, we returned the management of 92 Rogers Plus(R) stores to Rogers Wireless Inc. in accordance with the Amending Agreement dated March 27, 2004, between Rogers Wireless Inc. and InterTAN Canada Ltd. Results from the Rogers Plus(R) stores are presented as results from discontinued operations in all periods presented.

In February 2007, the board of directors authorized management to explore strategic alternatives for InterTAN, Inc., which could include the sale of the operation.

We closed a domestic segment operation in fiscal 2007 that previously had been held for sale. Results from this operation are presented as results from discontinued operations in all periods presented.

Management's Discussion and Analysis (MD&A) is designed to provide the reader of financial statements with a narrative discussion of our results of operations; financial position, liquidity and capital resources; critical accounting policies and significant estimates; and the impact of recently issued accounting standards. Our MD&A is presented in seven sections:

- o Executive Summary
- o Critical Accounting Policies
- o Results of Operations
- o Recent Accounting Pronouncements
- o Financial Condition
- o Financial Outlook
- o Forward-Looking Statements

This discussion should be read in conjunction with our Consolidated Financial Statements and accompanying Notes included in this report, the Annual Report on Form 10-K for the fiscal year ended February 28, 2007, as well as our reports on Form 8-K and other SEC filings. All per share amounts are presented on a fully

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diluted basis.

EXECUTIVE SUMMARY

Fiscal 2008 First Quarter Performance

- o Net sales declined 4.3 percent, driven by a comparable store sales decline of 5.6 percent. In the same period last fiscal year, we posted total sales growth of 17.4 percent and comparable store sales growth of 14.6 percent.

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- o In the domestic segment, direct channel sales, which include Web- and call center-originated sales, grew 21 percent and services revenues grew 70 percent over the same period last year.
- o Gross profit margin declined 195 basis points compared with the gross profit margin for the first quarter of the prior year due to a decrease in domestic segment extended warranty net sales as well as lower merchandise margins that were driven by a greater mix of lower-margin PC hardware sales.
- o SG&A expenses as a percentage of net sales increased from the prior year by 166 basis points, which primarily reflects approximately 90 basis points in net incremental expenses, related to investments in the domestic segment for information technology, multi-channel capabilities and innovation activities, as a percentage of consolidated net sales, and the de-leveraging impact of lower sales.
- o The loss from continuing operations before income taxes was 3.3 percent of net sales compared with earnings from continuing operations before income taxes of 0.3 percent of net sales in the same period last year.
- o We reported a net loss from continuing operations of \$54.8 million, or 33 cents per share, for the first quarter of fiscal 2008, compared with net earnings of \$5.3 million, or 3 cents per share, in the same period last year.

CRITICAL ACCOUNTING POLICIES

See the discussion of critical accounting policies under Management's Discussion and Analysis of Financial Condition and Results of Operations in our fiscal 2007 Annual Report on Form 10-K. These policies relate to inventory valuation, goodwill, accrued lease termination costs, stock-based compensation and pension plans. We have updated our critical accounting policy for income taxes due to our adoption of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" (FIN 48).

Income Taxes

We account for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes," which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of the temporary differences between the book and tax basis of recorded assets and liabilities. We make estimates and judgments with regard to the calculation of certain tax assets and liabilities. SFAS No. 109 requires that deferred tax assets be reduced by valuation allowances if it is more likely than not that some portion of the deferred tax asset will not be realized. Quarterly, we assess the likelihood that the benefits of a deferred tax asset will be realized by considering historical and projected taxable income and tax planning strategies. Should a change in circumstances lead to a change in our judgment regarding the realization of deferred tax assets in future years, we adjust the valuation

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allowances in the period that the change in circumstances occurs, along with a current charge or credit to net earnings. Significant changes to our estimates and assumptions may result in an increase or decrease to our tax expense in a subsequent period.

On March 1, 2007, we adopted FIN 48. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Positions taken by an entity in its income tax returns must satisfy a more-likely-than-not recognition threshold, assuming that the positions will be examined by taxing authorities with full knowledge of all relevant information, in order for the positions to be recognized in the consolidated financial statements. Quarterly, we evaluate the income tax positions taken by the company, or expected to be taken by the company, to determine whether these positions meet the more-likely-than-not threshold prescribed by FIN 48. We are required to make subjective judgments and assumptions regarding our income tax exposures and must consider a variety of factors, including the current tax statutes, the current status of audits performed by tax authorities, and the statute of limitations in each tax jurisdiction. To the extent an uncertain tax position is resolved for an amount that varies from the recorded estimated liability, our income tax expense in a given financial statement period could be materially affected.

