

Macy's, Inc.
Form 424B2
September 05, 2013
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Filed pursuant to Rule 424(b)(2)

SEC File No. 333-185321

333-185321-01

CALCULATION OF REGISTRATION FEE

Title of each Class of	Amount	Maximum	Maximum	
	To be	Offering Price	Aggregate	Amount of
Securities to be Registered	Registered	Per Unit	Offering Price	Registration Fee (1)
4.375% Senior Notes due 2023	\$400,000,000	99.314%	\$397,256,000	\$54,186

(1) Pursuant to Rule 475(r), the total registration fee for this offering is \$54,186.

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PROSPECTUS SUPPLEMENT

(TO PROSPECTUS DATED DECEMBER 7, 2012)

\$400,000,000

Macy's Retail Holdings, Inc.

4.375% Senior Notes Due 2023

Payment of principal and interest unconditionally guaranteed by

Macy's, Inc.

Macy's Retail Holdings, Inc. (Macy's Holdings) is offering \$400,000,000 aggregate principal amount of its 4.375% Senior Notes due September 1, 2023, which we refer to as the senior notes.

The senior notes mature on September 1, 2023, unless earlier redeemed in whole. Macy's Holdings will pay interest on the senior notes semi-annually in arrears on each March 1 and September 1. The first interest payment will be made on March 1, 2014. The senior notes will rank equal in right of payment to any other existing or future senior unsecured obligations of Macy's Holdings. The guarantee will rank equal in right of payment to all other existing and future senior unsecured obligations of Macy's, Inc.

Macy's Holdings may redeem the senior notes at any time at the redemption price set forth herein. Upon the occurrence of both (i) a change of control of Macy's, Inc. and (ii) within a specified period in relation to the change of control, the senior notes being downgraded by at least two of Fitch Ratings, Inc., Moody's Investors Service, Inc. and Standard & Poor's Ratings Services and being rated below an investment grade rating by at least two of such rating agencies, Macy's Holdings will be required to make an offer to purchase the senior notes at 101% of their principal amount. On and after June 1, 2023 Macy's Holdings may redeem the senior notes at par, plus accrued and unpaid interest.

Investing in the senior notes involves risks. See the Risk Factors section in our Annual Report on Form 10-K for the year ended February 2, 2013.

	Per Note	Senior Notes Total
Initial public offering price (1)	99.314%	\$ 397,256,000
Underwriting discounts and commissions	0.650%	\$ 2,600,000
Proceeds to Macy's Holdings (1)	98.664%	\$ 394,656,000

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(1) Plus accrued interest, if any, from September 6, 2013.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement or the accompanying prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the senior notes in book-entry form only through the facilities of The Depository Trust Company for the accounts of its participants, including Clearstream Banking, societe anonyme, and Euroclear Bank S.A./N.V., as operator of the Euroclear System, against payment in New York, New York on September 6, 2013.

Joint Book-Running Managers

**BofA Merrill Lynch
Goldman, Sachs & Co.**

**Credit Suisse
US Bancorp**
Co-Managers

**J.P. Morgan
Wells Fargo Securities**

**BNY Mellon Capital Markets, LLC
Loop Capital Markets
Ramirez & Co., Inc.**

**Citigroup
Mitsubishi UFJ Securities
Standard Chartered Bank**

**Fifth Third Securities, Inc.
PNC Capital Markets LLC
The Williams Capital Group, L.P.**

The date of this prospectus supplement is September 3, 2013.

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None of Macy's, Inc., Macy's Holdings or any underwriter has authorized anyone to provide any information or to make any representation other than those contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or in any free writing prospectus that we have prepared. We take no responsibility for, and can provide no assurance as to the reliability of, any other information that others may give you. This document may only be used where it is legal to sell the securities. The information in this document may be accurate only on the date of this document.

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SUMMARY

The following summary contains basic information about the senior notes and is not intended to be complete. For a more complete discussion of the senior notes, please refer to the section entitled "Description of Notes" in this prospectus supplement. You should read the entire prospectus supplement and the accompanying prospectus, as well as the documents incorporated by reference into them, before making an investment decision.

Issuer	Macy's Retail Holdings, Inc.
Guarantor	Macy's, Inc.
Securities Offered	\$400,000,000 aggregate principal amount of 4.375% Senior Notes due 2023 (the "senior notes").
Maturity Date	September 1, 2023.
Interest Payment Dates	Semi-annually in arrears on each March 1 and September 1, commencing on March 1, 2014. Interest on the senior notes being offered by this prospectus supplement will accrue from September 6, 2013.
Ranking	The senior notes will rank equal in right of payment to any other existing or future senior unsecured obligations of Macy's Holdings.
Guarantee	The obligations of Macy's Holdings under the senior notes will be fully and unconditionally guaranteed on a senior unsecured basis by Macy's, Inc. The guarantee will rank equal in right of payment to all other existing and future senior unsecured obligations of Macy's, Inc.
Optional Redemption	Macy's Holdings may, at its option, at any time in whole or from time to time in part, redeem the senior notes at the redemption prices described in this prospectus supplement, plus accrued interest to the date of redemption.
Change of Control	Upon the occurrence of both (i) a change of control of Macy's, Inc. and (ii) within a specified period in relation to the change of control, the senior notes being downgraded by at least two of Fitch Ratings, Inc., Moody's Investors Service, Inc. and Standard & Poor's Ratings Services and being rated below an investment grade rating by at least two of such rating agencies, Macy's Holdings will be required to make an offer to purchase the senior notes at a price equal to 101% of their principal amount, plus accrued and unpaid interest to the date of repurchase. See "Description of Notes" Change of Control.
Certain Covenants	The indenture, pursuant to which the senior notes will be issued, will contain covenants that will, among other things, limit the ability of Macy's Holdings to:

incur certain liens;

enter into sale and leaseback transactions; or

consolidate, merge or transfer all or substantially all of its assets.

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These covenants will be subject to important exceptions and qualifications, which are described in Description of Notes Certain Restrictive Covenants.

Denominations

Minimum denominations of \$2,000 and integral multiples of \$1,000 in excess thereof.

Settlement Date

September 6, 2013 (T +3).

Use of Proceeds

Macy s Holdings will use the net proceeds from the sale of the senior notes offered hereby for general corporate purposes, which may include working capital, capital expenditures, retirement of indebtedness and repurchasing outstanding common stock of Macy s, Inc.

Ratio of Earnings to Fixed Charges

Macy s, Inc. s ratios of earnings to fixed charges for the 26 weeks ended August 3, 2013 and for the fiscal years ended February 2, 2013, January 28, 2012 and January 29, 2011 were 4.0x, 4.1x, 4.5x and 2.9x, respectively.

For purposes of determining the ratio of earnings to fixed charges, earnings consist of income before income taxes plus fixed charges (excluding interest capitalized). Fixed charges represent interest incurred, premium on early retirement of debt, amortization of debt expenses, and that portion of rental expenses on operating leases deemed to be the equivalent of interest.

Trustee, Registrar and Paying Agent

The Bank of New York Mellon Trust Company, N.A.

Table of Contents**RECENT DEVELOPMENTS****Preliminary Unaudited Results of Operations for the 13 and 26 Weeks Ended August 3, 2013**

On August 14, 2013, Macy's, Inc. announced its unaudited results of operations data for the 13 and 26 weeks ended August 3, 2013, including the data set forth below.

	13 Weeks Ended		26 Weeks Ended	
	August 3, 2013	July 28, 2012	August 3, 2013	July 28, 2012
	(Millions)			
Net sales	\$ 6,066	\$ 6,118	\$ 12,453	\$ 12,261
Cost of sales (1)	3,533	3,555	7,444	7,312
Gross margin	2,533	2,563	5,009	4,949
Selling, general and administrative expenses	(1,999)	(2,009)	(4,040)	(4,004)
Operating income	534	554	969	945
Interest expense net (2)	(96)	(105)	(193)	(217)
Income before income taxes	438	449	776	728
Federal, state and local income tax expense (3)	(157)	(170)	(278)	(268)
Net income	\$ 281	\$ 279	\$ 498	\$ 460

- (1) Merchandise inventories are valued at the lower of cost or market using the last-in, first-out (LIFO) retail inventory method. Application of the LIFO retail inventory method did not result in the recognition of any LIFO charges or credits affecting cost of sales for the 13 and 26 weeks ended August 3, 2013 or July 28, 2012.
- (2) Interest expense for the 26 weeks ended July 28, 2012 includes approximately \$4 million of expenses associated with the early redemption of approximately \$173 million of 8.0% senior debentures due July 15, 2012.
- (3) Federal, state and local income taxes differ from the federal income tax statutory rate of 35%, principally because of the effect of state and local taxes, including the settlement of various tax issues and tax examinations.
- Macy's ratio of earnings to fixed charges for the 26 weeks ended August 3, 2013 is 4.0x. For purposes of determining the ratio of earnings to fixed charges, earnings consist of income before income taxes plus fixed charges (excluding interest capitalized). Fixed charges represent interest incurred, premium on early retirement of debt, amortization of debt expenses, and that portion of rental expenses on operating leases deemed to be the equivalent of interest.

The foregoing data should be read in conjunction with the consolidated financial statements (including the notes thereto) and the other information contained or incorporated by reference in this prospectus supplement and the accompanying prospectus. Because of the seasonal nature of the retail business, the results of operations for the 13 and 26 weeks ended August 3, 2013 and July 28, 2012 (which do not include the Christmas season) are not necessarily indicative of the results for the fiscal year.

Macy's, Inc.'s independent registered public accounting firm has not audited any of the information set forth above. Macy's, Inc.'s independent registered public accounting firm will audit Macy's financial statements for the fiscal year ending February 1, 2014 following the completion of such fiscal year. This audit could result in changes to the preliminary results indicated above.

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USE OF PROCEEDS

Macy's Holdings will use the net proceeds from the sale of the senior notes offered hereby for general corporate purposes, which may include working capital, capital expenditures, retirement of indebtedness and repurchasing outstanding common stock of Macy's, Inc.

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DESCRIPTION OF NOTES

The senior notes will be issued under an indenture, dated as of January 13, 2012 (the "Base Indenture"), among Macy's Holdings, as issuer, Macy's, Inc., as guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee (the "Trustee"), as supplemented by a Fifth Supplemental Trust Indenture, to be dated as of September 6, 2013 (the "Fifth Supplemental Indenture") and together with the Base Indenture, the "Indenture") relating to the senior notes. The following discussion includes a summary description of certain material terms of the Indenture. Because this is a summary, it does not include all of the information that is included in the Indenture, including the definitions of certain terms used below. You should read the Indenture carefully and in its entirety. You may request a copy of the Indenture at Macy's, Inc.'s address set forth under the caption "Where You Can Find More Information" in the accompanying prospectus.

