

STEIN MART INC  
Form 10-Q  
May 03, 2013  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended October 27, 2012

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 0-20052

**STEIN MART, INC.**

(Exact name of registrant as specified in its charter)

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|   |   |
|---|---|
| <b>Florida</b><br>(State or other jurisdiction of<br>incorporation or organization)             | <b>64-0466198</b><br>(I.R.S. Employer<br>Identification Number) |
| <b>1200 Riverplace Blvd., Jacksonville, Florida</b><br>(Address of principal executive offices) | <b>32207</b><br>(Zip Code)                                      |
| <b>Registrant's telephone number, including area code: (904) 346-1500</b>                       |   |

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 Web site, 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

The number of shares outstanding of the Registrant's common stock as of April 15, 2013 was 43,821,565.

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**EXPLANATORY NOTE**

This Form 10-Q of Stein Mart, Inc. (the Company) for the fiscal quarter ended October 27, 2012, includes restated Condensed Consolidated Financial Statements for the fiscal periods ended October 29, 2011 and includes the restated Condensed Consolidated Balance Sheet as of January 28, 2012.

The Company is restating such prior financial statements arising primarily from errors made in inventory markdowns, leasehold improvement costs, compensated absences (paid vacation), indirect overhead costs and other matters. In addition, prior year financial statements also reflect the correction of certain previously identified errors and out of period adjustments that were deemed immaterial to the annual or interim periods in which they relate.

On November 6, 2012, the Board of Directors of the Company, based on the recommendation of the Audit Committee and in consultation with management, concluded that our previously issued financial statements contained errors and that investors should no longer rely upon the Company's previously released financial statements. See Note 2 to our Condensed Consolidated Financial Statements for further information. All schedules and footnotes impacted indicate the restated amounts under the caption Restated.

In connection with the restatement of our financial statements described herein, management re-evaluated the Company's internal controls over financial reporting and disclosure controls and procedures and determined that material weaknesses existed as of October 27, 2012. For a discussion of management's consideration of the Company's internal control over financial reporting and the material weaknesses identified, see Item 4.

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**Table of Contents****Stein Mart, Inc.****Condensed Consolidated Balance Sheets****(Unaudited)**

(In thousands, except for share and per share data)

|  | October 27, 2012 | January 28, 2012<br>(Restated) (1) | October 29, 2011<br>(Restated) (1) |
|--|------------------|------------------------------------|------------------------------------|
| <b>ASSETS</b>  |                  |                                    |                                    |
| Current assets:  |                  |                                    |                                    |
| Cash and cash equivalents  | \$ 104,121       | \$ 94,053                          | \$ 101,941                         |
| Inventories  | 296,689          | 218,832                            | 272,427                            |
| Prepaid expenses and other current assets  | 17,566           | 34,139                             | 33,130                             |
| Total current assets   | 418,376          | 347,024                            | 407,498                            |
| Property and equipment, net  | 125,582          | 109,990                            | 107,041                            |
| Other assets   | 24,635           | 22,569                             | 19,693                             |
| Total assets   | \$ 568,593       | \$ 479,583                         | \$ 534,232                         |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>   |                  |                                    |                                    |
| Current liabilities:   |                  |                                    |                                    |
| Accounts payable   | \$ 185,037       | \$ 106,063                         | \$ 168,378                         |
| Accrued expenses and other current liabilities   | 65,499           | 68,063                             | 69,682                             |
| Total current liabilities  | 250,536          | 174,126                            | 238,060                            |
| Other liabilities  | 56,667           | 55,786                             | 50,084                             |
| Total liabilities  | 307,203          | 229,912                            | 288,144                            |
| <b>COMMITMENTS AND CONTINGENCIES</b>   |                  |                                    |                                    |
| Shareholders' equity:  |                  |                                    |                                    |
| Preferred stock - \$.01 par value; 1,000,000 shares authorized; no shares issued or outstanding  |                  |                                    |                                    |
| Common stock - \$.01 par value; 100,000,000 shares authorized; 43,608,228, 43,588,821 and 43,654,608 shares issued and outstanding, respectively |                  |                                    |                                    |
|  | 436              | 436                                | 437                                |
| Additional paid-in capital   | 15,430           | 15,268                             | 15,702                             |
| Retained earnings  | 246,866          | 235,386                            | 229,493                            |
| Accumulated other comprehensive (loss) income  | (1,342)          | (1,419)                            | 456                                |
| Total shareholders' equity   | 261,390          | 249,671                            | 246,088                            |
| Total liabilities and shareholders' equity   | \$ 568,593       | \$ 479,583                         | \$ 534,232                         |

(1) As described in Note 2 to these Condensed Consolidated Financial Statements, we have restated the Condensed Consolidated Financial Statements.

The accompanying notes are an integral part of these condensed consolidated financial statements.



**Table of Contents****Stein Mart, Inc.****Condensed Consolidated Statements of Income****(Unaudited)**

(In thousands, except per share amounts)

|  | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011<br>(Restated) (1) | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks<br>Ended<br>October 29, 2011<br>(Restated) (1) |
|--|------------------------------------|--|------------------------------------|---|
| Net sales                                    | \$ 273,729                         | \$ 263,232   | \$ 863,809                         | \$ 846,999  |
| Cost of merchandise sold                     | 203,039                            | 196,579  | 627,436                            | 614,875   |
| Gross profit                                 | 70,690                             | 66,653   | 236,373                            | 232,124   |
| Selling, general and administrative expenses | 74,431                             | 69,690   | 217,306                            | 208,941   |
| Operating (loss) income                      | (3,741)                            | (3,037)  | 19,067                             | 23,183  |
| Interest expense, net                        | 81                                 | 84   | 170                                | 251   |
| (Loss) income before income taxes            | (3,822)                            | (3,121)  | 18,897                             | 22,932  |
| Income tax (benefit) expense                 | (2,163)                            | (1,425)  | 7,417                              | 8,894   |
| Net (loss) income                            | \$ (1,659)                         | \$ (1,696)   | \$ 11,480                          | \$ 14,038   |
| Net (loss) income per share:                 |                                    |  |                                    |   |
| Basic  | \$ (0.04)                          | \$ (0.04)  | \$ 0.26                            | \$ 0.31   |
| Diluted                                      | \$ (0.04)                          | \$ (0.04)  | \$ 0.26                            | \$ 0.31   |
| Weighted-average shares outstanding:         |                                    |  |                                    |   |
| Basic  | 42,568                             | 43,248   | 42,622                             | 43,731  |
| Diluted                                      | 42,568                             | 43,248   | 42,769                             | 44,038  |

(1) As described in Note 2 to these Condensed Consolidated Financial Statements, we have restated the Condensed Consolidated Financial Statements.

The accompanying notes are an integral part of these condensed consolidated financial statements.

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**Stein Mart, Inc.**

**Condensed Consolidated Statements of Comprehensive Income**

**(Unaudited)**

(In thousands)

|   | 13 Weeks<br>Ended<br>October 27, 2012 | 13 Weeks<br>Ended<br>October 29, 2011<br>(Restated) (1) | 39 Weeks<br>Ended<br>October 27, 2012 | 39 Weeks<br>Ended<br>October 29, 2011<br>(Restated) (1) |
|---|---------------------------------------|---|---------------------------------------|---|
| Net (loss) income                             | \$ (1,659)                            | \$ (1,696)  | \$ 11,480                             | \$ 14,038   |
| Other comprehensive income, net of tax:       |                                       |   |                                       |   |
| Change in post-retirement benefit obligations | 26                                    |   | 77                                    |   |
| Comprehensive (loss) income                   | \$ (1,633)                            | \$ (1,696)  | \$ 11,557                             | \$ 14,038   |

(1) As described in Note 2 to these Condensed Consolidated Financial Statements, we have restated the Condensed Consolidated Financial Statements.