Our unrecognized tax benefits were \$35.5 million at May 31, 2007, and \$15.2 million at February 28, 2007. In conjunction with the adoption of FIN 48, we have classified unrecognized tax benefits not expected to be

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settled in one year as other liabilities on the consolidated balance sheet. Additional discussion and the impact of adopting this Interpretation are included in Note 4, Income Taxes, of the Notes to Consolidated Financial Statements, included in Item 1, Financial Statements, of this Quarterly Report on Form 10-Q.

RESULTS OF OPERATIONS

Our operations, consistent with other retailers in general, are subject to seasonal influences. Historically, we have realized more of our net sales and net earnings in the fourth quarter, which includes the majority of the holiday selling season, than in any other fiscal quarter. The net (loss) earnings of any quarter are seasonally disproportionate to net sales since administrative and certain operating expenses remain relatively constant during the year. Therefore, quarterly results should not be relied upon as necessarily indicative of results for the entire fiscal year.

Summary of Segment Performance

Where relevant, we have included separate discussions of our domestic and international segments. The following tables summarize performance by segment.

SEGMENT PERFORMANCE SUMMARY

| (Dollar amounts in millions) | Three Months Ended May 31, 2007 | | | |
|-------------------------------------|---------------------------------|--------|---------------|--------|
| | Domestic | % of | International | % of |
| | \$ | Sales | \$ | Sales |
| Net sales..... | \$ 2,376.9 | 100.0% | \$ 108.6 | 100.0% |
| Gross profit..... | \$ 520.5 | 21.9% | \$ 39.7 | 36.6% |
| Selling, general and administrative | | | | |

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| | | | | | | |
|---|----|--------|--------|----|------|-------|
| expenses..... | \$ | 612.5 | 25.8% | \$ | 35.9 | 33.0% |
| Net (loss) earnings from continuing operations..... | \$ | (57.4) | (2.4)% | \$ | 2.6 | 2.4% |

| (Dollar amounts in millions) | Domestic | | Three Months Ended May 31, 2006 | | | |
|---|----------|------------|---------------------------------|------------|-------|--------|
| | \$ | % of Sales | \$ | % of Sales | | |
| Net sales..... | \$ | 2,485.5 | 100.0% | \$ | 111.1 | 100.0% |
| Gross profit..... | \$ | 594.9 | 23.9% | \$ | 40.9 | 36.8% |
| Selling, general and administrative expenses..... | \$ | 587.6 | 23.6% | \$ | 46.7 | 42.0% |
| Net earnings (loss) from continuing operations..... | \$ | 9.3 | 0.4% | \$ | (4.0) | (3.6)% |

Net Sales

Consolidated

For the first quarter of fiscal 2008, our net sales decreased 4.3 percent to \$2.49 billion, and comparable store sales decreased 5.6 percent from the same period last fiscal year. A store's sales are included in comparable store sales after the store has been open for a full 12 months. Comparable store sales include Web-originated sales and sales from relocated and remodeled stores. Sales from closed stores are included in comparable store sales until the month in which the stores are closed. The calculation of comparable store sales excludes the impact of fluctuations in foreign currency exchange rates.

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Our major sales categories are

- o video, which includes televisions, imaging products, DVD hardware, camcorders, digital cameras, furniture, and related accessories;
- o information technology, which includes personal computer hardware, telecommunications products and related accessories;
- o audio, which includes home audio products, mobile audio products, portable audio products, navigation products, and related accessories;
- o entertainment, which includes movie software, music software, game software, game hardware and personal computer software; and
- o warranty, services and other, which includes extended warranty sales; revenues from computer-related services, mobile installations, home theater installations and product repairs; net financing; and revenues received from third parties for services subscriptions.

Domestic Segment

For the first quarter of fiscal 2008, the domestic segment's net sales were \$2.38 billion, a decrease of 4.4 percent from the same period last fiscal year. Comparable store sales decreased 6.0 percent driven by a decline in traffic and close rates as compared to the same period last fiscal year. For the quarter, direct channel sales grew 21 percent, and services revenues grew 70 percent over the same period last fiscal year.

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The domestic segment's net sales represented by each major sales category for the periods ended May 31, 2007 and 2006, are shown below.

NET SALES BY CATEGORY

| (Dollar amounts in millions) | Three Months Ended May 31 | | | |
|-----------------------------------|---------------------------|---------------|-----------|---------------|
| | 2007 | % of Sales | 2006 (a) | % of Sales |
| | \$ | | \$ | |
| Video..... | \$ 934.0 | 39.3% | \$1,031.9 | 41.5% |
| Information technology..... | 628.6 | 26.4 | 618.8 | 24.9 |
| Audio..... | 334.9 | 14.1 | 380.6 | 15.3 |
| Entertainment..... | 272.5 | 11.5 | 258.8 | 10.4 |
| Warranty, services and other..... | 206.9 | 8.7 | 195.5 | 7.9 |
| Net sales..... | \$2,376.9 | 100.0% | \$2,485.5 | 100.0% |

(a) Reclassifications have been made to conform with the current year presentation. These include reclassifying sales from video and information technology to warranty, services and other.