General

The senior notes are senior unsecured obligations of Macy's Holdings. The senior notes constitute a series of notes that will initially be limited to \$400,000,000 aggregate principal amount and will mature on September 1, 2023. Macy's Holdings will issue the senior notes in minimum denominations of \$2,000 and integral multiples of \$1,000 in excess thereof. The senior notes will bear interest at the applicable rate per year shown on the cover page of this prospectus supplement from September 6, 2013. Macy's Holdings will pay interest semi-annually in arrears on March 1 and September 1 of each year commencing on March 1, 2014 to the Person in whose name the senior notes (or any predecessor note) is registered at the close of business on February 15 or August 15, respectively, preceding such interest payment date. Interest on the senior notes will be calculated on the basis of a 360-day year consisting of 12 months of 30 days each.

The senior notes will be exchangeable and transfers thereof will be registrable, at an office or agency of Macy's Holdings, one of which will be maintained for such purpose in New York, New York (which initially will be the corporate trust office of the Trustee) or such other office or agency permitted under the Indenture.

The senior notes will rank equal in right of payment to any other existing or future senior unsecured obligations of Macy's Holdings. The senior notes will not be subject to any sinking fund.

Macy's Holdings does not intend to list the senior notes on a national securities exchange.

The Indenture does not contain any provisions that would limit the ability of Macy's Holdings to incur indebtedness or require the maintenance of financial ratios or specified levels of net worth or liquidity. However, the Indenture does:

provide that, subject to certain exceptions, neither Macy's Holdings nor any Restricted Subsidiary will subject its property or assets to any mortgage or other encumbrance unless the senior notes are secured equally and ratably with such other indebtedness thereby secured; and

contain certain limitations on the ability of Macy's Holdings and its Restricted Subsidiaries to enter into certain sale and leaseback arrangements.

Guarantee

The obligations of Macy's Holdings under the senior notes will be fully and unconditionally guaranteed (the "Guarantee") on a senior unsecured basis by Macy's, Inc. The Guarantee will rank equal in right of payment to all other existing and future senior unsecured obligations of Macy's, Inc.

Table of Contents**Further Issuances**

Macy's Holdings may, from time to time, without notice to or the consent of the holders of the senior notes, increase the principal amount of the senior notes under the Indenture and issue such increased principal amount (or any portion thereof), in which case any additional notes so issued will have the same form and terms (other than the date of issuance and, under certain circumstances, the date from which interest thereon will begin to accrue), and will carry the same right to receive accrued and unpaid interest, as the senior notes previously issued, and such additional notes will form a single series with the senior notes.

Redemption

Macy's Holdings may, at its option, redeem the senior notes, at any time in whole or from time to time in part, prior to June 1, 2023 (three months prior to the maturity date) on not less than 30 nor more than 60 days' prior notice transmitted to the holders of the senior notes to be redeemed. The senior notes will be so redeemable at a redemption price, plus accrued interest to the date of redemption, equal to the greater of (1) 100% of the principal amount of the senior notes to be redeemed and (2) the sum of the remaining scheduled payments of principal and interest on the senior notes to be redeemed that would be due after the related redemption date but for such redemption (except that, if such redemption date is not an interest payment date with respect to the senior notes, the amount of the next succeeding scheduled interest payment will be reduced by the amount of interest accrued thereon to the redemption date), discounted to the redemption date on a semi-annual basis (assuming a 360-day year consisting of twelve 30-day months) at the Treasury Rate plus 25 basis points.

At any time on and after June 1, 2023 (three months prior to the maturity date), Macy's Holdings may, at its option, redeem the senior notes in whole or from time to time in part on not less than 30 nor more than 60 days' prior notice transmitted to the holders of senior notes to be redeemed. The senior notes will be so redeemable at a redemption price equal to 100% of the principal amount of the senior notes to be redeemed plus accrued and unpaid interest on the senior notes to be redeemed to the date of redemption.

Comparable Treasury Issue means the United States Treasury security selected by an Independent Investment Banker that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining term of the senior notes. *Independent Investment Banker* means one of the Reference Treasury Dealers appointed by Macy's Holdings.

Comparable Treasury Price means, with respect to any redemption date, (1) the average of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) on the third business day preceding such redemption date, as set forth in the daily statistical release (or any successor release) published by the Federal Reserve Bank of New York and designated *Composite 3:30 p.m. Quotations for U.S. Government Securities* or (2) if such release (or any successor release) is not published or does not contain such prices on such business day, (a) the average of the Reference Treasury Dealer Quotations for such redemption date, after excluding the highest and lowest of such Reference Treasury Dealer Quotations, or (b) if Macy's Holdings obtains fewer than four such Reference Treasury Dealer Quotations, the average of all such Quotations.

Reference Treasury Dealer means each of Credit Suisse Securities (USA) LLC, J.P. Morgan Securities LLC, Merrill Lynch, Pierce, Fenner & Smith Incorporated and their respective successors and one other nationally recognized investment banking firm that is a primary U.S. Government securities dealer in New York City (a *Primary Treasury Dealer*) specified from time to time by Macy's Holdings, except that if any of the foregoing ceases to be a *Primary Treasury Dealer*, Macy's Holdings is required to designate as a substitute another nationally recognized investment banking firm that is a *Primary Treasury Dealer*.

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Reference Treasury Dealer Quotations means, with respect to each Reference Treasury Dealer and any redemption date, the average, as determined by Macy's Holdings, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) quoted in writing to Macy's Holdings by such Reference Treasury Dealer as of 3:30 p.m., New York City time, on the third business day preceding such redemption date.

Treasury Rate means, with respect to any redemption date, the rate per annum equal to the semi-annual equivalent yield to maturity (computed as of the second business day immediately preceding such redemption date) of the Comparable Treasury Issue, assuming a price for the Comparable Treasury Issue (expressed as a percentage of its principal amount) equal to the Comparable Treasury Price for such redemption date.

On and after any redemption date, interest will cease to accrue on the senior notes called for redemption. On or prior to any redemption date, Macy's Holdings is required to deposit with a paying agent money sufficient to pay the redemption price of and accrued interest on the senior notes to be redeemed on such date. If Macy's Holdings is going to redeem less than all the senior notes, (a) if such senior notes are represented by global notes, interests in such global notes will be selected for redemption in accordance with the customary procedures of DTC, or (b) if such senior notes are represented by senior notes in certificated form, the Trustee will select the senior notes to be redeemed by such method as the Trustee deems fair and appropriate in accordance with methods generally used at the time of selection by fiduciaries in similar circumstances.

Change of Control

If a Change of Control Triggering Event occurs, unless Macy's Holdings has exercised its right to redeem the senior notes in whole as described above, holders of senior notes will have the right to require Macy's Holdings to repurchase all or any part (equal to \$2,000 or an integral multiple of \$1,000 in excess thereof) of their senior notes pursuant to the offer described below (the *Change of Control Offer*) on the terms set forth in the Indenture. In the Change of Control Offer, Macy's Holdings will be required to offer payment in cash equal to 101% of the aggregate principal amount of senior notes repurchased plus accrued and unpaid interest, if any, on the senior notes repurchased, to the date of purchase (the *Change of Control Payment*). Within 30 days following any Change of Control Triggering Event or, at the option of Macy's Holdings, prior to any Change of Control, but after public announcement of the transaction or transactions that constitute or may constitute the Change of Control, Macy's Holdings will be required to mail a notice to holders of senior notes describing the transaction or transactions that constitute or may constitute the Change of Control Triggering Event and offering to repurchase the senior notes on the date specified in the notice, which date will be no earlier than 30 days and no later than 60 days from the date such notice is mailed (the *Change of Control Payment Date*), pursuant to the procedures required by the Indenture and described in such notice, which offer will constitute the Change of Control Offer. The notice will, if mailed prior to the date on which the Change of Control occurs, state that the Change of Control Offer is conditioned on the Change of Control Triggering Event occurring on or prior to the applicable Change of Control Payment Date.

On the Change of Control Payment Date, Macy's Holdings will be required, to the extent lawful, to:

accept for payment all senior notes or portions of senior notes properly tendered pursuant to the Change of Control Offer;

deposit with the paying agent an amount equal to the Change of Control Payment in respect of all senior notes or portions of senior notes properly tendered; and

deliver or cause to be delivered to the Trustee the senior notes properly accepted together with an officers' certificate stating the aggregate principal amount of senior notes or portions of senior notes being purchased.

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Macy's Holdings will not be required to make a Change of Control Offer upon the occurrence of a Change of Control Triggering Event if a third party makes such an offer in the manner, at the times and otherwise in compliance with the requirements for an offer made by Macy's Holdings and the third party repurchases all senior notes properly tendered and not withdrawn under its offer. In addition, Macy's Holdings will not be required to repurchase any senior notes if it has given written notice of a redemption in whole of the senior notes as provided under Redemption .

Macy's Holdings will be required to comply with the requirements of Rule 14e-1 under the Securities Exchange Act of 1934, as amended (the *Exchange Act*) and any other securities laws and regulations thereunder to the extent those laws and regulations are applicable in connection with the repurchase of the senior notes as a result of a Change of Control Triggering Event. To the extent that the provisions of any securities laws or regulations conflict with the Change of Control provisions of the Indenture, Macy's Holdings will be required to comply with the applicable securities laws and regulations and will not be deemed to have breached its obligations under the Change of Control provisions of the Indenture by virtue of such compliance.

For purposes of the foregoing discussion of a repurchase at the option of holders, the following definitions are applicable:

Change of Control means the occurrence of any of the following: (1) the direct or indirect sale, lease, transfer, conveyance or other disposition (other than by way of merger or consolidation), in one or a series of related transactions, of all or substantially all of the properties or assets of Macy's, Inc. and its subsidiaries taken as a whole to any Person other than Macy's, Inc. or one of its subsidiaries; (2) the consummation of any transaction (including, without limitation, any merger or consolidation) the result of which is that any Person becomes the beneficial owner, directly or indirectly, of more than 50% of the then outstanding number of shares of Macy's, Inc.'s Voting Stock or other Voting Stock into which the Voting Stock of Macy's, Inc. is reclassified, consolidated, exchanged or changed, measured by voting power rather than number of shares; (3) Macy's, Inc. consolidates with, or merges with or into, any Person, or any Person consolidates with, or merges with or into Macy's, Inc., in any such event pursuant to a transaction in which any of the outstanding shares of Macy's, Inc.'s Voting Stock or the Voting Stock of such other Person is converted into or exchanged for cash, securities or other property, other than any such transaction where the shares of Macy's, Inc.'s Voting Stock outstanding immediately prior to such transaction constitute, or are converted into or exchanged for, a majority of the Voting Stock of the resulting or surviving Person or any direct or indirect parent company of the resulting or surviving Person immediately after giving effect to such transaction; (4) the first day on which a majority of the members of Macy's, Inc.'s Board of Directors are not Continuing Directors; or (5) the adoption of a plan providing for the liquidation or dissolution of Macy's, Inc. Notwithstanding the foregoing, a transaction will not be deemed to involve a Change of Control under clause (2) above if (i) Macy's, Inc. becomes a direct or indirect wholly owned subsidiary of a holding company and (ii)(A) the direct or indirect holders of the Voting Stock of such holding company immediately following that transaction are substantially the same as the holders of Macy's, Inc.'s Voting Stock immediately prior to that transaction or (B) immediately following that transaction no Person (other than a holding company satisfying the requirements of this sentence) is the beneficial owner, directly or indirectly, of more than 50% of the Voting Stock of such holding company. The term Person, as used in this definition, has the meaning given thereto in Section 13(d)(3) of the Exchange Act.