The accompanying notes are an integral part of these condensed consolidated financial statements.



**Table of Contents****Stein Mart, Inc.****Condensed Consolidated Statements of Cash Flows****(Unaudited)**

(In thousands)

|   | 39 Weeks<br>Ended<br>October 27, 2012 | 39 Weeks<br>Ended<br>October 29, 2011<br>(Restated) (1) |
|---|---------------------------------------|---|
| <b>Cash flows from operating activities:</b>                                      |                                       |   |
| Net income  | \$ 11,480                             | \$ 14,038   |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                       |   |
| Depreciation and amortization   | 17,245                                | 13,610  |
| Share-based compensation  | 3,769                                 | 2,544   |
| Store closing charges   | 654                                   | 327   |
| Loss on disposals of property and equipment                                       | 929                                   | 219   |
| Deferred income taxes   | (2,972)                               | 11,422  |
| Tax deficiency from equity issuances  | (682)                                 | (233)   |
| Excess tax benefits from share-based compensation                                 | (59)                                  | (303)   |
| Changes in assets and liabilities:  |                                       |   |
| Inventories   | (77,857)                              | (42,731)  |
| Prepaid expenses and other current assets   | 15,105                                | (11,215)  |
| Other assets  | (1,235)                               | (639)   |
| Accounts payable  | 78,974                                | 72,833  |
| Accrued expenses and other current liabilities                                    | (1,219)                               | (1,830)   |
| Other liabilities   | 5,559                                 | 3,144   |
| Net cash provided by operating activities   | 49,691                                | 61,186  |
| <b>Cash flows from investing activities:</b>                                      |                                       |   |
| Acquisition of property and equipment   | (32,732)                              | (29,468)  |
| Net cash used in investing activities   | (32,732)                              | (29,468)  |
| <b>Cash flows from financing activities:</b>                                      |                                       |   |
| Capital lease payments  | (4,025)                               | (2,056)   |
| Excess tax benefits from share-based compensation                                 | 59                                    | 303   |
| Proceeds from exercise of stock options and other                                 | 434                                   | 2,500   |
| Repurchase of common stock  | (3,359)                               | (10,242)  |
| Net cash used in financing activities   | (6,891)                               | (9,495)   |
| Net increase in cash and cash equivalents   | 10,068                                | 22,223  |
| Cash and cash equivalents at beginning of year                                    | 94,053                                | 79,718  |
| Cash and cash equivalents at end of period  | \$ 104,121                            | \$ 101,941  |

(1)

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As described in Note 2 to these Condensed Consolidated Financial Statements, we have restated the Condensed Consolidated Financial Statements.

The accompanying notes are an integral part of these condensed consolidated financial statements.

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**STEIN MART, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

(Dollars in tables in thousands, except per share amounts)

**1. Basis of Presentation**

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles ( GAAP ) for interim financial information and with the instructions to Form 10-Q. However, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting primarily of normal and recurring adjustments) considered necessary for a fair statement have been included. Due to the seasonality of our business, results for any quarter are not necessarily indicative of the results that may be achieved for a full fiscal year.

As used herein, the terms we , our , us , Stein Mart and the Company refer to Stein Mart, Inc. and its wholly-owned subsidiaries.

**Recent Accounting Pronouncements**

In June 2011, the Financial Accounting Standards Board ( FASB ) amended Accounting Standards Codification ( ASC ) Topic 220, *Comprehensive Income*. The amended guidance requires most entities to present changes in net income and other comprehensive income in either a single statement of comprehensive income or two separate, but consecutive, statements. The objective of these amendments is to improve the comparability, consistency, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. We adopted this guidance in the first quarter of fiscal year 2012 and have included the Condensed Consolidated Statements of Comprehensive Income in our financial statements.

**2. Restatement of Previously Issued Financial Statements**

Our Condensed Consolidated Balance Sheets as of January 28, 2012 and October 29, 2011, our Condensed Consolidated Statements of Income and Condensed Consolidated Statements of Comprehensive Income for the 13 and 39 weeks ended October 29, 2011 and our Condensed Consolidated Statement of Cash Flows for the 39 weeks ended October 29, 2011, have been restated for errors made with regard to inventory markdowns, leasehold improvement costs, compensated absences (paid vacation) and other errors further described below. The restated financial statements also reflect the correction of certain previously identified errors and out of period adjustments that were deemed immaterial to the annual or interim period in which they were recorded and have now been restated to properly reflect the corrections in the appropriate periods.

*Reclassifications*

We have made certain reclassifications in the Condensed Consolidated Statements of Income related to breakage income on unused gift and merchandise return cards and credit card income related to our co-branded and private label credit card agreement which were presented in Other income, net and have been reclassified to Selling, general and administrative expenses ( SG&A ). We have also made certain other insignificant reclassifications. There were no reclassifications made to the Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Comprehensive Income or Condensed Consolidated Statements of Cash Flows.

*Adjustments*

The following is a description of the areas in which the errors were identified and for which we made correcting adjustments to our Condensed Consolidated Financial Statements. The associated income tax expense or benefit and related deferred tax asset or liability for each error has also been corrected.

(1) Inventory markdowns - We identified and corrected errors related to the incorrect treatment of certain inventory markdowns as promotional (temporary). Based on analysis of various factors, these inventory markdowns should have been accounted for as permanent markdowns. Under the retail inventory method of accounting used by us, promotional markdowns do not impact the value of unsold inventory and thus do not impact cost of sales until the merchandise is sold. Conversely, permanent markdowns reduce the value of unsold inventory and impact cost of sales at the time the markdowns are taken.

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(2) Leasehold improvement costs - We identified and corrected errors to report fixed assets related to leasehold improvements at their gross amount with lessor reimbursements for the related construction recorded as deferred rent credits. Landlord (lessor) reimbursements to us (lessee) for store interior construction had been incorrectly accounted for as reductions in the fixed assets related to leasehold improvements. This practice was based on the prior belief that our leasehold improvements increased the fair value of the lessor's property. Management now believes that there was no significant increase in the fair value of the lessor's leased assets and therefore these leasehold improvements should have been recorded, depreciated over and subject to impairment exclusive of lessor reimbursements in the respective periods.

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(3) Compensated absences (paid vacation) - We identified and corrected errors to record liabilities for compensated absences (paid vacation) which were not previously recorded.

(4) Leased department commissions - We corrected the presentation of leased department commissions in the Condensed Consolidated Statements of Income. Leased department commissions were presented in Other income, net of related expenses and have been corrected to report Net sales (increase of \$4.7 million and \$14.8 million for the 13 and 39 weeks ended October 29, 2011, respectively) and SG&A (increase of \$1.6 million and \$4.9 million for the 13 and 39 weeks ended October 29, 2011, respectively) on a gross basis. There was no impact to Net income related to this change.

(5) Insurance-related assets and liabilities - We corrected the presentation of insurance-related assets and liabilities in the Condensed Consolidated Balance Sheets. The long-term portion of insurance assets (\$7.1 million and \$6.4 million as of January 28, 2012 and October 29, 2011, respectively) was previously incorrectly reported as Prepaid expenses and other current assets and is now reported as Other assets. The long-term portion of insurance liabilities (\$11.5 million and \$11.3 million as of January 28, 2012 and October 29, 2011, respectively) was previously incorrectly reported as Accrued expenses and other current liabilities and is now reported as Other liabilities. There was no impact on Total assets or Total liabilities related to this change.