In the video category, we produced a double-digit comparable store sales decrease in the first quarter. Total television comparable store sales decreased by double digits, as a significant comparable store sales decrease in projection and tube televisions more than offset high single-digit comparable store sales growth in flat panel televisions. Comparable store sales of digital imaging products and accessories decreased by single digits. Comparable store sales of camcorders and DVD hardware declined by double digits.

In the information technology category, we produced a single-digit comparable store sales increase in the first quarter. Comparable store sales of notebook computers increased by double digits, and comparable store sales of desktop computers were approximately flat compared with the prior year period.

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In the audio category, we produced a double-digit comparable store sales decrease in the first quarter. Double-digit declines in comparable store sales of portable digital audio, mobile, home audio and digital satellite radio products were partially offset by a significant double-digit comparable store sales increase in navigation products.

In the entertainment category, we produced a single-digit comparable store sales increase in the first quarter, reflecting strong double-digit comparable store sales increases in video gaming products and PC software. Comparable store sales of video software declined by low-double digits and comparable store sales in music software declined by strong double digits.

The domestic segment sells extended warranty programs on behalf of unrelated third parties who are the primary obligors. Extended warranty net sales were \$73.7 million, or 3.1 percent of domestic segment net sales, in the first quarter of fiscal 2008, compared with \$92.3 million, or 3.7 percent of domestic segment net sales, in the same period last fiscal year. Services revenues increased 70 percent to \$64.4 million from \$37.9 million in the same period last fiscal year.

The following table provides the number of our domestic segment stores:

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DOMESTIC SEGMENT STORE MIX

| | May 31, 2007 | Feb. 28, 2007 |
|---|--------------|---------------|
| Superstores..... | 643 | 642 |
| Other stores..... | 13 | 12 |
| Total domestic segment stores..... | 656 | 654 |

During the first quarter of fiscal 2008, we opened one relocated Superstore, replacing a store that was closed in February 2007.

International Segment

The international segment's net sales decreased 2.2 percent to \$108.6 million for the first quarter of fiscal 2008, compared with \$111.1 million for the first quarter of last fiscal year. The decrease was driven by the impact of closing 53 retail stores, net of openings, during the fourth quarter of fiscal 2007. The effect of fluctuations in foreign currency exchange rates favorably impacted the sales decline by approximately 1 percentage point. Comparable store sales increased 4.4 percent for the quarter in local currency.

NET SALES BY CATEGORY

| (Dollar amounts in millions) | Three Months Ended May 31 | | | |
|-----------------------------------|---------------------------|---------------|----------------|---------------|
| | 2007 | % of Sales | 2006 | % of Sales |
| | \$ | | \$ | |
| Video..... | \$ 20.0 | 18.5% | \$ 20.5 | 18.5% |
| Information technology..... | 39.8 | 36.6 | 44.6 | 40.1 |
| Audio..... | 36.5 | 33.6 | 35.8 | 32.2 |
| Entertainment..... | 5.0 | 4.6 | 3.2 | 2.9 |
| Warranty, services and other..... | 7.3 | 6.7 | 7.0 | 6.3 |
| Net sales..... | \$108.6 | 100.0% | \$111.1 | 100.0% |

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INTERNATIONAL SEGMENT STORE MIX

| | May 31, 2007 | Feb. 28, 2007 |
|--|--------------|---------------|
| Company-owned stores..... | 505 | 509 |
| Dealer outlets..... | 294 | 296 |
| Battery Plus(R) stores..... | 1 | 1 |
| Total international segment stores..... | 800 | 806 |

Effective January 28, 2007, we returned the management of 92 Rogers Plus(R) stores to Rogers Wireless Inc. in accordance with the Amending Agreement dated March 27, 2004, between Rogers Wireless Inc. and InterTAN Canada Ltd. As of May 31, 2006, there were 93 Rogers Plus(R) stores in operation. Results from these stores are presented as results from discontinued operations in all periods presented.

Gross Profit Margin

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Consolidated

The gross profit margin was 22.5 percent of net sales in the first quarter of fiscal 2008, compared with 24.5 percent for the same period last fiscal year.