Change of Control Triggering Event means the occurrence of both a Change of Control and a Rating Event.

Continuing Directors means, as of any date of determination, any member of the Board of Directors of Macy's, Inc. who (1) was a member of such Board of Directors on the date of the Fifth Supplemental Indenture; or (2) was nominated for election or elected to such Board of Directors with the approval of a majority of the Continuing Directors who were members of such Board of Directors at the time of such nomination or election (either by a specific vote or by approval of Macy's, Inc.'s proxy statement in which such member was named as a nominee for election as a director, without objection to such nomination).

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Fitch means Fitch Ratings, Inc. or its successor.

Investment Grade Rating means a rating equal to or higher than BBB- (or the equivalent) by Fitch, Baa3 (or the equivalent) by Moody's and BBB- (or the equivalent) by S&P.

Moody's means Moody's Investors Service, Inc. or its successor.

Rating Agencies means (1) each of Fitch, Moody's and S&P; and (2) if any of Fitch, Moody's or S&P ceases to rate the senior notes or fails to make a rating of the senior notes publicly available for reasons outside of Macy's Holdings' control, a nationally recognized statistical rating organization within the meaning of Rule 15c3-1(c)(2)(vi)(F) under the Exchange Act, selected by Macy's Holdings (as certified by a resolution of its Board of Directors) as a replacement agency for Fitch, Moody's or S&P, or all of them, as the case may be.

Rating Event means the rating on the senior notes is lowered by at least two of the three Rating Agencies and the senior notes are rated below an Investment Grade Rating by at least two of the three Rating Agencies, on any day during the period (which period will be extended so long as the rating of the applicable senior notes is under publicly announced consideration for a possible downgrade by any of the Rating Agencies) commencing 60 days prior to the first public notice of the occurrence of a Change of Control or the intention of Macy's, Inc. to effect a Change of Control and ending 60 days following consummation of such Change of Control.

S&P means Standard & Poor's Ratings Services, a division of McGraw Hill Financial, Inc., or its successor.

Voting Stock means, with respect to any specified Person (as that term is used in Section 13(d)(3) of the Exchange Act) as of any date, the capital stock of such Person that is at the time entitled to vote generally in the election of the board of directors of such Person.

Holder may not be entitled to require Macy's Holdings to purchase their senior notes in certain circumstances involving a significant change in the composition of Macy's, Inc.'s Board of Directors, including in connection with a proxy contest, where Macy's, Inc.'s Board of Directors initially publicly opposes the election of a dissident slate of directors, but subsequently approves such directors as Continuing Directors for purposes of the Indenture. This may result in a change in the composition of the Board of Directors that, but for such subsequent approval, would have otherwise constituted a Change of Control requiring a Change of Control Offer under the terms of the Indenture.

Under a recent Delaware Chancery Court interpretation of the foregoing definition of Continuing Directors, a board of directors may approve for purposes of such definition, a slate of shareholder-nominated directors without endorsing them, while simultaneously recommending and endorsing its own slate. This interpretation permits Macy's, Inc.'s Board of Directors to approve a slate of directors that includes a majority of dissident directors nominated pursuant to a proxy contest and the ultimate election of such dissident slate would not constitute a Change of Control that would trigger the holder's right to require Macy's Holdings to repurchase its senior notes as described above.

The definition of Change of Control includes a phrase relating to the direct or indirect sale, lease, transfer, conveyance or other disposition of all or substantially all of the properties and assets of Macy's, Inc. and its subsidiaries taken as a whole. Although there is a limited body of case law interpreting the phrase substantially all, there is no precise established definition of the phrase under applicable law. Accordingly, the ability of a holder of senior notes to require Macy's Holdings to repurchase its senior notes as a result of a sale, lease, transfer, conveyance or other disposition of less than all of the properties and assets of Macy's, Inc. and its subsidiaries taken as a whole to another person or group may be uncertain.

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Book-Entry System

The senior notes will initially be issued in the form of a global security held in book-entry form. Accordingly, The Depository Trust Company (DTC) or its nominee will be the sole registered holder of the senior notes for all purposes under the Indenture. DTC has advised Macy's Holdings that DTC is a limited-purpose trust company organized under the Banking Law of the State of New York, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code, and a clearing agency registered under the Exchange Act.

DTC was created to hold the securities of its participants and to facilitate the clearance and settlement of securities transactions among its participants in such securities through electronic book-entry changes in accounts of the participants, thereby eliminating the need for physical movement of securities certificates. DTC's participants include securities brokers and dealers (including the underwriters), banks, trust companies, clearing corporations and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (DTCC). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to DTC's book-entry system is also available to others such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a participant, either directly or indirectly. See Description of Debt Securities Global Securities in the accompanying prospectus.

Clearstream Banking, societe anonyme (Clearstream), is incorporated under the laws of Luxembourg as a professional depository. Clearstream holds securities for its participating organizations (Clearstream Participants) and facilitates the clearance and settlement of securities transactions between Clearstream Participants through electronic book-entry changes in accounts of Clearstream Participants, thereby eliminating the need for physical movement of certificates. Clearstream provides Clearstream Participants with, among other things, services for safekeeping, administration, clearance and establishment of internationally traded securities and securities lending and borrowing. Clearstream interfaces with domestic markets in several countries. Clearstream is subject to regulation by the Commission de Surveillance du Secteur Financier and the Luxembourg Central Bank. Clearstream Participants are recognized financial institutions around the world, including underwriters, securities brokers and dealers, banks, trust companies, clearing corporations and certain other organizations, and may include the underwriters. Indirect access to Clearstream is also available to others, such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a Clearstream Participant either directly or indirectly.

Distributions with respect to senior notes held beneficially through Clearstream will be credited to cash accounts of Clearstream Participants in accordance with its rules and procedures to the extent received by DTC for Clearstream.

Euroclear was created in 1968 to hold securities for participants of Euroclear (Euroclear Participants) and to clear and settle transactions between Euroclear Participants through simultaneous electronic book-entry delivery against payment, thereby eliminating the need for physical movement of certificates and any risk from lack of simultaneous transfers of securities and cash. Euroclear includes various other services, including securities lending and borrowing and interfaces with domestic markets and in several markets in several countries. Euroclear is operated by Euroclear Bank S.A./N.V. (the Euroclear Operator), under contract with Euroclear plc, a U.K. corporation. All operations are conducted by the Euroclear Operator, and all Euroclear securities clearance accounts and Euroclear cash accounts are accounts with the Euroclear Operator. Euroclear Participants include banks (including central banks), securities brokers and dealers and other professional financial intermediaries and may include the underwriters. Indirect access to Euroclear is also available to other firms that clear through or maintain a custodial relationship with a Euroclear Participant, either directly or indirectly.

The Euroclear Operator is regulated and examined by the Belgian Banking and Finance Commission and the National Bank of Belgium.

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Links have been established among DTC, Clearstream and Euroclear to facilitate the initial issuance of the senior notes sold outside of the United States and cross-market transfers of the senior notes associated with secondary market trading.

Although DTC, Clearstream and Euroclear have agreed to the procedures provided below in order to facilitate transfers, they are under no obligation to perform these procedures, and these procedures may be modified or discontinued at any time.

Clearstream and Euroclear will record the ownership interests of their participants in much the same way as DTC, and DTC will record the total ownership of each of the U.S. agents of Clearstream and Euroclear, as participants in DTC. When senior notes are to be transferred from the account of a DTC participant to the account of a Clearstream participant or a Euroclear participant, the purchaser must send instructions to Clearstream or Euroclear through a participant at least one day prior to settlement. Clearstream or Euroclear, as the case may be, will instruct its U.S. agent to receive senior notes against payment. After settlement, Clearstream or Euroclear will credit its participant's account. Credit for the senior notes will appear the next day (European time).

Because settlement is taking place during New York business hours, DTC participants will be able to employ their usual procedures for sending senior notes to the relevant U.S. agent acting for the benefit of Clearstream or Euroclear participants. The sale proceeds will be available to the DTC seller on the settlement date. As a result, to the DTC participant, a cross-market transaction will settle no differently than a trade between two DTC participants. When a Clearstream or Euroclear participant wishes to transfer senior notes to a DTC participant, the seller will be required to send instructions to Clearstream or Euroclear through a participant at least one business day prior to settlement. In these cases, Clearstream or Euroclear will instruct its U.S. agent to transfer these senior notes against payment for them. The payment will then be reflected in the account of the Clearstream or Euroclear participant the following day, with the proceeds back valued to the value date, which would be the preceding day, when settlement occurs in New York if settlement is not completed on the intended value date, that is, the trade fails, proceeds credited to the Clearstream or Euroclear participant's account will instead be valued as of the actual settlement date.

You should be aware that you will only be able to make and receive deliveries, payments and other communications involving the senior notes through Clearstream and Euroclear on the days when those clearing systems are open for business. Those systems may not be open for business on days when banks, brokers and other institutions are open for business in the United States. In addition, because of time zone differences there may be problems with completing transactions involving Clearstream and Euroclear on the same business day as in the United States.

Payment

The payment of principal of and interest on senior notes represented by a global security will be made in immediately available funds in accordance with the applicable requirements of the depository for the global security.

Certain Restrictive Covenants

The Indenture will contain the following restrictive covenants.

Limitation on Liens. Macy's Holdings and the Restricted Subsidiaries will not be permitted to create, incur, assume or suffer to exist any liens upon any of their respective assets, other than Permitted Liens, unless the senior notes are secured by an equal and ratable lien on the same assets. The terms of other existing and future indebtedness of Macy's Holdings may require that such other indebtedness be similarly secured by an equal and ratable lien on such assets.

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Limitation on Sale and Leaseback. Macy's Holdings and the Restricted Subsidiaries will not be permitted to enter into any sale and leaseback transaction unless the net cash proceeds therefrom are applied as follows: to the extent that the aggregate amount of net cash proceeds from such sale and leaseback transaction that have not been reinvested in the business of Macy's Holdings or its Subsidiaries or used to reduce Senior Indebtedness of Macy's Holdings or its Subsidiaries within 12 months of the receipt of such proceeds exceeds \$100.0 million (Excess Sale Proceeds) from time to time, such Excess Sale Proceeds will be used to offer to repurchase the senior notes (on a pro rata basis with any other Senior Indebtedness of Macy's Holdings or its Subsidiaries required by the terms of such Indebtedness to be repurchased with such Excess Sale Proceeds, based on the principal amount of such Senior Indebtedness required to be repurchased) at 100% of their principal amount, plus accrued and unpaid interest, and to pay related costs and expenses.