(6) Capitalized indirect overhead - We identified and corrected errors related to the capitalization of indirect overhead costs.

(7) Other - We corrected certain previously identified errors and out of period adjustments that were deemed immaterial to the annual or interim period in which they were recorded and restated prior periods to reflect these corrections in the appropriate periods. The amounts relate to credit card reward income breakage, credit card receivables, software costs, and assets no longer in use.

The net effect of the adjustments on the Condensed Consolidated Statements of Income for the 13 and 39 weeks ended October 29, 2011 is as follows:

|   | Decrease (Increase)<br>in Net Loss<br>13 Weeks<br>Ended<br>October 29,<br>2011 | Increase (Decrease)<br>in Net Income<br>39 Weeks Ended<br>October 29,<br>2011 |
|---|--|---|
| Inventory markdowns                           | \$ (975)   | \$ (2,122)  |
| Leasehold improvement costs                   | 453  | 1,442   |
| Indirect overhead                             | 2,409  | 2,126   |
| Other   | 409  | (1,562)   |
| <b>Total adjustments before tax</b>           | <b>2,296</b>   | <b>(116)</b>  |
| Income tax expense (benefit) from adjustments | 886  | (44)  |
| <b>Decrease in Net (loss) income:</b>         | <b>\$ 1,410</b>  | <b>\$ (72)</b>  |

The adjustments in Other in the 39 weeks ended October 29, 2011 relate primarily to the correction of a previously recorded out of period adjustment related to credit card reward income breakage of \$2.0 million.

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The following tables present the effect of the aforementioned adjustments on our Condensed Consolidated Balance Sheets as of January 28, 2012 and October 29, 2011 and indicate the category of the adjustments by reference to the above descriptions of the errors for which we made corrections:

|   | As Previously<br>Reported | As of January 28, 2012<br>Adjustments | Description of<br>Adjustments | As Restated |
|---|---------------------------|---------------------------------------|-------------------------------|-------------|
| <b>ASSETS</b>   |                           |                                       |                               |             |
| Current assets:   |                           |                                       |                               |             |
| Cash and cash equivalents   | \$ 94,053                 | \$                                    |                               | \$ 94,053   |
| Inventories   | 220,775                   | (1,943)                               | (1)                           | 218,832     |
| Prepaid expenses and other current assets   | 36,838                    | (2,699)                               | (2)(5)(7)                     | 34,139      |
| Total current assets  | 351,666                   | (4,642)                               |                               | 347,024     |
| Property and equipment, net   | 104,141                   | 5,849                                 | (2)(7)                        | 109,990     |
| Other assets  | 17,409                    | 5,160                                 | (2)(5)                        | 22,569      |
| Total assets  | \$ 473,216                | \$ 6,367                              |                               | \$ 479,583  |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>  |                           |                                       |                               |             |
| Current liabilities:  |                           |                                       |                               |             |
| Accounts payable  | \$ 106,063                | \$                                    |                               | \$ 106,063  |
| Accrued expenses and other current liabilities  | 72,731                    | (4,668)                               | (3)(5)                        | 68,063      |
| Total current liabilities   | 178,794                   | (4,668)                               |                               | 174,126     |
| Other liabilities   | 35,084                    | 20,702                                | (2)(5)                        | 55,786      |
| Total liabilities   | 213,878                   | 16,034                                |                               | 229,912     |
| Shareholders equity:  |                           |                                       |                               |             |
| Preferred stock - \$.01 par value; 1,000,000 shares authorized; no shares issued or outstanding         |                           |                                       |                               |             |
| Common stock - \$.01 par value; 100,000,000 shares authorized; 43,588,821 shares issued and outstanding | 436                       |                                       |                               | 436         |
| Additional paid-in capital  | 15,268                    |                                       |                               | 15,268      |
| Retained earnings   | 245,053                   | (9,667)                               | (1)(2)(3)(7)                  | 235,386     |
| Accumulated other comprehensive loss  | (1,419)                   |                                       |                               | (1,419)     |
| Total shareholders equity   | 259,338                   | (9,667)                               |                               | 249,671     |
| Total liabilities and shareholders equity   | \$ 473,216                | \$ 6,367                              |                               | \$ 479,583  |

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|   | As Previously<br>Reported | As of October 29, 2011<br>Adjustments | Description of<br>Adjustments | As Restated |
|---|---------------------------|---------------------------------------|-------------------------------|-------------|
| <b>ASSETS</b>   |                           |                                       |                               |             |
| Current assets:   |                           |                                       |                               |             |
| Cash and cash equivalents   | \$ 102,495                | \$ (554)                              | (7)                           | \$ 101,941  |
| Inventories   | 274,538                   | (2,111)                               | (1)(6)                        | 272,427     |
| Prepaid expenses and other current assets   | 38,681                    | (5,551)                               | (2)(5)(7)                     | 33,130      |
| Total current assets  | 415,714                   | (8,216)                               |                               | 407,498     |
| Property and equipment, net   | 100,564                   | 6,477                                 | (2)(7)                        | 107,041     |
| Other assets  | 14,976                    | 4,717                                 | (2)(5)                        | 19,693      |
| Total assets  | \$ 531,254                | \$ 2,978                              |                               | \$ 534,232  |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>  |                           |                                       |                               |             |
| Current liabilities:  |                           |                                       |                               |             |
| Accounts payable  | \$ 168,378                | \$                                    |                               | \$ 168,378  |
| Accrued expenses and other current liabilities  | 74,641                    | (4,959)                               | (3)(5)                        | 69,682      |
| Total current liabilities   | 243,019                   | (4,959)                               |                               | 238,060     |
| Other liabilities   | 32,305                    | 17,779                                | (2)(5)                        | 50,084      |
| Total liabilities   | 275,324                   | 12,820                                |                               | 288,144     |
| Shareholders' equity:   |                           |                                       |                               |             |
| Preferred stock - \$.01 par value; 1,000,000 shares authorized; no shares issued or outstanding         |                           |                                       |                               |             |
| Common stock - \$.01 par value; 100,000,000 shares authorized; 43,654,608 shares issued and outstanding | 437                       |                                       |                               | 437         |
| Additional paid-in capital  | 15,702                    |                                       |                               | 15,702      |
| Retained earnings   | 239,335                   | (9,842)                               | (1)(2)(3)(6)(7)               | 229,493     |
| Accumulated other comprehensive loss  | 456                       |                                       |                               | 456         |
| Total shareholders' equity  | 255,930                   | (9,842)                               |                               | 246,088     |
| Total liabilities and shareholders' equity  | \$ 531,254                | \$ 2,978                              |                               | \$ 534,232  |