Domestic Segment

The domestic segment's gross profit margin was 21.9 percent of domestic segment net sales in the first quarter of fiscal 2008, compared with 23.9 percent for the same period last fiscal year. The 204 basis points decrease impacted the consolidated gross profit margin decline by 197 basis points. The decline was driven primarily by a decrease of 61 basis points in extended warranty net sales as a percent of domestic segment net sales as well as a decrease of 116 basis points in merchandise margins as a percent of domestic segment net sales. The lower merchandise margins were driven by a greater mix of lower-margin PC hardware sales which reflects both strength in that business as well as below-plan sales in the television category.

International Segment

The international segment's gross profit margin was 36.6 percent of international segment net sales in the first quarter of fiscal 2008, compared with 36.8 percent for the same period last fiscal year. The international segment's gross profit margin decline of 22 basis points did not materially impact the consolidated gross profit margin rate. The decrease resulted primarily from a mix shift from higher-margin categories, such as parts, batteries and accessories, to lower-margin categories, such as video games, navigation products and PC hardware.

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Selling, General and Administrative Expenses

Consolidated

| (Dollar amounts in millions) | Three Months Ended May 31 | | | |
|--|---------------------------|--------------|----------------|--------------|
| | 2007 | | 2006 | |
| | \$ | % of Sales | \$ | % of Sales |
| Store expenses..... | \$556.7 | 22.4% | \$534.0 | 20.6% |
| General and administrative expenses..... | 85.5 | 3.4 | 87.4 | 3.4 |
| Stock-based compensation expense..... | 4.5 | 0.2 | 8.7 | 0.3 |
| Remodel expenses..... | - | - | - | - |
| Relocation expenses..... | 1.1 | - | 1.5 | 0.1 |
| Pre-opening expenses..... | 0.5 | - | 2.6 | 0.1 |
| Total | \$648.4 | 26.1% | \$634.3 | 24.4% |

Selling, general and administrative expenses were 26.1 percent of consolidated net sales in the first quarter of fiscal 2008, compared with 24.4 percent for the same period last fiscal year. The domestic segment contributed 201 basis points to the 166 basis point increase in the consolidated expense-to-sales ratio, while the international segment's decline in expenses partially offset the increase in the domestic segment's expense-to-sales ratio.

Domestic Segment

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| (Dollar amounts in millions) | Three Months Ended May 31 | | 2006 | |
|--|---------------------------|------------|---------|------------|
| | 2007 | % of Sales | \$ | % of Sales |
| Store expenses..... | \$524.2 | 22.1% | \$496.9 | 20.0% |
| General and administrative expenses..... | 82.4 | 3.5 | 78.9 | 3.2 |
| Stock-based compensation expense..... | 4.3 | 0.2 | 7.6 | 0.3 |
| Remodel expenses..... | - | - | - | - |
| Relocation expenses..... | 1.1 | - | 1.5 | 0.1 |
| Pre-opening expenses..... | 0.5 | - | 2.6 | 0.1 |
| Total | \$612.5 | 25.8% | \$587.6 | 23.6% |

For the three months ended May 31, 2007, the domestic segment's expense-to-sales ratio increased 213 basis points from the same period last fiscal year. The increase primarily reflects approximately 90 basis points in net incremental expenses, related to investments in information technology, multi-channel capabilities and innovation activities, as a percentage of consolidated net sales, and the de-leveraging impact of lower sales. The segment incurred general and administrative expenses of \$4.9 million, or 20 basis points as a percentage of consolidated net sales, associated with severance from restructuring activities.

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International Segment

| (Dollar amounts in millions) | Three Months Ended May 31 | | 2006 | |
|--|---------------------------|------------|--------|------------|
| | 2007 | % of Sales | \$ | % of Sales |
| Store expenses..... | \$32.6 | 30.0% | \$37.1 | 33.4% |
| General and administrative expenses..... | 3.1 | 2.9 | 8.5 | 7.7 |
| Stock-based compensation expense..... | 0.2 | 0.1 | 1.1 | 1.0 |
| Total | \$35.9 | 33.0% | \$46.7 | 42.0% |

For the first quarter of fiscal 2007, the international segment's expense-to-sales ratio decreased 900 basis points from the same period last year primarily due to \$7.5 million of additional sales proceeds related to a former subsidiary, reducing current period general and administrative expenses. The international segment also benefited from the impact of store closings during the fourth quarter of last fiscal year.

Income Tax (Benefit) Expense

The consolidated effective income tax rate applicable to results from continuing operations was 33.5 percent for the three months ended May 31, 2007, and 36.1 percent for the three months ended May 31, 2006. The decrease in the effective tax rate is the result of an increase in tax-exempt investment income in proportion to projected earnings.