To the extent that the aggregate purchase price for the senior notes or other Senior Indebtedness tendered pursuant to such an offer to purchase is less than the aggregate purchase price offered in such offer, an amount of Excess Sale Proceeds equal to such shortfall will cease to be Excess Sale Proceeds and may thereafter be used for general corporate purposes. If the aggregate purchase price for the senior notes or other Senior Indebtedness tendered pursuant to such an offer to purchase exceeds the amount of such Excess Sale Proceeds, the Trustee will select the senior notes or other Senior Indebtedness to be purchased by such method as the Trustee deems fair and appropriate.

The net cash proceeds from any sale or leaseback transaction will be determined net of the following:

all fees and expenses incurred and all taxes and reserves required to be accrued as a liability as a consequence of such a sale and leaseback transaction;

all payments made on any Indebtedness that is secured by assets subject to a sale and leaseback transaction; and

all distributions and other payments made to minority interest holders in Subsidiaries of Macy's Holdings or joint ventures as a result of a sale and leaseback transaction.

Cash Equivalents will be deemed to be proceeds upon receipt of such Cash Equivalents and cash payments under promissory notes secured by letters of credit or similar assurances of payment issued by commercial banks of recognized standing will be deemed to be proceeds upon receipt of such payments.

If an offer to purchase the senior notes is made, Macy's Holdings will comply with all tender offer rules, including but not limited to Section 14(e) of the Exchange Act and Rule 14e-1 thereunder, to the extent applicable to such offer to purchase. To the extent that the provisions of any securities laws or regulations conflict with the provisions of the Indenture related to limitations on sale and leaseback transactions, Macy's Holdings will comply with the applicable securities laws and regulations and will not be deemed to have breached its obligations under the provisions of the Indenture related to limitations on sale and leaseback transactions by virtue of such conflicts.

Limitations on Merger and Other Transactions

Prior to the satisfaction and discharge of the Indenture, Macy's Holdings will not be permitted to consolidate with or merge with or into any other Person, or transfer (by lease, assignment, sale, or otherwise) all or substantially all of its properties and assets to another Person unless:

(1) either

(a) Macy's Holdings is the continuing or surviving Person in the consolidation or merger; or

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(b) the Person (if other than Macy's Holdings) formed by the consolidation or into which Macy's Holdings is merged or to which all or substantially all of the properties and assets of Macy's Holdings are transferred is a corporation, partnership, limited liability company, business trust, trust or other legal entity organized and validly existing under the laws of the United States, any State thereof, or the District of Columbia, and expressly assumes, by a supplemental indenture, all of Macy's Holdings' obligations under the senior notes and the Indenture;

(2) immediately after the transaction and the incurrence or anticipated incurrence of any indebtedness to be incurred in connection therewith, no Default exists; and

(3) an officer's certificate is delivered to the Trustee to the effect that both of the conditions set forth above have been satisfied and an opinion of outside counsel has been delivered to the Trustee to the effect that condition (1) set forth above has been satisfied.

The continuing, surviving or successor Person will succeed to and be substituted for Macy's Holdings with the same effect as if it had been named in the Indenture as a party thereto, and thereafter the predecessor Person will be relieved of all obligations and covenants under the Indenture and the senior notes.

Events of Default

The following are Events of Default with respect to the senior notes:

(1) failure to pay principal of or premium, if any, on any senior note when due and payable;

(2) failure to pay any interest on any senior note when due and payable, which failure continues for 30 calendar days;

(3) failure to perform, or breach of, any other of Macy's Holdings' covenants or warranties in the Indenture (other than a covenant or warranty included therein solely for the benefit of a series of debt securities other than the senior notes), which failure or breach continues for 60 calendar days after written notice as provided in the Indenture;

(4) any nonpayment at maturity or other default (beyond any applicable grace period) under any agreement or instrument relating to any other Indebtedness of Macy's Holdings or any Restricted Subsidiary (the unpaid principal amount of which is not less than \$100.0 million), which default results in the acceleration of the maturity of such Indebtedness prior to its stated maturity or occurs at the final maturity thereof;

(5) the entry of any final judgments or orders against Macy's Holdings, Macy's, Inc. or any of their respective Restricted Subsidiaries in excess of \$100.0 million individually or in the aggregate (not covered by insurance) that is not paid, discharged or otherwise stayed (by appeal or otherwise) within 60 calendar days after the entry of such judgments or orders;

(6) the Guarantee ceases to be in full force and effect (except as contemplated by the terms of the Indenture) or is declared in a judicial proceeding to be null and void, or Macy's, Inc. denies or disaffirms in writing its obligation under the Guarantee;

(7) specified events of bankruptcy, insolvency or reorganization of Macy's Holdings, Macy's, Inc. or any Significant Subsidiary or any group of Subsidiaries of Macy's Holdings or Macy's, Inc. that, if considered in the aggregate, would be a Significant Subsidiary; and

(8) the failure to redeem the senior notes when required pursuant to the terms and conditions thereof or to pay the repurchase price for senior notes to be repurchased in accordance with the Indenture.

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Macy's Holdings will be required to provide the Trustee with notice of any uncured Event of Default within 10 calendar days after any responsible officer of Macy's Holdings becomes aware of or receives actual notice of the occurrence thereof. The Trustee will be required, within 90 calendar days after the occurrence of a default in respect of the senior notes, to give to the holders of the senior notes notice of all such uncured defaults known to it, except that:

in the case of a default in the performance of any covenant of the character contemplated in clause (3) above, no such notice to holders of the senior notes will be given until at least 30 calendar days after the occurrence of such default; and

other than in the case of a default of the character contemplated in clause (1) or (2) above, the Trustee may withhold such notice if and so long as it in good faith determines that the withholding of such notice is in the interests of the holders of the senior notes.

If an Event of Default described in clause (7) above occurs, the principal of, and any premium and accrued interest on the senior notes will become immediately due and payable without any declaration or other act on the part of the Trustee or any holder of the senior notes. If any other Event of Default with respect to the senior notes occurs and is continuing, either the Trustee or the holders of at least 25% in principal amount of the outstanding senior notes, by notice as provided in the Indenture, may declare the principal amount of the senior notes to be due and payable immediately. However, at any time after a declaration of acceleration with respect to the senior notes has been made, but before a judgment or decree based on such acceleration has been obtained, the holders of a majority in principal amount of the outstanding senior notes may, under specified circumstances, rescind and annul such acceleration.

Subject to the duty of the Trustee to act with the required standard of care during an Event of Default, the Trustee will have no obligation to exercise any of its rights or powers under the Indenture at the request or direction of any of the holders of the senior notes unless such holders shall have offered to the Trustee reasonable security or indemnity. Subject to the provisions of the Indenture, including those requiring security or indemnification of the Trustee, the holders of a majority in principal amount of the senior notes will have the right to direct the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred on the Trustee, with respect to the senior notes.

No holder of a senior note will have any right to institute any proceeding with respect to the Indenture or for any remedy thereunder unless:

the holder has previously given to the Trustee written notice of a continuing Event of Default;

the holders of at least 25% in aggregate principal amount of the outstanding senior notes have also made such a written request;

the holder or holders have offered reasonable indemnity to the Trustee to institute the proceeding as trustee;

the Trustee has failed to institute such proceeding within 60 calendar days after receipt of the written request; and

during such 60-day period, the Trustee has not received from the holders of a majority in aggregate principal amount of the outstanding senior notes a direction inconsistent with the written request.

However, the limitations described above will not apply to a suit instituted by a holder of senior notes for enforcement of payment of the principal of, and any principal or interest on, the senior notes on or after the applicable due dates expressed in the senior notes.

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Macy's Holdings will be required to furnish to the Trustee annually a statement as to the performance of its obligations under the Indenture and as to any default in such performance.

Defeasance

Except as described below, upon compliance with the applicable requirements described below:

(1) Macy's Holdings and Macy's, Inc. will be deemed to have been discharged from their respective obligations with respect to the senior notes; or

(2) Macy's Holdings will be released from its obligations to comply with certain of the covenants in the Indenture with respect to the senior notes, and the occurrence of an event described in any of clauses (3), (4) and (8) under "Events of Default" above will no longer be an Event of Default with respect to the senior notes, except to the limited extent described below.

Following any defeasance described in clause (1) or (2) above, Macy's Holdings will continue to have specified obligations under the Indenture, including obligations to register the transfer or exchange of the senior notes; replace destroyed, stolen, lost, or mutilated senior notes; maintain an office or agency in respect of the senior notes; and hold funds for payment to holders of senior notes in trust. In the case of any defeasance described in clause (2) above, any failure by Macy's Holdings to comply with its continuing obligations may constitute an Event of Default with respect to the senior notes as described in clause (3) under "Events of Defaults" above.

In order to effect any defeasance described in clause (1) or (2) above, Macy's Holdings or Macy's, Inc. must irrevocably deposit with the Trustee, in trust, money or specified government obligations (or depositary receipts therefor) that through the scheduled payment of principal and interest in accordance with their terms will provide, without reinvestment, money in an amount sufficient to pay all of the principal of, and any premium and interest on, the senior notes on the dates such payments are due in accordance with the terms of the senior notes. In addition, the following conditions must be satisfied:

no Event of Default or event with which the giving of notice or lapse of time, or both, would become an Event of Default under the Indenture shall have occurred with respect to the senior notes and be continuing on the date of such deposit;

no Event of Default or any event described in clause (7) under "Events of Default" above shall have occurred and be continuing at any time on or prior to the 124th calendar day following the date of deposit;

in the event of defeasance described in clause (1) above, Macy's Holdings shall have delivered to the Trustee an opinion of outside counsel stating that (a) it has received from, or there has been published by, the United States Internal Revenue Service a ruling or (b) there has been a change in applicable federal income tax law, in either case to the effect that, among other things, the holders of the outstanding senior notes will not recognize gain or loss for United States federal income tax purposes as a result of such deposit, defeasance and discharge and will be subject to United States federal income tax on the same amount, in the same manner, and at the same times as if such deposit, defeasance and discharge had not occurred;

in the event of any defeasance in clause (2) above, Macy's Holdings shall have delivered to the Trustee an opinion of outside counsel to the effect that, among other things, the holders of the outstanding senior notes will not recognize gain or loss for United States federal income tax purposes as a result of such deposit or defeasance and will be subject to United States federal income tax on the same amount, in the same manner, and at the same times as if such deposit or defeasance had not occurred;

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Macy's Holdings shall have delivered to the Trustee a certificate from a nationally recognized firm of independent accountants expressing their opinion that the payments of principal and interest when due on the deposited government obligations without reinvestment plus any deposited money without investment will provide the cash at such times and in such amounts as will be sufficient to pay the principal of and any premium and interest when due on the senior notes or on any earlier date or dates on which the senior notes will be subject to redemption at the option of the holder;

such defeasance will not cause the Trustee to have a conflicting interest within the meaning of the Trust Indenture Act of 1939, as amended (the "Trust Indenture Act") (assuming all senior notes are in default within the meaning of the Trust Indenture Act);

Macy's Holdings shall have delivered to the Trustee an officer's certificate and an opinion of counsel, each stating that all conditions precedent with respect to such defeasance have been complied with;

such defeasance will not result in the trust arising from such deposit constituting an investment company within the meaning of the Investment Company Act of 1940, as amended (the "Investment Company Act"), unless such trust will be qualified under the Investment Company Act or will be exempt from regulation thereunder; and

there shall have been delivered to the Trustee the certificate of a responsible officer of Macy's Holdings certifying, on behalf of Macy's Holdings, to the effect that such defeasance shall not result in a breach or violation of, or constitute a default under, any agreement to which Macy's Holdings is a party or violate any law to which Macy's Holdings is subject.