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The following tables present the effect of the aforementioned reclassifications and adjustments on our Condensed Consolidated Statements of Income for the 13 and 39 weeks ended October 29, 2011 and indicate the category of the adjustments by reference to the above descriptions of the errors for which we made corrections:

|  | 13 Weeks Ended October 29, 2011 |                   |             |                            |             |
|--|---------------------------------|-------------------|-------------|----------------------------|-------------|
|  | As Previously Reported          | Reclassifications | Adjustments | Description of Adjustments | As Restated |
| Net sales                                    | \$ 258,520                      | \$                | \$ 4,712    | (4)                        | \$ 263,232  |
| Cost of merchandise sold                     | 199,264                         |                   | (2,685)     | (1)(2)(6)                  | 196,579     |
| Gross profit                                 | 59,256                          |                   | 7,397       |                            | 66,653      |
| Selling, general and administrative expenses | 71,291                          | (3,560)           | 1,959       | (2)(3)(4)(7)               | 69,690      |
| Other income, net                            | 6,602                           | (3,460)           | (3,142)     | (4)                        |             |
| Operating loss                               | (5,433)                         | 100               | 2,296       |                            | (3,037)     |
| Interest (income) expense, net               | (16)                            | 100               |             |                            | 84          |
| Loss before income taxes                     | (5,417)                         |                   | 2,296       |                            | (3,121)     |
| Income tax benefit                           | (2,311)                         |                   | 886         | (1)(2)(3)(6)(7)            | (1,425)     |
| Net loss                                     | \$ (3,106)                      | \$                | \$ 1,410    |                            | \$ (1,696)  |
| Net income per share:                        |                                 |                   |             |                            |             |
| Basic  | \$ (0.07)                       | \$                | \$ 0.03     |                            | \$ (0.04)   |
| Diluted                                      | \$ (0.07)                       | \$                | \$ 0.03     |                            | \$ (0.04)   |

|  | 39 Weeks Ended October 29, 2011 |                   |             |                            |             |
|--|---------------------------------|-------------------|-------------|----------------------------|-------------|
|  | As Previously Reported          | Reclassifications | Adjustments | Description of Adjustments | As Restated |
| Net sales                                    | \$ 832,233                      | \$                | \$ 14,766   | (4)                        | \$ 846,999  |
| Cost of merchandise sold                     | 617,686                         |                   | (2,811)     | (1)(2)(6)                  | 614,875     |
| Gross profit                                 | 214,547                         |                   | 17,577      |                            | 232,124     |
| Selling, general and administrative expenses | 211,581                         | (10,488)          | 7,848       | (2)(3)(4)(7)               | 208,941     |
| Other income, net                            | 20,059                          | (10,214)          | (9,845)     | (4)                        |             |
| Operating income                             | 23,025                          | 274               | (116)       |                            | 23,183      |
| Interest (income) expense, net               | (23)                            | 274               |             |                            | 251         |
| Income before income taxes                   | 23,048                          |                   | (116)       |                            | 22,932      |
| Income tax expense                           | 8,938                           |                   | (44)        | (1)(2)(3)(6)(7)            | 8,894       |
| Net income                                   | \$ 14,110                       | \$                | \$ (72)     |                            | \$ 14,038   |
| Net income per share:                        |                                 |                   |             |                            |             |
| Basic  | \$ 0.31                         | \$                | \$          |                            | \$ 0.31     |
| Diluted                                      | \$ 0.31                         | \$                | \$          |                            | \$ 0.31     |





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The following tables present the effect of the aforementioned adjustments on our Condensed Consolidated Statements of Comprehensive Income for the 13 and 39 weeks ended October 29, 2011 and indicate the category of the adjustments by reference to the above descriptions of the errors for which we made corrections:

|   | 13 Weeks Ended October 29, 2011 |             |                            |             |
|---|---------------------------------|-------------|----------------------------|-------------|
|   | As Previously Reported          | Adjustments | Description of Adjustments | As Restated |
| Net loss                                      | \$ (3,106)                      | \$ 1,410    | (1)(2)(3)(6)(7)            | \$ (1,696)  |
| Other comprehensive income, net of tax:       |                                 |             |                            |             |
| Change in post-retirement benefit obligations |                                 |             |                            |             |
| Comprehensive loss                            | \$ (3,106)                      | \$ 1,410    |                            | \$ (1,696)  |

|   | 39 Weeks Ended October 29, 2011 |             |                            |             |
|---|---------------------------------|-------------|----------------------------|-------------|
|   | As Previously Reported          | Adjustments | Description of Adjustments | As Restated |
| Net income                                    | \$ 14,110                       | \$ (72)     | (1)(2)(3)(6)(7)            | \$ 14,038   |
| Other comprehensive income, net of tax:       |                                 |             |                            |             |
| Change in post-retirement benefit obligations |                                 |             |                            |             |
| Comprehensive income                          | \$ 14,110                       | \$ (72)     |                            | \$ 14,038   |

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The following table presents the effect of the aforementioned adjustments on our Condensed Consolidated Statement of Cash Flows for the 39 weeks ended October 29, 2011 and indicates the category of the adjustments by reference to the above descriptions of the errors for which we made corrections:

|   | As Previously<br>Reported | 39 Weeks Ended October 29, 2011<br>Adjustments | Description of<br>Adjustments | As Restated |
|---|---------------------------|--|-------------------------------|-------------|
| <b>Cash flows from operating activities:</b>                                      |                           |  |                               |             |
| Net income  | \$ 14,110                 | \$ (72)  | (1)(2)(3)(6)(7)               | \$ 14,038   |
| Adjustments to reconcile net income to net cash provided by operating activities: |                           |  |                               |             |
| Depreciation and amortization   | 13,714                    | (104)  | (2)(7)                        | 13,610      |
| Share-based compensation  | 2,544                     |  |                               | 2,544       |
| Store closing charges   | 327                       |  |                               | 327         |
| Loss on disposal of property and equipment  |                           | 219  | (7)                           | 219         |
| Deferred income taxes   | 11,652                    | (230)  | (1)(2)(3)(6)(7)               | 11,422      |
| Tax deficiency from equity issuances  | (233)                     |  |                               | (233)       |
| Excess tax benefits from share-based compensation                                 | (303)                     |  |                               | (303)       |
| Changes in assets and liabilities:  |                           |  |                               |             |
| Inventories   | (42,243)                  | (488)  | (1)(6)                        | (42,731)    |
| Prepaid expenses and other current assets   | (13,339)                  | 2,124  | (2)(5)(7)                     | (11,215)    |
| Other assets  | (1,222)                   | 583  | (2)(5)                        | (639)       |
| Accounts payable  | 72,833                    |  |                               | 72,833      |
| Accrued expenses and other current liabilities                                    | (2,878)                   | 1,048  | (3)(5)                        | (1,830)     |
| Other liabilities   | 1,223                     | 1,921  | (2)(5)                        | 3,144       |
| Net cash provided by operating activities   | 56,185                    | 5,001  |                               | 61,186      |
| <b>Cash flows from investing activities:</b>                                      |                           |  |                               |             |
| Acquisition of property and equipment   | (24,366)                  | (5,102)  | (2)(7)                        | (29,468)    |
| Net cash used in investing activities   | (24,366)                  | (5,102)  |                               | (29,468)    |
| <b>Cash flows from financing activities:</b>                                      |                           |  |                               |             |
| Capital lease payments  | (2,056)                   |  |                               | (2,056)     |
| Excess tax benefits from share-based compensation                                 | 303                       |  |                               | 303         |
| Proceeds from exercise of stock options and other                                 | 2,500                     |  |                               | 2,500       |
| Repurchase of common stock  | (10,242)                  |  |                               | (10,242)    |
| Net cash used in financing activities   | (9,495)                   |  |                               | (9,495)     |
| Net increase in cash and cash equivalents   | 22,324                    | (101)  | (7)                           | 22,223      |
| Cash and cash equivalents at beginning of year                                    | 80,171                    | (453)  | (7)                           | 79,718      |
| Cash and cash equivalents at end of period  | \$ 102,495                | \$ (554)                                       |                               | \$ 101,941  |

**Table of Contents****3. Fair Value Measurements***Assets and Liabilities Measured at Fair Value on a Recurring Basis*

We have money market fund investments classified as cash equivalents which are Level 1 assets because fair value is based on readily available market prices. The fair value of these assets was \$91.2 million at October 27, 2012, \$83.1 million at January 28, 2012 and \$78.1 million at October 29, 2011.