Net (Loss) Earnings from Continuing Operations

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The net loss from continuing operations was \$54.8 million, or 33 cents per share, in the three months ended May 31, 2007, compared with net earnings from continuing operations of \$5.3 million, or 3 cents per share, in the same period last fiscal year.

Earnings (Loss) from Discontinued Operations

For the quarter ended May 31, 2007, the net earnings from discontinued operations totaled \$0.2 million, which is net of \$0.2 million of income taxes, and primarily related to the operations of the Rogers Plus(R) stores, of which the management was returned to Rogers Wireless Inc. in January 2007.

For the quarter ended May 31, 2006, the net loss from discontinued operations totaled \$0.7 million, which is net of \$0.4 million of income taxes, and related to the operations of the Rogers Plus(R) stores and a domestic segment operation that was closed in fiscal 2007.

Cumulative Effect of Change in Accounting Principle

In the first quarter of fiscal 2007, we adopted Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment," using the modified prospective transition method, resulting in a non-cash after-tax benefit of \$1.8 million.

RECENT ACCOUNTING PRONOUNCEMENTS

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" (FIN 48). FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

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We adopted FIN 48 on March 1, 2007. Additional discussion and the impact of adopting this Interpretation are included in Note 4, Income Taxes, of the Notes to Consolidated Financial Statements, included in Item 1, Financial Statements, of this Quarterly Report on Form 10-Q.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements." SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires additional disclosures about fair value measurements. The provisions of SFAS No. 157 are effective for us beginning with the first quarter of fiscal 2009. We have not yet determined the impact of adopting this standard.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities." SFAS No. 159 permits entities to choose to measure many financial instruments and certain assets and liabilities at fair value. SFAS No. 159 will be effective for us beginning with the first quarter of 2009. We have not yet determined the impact of adopting this standard.

FINANCIAL CONDITION

Liquidity and Capital Resources

Cash Flows

Cash Flows Summary

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The following table summarizes our cash flows for the three months ended May 31, 2007 and 2006:

| (Amounts in millions) | Three Months Ended May 31 | |
|--|------------------------------|------------|
| | 2007 | 2006 |
| ----- | | |
| Net cash (used in) provided by: | | |
| Operating activities..... | \$ (254.6) | \$ (151.2) |
| Investing activities..... | 290.1 | 244.4 |
| Financing activities..... | (76.1) | (15.3) |
| Discontinued operations..... | 11.2 | (1.6) |
| Effect of exchange rate changes on cash..... | 0.6 | 0.2 |
| | ----- | |
| (Decrease) increase in cash and cash equivalents..... | \$ (28.8) | \$ 76.5 |
| | ===== | |

Operating Activities

For the three months ended May 31, 2007, net cash used in operating activities was \$254.6 million, compared with net cash used in operating activities of \$151.2 million in the three months ended May 31, 2006. The change was due primarily to a net loss of \$54.6 million for the three months ended May 31, 2007, compared with net earnings of \$6.4 million for the three months ended May 31, 2006. Also driving the increase in cash used by operations were changes in net-owned inventory, calculated as merchandise inventory less merchandise payable. During the three months ended May 31, 2007, the increase in net-owned inventory was \$108.6 million. During the three months ended May 31, 2006, net-owned inventory increased by \$88.1 million.

Investing Activities

Net cash provided by investing activities was \$290.1 million for the three months ended May 31, 2007, compared with \$244.4 million for the three months ended May 31, 2006. The increase in cash provided by investing activities was due primarily to an increase in net sales and maturities of investment securities, partially offset by increased purchases of property and equipment as we make investments in new Superstores, store refreshes and category resets.

Financing Activities

For the three months ended May 31, 2007, net cash used in financing activities was \$76.1 million, compared with net cash used in financing activities of \$15.3 million in the three months ended May 31, 2006. The change

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was due primarily to a decrease in overdraft balances and a decrease in the cash provided by the issuance of common stock.

The board of directors has authorized the repurchase of up to \$1.2 billion of common stock, of which \$233.7 million remained available at May 31, 2007. During the three months ended May 31, 2007, we used cash to repurchase 2.5 million shares of common stock at an average price of \$18.68 per share, for a total price of \$46.7 million, excluding commission fees. During the same period last fiscal year, we used cash to repurchase 1.7 million shares of common stock at an average price of \$28.92 per share, for a total price of \$50.0 million, excluding commission fees. As of May 31, 2007, we had repurchased 60.4 million shares of common stock at an average price of \$16.01 per share, for a total price of \$966.3 million, excluding commission fees, cumulatively since inception of the stock repurchase program.

During fiscal 2007, the board of directors authorized an increase in our

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quarterly dividend rate to \$0.04 per share from the previous quarterly dividend of \$0.0175 per share on our common stock. The dividend rate change was effective with the declaration of the quarterly dividend in the third quarter of fiscal 2007, resulting in an increase in cash used to pay dividends in the three months ended May 31, 2007, compared with the three months ended May 31, 2006.