If Macy's Holdings fails to comply with its remaining obligations under the Indenture after a defeasance with respect to the senior notes as described under clause (2) above and the senior notes are declared due and payable because of the occurrence of any undefeased Event of Default, the amount of money and government obligations on deposit with the Trustee may be insufficient to pay amounts due on the senior notes at the time of the acceleration resulting from such Event of Default. If such a failure occurs, Macy's Holdings will remain liable in respect of such payments.

Certain Defined Terms

Capitalized terms used but not defined herein have the meanings given to such terms in the Indenture. In addition, for purposes of the Indenture, the following definitions apply:

Bank Facilities means the Credit Agreement, dated as of May 10, 2013, among Macy's, Inc., Macy's Holdings, the lenders party thereto, JPMorgan Chase Bank, N.A., as administrative agent and paying agent, and Bank of America, N.A., as administrative agent, as the same may be amended, supplemented or otherwise modified from time to time.

Cash Equivalent means:

(1) obligations issued or unconditionally guaranteed as to principal and interest by the United States of America or by any agency or authority controlled or supervised by and acting as an instrumentality of the United States of America;

(2) obligations (including, but not limited to, demand or time deposits, bankers' acceptances and certificates of deposit) issued by a depository institution or trust company or a wholly owned Subsidiary or branch office of any depository institution or trust company, provided that (a) such depository institution or trust company has, at the time of Macy's Holdings' or any Restricted Subsidiary's Investment therein or contractual commitment providing for such Investment, capital,

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surplus, or undivided profits (as of the date of such institution's most recently published financial statements) in excess of \$100.0 million and (b) the commercial paper of such depository institution or trust company, at the time of Macy's Holdings' or any Restricted Subsidiary's Investment therein or contractual commitment providing for such Investment, is rated at least A1 by S&P, P-1 by Moody's or F1 by Fitch;

(3) debt obligations (including, but not limited to, commercial paper and medium term notes) issued or unconditionally guaranteed as to principal and interest by any corporation, state or municipal government or agency or instrumentality thereof, or foreign sovereignty, if the commercial paper of such corporation, state or municipal government, or foreign sovereignty, at the time of Macy's Holdings' or any Restricted Subsidiary's Investment therein or contractual commitment providing for such Investment, is rated at least A1 by S&P, P-1 by Moody's or F1 by Fitch;

(4) repurchase obligations with a term of not more than seven days for underlying securities of the type described above entered into with a depository institution or trust company meeting the qualifications described in clause (2) above; and

(5) Investments in money market or mutual funds that invest predominantly in Cash Equivalents of the type described in clauses (1), (2), (3) and (4) above; provided, however, that, in the case of the clauses (1) through (3) above, each such Investment has a maturity of one year or less from the date of acquisition thereof.

Consolidated Net Tangible Assets means total assets (less depreciation and valuation reserves and other reserves and items deductible from gross book value of specific asset accounts under GAAP) after deducting therefrom (1) all current liabilities and (2) all goodwill, trade names, trademarks, patents, unamortized debt discount, organization expenses and other like intangibles, all as set forth on the most recent balance sheet of Macy's Holdings and its consolidated Subsidiaries and computed in accordance with GAAP.

Existing Indebtedness means all Indebtedness under or evidenced by:

the senior notes;

Macy's Holdings' 7.875% Senior notes due 2015;

Macy's Holdings' 6.375% Senior notes due 2037;

Macy's Holdings' 5.90% Senior notes due 2016;

Macy's Holdings' 5.75% Senior notes due 2014;

Macy's Holdings' 6.9% Senior debentures due 2029;

Macy's Holdings' 6.7% Senior debentures due 2034;

Macy's Holdings' 7.45% Senior debentures due 2017;

Macy's Holdings' 6.65% Senior debentures due 2024;

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Macy's Holdings 7.0% Senior debentures due 2028;

Macy's Holdings 8.75% Senior debentures due 2029;

Macy's Holdings 6.9% Senior debentures due 2032;

Macy's Holdings 8.5% Senior debentures due 2019;

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Macy's Holdings 6.7% Senior debentures due 2028;

Macy's Holdings 7.875% Senior debentures due 2030;

Macy's Holdings 7.875% Senior debentures due 2036;

Macy's Holdings 6.79% Senior debentures due 2027;

Macy's Holdings 8.125% Senior debentures due 2035;

Macy's Holdings 7.45% Senior debentures due 2016;

Macy's Holdings 7.50% Senior debentures due 2015;

Macy's Holdings 10.25% Senior debentures due 2021;

Macy's Holdings 7.6% Senior debentures due 2025;

Macy's Holdings 9.5% amortizing debentures due 2021;

Macy's Holdings 9.75% amortizing debentures due 2021;

Macy's Holdings 3.875% Senior notes due 2022;

Macy's Holdings 5.125% Senior notes due 2042;

Macy's Holdings 2.875% Senior notes due 2023;

Macy's Holdings 4.3% Senior notes due 2043;

capital lease obligations of Macy's Holdings and its Restricted Subsidiaries existing on the date of issuance of the senior notes; and

the other secured Indebtedness of Macy's Holdings or secured or unsecured Indebtedness of its Restricted Subsidiaries existing on the date of issuance of the senior notes.

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Indebtedness means, as applied to any Person, without duplication:

- (1) all obligations of such Person for borrowed money;
- (2) all obligations of such Person for the deferred purchase price of property or services (other than property and services purchased, and expense accruals and deferred compensation items arising, in the ordinary course of business);
- (3) all obligations of such Person evidenced by notes, bonds, debentures, mandatorily redeemable preferred stock or other similar instruments (other than performance, surety and appeals bonds arising in the ordinary course of business);
- (4) all payment obligations created or arising under any conditional sale, deferred price or other title retention agreement with respect to property acquired by such Person (unless the rights and remedies of the seller or lender under such agreement in the event of default are limited to repossession or sale of such property);
- (5) any capital lease obligation of such Person;

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(6) all reimbursement, payment or similar obligations, contingent or otherwise, of such Person under acceptance, letter of credit or similar facilities (other than letters of credit in support of trade obligations or incurred in connection with public liability insurance, workers compensation, unemployment insurance, old-age pensions and other social security benefits other than in respect of employee benefit plans subject to ERISA);

(7) all obligations of such Person, contingent or otherwise, under any guarantee by such Person of the obligations of another Person of the type referred to in clauses (1) through (6) above; and

(8) all obligations referred to in clauses (1) through (6) above secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any mortgage or security interest in property (including without limitation accounts, contract rights and general intangibles) owned by such Person and as to which such Person has not assumed or become liable for the payment of such obligations other than to the extent of the property subject to such mortgage or security interest;

except that Indebtedness of the type referred to in clauses (7) and (8) above will be included within the definition of Indebtedness only to the extent of the least of (a) the amount of the underlying Indebtedness referred to in the applicable clause (1) through (6) above; (b) in the case of clause (7), the limit on recoveries, if any, from such Person under obligations of the type referred to in clause (7) above; and (c) in the case of clause (8), the aggregate value (as determined in good faith by Macy's Holdings Board of Directors) of the security for such Indebtedness.

Investment means, with respect to any Person, any direct or indirect loan or other extension of credit or capital contribution to (by means of any transfer of cash or other property to others or any payment for property or services for the account or use of others), or any purchase or acquisition by such Person of any capital stock, bonds, notes, debentures or other securities or evidences of Indebtedness issued by any other Person. The amount of any Investment shall be the original cost thereof, plus the cost of all additions thereto, without any adjustments for increases or decreases in value, write-ups, write-downs or write-offs with respect to such Investment.

Permitted Liens means:

(1) liens (other than liens on inventory) securing:

(a) Existing Indebtedness;

(b) Indebtedness under the Bank Facilities in an aggregate principal amount at any one time not to exceed \$2,800.0 million, less (1) principal payments actually made by Macy's Holdings on any term loan facility under such Bank Facilities (other than principal payments made in connection with or pursuant to a refinancing of the Bank Facilities in compliance with clause (1)(i) below) and (2) any amounts by which any revolving credit facility commitments under the Bank Facilities are permanently reduced (other than permanent reductions made in connection with or pursuant to a refinancing of the Bank Facilities in compliance with clause (1)(i) below), except that under no circumstances will the total allowable indebtedness under this clause (1)(b) be less than \$1,790 million (subject to increase from and after the date of issuance of the senior notes at a rate, compounded annually, equal to 3% per annum) if incurred for the purpose of providing Macy's Holdings and its Subsidiaries with working capital, including without limitation bankers' acceptances, letters of credit and similar assurances of payment, whether as part of the Bank Facilities or otherwise;

(c) Indebtedness existing as of the date of issuance of the senior notes of any Subsidiary of Macy's Holdings engaged primarily in the business of owning or leasing real property;

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- (d) Indebtedness incurred for the purpose of financing store construction and remodeling or other capital expenditures;
- (e) Indebtedness in respect of the deferred purchase price of property or arising under any conditional sale or other title retention agreement;
- (f) Indebtedness of a Person acquired by Macy's Holdings or a Subsidiary of Macy's Holdings at the time of such acquisition;
- (g) to the extent deemed to be Indebtedness, obligations under swap agreements, cap agreements, collar agreements, insurance agreements or any other agreement or arrangement, in each case designed to provide protection against fluctuations in interest rates, the cost of currency or the cost of goods (other than inventory);
- (h) other Indebtedness in outstanding amounts not to exceed, in the aggregate, the greater of \$750.0 million and 12.5% of Consolidated Net Tangible Assets of Macy's Holdings and the Restricted Subsidiaries at any particular time; and
- (i) Indebtedness incurred in connection with any extension, renewal, refinancing, replacement or refunding (including successive extensions, renewals, refinancings, replacements or refundings), in whole or in part, of any Indebtedness of Macy's Holdings or the Restricted Subsidiaries; provided that the principal amount of the Indebtedness so incurred does not exceed the sum of the principal amount of the Indebtedness so extended, renewed, refinanced, replaced or refunded, plus all interest accrued thereon and all related fees and expenses (including any payments made in connection with procuring any required lender or similar consents);
- (2) liens incurred and pledges and deposits made in the ordinary course of business in connection with liability insurance, workers compensation, unemployment insurance, old-age pensions and other social security benefits other than in respect of employee benefit plans subject to ERISA;
- (3) liens securing performance, surety and appeal bonds and other obligations of like nature incurred in the ordinary course of business;
- (4) liens on goods and documents securing trade letters of credit;
- (5) liens imposed by law, such as carriers, warehousemen, mechanics, materialmen and vendors liens, incurred in the ordinary course of business and securing obligations which are not yet due or which are being contested in good faith by appropriate proceedings;
- (6) liens securing the payment of taxes, assessments and governmental charges or levies (a) either (1) not delinquent or (2) being contested in good faith by appropriate legal or administrative proceedings and (b) as to which adequate reserves shall have been established on the books of the relevant Person in conformity with GAAP;
- (7) zoning restrictions, easements, rights of way, reciprocal easement agreements, operating agreements, covenants, conditions or restrictions on the use of any parcel of property that are routinely granted in real estate transactions or do not interfere in any material respect with the ordinary conduct of the business of Macy's Holdings and its Subsidiaries or the value of such property for the purpose of such business;
- (8) liens on property existing at the time such property is acquired;