**4. Gift Card and Merchandise Return Cards**

During the second quarter of 2012, we updated certain assumptions on our obligations for unused gift and merchandise return card balances. For the 13 weeks ended October 27, 2012 and October 29, 2011, we recognized breakage income on unused gift and merchandise return cards of \$0.1 million and \$0.2 million, respectively. For the 39 weeks ended October 27, 2012 and October 29, 2011, we recognized breakage income on unused gift and merchandise return cards of \$2.7 million and \$0.7 million, respectively. Breakage income is included in Selling, general and administrative expenses in the Condensed Consolidated Statements of Income.

**5. Revolving Credit Agreement**

On October 28, 2011, we entered into an amended and restated revolving credit agreement (the *Credit Agreement*) with Wells Fargo Bank, N.A. The Credit Agreement provides for a \$100 million senior secured revolving credit facility which can be increased to \$150 million. The Credit Agreement matures on February 28, 2017. Borrowings under the Credit Agreement are based on and collateralized by eligible credit card receivables and inventory.

The amount available for direct borrowing was \$93.1 million at October 27, 2012, and is based on 90% of eligible credit card receivables and inventories less reserves, as defined in the Credit Agreement. The amount available for borrowing represents the capped borrowing base of \$100 million reduced by outstanding letters of credit of \$6.9 million. The Credit Agreement contains customary affirmative and negative covenants, including limitations on granting of liens, certain investments, additional indebtedness, prepayments on indebtedness and disposition of inventory. We had no direct borrowings at October 27, 2012.

**6. Income Taxes**

The effective tax rate ( *ETR* ) for the third quarter of 2012 and 2011 was (56.6) percent and (45.7) percent, respectively. The ETR for the third quarter of 2012 and 2011 was a benefit rate due to the loss incurred in the quarter. The ETR for the 39 weeks ended October 27, 2012 and October 29, 2011 was 39.2 percent and 38.8 percent, respectively. The ETR for the 39 weeks ended October 27, 2012 and October 29, 2011 was higher than the statutory rate due primarily to the impact of non-deductible expenses related to post-retirement benefit costs.

**7. Shareholders' Equity***Stock Repurchase Plan*

During the 39 weeks ended October 27, 2012, we repurchased 494,330 shares of our common stock at a total cost of \$3.4 million. Repurchases during the 39 weeks ended October 29, 2011 were 1.4 million shares of our common stock at a total cost of \$10.2 million.

*Share-Based Compensation*

For the 13 and 39 weeks ended October 27, 2012, and October 29, 2011, pre-tax share-based compensation expense was recorded as follows:

|  | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011 | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011 |
|--|------------------------------------|------------------------------------|------------------------------------|------------------------------------|
| Cost of merchandise sold                     | \$ 966                             | \$ 409                             | \$ 2,211                           | \$ 1,695                           |
| Selling, general and administrative expenses | 681                                | 201                                | 1,558                              | 849                                |

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|  |    |       |    |     |    |       |    |       |
|--|----|-------|----|-----|----|-------|----|-------|
| Total share-based compensation expense | \$ | 1,647 | \$ | 610 | \$ | 3,769 | \$ | 2,544 |
|--|----|-------|----|-----|----|-------|----|-------|

**Table of Contents****8. Earnings Per Share**

We calculate earnings per share ( EPS ) using the two-class method. Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and are included in the computation of EPS. Our restricted stock awards are considered participating securities because they contain non-forfeitable rights to dividends.

The following table presents the calculation of basic and diluted (loss) earnings per share (shares in thousands):

|  | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011<br>(Restated) | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011<br>(Restated) |
|--|------------------------------------|--|------------------------------------|--|
| <b>Basic (Loss) Earnings Per Common Share:</b>         |                                    |  |                                    |  |
| Net (loss) income                                      | \$ (1,659)                         | \$ (1,696)                                       | \$ 11,480                          | \$ 14,038  |
| Income allocated to participating securities           |                                    |  | 317                                | 380  |
| Net (loss) income available to common shareholders     | \$ (1,659)                         | \$ (1,696)                                       | \$ 11,163                          | \$ 13,658  |
| Basic weighted-average shares outstanding              | 42,568                             | 43,248   | 42,622                             | 43,731   |
| Basic (loss) earnings per share                        | \$ (0.04)                          | \$ (0.04)  | \$ 0.26                            | \$ 0.31  |
| <b>Diluted (Loss) Earnings Per Common Share:</b>       |                                    |  |                                    |  |
| Net (loss) income                                      | \$ (1,659)                         | \$ (1,696)                                       | \$ 11,480                          | \$ 14,038  |
| Income allocated to participating securities           |                                    |  | 316                                | 378  |
| Net (loss) income available to common shareholders     | \$ (1,659)                         | \$ (1,696)                                       | \$ 11,164                          | \$ 13,660  |
| Basic weighted-average shares outstanding              | 42,568                             | 43,248   | 42,622                             | 43,731   |
| Incremental shares from share-based compensation plans |                                    |  | 147                                | 307  |
| Diluted weighted-average shares outstanding            | 42,568                             | 43,248   | 42,769                             | 44,038   |
| Diluted (loss) earnings per share                      | \$ (0.04)                          | \$ (0.04)  | \$ 0.26                            | \$ 0.31  |

Due to the Company's net loss position for the third quarters of 2012 and 2011, 1.3 million weighted average unvested restricted shares (participating securities) and 0.3 million weighted average common stock equivalents (non-participating securities) were not considered in the calculation of net loss available to common shareholders used for both basic and diluted EPS for both periods. In addition, options to acquire shares and performance share awards totaling approximately 0.9 million and 1.7 million shares of common stock that were outstanding during the third quarters of 2012 and 2011, respectively, were not included in the computation of diluted loss per share. Options excluded were those that had exercise prices greater than the average market price of the common shares such that inclusion would have been anti-dilutive. Performance share awards were not included based on level of performance.

For the first 9 months of 2012 and 2011, options to acquire and performance share awards totaling approximately 0.9 million and 1.2 million shares of common stock, respectively, were not included in the computation of diluted earnings per share for the aforementioned reasons.

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**STEIN MART, INC.**

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

As used herein, the terms "we", "our", "us", "Stein Mart" and the "Company" refer to Stein Mart, Inc. and its wholly-owned subsidiaries.

**Forward-Looking Statements**

This report contains forward-looking statements which are subject to certain risks, uncertainties or assumptions and may be affected by certain factors, including but not limited to the matters discussed in Item 1A. Risk Factors of our Form 10-K. Wherever used, the words "plan", "expect", "anticipate", "believe", "estimate" and similar expressions identify forward-looking statements. Should one or more of these risks, uncertainties or other factors materialize, or should underlying assumptions prove incorrect, actual results, performance or achievements may vary materially from any future results, performance or achievements expressed or implied by such forward-looking statements. Forward-looking statements are based on beliefs and assumptions of our management and on information currently available to such management. Forward-looking statements speak only as of the date they are made, and we undertake no obligation to publicly update or revise our forward-looking statements in light of new information or future events. Undue reliance should not be placed on such forward-looking statements, which are based on current expectations. Forward-looking statements are no guarantees of performance.

**Restatement of Financial Statements**

The discussion and analysis set forth below in this Item 2 has been affected by the restatement of our financial statements as described in Note 2 of the Notes to Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report. Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our unaudited Condensed Consolidated Financial Statements and the notes thereto.

**Overview**

Stein Mart is a national retailer offering the fashion merchandise, service and presentation of a better department or specialty store at prices competitive with off-price retail chains. Our focused assortment of merchandise features current-season moderate to better fashion apparel for women and men, as well as accessories, shoes and home fashions.