Cash, Cash Equivalents and Short-term Investments

At May 31, 2007, we had cash, cash equivalents and short-term investments of \$364.1 million, compared with \$739.5 million at February 28, 2007. The \$375.4 million decline in the cash position primarily reflects cash used by operations of \$254.6 million, including a \$108.6 million increase in net-owned inventory. Also driving the decrease in cash were \$65.7 million in purchases of property and equipment and \$53.5 million in stock repurchase activities and dividend payments.

Net-owned Inventory

Merchandise inventory increased to \$1.75 billion at May 31, 2007, from \$1.64 billion at February 28, 2007. Net-owned inventory, calculated as merchandise inventory less merchandise payable, increased by \$108.6 million from February 28, 2007, to May 31, 2007. Domestic segment net-owned inventory increased by \$76.6 million from February 28, 2007, to May 31, 2007, primarily due to seasonal inventory build.

Capital Expenditures

Capital expenditures, net of landlord reimbursements, were \$63.3 million in the three months ended May 31, 2007, compared with \$33.9 million in the same period last fiscal year. The increase in capital expenditures was driven primarily by increased investments in new and relocating Superstores.

Sources of Liquidity

We have a \$500 million revolving credit facility secured by inventory and accounts receivable. This facility is scheduled to mature in June 2009. The credit facility provides for a \$400 million borrowing limit for the domestic segment and a \$100 million borrowing limit for the international segment. At May 31, 2007, short-term borrowings were \$4.7 million and related to our international segment. At May 31, 2007, outstanding letters of credit were \$57.5 million, leaving \$437.8 million available for borrowing. We were in compliance with all covenants at May 31, 2007.

Our primary sources of liquidity include available cash, the expected reduction in net-owned inventory, borrowing capacity under the credit facility and landlord reimbursements. We expect that our primary sources of liquidity will be sufficient to fund capital expenditures and working capital for the foreseeable future.

Contractual Obligations and Contingencies

In March 2007, we signed a seven-year, \$775 million information technology services contract with IBM. Also, as a result of the adoption of FIN 48, we had \$31.1 million of unrecognized tax benefits and the related accrued interest recorded in other liabilities on the consolidated balance sheet at May 31, 2007. We are not able to reasonably estimate in which future periods these unrecognized tax benefits will be settled.

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FINANCIAL OUTLOOK

In the first quarter, the amount of change that we introduced to the company led to significant volatility, which we expect to continue through the summer as we roll out the new retail operating platform, convert to the new point-of-sale system in additional stores, gain experience with the new organizational

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structure and develop competence with using our new merchandising and marketing systems. Combined with an uncertain macroeconomic environment, it is difficult to project sales and earnings performance for the balance of the fiscal year. As a result, we withdrew financial guidance on June 20, 2007.

We continue to expect to open 60 to 65 new and relocated domestic segment Superstores in fiscal 2008. Domestic segment Superstore openings estimates are shown in the following table. The timing of store openings depends upon a number of factors and can change during the year. We expect more than half of the openings to be in a 20,000 square foot format. Initial results from the 20,000 square foot formats indicate reduced capital expenditures and operating expenses, resulting in higher returns, as compared with the 30,000 square foot formats.

Domestic Segment Superstore Openings Estimates(a)

| | Q1 (a) | Q2 | Q3 | Q4 | FY08 |
|---------------------------------------|----------|-----------|--------------|--------------|--------------|
| Incremental Superstores..... | 0 | 10 | 17-18 | 16-18 | 43-46 |
| Relocated Superstores..... | 1 | 4 | 7-8 | 5-6 | 17-19 |
| Total Superstore openings..... | 1 | 14 | 24-26 | 21-24 | 60-65 |

(a) First quarter openings are actual. On February 26, 2007, we closed one store in advance of opening a replacement store in the first quarter of fiscal 2008. The replacement store is included in relocations for the first quarter of fiscal 2008.

In fiscal 2009, we expect to open 75 to 100 Superstores.

FORWARD-LOOKING STATEMENTS

The provisions of the Private Securities Litigation Reform Act of 1995 provide companies with a "safe harbor" when making forward-looking statements. This "safe harbor" encourages companies to provide prospective information about their companies without fear of litigation. We wish to take advantage of the "safe harbor" provisions of the Act. Our statements that are not historical facts, including statements about management's expectations for fiscal 2008 and beyond, are forward-looking statements and involve various risks and uncertainties. In most cases, you can identify our forward-looking statements by words such as "expect," "anticipate," "believe," "should," "may," "plan," "will" or similar words.