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(9) purchase money liens upon or in any property acquired or held in the ordinary course of business to secure Indebtedness incurred solely for the purpose of financing the acquisition of such property;

(10) liens on the assets of any Subsidiary of Macy's Holdings at the time such Subsidiary is acquired;

(11) liens with respect to obligations in outstanding amounts not to exceed \$100.0 million at any particular time and that (a) are not incurred in connection with the borrowing of money or obtaining advances or credit (other than trade credit in the ordinary course of business) and (b) do not in the aggregate interfere in any material respect with the ordinary conduct of the business of Macy's Holdings and its Subsidiaries; and

(12) without limiting the ability of Macy's Holdings or any Restricted Subsidiary to create, incur, assume or suffer to exist any lien otherwise permitted under any of the foregoing clauses, any extension, renewal or replacement, in whole or in part, of any lien described in the foregoing clauses; provided that any such extension, renewal or replacement lien is limited to the property or assets covered by the lien extended, renewed or replaced or substitute property or assets, the value of which is determined by the Board of Directors of Macy's Holdings to be not materially greater than the value of the property or assets for which the substitute property or assets are substituted.

Person means any individual, partnership, corporation, limited liability company, joint stock company, business trust, trust, unincorporated association, joint venture or other entity, or a government or political subdivision or agency thereof.

Restricted Subsidiary means any Subsidiary of Macy's Holdings other than an Unrestricted Subsidiary.

Senior Indebtedness means any Indebtedness of Macy's Holdings or its Subsidiaries other than Subordinated Indebtedness.

Significant Subsidiary means any Subsidiary that accounts for (1) 10.0% or more of the total consolidated assets of any Person and its Subsidiaries as of any date of determination or (2) 10.0% or more of the total consolidated revenues of any Person and its Subsidiaries for the most recently concluded fiscal quarter.

Subordinated Indebtedness means any Indebtedness of Macy's Holdings which is expressly subordinated in right of payment to the senior notes or any Indebtedness of Macy's, Inc. which is expressly subordinated in right of payment to the Guarantee.

Subsidiary means, as applied, with respect to any Person, any corporation, partnership or other business entity of which, in the case of a corporation, more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the board of directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation has or might have voting power upon the occurrence of any contingency), or, in the case of any partnership or other legal entity, more than 50% of the ordinary equity capital interests, is at the time directly or indirectly owned or controlled by such Person, by such Person and one or more of its other Subsidiaries or by one or more of such Person's other Subsidiaries.

Unrestricted Subsidiary means any entity designated as such (1) in the Fifth Supplemental Indenture (including Macy's Holdings' existing receivables finance Subsidiaries and Macy's Credit and Customer Services, Inc.) or (2) by Macy's Holdings' Board of Directors, provided that such entity is a special purpose entity formed for financing purposes.

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U.S. FEDERAL INCOME TAX CONSIDERATIONS

The following is a summary, subject to the limitations set forth herein, of the material U.S. federal income tax considerations relating to the purchase, ownership and disposition of the senior notes by initial investors. It is not a complete analysis of all the potential tax considerations relating to the senior notes. This summary is based upon the provisions of the Internal Revenue Code of 1986, as amended (the Code), Treasury Regulations promulgated under the Code, administrative rulings and pronouncements and judicial decisions, all as in effect on the date hereof. These authorities may be changed, perhaps with retroactive effect, and are subject to differing interpretations so as to result in U.S. federal income tax consequences different from those set forth below. Macy's Holdings has not sought any ruling from the Internal Revenue Service (the IRS) and Macy's Holdings cannot assure you that the IRS will agree with such statements.

Except as otherwise provided, this summary is limited to initial investors who purchase senior notes for cash at the initial issue price (i.e., the initial offering price to the public, excluding bond houses and brokers, at which price a substantial amount of the senior notes is sold) pursuant to this offering and who will hold the senior notes as capital assets (i.e., generally for investment purposes). This summary does not address the tax considerations arising under the laws of any foreign, state or local jurisdiction. In addition, this discussion does not address all tax considerations that may be applicable to holders particular circumstances or to holders that may be subject to special tax rules, such as, for example:

holders subject to the alternative minimum tax;

banks, insurance companies, and other financial institutions;

regulated investment companies;

real estate investment trusts;

tax-exempt organizations;

brokers and dealers in securities or commodities;

expatriates;

traders in securities that elect to use a mark-to-market method of accounting for their securities holdings;

U.S. Holders (as defined below) whose functional currency is not the U.S. dollar;

persons that will hold the senior notes as a position in a hedging transaction, straddle, conversion transaction or other risk reduction transaction;

persons deemed to sell the senior notes under the constructive sale provisions of the Code; or

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entities or arrangements treated as partnerships for U.S. federal income tax purposes or other pass-through entities, or investors in such entities.

If an entity or arrangement treated as a partnership for U.S. federal income tax purposes holds senior notes, the tax treatment of a partner in such partnership will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding senior notes, you should consult your tax advisor regarding the tax consequences of the purchase, ownership and disposition of the senior notes.

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This summary of U.S. federal income tax considerations is for general information only and is not tax advice for any particular investor. You are urged to consult your tax advisor with respect to the application of U.S. federal income tax laws to your particular situation, as well as any tax consequences arising under the U.S. federal estate or gift tax rules or under the laws of any state, local, foreign or other taxing jurisdiction or under any applicable tax treaty.

Consequences to U.S. Holders

The following discussion will generally apply to you if you are a U.S. Holder of the senior notes. You are a U.S. Holder if you are a beneficial owner of a senior note and you are, for U.S. federal income tax purposes:

an individual who is a citizen or resident of the United States;

a corporation (or other entity treated as a corporation for U.S. federal income tax purposes) created or organized in or under the laws of the United States, any state thereof, or the District of Columbia;

an estate the income of which is subject to U.S. federal income taxation regardless of its source; or

a trust that (1) is subject to the supervision of a court within the United States and the control of one or more United States persons (as defined in the Code) or (2) has a valid election in effect under applicable Treasury Regulations to be treated as a United States person.

Payments of Interest

Stated interest on a senior note will generally be taxable to a U.S. Holder as ordinary income at the time it is paid or accrued in accordance with the U.S. Holder's regular method of accounting for U.S. federal income tax purposes.

In certain circumstances (see Description of Notes Change of Control), Macy's Holdings may be obligated to pay amounts in excess of stated interest or principal on the senior notes. The obligation to make these payments may implicate the provisions of the Treasury Regulations relating to contingent payment debt instruments. Treasury Regulations provide special rules for contingent payment debt instruments which, if applicable, could cause the timing, amount and character of a holder's income, gain or loss with respect to the senior notes to be different from the consequences discussed herein. Although the issue is not free from doubt, Macy's Holdings believes that the possibility of the payment of such additional amounts does not result in the senior notes being treated as contingent payment debt instruments under the applicable Treasury Regulations. This position is not binding on the IRS, which may take a contrary position and treat the senior notes as contingent payment debt instruments. If the senior notes were deemed to be contingent payment debt instruments, a U.S. Holder would generally be required to treat any gain recognized on the sale or other disposition of the senior notes as ordinary income rather than as capital gain. Furthermore, a U.S. Holder would be required to accrue interest income on a constant yield basis at an assumed yield determined at the time of issuance of the senior notes, with adjustments to such accruals when any payments are made that differ from the payments calculated based on the assumed yield. The remainder of this discussion assumes that the senior notes are not treated as contingent payment debt instruments. U.S. Holders should consult their own tax advisors about the treatment of additional payments that might be made in respect of the senior notes. U.S. Holders should consult their own tax advisors about the treatment of additional payments that might be made in respect of the senior notes.

Sale or Other Taxable Disposition of Senior Notes

Upon the sale, exchange, redemption or other taxable disposition of a senior note, a U.S. Holder generally will recognize taxable gain or loss equal to the difference between the amount realized on such

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disposition (except to the extent any amount realized is attributable to accrued but unpaid interest, which if not previously included in income, will be treated as interest as described in *Payments of Interest* above) and the holder's adjusted tax basis in the senior note. A U.S. Holder's adjusted tax basis in a senior note generally will equal the cost of the senior note to such holder, decreased by any payments of principal received. Gain or loss recognized on the disposition of a senior note generally will be capital gain or loss, and will be long-term capital gain or loss if, at the time of such disposition, the U.S. Holder's holding period for the senior note is more than one year. Long-term capital gains of individuals and other non-corporate taxpayers are generally eligible for reduced rates of taxation. The deductibility of capital losses is subject to certain limitations.

Medicare Tax

For taxable years beginning after December 31, 2012, certain U.S. Holders who are individuals, estates or trusts and whose income exceeds certain thresholds will be subject to a 3.8% Medicare tax on the lesser of (i) the U.S. Holder's net investment income for the relevant taxable year (undistributed net investment income in the case of an estate or trust) and (ii) the excess of the U.S. Holder's modified adjusted gross income for the taxable year over a certain threshold (which in the case of individuals will be between \$125,000 and \$250,000, depending on the individual's circumstances). For these purposes, net investment income will generally include interest on and capital gains from the sale or other disposition of the senior notes, unless such interest or gains are derived in the ordinary course of the conduct of a trade or business (other than a trade or business that consists of certain passive or trading activities). If you are a U.S. Holder who is an individual, estate or trust, you are urged to consult your tax advisor regarding the applicability of the Medicare tax to your income and gains in respect of the senior notes.

Information Reporting and Backup Withholding

In general, information reporting requirements will apply to payments of interest on the senior notes and the proceeds of the sale and other taxable disposition (including a retirement or redemption) of senior notes unless the U.S. Holder is an exempt recipient. A backup withholding tax (currently at a rate of 28%) may apply to such payments if the U.S. Holder fails to provide its taxpayer identification number or certification of exempt status or has been notified by the IRS that payments to the U.S. Holder are subject to backup withholding. Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules will generally be allowed as a credit against a U.S. Holder's U.S. federal income tax liability and may entitle a U.S. Holder to a refund, provided that the required information is timely furnished to the IRS. You are urged to consult your own tax advisor regarding the application of backup withholding rules in your particular situation, the availability of an exemption from backup withholding and the procedure for obtaining such an exemption, if applicable.