**Financial Overview for the 13 and 39 weeks ended October 27, 2012**

Sales were \$273.7 million for the 13 weeks ended October 27, 2012, an increase from \$263.2 million for the 13 weeks ended October 29, 2011, and \$863.8 million for the 39 weeks ended October 27, 2012, an increase from \$847.0 million for the 39 weeks ended October 29, 2011.

Comparable store sales increased 3.1 percent compared to the 13 weeks ended October 27, 2012, and increased 1.3 percent compared to the 39 weeks ended October 27, 2012.

Net loss was \$1.7 million or \$0.04 per diluted share for the 13 weeks ended October 27, 2012 and 13 weeks ended October 29, 2011.

Net income was \$11.5 million or \$0.26 per diluted share for the 39 weeks ended October 27, 2012 compared to net income of \$14.0 million or \$0.31 per diluted share for the 39 weeks ended October 29, 2011.

The effective tax rate was (56.6) percent for the 13 weeks ended October 27, 2012, compared to (45.7) percent for the 13 weeks ended October 29, 2011 and 39.2 percent for the 39 weeks ended October 27, 2012, compared to 38.8 percent for the 39 weeks ended October 29, 2011.

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2011.

Cash and cash equivalents as of October 27, 2012 was \$104.1 million compared to \$94.1 million as of January 28, 2012, and \$101.9 million as of October 29, 2011. We had no direct borrowings on our revolving credit agreement as of October 27, 2012, January 28, 2012, and October 29, 2011.



**Table of Contents****Stores**

There were 262 stores open as of October 27, 2012 and October 29, 2011.

|                                 | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011 | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011 |
|---------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|
| Stores at beginning of period   | 263                                | 260                                | 262                                | 264                                |
| Stores opened during the period | 3                                  | 2                                  | 5                                  | 2                                  |
| Stores closed during the period | (4)                                |                                    | (5)                                | (4)                                |
| Stores at the end of period     | 262                                | 262                                | 262                                | 262                                |

**Results of Operations**

The following table sets forth the Condensed Consolidated Statements of Income expressed as a percentage of our net sales:

|  | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011<br>(Restated) | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011<br>(Restated) |
|--|------------------------------------|--|------------------------------------|--|
| Net sales                                    | 100.0%                             | 100.0%   | 100.0%                             | 100.0%   |
| Cost of merchandise sold                     | 74.2%                              | 74.7%  | 72.6%                              | 72.6%  |
| Gross profit                                 | 25.8%                              | 25.3%  | 27.4%                              | 27.4%  |
| Selling, general and administrative expenses | 27.2%                              | 26.4%  | 25.2%                              | 24.6%  |
| (Loss) income from operations                | (1.4)%                             | (1.1)%   | 2.2%                               | 2.8%   |
| Interest expense, net                        | 0.0%                               | 0.0%   | 0.0%                               | 0.0%   |
| (Loss) income before income taxes            | (1.4)%                             | (1.1)%   | 2.2%                               | 2.8%   |
| Income tax (benefit) expense                 | (0.8)%                             | (0.5)%   | 0.9%                               | 1.1%   |
| Net (loss) income                            | (0.6)%                             | (0.6)%   | 1.3%                               | 1.7%   |

**Net Sales.** The following table compares net sales for the 13 and 39 weeks ended October 27, 2012 to the 13 and 39 weeks ended October 29, 2011 (dollar amounts in thousands):

|                         | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase  | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase  |
|-------------------------|------------------------------------|--|-----------|------------------------------------|--|-----------|
| Net sales               | \$ 273,729                         | \$ 263,232                                       | \$ 10,497 | \$ 863,809                         | \$ 846,999                                       | \$ 16,810 |
| Sales percent increase: |                                    |  |           |                                    |  |           |
| Total net sales         |                                    |  | 4.0%      |                                    |  | 2.0%      |
| Comparable store sales  |                                    |  | 3.1%      |                                    |  | 1.3%      |

For the 13 weeks ended October 27, 2012, the comparable store sales increase was driven by higher units per transaction and higher number of transactions than the same period in the previous year. For the 39 weeks ended October 27, 2012, the comparable store sales increase was driven by higher average unit selling prices and higher number of transactions than the same period in the previous year.

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**Gross Profit.** The following table compares gross profit for the 13 and 39 weeks ended October 27, 2012 to the 13 and 39 weeks ended October 29, 2011 (dollar amounts in thousands):

|                         | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase |
|-------------------------|------------------------------------|--|----------|------------------------------------|--|----------|
| Gross profit            | \$ 70,690                          | \$ 66,653  | \$ 4,037 | \$ 236,373                         | \$ 232,124                                       | \$ 4,249 |
| Percentage of net sales | 25.8%                              | 25.3%  | 0.5%     | 27.4%                              | 27.4%  | 0.0%     |

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For the 13 weeks ended October 27, 2012, the increase in the gross profit rate was a result of lower markdowns, partially offset by lower initial markup and slightly higher occupancy and buying costs. Markdowns and initial markups were lower due to the company decreasing coupons and selectively lowering prices on certain merchandise in accordance with its new pricing strategy.

For the 39 weeks ended October 27, 2012, gross profit as a percent of sales was consistent with the prior year.

**Selling, General and Administrative Expenses ( SG&A ).** The following table compares SG&A expenses for the 13 and 39 weeks ended October 27, 2012 to the 13 and 39 weeks ended October 29, 2011, (dollar amounts in thousands):

|  | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase |
|--|------------------------------------|--|----------|------------------------------------|--|----------|
| Selling, general and administrative expenses | \$ 74,431                          | \$ 69,690  | \$ 4,741 | \$ 217,306                         | \$ 208,941                                       | \$ 8,365 |
| Percentage of net sales                      | 27.2%                              | 26.4%  | 0.8%     | 25.2%                              | 24.6%  | 0.6%     |

For the 13 weeks ended October 27, 2012, SG&A expenses increased primarily due to \$2.1 million decrease in credit card program income, \$2.2 million increase in store expenses, and \$1.9 million increase in depreciation expense and partially offset by a \$1.5 million decrease in advertising expenses. Credit card program income decreased primarily due to a performance-based incentive from GE Capital Retail Bank ( GE ) related to the final program year of our prior co-brand agreement received in 2011 as well as the elimination of new account fees when we entered into the Amended and Restated Co-Brand and Private Label Credit Card Consumer Program Agreement with GE in October 2011. Store expenses increased primarily due to higher compensation costs. Advertising expenses decreased due to the reduction of certain media usage.

For the 39 weeks ended October 27, 2012, SG&A expenses increased primarily due to \$4.6 million decrease in credit card program income, \$3.5 million increase in depreciation expense, \$2.2 million increase in corporate expenses and \$2.8 million increase in store expenses, partially offset by \$3.5 million decrease in advertising expenses and \$2.1 million increase in breakage income on unused gift cards and merchandise return cards. Corporate expenses increased primarily due to higher compensation and benefit costs. Store expenses increased primarily due to higher compensation costs, partially offset by a decrease in credit card interchange fees. The increase in breakage income on unused gift cards and merchandise return cards is a result of an update in our breakage assumptions during the second quarter of 2012. The decrease in credit card program income and advertising expenses and are due to aforementioned reasons.