Forward-looking statements are estimates and projections reflecting our judgment and involve a number of risks and uncertainties that could cause actual results to differ materially from those suggested by the forward-looking statements. Although we believe that the estimates and projections reflected in the forward-looking statements are reasonable, our expectations may prove to be incorrect. The retail industry and the specialty retail industry, in particular, are dynamic by nature and have undergone significant changes in recent years. Our ability to anticipate and successfully respond to the continuing challenges of our industry is key to achieving our expectations. Important factors that could cause actual results to differ materially from estimates or projections contained in our forward-looking statements include the following:

- o changes in the amount and degree of competition, pricing and promotional pressure exerted by current competitors and potential new competition from competitors using either similar or alternative methods or channels of distribution such as the Internet, telephone shopping services and mail order;
- o our response to pricing and promotional activities of our competitors;

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- o the successful implementation of our initiatives to accelerate sales growth, gross margin improvement and expense reductions;
- o our ability to reduce our overall cost and expense structure and to maintain cost reductions while growing sales;

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- o our ability to control and leverage expenses as a percentage of sales;
- o changes in general economic conditions including, but not limited to, financial market performance, consumer credit availability, interest rates, inflation, energy prices, personal discretionary spending levels, trends in consumer retail spending, (both in general and in our product categories), unemployment and consumer sentiment about the economy in general;
- o the level of consumer response to new products or product features in the merchandise categories we sell and changes in our merchandise sales mix;
- o the pace of commoditization of digital products;
- o the impact of inventory and supply chain management initiatives on inventory levels and profitability;
- o our ability to generate sales and margin growth through expanded services offerings;
- o the impact of new products and product features on the demand for existing products and the pricing and profit margins associated with the products we sell;
- o significant changes in retail prices for products and services we sell;
- o changes in availability or cost of financing for working capital and capital expenditures, including financing to support development of our business;
- o the lack of availability or access to sources of inventory or the loss or disruption in supply from one of our major suppliers;
- o our inability to liquidate excess inventory should excess inventory develop;
- o our inability to maintain sales and profitability improvement programs for our Circuit City Superstores, including our store revitalization plan;
- o our ability to continue to generate strong sales growth through our direct sales channel;
- o the availability of appropriate real estate locations for relocations and new stores;
- o the cost and timeliness of new store openings and relocations;
- o consumer reaction to new store locations and changes in our store design and merchandise;
- o our ability and the ability of Chase Card Services to successfully market and promote the third party credit card program being offered by Chase Card Services;
- o the extent to which customers respond to promotional financing offers and the types of promotional terms we offer;
- o our ability to attract and retain an effective management team or changes in the costs or availability of a suitable work force to manage and support our service-driven operating strategies;
- o the impact of initiatives related to upgrading merchandising, marketing, point of sale and information systems on revenue and operating margin and the costs associated with these investments;
- o changes in production or distribution costs or costs of materials for our advertising;
- o effectiveness of our advertising and marketing programs for increasing consumer traffic and sales;
- o the imposition of new restrictions or regulations regarding the sale of products and/or services we sell, changes in tax rules and regulations applicable to, the imposition of new environmental restrictions, regulations or laws or the discovery of environmental conditions at current or future locations, or any failure to comply with such laws or any adverse change in such laws;
- o our strategic evaluation of the international segment;

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- o further deterioration of the expected future performance of our international segment resulting in an additional goodwill impairment charge;
- o the timely production and delivery of private-label merchandise and level of consumer demand for those products;
- o reduced investment returns or other changes relative to the assumptions for our pension plans that impact our pension expense;
- o changes in our anticipated cash flow;
- o whether, when and in what amounts share repurchases may be made under our stock buyback program;
- o adverse results in significant litigation matters;
- o currency exchange rate fluctuations between Canadian and U.S. dollars and other currencies;
- o the global regulatory and trade environment;
- o the disruption of global, national or regional transportation systems; and
- o the occurrence of severe weather events or natural disasters that could significantly damage or destroy stores or prohibit consumers from traveling to our retail locations, especially during peak selling periods.

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We believe our forward-looking statements are reasonable. However, undue reliance should not be placed on forward-looking statements, which are based on current expectations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk from potential changes in the U.S./Canadian currency exchange rates as they relate to inventory purchases and the translation of our international segment's financial results.