Consequences to Non-U.S. Holders

The following discussion will generally apply to you if you are a Non-U.S. Holder of senior notes. The term *Non-U.S. Holder* means a beneficial owner of a senior note that is, for U.S. federal income tax purposes, a nonresident alien individual or a corporation, estate or trust and that is not a U.S. Holder.

Payments of Interest

A Non-U.S. Holder will not be subject to U.S. federal withholding tax with respect to any payment of interest on its senior notes that is not effectively connected with the conduct of a U.S. trade or business provided that:

the Non-U.S. Holder does not actually or constructively (under applicable attribution rules) own 10% or more of the total combined voting power of Macy's Holdings voting stock, within the meaning of Section 871(h)(3) of the Code;

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the Non-U.S. Holder is not a bank that receives such interest in a transaction described in Section 881(c)(3)(A) of the Code;

the Non-U.S. Holder is not a controlled foreign corporation that is related to Macy's Holdings directly or indirectly through stock ownership; and

(a) the Non-U.S. Holder provides its name and address, and certifies, under penalties of perjury, that it is not a United States person (which certification generally may be made on an IRS Form W-8BEN) or (b) a securities clearing organization, bank, or other financial institution that holds customers' securities in the ordinary course of its business holds the senior note on a Non-U.S. Holder's behalf and certifies, under penalties of perjury, either that it has received IRS Form W-8BEN (or similar withholding certificate) from the holder or from another qualifying financial institution intermediary or that it is permitted to establish and has established the holder's foreign status through other documentary evidence, and otherwise complies with applicable requirements. If the senior notes are held by or through certain foreign intermediaries or certain foreign partnerships, such foreign intermediaries or partnerships must also satisfy the certification requirements of applicable Treasury Regulations.

A Non-U.S. Holder that cannot satisfy the requirements described above will be subject to a 30% U.S. federal withholding tax with respect to payments of interest on the senior notes, unless the Non-U.S. Holder provides Macy's Holdings (or its agent) with a properly executed (1) IRS Form W-8BEN claiming an exemption from or reduction in withholding under an applicable tax treaty or (2) IRS Form W-8ECI stating that interest paid on the senior note is not subject to withholding tax because it is effectively connected with the holder's conduct of a trade or business in the United States.

If a Non-U.S. Holder is engaged in a trade or business in the United States and interest on a senior note is effectively connected with the conduct of that trade or business, the Non-U.S. Holder will instead be required to pay U.S. federal income tax on that interest on a net income basis in the same manner as if the Non-U.S. Holder were a U.S. Holder. If a Non-U.S. Holder is eligible for the benefits of an income tax treaty between the United States and the Non-U.S. Holder's country of residence, any effectively connected income generally will be subject to U.S. federal income tax only if it is also attributable to a permanent establishment or fixed base maintained by the Non-U.S. Holder in the United States. In addition, if a Non-U.S. Holder is a foreign corporation, it may be subject to branch profits tax equal to 30% (or lower applicable treaty rate) of its earnings and profits for the taxable year, subject to adjustments, that are effectively connected with its conduct of a trade or business in the United States. For this purpose, interest on the senior notes which is effectively connected with the conduct of a trade or business in the United States by a Non-U.S. Holder would be included in earnings and profits.

Sale or Other Taxable Disposition of Senior Notes

Any gain recognized upon the sale, exchange, redemption or other taxable disposition of a senior note (except with respect to accrued and unpaid interest, which would be treated as interest as described in *Payments of Interest* above) will not be subject to U.S. federal withholding tax. Such gain also generally will not be subject to U.S. federal income tax unless:

that gain is effectively connected with a Non-U.S. Holder's conduct of a trade or business in the United States (and, if an income tax treaty applies, is attributable to a U.S. permanent establishment); or

the Non-U.S. Holder is an individual who is present in the United States for 183 days or more in the taxable year of the disposition, and certain other conditions are met.

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A Non-U.S. Holder described in the first bullet point above will generally be required to pay U.S. federal income tax on the net gain derived from the sale in the same manner as if the Non-U.S. Holder were a U.S. Holder. If a Non-U.S. Holder is eligible for the benefits of an income tax treaty between the United States and the Non-U.S. Holder's country of residence, any effectively connected gain generally will be subject to U.S. federal income tax only if it is also attributable to a permanent establishment or fixed base maintained by the Non-U.S. Holder in the United States. In addition, if such Non-U.S. Holder is a foreign corporation, it may also be required to pay branch profits tax at a 30% rate or a lower rate if so specified by an applicable tax treaty.

A Non-U.S. Holder described in the second bullet point will generally be subject to U.S. federal income tax at a rate of 30% on the amount by which its capital gains allocable to U.S. sources, including gain from such disposition, exceed any capital losses allocable to U.S. sources, except as otherwise required by an applicable income tax treaty.

Medicare Tax

As discussed in more detail under *Consequences to U.S. Holders Medicare Tax*, a 3.8% Medicare tax will apply in addition to regular income tax, to certain net investment income for taxable years beginning after December 31, 2012. The Medicare tax generally applies only to certain U.S. persons with income in excess of certain thresholds. However, the IRS has indicated in proposed Treasury Regulations that the 3.8% Medicare tax may be applicable to Non-U.S. Holders that are estates or trusts and have one or more U.S. beneficiaries. Non-U.S. Holders are urged to consult their own tax advisors about the possible application of the Medicare tax to any interest on, or gain realized upon a sale or other disposition of the notes.

Information Reporting and Backup Withholding

In general, information returns will be filed with the IRS in connection with payments of interest on the senior notes and proceeds from the sale or other taxable disposition (including a retirement or redemption) of the senior notes. Copies of the information returns reporting such payments and any withholding may also be made available to the tax authorities in the country in which the Non-U.S. Holder resides under the provisions of an applicable tax treaty. Backup withholding (currently at a 28% rate) may apply to certain payments of principal and interest on the senior notes to Non-U.S. Holders, as well as to the proceeds of certain sales of senior notes made through brokers, unless the Non-U.S. Holder has made appropriate certifications as to its foreign status, or has otherwise established an exemption. The certification of foreign status described above under *Payments of Interest* is generally effective to establish an exemption from backup withholding. Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules will generally be allowed as a credit against a Non-U.S. Holder's U.S. federal income tax liability and may entitle a Non-U.S. Holder to a refund, provided that the required information is timely furnished to the IRS. You are urged to consult your own tax advisor regarding the application of backup withholding rules in your particular situation, the availability of an exemption from backup withholding and the procedure for obtaining such an exemption, if applicable.

FATCA

The Foreign Account Tax Compliance Act provisions of the Hiring Incentives to Restore Employment Act and Treasury Regulations thereunder, commonly referred to as *FATCA*, when applicable, will impose a U.S. federal withholding tax of 30% on certain types of payments, including payments of U.S.-source interest and gross proceeds from the sale of certain securities producing such U.S. source interest made to (i) foreign financial institutions unless they agree to collect and disclose to the IRS information regarding their direct and indirect U.S. account holders, and (ii) certain non-financial foreign entities unless they certify certain information regarding their direct and indirect U.S. owners.

Under recently issued final Treasury Regulations, as modified by IRS Notice 2013-43, the withholding obligations described above generally will apply to payments of U.S. source interest on debt instruments made on or after July 1, 2014, and to payments of gross proceeds from a sale or other disposition of debt instruments on or

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after January 1, 2017. However, the recently issued final Treasury Regulations, as modified by IRS Notice 2013-43, also provide that the FATCA withholding obligations described above do not apply to debt instruments issued before, and which are not the subject of a significant modification (in such a way that they are considered to be re-issued for U.S. federal income tax purposes) on or after, July 1, 2014. Accordingly, FATCA withholding is not expected to be required on the senior notes. You are urged to consult your own tax advisors regarding FATCA and the application of these requirements to your investment in the senior notes.

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Under the terms and subject to the conditions contained in an underwriting agreement dated September 3, 2013, Macy's Holdings has agreed to sell to the underwriters named below, for whom Credit Suisse Securities (USA) LLC, J.P. Morgan Securities LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated are acting as representatives, and the underwriters have agreed to buy, the principal amount of the senior notes set forth opposite the underwriter's name:

Underwriter	Principal Amount of Senior Notes
Credit Suisse Securities (USA) LLC	\$ 100,000,000
J.P. Morgan Securities LLC	100,000,000
Merrill Lynch, Pierce, Fenner & Smith Incorporated	100,000,000
U.S. Bancorp Investments, Inc.	24,000,000
Wells Fargo Securities, LLC	24,000,000
Goldman, Sachs & Co.	10,000,000
Fifth Third Securities, Inc.	10,000,000
PNC Capital Markets LLC	10,000,000
BNY Mellon Capital Markets, LLC	4,000,000
Citigroup Global Markets Inc.	4,000,000
Mitsubishi UFJ Securities (USA), Inc.	4,000,000
Standard Chartered Bank	4,000,000
Loop Capital Markets LLC	2,000,000
Samuel A. Ramirez & Company, Inc.	2,000,000
The Williams Capital Group, L.P.	2,000,000
Total	\$ 400,000,000

The underwriting agreement provides that the underwriters are obligated to purchase all of the senior notes if any are purchased. The underwriting agreement also provides that, if an underwriter defaults, the purchase commitments of non-defaulting underwriters may be increased or the offering of senior notes may be terminated. The offering of the senior notes by the underwriters is subject to receipt and acceptance and subject to the underwriters' right to reject any order in whole or in part.

The underwriters propose to offer the senior notes initially at the public offering price on the cover page of this prospectus supplement and to selling group members at that price less a selling concession of 0.40% of the principal amount per senior note. The underwriters may allow, and selling group members may reallow, a discount of 0.25% of the principal amount per senior note on sales to other broker/dealers. After the initial public offering, the representatives may change the public offering price and other selling terms.

The following table summarizes the compensation we will pay.

	Per Senior Note	Total
Underwriting Discounts and Commissions paid by us	0.650%	\$ 2,600,000

We estimate that our out-of-pocket expenses for this offering will be approximately \$750,000.

Macy's Holdings has agreed to indemnify the several underwriters against liabilities under the Securities Act or to contribute to payments which the underwriters may be required to make in that respect.

The senior notes are a new issue of securities with no established trading market. The senior notes will not be listed on any securities exchange or on any automated dealer quotation system. The representatives may make a secondary market for the senior notes. However, they are not obligated to do so and may discontinue making a secondary market for the senior notes at any time without notice. No assurance can be given as

to how

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liquid the trading market for the senior notes will be or that an active public market for the senior notes will develop. If an active public trading market for the senior notes does not develop, the market price and liquidity of the senior notes may be adversely affected.

In connection with the offering, the representatives may engage in stabilizing transactions, syndicate covering transactions and penalty bids in accordance with Regulation M under the Exchange Act.

Stabilizing transactions permit bids to purchase the underlying security so long as the stabilizing bids do not exceed a specified maximum.

Syndicate covering transactions involve purchases of the senior notes in the open market after the distribution has been completed in order to cover syndicate short positions. A short position is more likely to be created if the representatives are concerned that there may be downward pressure on the price of the senior notes in the open market after pricing that could adversely affect investors who purchase in the offering.