**Income Taxes.** The following table compares income tax (benefit) expense for the 13 and 39 weeks ended October 27, 2012 to the 13 and 39 weeks ended October 29, 2011 (dollar amounts in thousands):

|                              | 13 Weeks Ended<br>October 27, 2012 | 13 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase | 39 Weeks Ended<br>October 27, 2012 | 39 Weeks Ended<br>October 29, 2011<br>(Restated) | Increase/<br>(Decrease) |
|------------------------------|------------------------------------|--|----------|------------------------------------|--|-------------------------|
| Income tax (benefit) expense | \$ (2,163)                         | \$ (1,425)                                       | \$ 738   | \$ 7,417                           | \$ 8,894   | \$ (1,477)              |
| Effective tax rate           | (56.6)%                            | (45.7)%  | 10.9%    | 39.2%                              | 38.8%  | 0.4%                    |

For the 13 weeks ended October 27, 2012 and October 29, 2011, the effective tax rate was a benefit rate due to the loss for each of the respective quarters. For the 39 weeks ended October 27, 2012 and October 29, 2011, the effective tax rate was higher than the statutory rate due primarily to the impact of non-deductible expenses related to post-retirement benefit costs.

**Liquidity and Capital Resources**

Our primary source of liquidity is the sale of merchandise inventories. Capital requirements and working capital needs are funded through a combination of internally generated funds, available cash, credit terms from vendors and a \$100 million revolving credit facility with Wells Fargo Bank, N.A. Working capital is needed to support store inventories and capital investments for system improvements, new store openings and to maintain existing stores. Historically, our working capital needs are lowest in the first quarter and highest at the end of the third quarter and beginning of the fourth quarter as we build inventories for the holiday selling season. As of October 27, 2012, we had cash and cash equivalents of \$104.1 million and no direct borrowings under our revolving credit facility.

Net cash provided by operating activities was \$49.7 million for the 39 weeks ended October 27, 2012 compared to net cash provided by operating activities of \$61.2 million for the 39 weeks ended October 29, 2011. Cash provided by operating activities results primarily from

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operating income and changes in working capital. Cash provided by operating activities for the 39 weeks ended October 27, 2012 includes an income tax refund of approximately \$6.6 million. Cash provided by operating activities for the 39 weeks ended October 29, 2011 includes a positive working capital impact from lengthening vendor payment terms implemented in early 2011.

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Net cash used in investing activities was \$32.7 million for the 39 weeks ended October 27, 2012 compared to \$29.5 million for the 39 weeks ended October 29, 2011. Capital expenditures relate to information systems hardware and software as well as new and existing store improvements. The increase in capital expenditures relates primarily to an increase in new store improvements.

Net cash used in financing activities was \$6.9 million for the 39 weeks ended October 27, 2012 compared to \$9.5 million for the 39 weeks ended October 29, 2011. During the 39 weeks ended October 27, 2012, we repurchased shares of common stock for \$3.4 million and had payments on capital leases of \$4.0 million. During the 39 weeks ended October 29, 2011, we repurchased shares of common stock for \$10.2 million, received proceeds from stock option exercises of \$2.5 million and had payments on capital leases of \$2.0 million.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

For information regarding our exposure to certain market risk, see Quantitative and Qualitative Disclosures About Market Risk in Part II, Item 7A of our Form 10-K for the year ended January 28, 2012. There were no material changes to our market risk during the quarter ended October 27, 2012.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, we have carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act ), as of the end of the period covered by this report.

Based on the evaluation discussed above, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were not effective as of the end of the period covered by this report due to the material weaknesses identified in the Company s internal control over financial reporting described below.

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the Company s annual or interim financial statements will not be prevented or detected on a timely basis. Based on this definition, management has concluded that the material weaknesses noted below existed in the Company s internal control over financial reporting.

The following material weaknesses were identified in 2012. These led to errors which resulted in the need to restate our 2010 and 2011 financial statements and our interim financial statements for the first quarter of 2012 and each interim period in 2011. The resulting misstatements are more fully described in Note 2 Restatement of Previously Issued Financial Statements in the financial statements included in this Form 10-Q.

*Inventory Markdowns:* We did not maintain effective internal controls over inventory markdowns that impacted the valuation and accuracy of the accounting for and disclosures of Inventory and Cost of merchandise sold. Specifically, we did not design effective controls for the finance department to monitor and evaluate the appropriate accounting for markdowns. Additionally, our finance and merchandising departments did not communicate effectively so that the finance department could develop appropriate accounting policies relative to markdowns. Because the Company values inventories at the lower of average cost or market on a first-in, first-out basis using the retail inventory method of accounting, the characterization of markdowns as either permanent or promotional has a direct impact on the calculation of ending inventory value and thus cost of merchandise sold. More specifically, inventory is reduced by permanent markdowns for all on-hand units at the time the markdown is taken but is not reduced by promotional markdowns until the units are sold. These material weaknesses resulted in the misstatement of our Inventory and Cost of merchandise sold.

*Leasehold improvement costs:* We did not maintain effective internal controls over leasehold improvements that impacted the presentation and disclosure and accuracy of the accounting for and disclosures of Prepaid expenses and other current assets, Property and equipment, net, Other assets, Other liabilities, Cost of merchandise sold and Selling, general and administrative expenses. Specifically, we did not design effective controls for financial management to adequately validate the assertions made by real estate operations management regarding the future value of leasehold improvements made by the Company and consequently did not record tenant improvement allowances ( TIA ) provided by landlords for our stores in accordance with accounting standards. TIA provided as leasehold incentives to us was thus improperly netted against property and equipment instead of being accounted for as a deferred rent credit. This material weakness resulted in the misstatement of our Prepaid expenses

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and other current assets, Property and equipment, net, Other assets, Other liabilities, Cost of merchandise sold and Selling, general and administrative expenses.

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*Compensated absences (paid vacation):* We did not maintain effective internal controls over the establishment of compensated absences (paid vacation) accruals that impacted accuracy, completeness and valuation of the accounting for and disclosures of Accrued expenses and other current liabilities and Selling, general and administrative expenses. Specifically, we did not design effective controls for financial management to effectively communicate with human resources personnel to fully understand the Company’s vacation policy. The Company’s vacation policy is an earn in one year, take in the next policy whereby at the end of any year, the policy leaves associates with a full year of earned, but untaken vacation. In the past, the policy was incorrectly interpreted by financial management to be an earn and take in the same year policy; thus the Company has historically not recorded a vacation accrual. This material weakness resulted in the misstatement of our Accrued expenses and other current liabilities and Selling, general and administrative expenses.

*Indirect overhead cost capitalization:* We did not maintain effective internal controls over indirect overhead cost capitalization that impacted the valuation and accuracy of the accounting for and disclosures of Inventory and Cost of merchandise sold. Specifically, we did not design effective controls to calculate the indirect cost capitalization adjustment in interim periods. Although we have a control in place to evaluate the key assumptions and the resulting calculation of the indirect cost capitalization adjustment on an annual basis, we did not conduct an analysis at interim period ends. This material weakness resulted in the misstatement of our Inventory and Cost of merchandise sold in interim periods.

*Software assets amortization periods and retirements:* We did not maintain effective internal controls over the appropriate amortization periods and the timing of retirements of software assets that impact the accuracy, completeness, presentation and disclosure of the accounting for and disclosures of Prepaid expenses and other current assets, Property and equipment, net, and Selling, general and administrative expenses. Specifically, we did not design effective controls for information technology personnel to effectively communicate the nature of certain software expenditures to the finance department resulting in the amortization of software costs over an improper period. Additionally, we did not design effective controls for financial management to effectively communicate with information technology personnel to timely identify and remove retired software assets from the accounting records. These material weaknesses resulted in the misstatement of our Prepaid expenses and other current assets, Property and equipment, net, and Selling, general and administrative expenses.

The material weaknesses identified during 2012 have caused us to conclude that we had a material weakness in our control environment related to the level of information and communication between the finance department and other departmental functions being insufficient in preventing and detecting material misstatements to the Company’s financial statements. This material weakness contributed to the above material weaknesses.