Inventory Purchases

A portion of InterTAN's purchases are from vendors requiring payment in U.S. dollars. Accordingly, there is risk that the value of the Canadian dollar could fluctuate relative to the U.S. dollar from the time the goods are ordered until payment is made. InterTAN's management monitors the foreign exchange risk associated with its U.S. dollar open orders on a regular basis by reviewing the amount of such open orders; exchange rates, including forecasts from major financial institutions; local news; and other economic factors. At May 31, 2007, U.S. dollar open purchase orders totaled approximately \$10.8 million. A 10 percent decline in the value of the Canadian dollar would result in an increase in product cost of approximately \$1.1 million for those orders. The incremental cost of such a decline in currency values, if incurred, would be reflected in higher cost of sales in future periods. In these circumstances, management would take product pricing action, to the degree commercially feasible.

Translation of Financial Results

Because we translate our international segment's financial results from Canadian dollars to U.S. dollars, fluctuations in the value of the Canadian dollar have a direct effect on reported consolidated results. We do not hedge against the possible impact of this risk. A 10 percent adverse change in the foreign currency exchange rate would not have a significant impact on our consolidated results of operations or financial position.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of the company's management, including the chief executive officer, the company has evaluated the

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effectiveness of its "disclosure controls and procedures," as that term is defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this Quarterly Report on Form 10-Q. Based upon the evaluation, the chief executive officer concluded that the company's disclosure controls and procedures are effective.

Changes in Internal Control over Financial Reporting

There were no changes in the company's internal control over financial reporting that occurred during the quarter ended May 31, 2007, that have materially affected, or are reasonably likely to materially affect, the company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

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ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended February 28, 2007, which could materially affect our business, financial condition or future results. There have been no material changes to those risk factors since we filed our 2007 Annual Report on Form 10-K. The risks described in our Annual Report on Form 10-K are not the only risks facing our company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

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

The following table provides information about common stock repurchases by or on behalf of the company during the quarter ended May 31, 2007:

| (Amounts in millions except per share data and footnote (a) data) | Total Number of Shares Purchased(a) | Average Price Paid per Share(a) | Tot o Pur Part A |
|---|---|--|------------------------------|
| March 1 - March 31, 2007..... | - | \$ - | |
| April 1 - April 30, 2007..... | 2.5 | \$18.68 | |
| May 1 - May 31, 2007..... | - | \$ - | |
| | | | |
| Total fiscal 2008 first quarter..... | 2.5 | \$18.68 | |

(a) In addition to purchases under the share repurchase authorization, these columns include shares of common stock withheld to pay tax withholding obligations for employees in connection with the vesting of stock awards. The withholding of 1,193 shares in the month of March and 116 shares in the month of April are not considered part of the share repurchase program described in (b) below.

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(b) In January 2003, the company announced that the board of directors had authorized the repurchase of up to \$200 million of common stock. In June 2004, the company announced a \$200 million increase in its stock repurchase authorization, raising the repurchase capacity to \$400 million. In March 2005, the company announced a \$400 million increase in its stock repurchase authorization, raising the repurchase capacity to \$800 million. In June 2006, the company announced a \$400 million increase in its stock repurchase authorization, raising the repurchase capacity to \$1.2 billion. There is no expiration date under the authorization. At May 31, 2007, \$233.7 million remained available for stock repurchases under the \$1.2 billion stock repurchase authorization.

ITEM 6. EXHIBITS

Articles of Incorporation and Bylaws

- 3.1 Circuit City Stores, Inc. Amended and Restated Articles of Incorporation, effective February 3, 1997, as amended through August 16, 2005, filed as Exhibit 3.1 to the company's Form 8-A/A filed September 13, 2005 (File No. 1-5767), are expressly incorporated herein by this reference.
- 3.2 Circuit City Stores, Inc. Bylaws, as amended April 17, 2007, filed as Exhibit 3.1 to the company's Current Report on Form 8-K filed April 19, 2007 (File No. 1-5767), are expressly incorporated herein by this reference.
- 3.3 Circuit City Stores, Inc. Bylaws, as amended June 26, 2007, filed as Exhibit 3.1 to the company's Current Report on Form 8-K filed July 2, 2007 (File No. 1-5767), are expressly incorporated herein by this reference.

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Rule 13a-14(a)/15d-14(a) Certifications

- 31.1 Certification of CEO and Principal Financial Officer under Rule 13a-14(a) of the Securities Exchange Act of 1934

Section 1350 Certifications

- 32.1 Certification of CEO and Principal Financial Officer under Section 906 of the Sarbanes-Oxley Act of 2002

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SIGNATURES

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.

CIRCUIT CITY STORES, INC.
(Registrant)

By: /s/ Philip J. Schoonover

Philip J. Schoonover
Chairman, President and Chief Executive Of

Principal Financial Officer

By: /s/ Philip J. Dunn

Philip J. Dunn
Senior Vice President, Treasurer,
Controller and
Chief Accounting Officer

July 3, 2007

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