The following material weakness was identified in 2011 and still existed as of October 27, 2012:

*Information technology communication:* We did not maintain effective internal controls over information technology communication that impacted the accuracy and valuation of the accounting for and disclosures of cost of merchandise sold and inventory. Specifically, we did not design effective controls for our IT department to effectively communicate system incidents to the appropriate personnel. We determined that IT operations personnel followed protocols for issue resolution; however, because of the uniqueness and potential impacts of certain incidents, further escalation to the finance organization should have occurred. IT personnel did not notify the finance organization that historical records had been removed to free up system capacity and that certain transactions had been reprocessed. This prevented accounting personnel from identifying an error in the Perpetual System unit balances and analyzing the potential impact related to permanent markdowns on a timely basis. This material weakness resulted in an adjustment in the third quarter of 2011 to Cost of merchandise sold and Inventory by not recording all permanent markdowns actually taken.

The above material weaknesses could result in further misstatement of the financial statements or disclosures that would result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected.

**Remediation Efforts to Address Material Weaknesses**

In November 2012, our Board of Directors created an Accounting Review Committee to review the accounting errors that led to our financial statement restatement. The Accounting Review Committee focused its attention on the issue of inventory markdowns. The Accounting Review Committee retained a national law firm, which engaged a national consulting firm that specializes in accounting services, to commence a full review of the Company’s past practices for inventory markdowns. Based upon its review, the Accounting Review Committee found no misconduct or intention to misstate financial results by current or former employees or directors.

Identified in 2012:

*Inventory Markdowns:* We are implementing the following activities to remediate the markdown material weaknesses noted above: 1) Merchandising and financial management will update the existing policies and procedures to reflect the agreed upon characteristics of





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markdowns as promotional or permanent; 2) At quarter end, financial management will review markdown activity to determine if all items have been recorded in accordance with markdown policies; 3) At quarter end financial management will meet with merchandising management to review the seasonal inventory levels. Based on this analysis, they will assess comparability and appropriateness of permanent markdowns and related markdown levels; 4) Financial management will review promotional markdowns in detail to determine whether pricing actions before and after quarter-end indicate situations where markdowns should be more appropriately identified as permanent; and 5) Financial management will approve changes, if any, in seasonal merchandise mark out-of-stock dates.

*Leasehold improvement costs:* We are implementing the following activities to remediate the leasehold accounting material weakness noted above: 1) The existing policy and procedures related to leases will be updated to reflect the proper accounting treatment of lease terms and financial management will review the terms of all new leases that contain TIA in accordance with the new policy to determine that leasehold improvements and deferred rent credits are correctly recorded; 2) The finance department will meet with real estate management annually to review the lease accounting policy and validate the underlying assertions made by the real estate department upon which the policy is predicated; and 3) We will be purchasing a software application that in addition to streamlining our processes for tracking and recording leases will facilitate communication between finance and our real estate department.

*Compensated absences (paid vacation):* We are implementing the following activities to remediate the compensated absences (paid vacation) material weakness noted above: The accounting policy for recording accrued vacation will be updated by the finance department to reflect the proper accounting treatment of compensated absences (paid vacation) in accordance with the Company's vacation policy and changes to the Company's vacation policy will require approval by the finance department. Additionally, financial management will review and approve the vacation accrual on a quarterly basis and determine that the accrual calculation is consistent with the Company's vacation policy.

*Indirect overhead cost capitalization:* We are implementing the following activities to remediate the indirect cost capitalization material weakness noted above: The accounting policy for recording the indirect cost capitalization adjustment will be changed to include quarterly review of the indirect overhead rate assumptions and preparation of the resulting inventory adjustment on a quarterly basis. Additionally, financial management will review and approve the indirect cost capitalization adjustment on a quarterly basis.

*Software assets amortization periods and retirements:* We are implementing the following activities to remediate the software assets amortization periods and retirements material weaknesses noted above: Financial management reviews software asset additions with IT personnel and approves the software asset amortization period and capitalization prior to recording in the fixed asset subledger. For retirements, we added procedures for IT personnel and financial management to review the software assets listing to identify assets no longer in use on an annual basis.

Identified in the third quarter of 2011:

*Information technology communication:* We implemented or are implementing the following activities to remediate the information technology material weakness noted above: 1) In the first quarter of 2012, we added procedures to regularly review systematic schedule changes that have been temporarily placed on hold; 2) In the first quarter of 2012, we monitored the capacity issue on our legacy inventory system on a daily basis until we replaced the system in May 2012; and 3) We are implementing procedures to ensure formal communication and documentation with finance and other department heads related to issue resolution.

In addition to the remediation efforts set forth above, we re-evaluated the composition and structure of our finance organization and made several changes including replacing associates in several key positions, modifying associate responsibilities, adding resources and realigning reporting assignments to strengthen the skills and capabilities of the organization and to improve the level of information and communication between departmental functions. Additionally, we are implementing a quarterly sub-certification process whereby all members of upper management and certain other management will review our filings and confirm their responsibility for, among other things, the effectiveness of key controls in their functional areas and that they are unaware of inaccuracies or omissions in our financial statements.

### **Changes in Internal Control Over Financial Reporting**

There were no changes in the Company's internal control over financial reporting (as that term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter ended October 27, 2012 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents****PART II - OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS**

We are involved in various routine legal proceedings incidental to the conduct of our business. Management, based upon the advice of outside legal counsel, does not believe that any of these legal proceedings will have a material adverse effect on our financial condition, results of operations or cash flows.

**ITEM 1A. RISK FACTORS**

The risks described in Item 1A, Risk Factors, in our Annual Report on Form 10-K for the fiscal year ended January 28, 2012 and our Form 10Q/A for the fiscal period ended April 28, 2012, could materially and adversely affect our business, financial condition and results of operations.

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

The following table provides information regarding repurchases of our common stock during the quarter ended October 27, 2012:

|                    |                    | ISSUER PURCHASES OF EQUITY SECURITIES |                              |  |  |
|--------------------|--------------------|---------------------------------------|------------------------------|--|--|
| Period             |                    | Total number of shares purchased      | Average price paid per share | Total number of shares purchased as part of publicly announced plans or programs (1) | Maximum number of shares that may yet be purchased under the plans or programs (1) |
| July 29, 2012      | August 25, 2012    | 69,371                                | \$ 7.99                      | 69,371   | 1,006,219  |
| August 26, 2012    | September 29, 2012 | 32,938                                | \$ 8.12                      | 32,938   | 973,281  |
| September 30, 2012 | October 27, 2012   | 1,992                                 | \$ 8.45                      | 1,992  | 971,289  |
| Total              |                    | 104,301                               | \$ 8.04                      | 104,301  | 971,289  |

(1) Our Open Market Repurchase Program is conducted pursuant to authorizations made from time to time by our Board of Directors.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

Not applicable.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**ITEM 5. OTHER INFORMATION**

Not applicable.

**ITEM 6. EXHIBITS**

- 31.1 Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) or 15d-14(a)
- 31.2 Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) or 15d-14(a)
- 32.1 Certification of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350
- 32.2 Certification of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350
- 101 Interactive data files from Stein Mart, Inc.'s Quarterly Report on Form 10-Q for the quarter ended October 27, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Income, (iii) the Condensed Consolidated Statements of Comprehensive Income, (iv) the Condensed Consolidated Statements of Cash Flows, and (v) the Notes to Condensed Consolidated Financial Statements

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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.

STEIN MART, INC.

Date: May 3, 2013

By: /s/ Jay Stein

**Jay Stein**

Chairman of the Board and Interim Chief Executive Officer

/s/ Gregory W. Kleffner

**Gregory W. Kleffner**

Executive Vice President and Chief Financial Officer