Penalty bids permit the representatives to reclaim a selling concession from a syndicate member when the senior notes originally sold by the syndicate member are purchased in a stabilizing transaction or a syndicate covering transaction to cover syndicate short positions.

These stabilizing transactions, syndicate covering transactions and penalty bids may have the effect of raising or maintaining the market price of the senior notes or preventing or retarding a decline in the market price of the senior notes. As a result the price of the senior notes may be higher than the price that might otherwise exist in the open market. These transactions, if commenced, may be discontinued at any time.

The senior notes are being offered for sale in the United States and in jurisdictions outside the United States, subject to applicable law.

In relation to each Member State of the European Economic Area that has implemented the Prospectus Directive (as defined below) (each, a Relevant Member State), each underwriter has represented and agreed that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the Relevant Implementation Date) it has not made and will not make an offer of the senior notes which are the subject of the offering contemplated by this prospectus supplement to the public in that Relevant Member State other than:

- (1) at any time to any legal entity which is a qualified investor as defined in the Prospectus Directive;
- (2) at any time to fewer than 100 or, if the Relevant Member State has implemented the relevant provision of the 2010 PD Amending Directive, as defined below, 150 legal persons (other than qualified investors as defined in the Prospectus Directive) subject to obtaining the prior consent of the underwriters; or
- (3) at any time in any other circumstances falling within Article 3(2) of the Prospectus Directive;

provided that no such offer of senior notes referred to in (1) to (3) above shall require the publication by Macy's Holdings or any underwriter of a prospectus pursuant to Article 3 of the Prospectus Directive, or supplement to a prospectus pursuant to Article 16 of the Prospectus Directive.

For the purposes of this provision, the expression an offer to the public in relation to any senior notes in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the senior notes to be offered so as to enable an investor to decide to purchase or subscribe to the senior notes, as the same may be varied in that Relevant Member State by any measure implementing the Prospectus Directive in that Relevant Member State, and the expression Prospectus Directive means Directive 2003/71/EC (and the amendments thereto, including the 2010 PD Amending Directive, to the

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extent implemented in the Relevant Member State), and includes any relevant implementing measure in the Relevant Member State and the expression "2010 PD Amending Directive" means Directive 2010/73/EU.

This document is for distribution only to persons who (i) have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended, the "Financial Promotion Order"), (ii) are persons falling within Article 49(2)(a) to (d) ("high net worth companies, unincorporated associations etc.") of the Financial Promotion Order, (iii) are outside the United Kingdom, or (iv) are persons to whom an invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the "FSMA")) in connection with the issue or sale of any securities may otherwise lawfully be communicated or caused to be communicated (all such persons together being referred to as "relevant persons"). This document is directed only at relevant persons and must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this document relates is available only to relevant persons and will be engaged in only with relevant persons.

Each underwriter has represented and agreed that:

(1) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue or sale of the senior notes in circumstances in which Section 21(1) of the FSMA does not apply to Macy's Holdings; and

(2) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the senior notes in, from or otherwise involving the United Kingdom.

The senior notes may not be offered or sold by means of any document other than (1) in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), or (2) to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap.571, Laws of Hong Kong) and any rules made thereunder, or (3) in other circumstances which do not result in the document being a "prospectus" within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), and no advertisement, invitation or document relating to the senior notes may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to senior notes which are or are intended to be disposed of only to persons outside Hong Kong or only to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

This prospectus supplement has not been and will not be circulated or distributed in the People's Republic of China (the "PRC"), and senior notes may not be offered or sold, and will not be offered or sold to any person for re-offering or resale, directly or indirectly, to any resident of the PRC except pursuant to applicable laws and regulations of the PRC. For the purpose of this paragraph only, the PRC does not include Taiwan and the special administrative regions of Hong Kong and Macau.

The securities have not been and will not be registered under the Securities and Exchange Law of Japan (the "Securities and Exchange Law") and each underwriter has agreed that it will not offer or sell any securities, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organized under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to a resident of Japan, except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Securities and Exchange Law and any other applicable laws, regulations and ministerial guidelines of Japan.

This prospectus has not been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, this prospectus and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the senior notes may not be circulated or distributed, nor may the

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senior notes be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (1) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the "SFA"), (2) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA, or (3) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the senior notes are subscribed or purchased under Section 275 by a relevant person which is: (1) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (2) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries rights and interest in that trust shall not be transferable for six months after that corporation or that trust has acquired the senior notes under Section 275 except: (a) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA; (b) where no consideration is given for the transfer; or (c) by operation of law.

The underwriters and their respective affiliates are full service institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, investment research, principal investment, hedging, financing and brokerage activities. The underwriters and their respective affiliates have provided, and may in the future provide, financial advisory, investment banking and/or commercial banking services to Macy's, Inc., Macy's Holdings and their subsidiaries from time to time. The underwriters and their respective affiliates have received, and will in the future receive, customary fees in connection with providing these services. In particular, affiliates of Credit Suisse Securities (USA) LLC, J.P. Morgan Securities LLC, Merrill Lynch, Pierce, Fenner & Smith Incorporated, Goldman, Sachs & Co., U.S. Bancorp Investments, Inc., Wells Fargo Securities, LLC and certain other underwriters are parties to and lenders under our existing revolving credit facility and affiliates of Credit Suisse Securities (USA) LLC are parties to our existing letter of credit facility. Our existing revolving credit facility and our existing letter of credit facility were negotiated on an arms length basis and contain customary terms pursuant to which the lenders receive customary fees.

In addition, in the ordinary course of their business activities, the underwriters and their affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers. Such investments and securities activities may involve securities and/or instruments of ours or our affiliates. Certain of the underwriters or their affiliates that have a lending relationship with us routinely hedge, and certain others of those underwriters may hedge, their credit exposure to us consistent with their customary risk management policies. Typically, such underwriters and their affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions in our securities, including potentially the senior notes offered hereby. Any such credit default swaps or short positions could adversely affect future trading prices of the senior notes offered hereby. The underwriters and their affiliates may also make investment recommendations and/or publish or express independent research views in respect of such securities or financial instruments and may hold, or recommend to clients that they acquire, long and/or short positions in such securities and instruments.

Standard Chartered Bank will not effect any offers or sales of any senior notes in the United States unless it is through one or more U.S. registered broker-dealers as permitted by the regulations of FINRA.

EXPERTS

The consolidated financial statements and schedules of Macy's, Inc. as of February 2, 2013 and January 28, 2012, and for each of the fiscal years in the three-year period ended February 2, 2013, and

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management's assessment of the effectiveness of internal control over financial reporting as of February 2, 2013 have been incorporated by reference in the accompanying prospectus in reliance upon the reports of KPMG LLP, independent registered public accounting firm, incorporated by reference in the accompanying prospectus, and upon the authority of said firm as experts in accounting and auditing.

LEGAL MATTERS

The validity of the senior notes and guarantees offered hereby will be passed upon for Macy's Holdings and Macy's, Inc. by Jones Day, Dallas, Texas. Certain legal matters will be passed upon for the underwriters by Shearman & Sterling LLP, New York, New York.

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PROSPECTUS

MACY S, INC.

Common Stock

Preferred Stock

Depositary Shares

Warrants

Purchase Contracts

Units

Guarantees of Debt Securities

MACY S RETAIL HOLDINGS, INC.

Debt Securities

Warrants

Purchase Contracts

Units

Macy s, Inc., referred to as Macy s, and/or Macy s Retail Holdings, Inc., a wholly owned subsidiary of Macy s, referred to as Macy s Holdings, may offer from time to time to sell, in one or more series, any combination of the securities described in this prospectus. Such securities may be offered and sold by us in one or more offerings in amounts, at prices and on other terms to be determined at the time of the offering.

We may offer and sell these securities to or through one or more underwriters, dealers and agents, or directly to purchasers, on a continuous or delayed basis.

The principal executive offices of Macy s and Macy s Holdings are located at 7 West Seventh Street, Cincinnati, Ohio 45202, and the telephone number for each is (513) 579-7000.

This prospectus describes some of the general terms that may apply to these securities. The specific terms of any securities to be offered will be described in a supplement to this prospectus.

Neither the Securities and Exchange Commission nor any other regulatory body has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is December 7, 2012.

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The registration statement containing this prospectus, including the exhibits to the registration statement, provides additional information about us and the securities offered under this prospectus. The registration statement, including the exhibits and the documents incorporated herein by reference, can be read on the Securities and Exchange Commission website or at the Securities and Exchange Commission offices mentioned under the heading **Where You Can Find More Information.**

ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we filed with the Securities and Exchange Commission, or the SEC, using a shelf registration process. Under this shelf process, we may sell from time to time the securities described in this prospectus in one or more offerings in amounts, at prices and on other terms to be determined at the time of the offering.

This prospectus provides you with a general description of the securities. Each time we offer the securities, we will provide a prospectus supplement that will contain specific information about the terms of that offering. The prospectus supplement may also supplement, modify or supersede other information contained in this prospectus. You should read both this prospectus and any prospectus supplement together with the information incorporated by reference as described below under the heading **Incorporation by Reference**.

Because we are a well-known seasoned issuer, as defined in Rule 405 under the Securities Act of 1933 (the **Securities Act**) we may add to and offer additional securities including secondary securities, by filing a prospectus supplement or term sheet with the SEC at the time of the offer.

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You should rely only on the information provided in this prospectus and in any prospectus supplement, including the information incorporated by reference. We have not authorized anyone to provide you with different information. We are not offering the securities in any state where the offer is not permitted. You should not assume that the information in this prospectus, or any supplement to this prospectus, is accurate at any date other than the date indicated on the cover page of these documents.

Unless the context implies otherwise, references in this prospectus to *we*, *us* or *our* are references to either Macy's or Macy's Holdings or both.

WHERE YOU CAN FIND MORE INFORMATION

Macy's files annual, quarterly and current reports, proxy statements and other information with the SEC. Macy's SEC filings are available to the public from the SEC's website at www.sec.gov or from Macy's website at www.macysinc.com. You may also read and copy any document Macy's files at the SEC's public reference room in Washington, D.C., located at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Information about Macy's is also available at Macy's website at www.macysinc.com. However, the information on that website is not part of this prospectus.

INCORPORATION BY REFERENCE

The SEC allows us to incorporate by reference in this prospectus the information in the documents that Macy's files with it, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be a part of this prospectus. Any information that is part of this prospectus or any prospectus supplement that speaks as of a later date than any other information that is part of this prospectus or any prospectus supplement updates or supersedes such other information. We incorporate by reference in this prospectus the documents listed below and any future documents or portions thereof that Macy's files with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 (the *Exchange Act*) on or after the date of this prospectus until we sell all of the securities that may be offered by this prospectus.

Macy's Annual Report on Form 10-K for the fiscal year ended January 28, 2012;

Macy's Quarterly Reports on Form 10-Q for the fiscal quarters ended April 28, 2012, July 28, 2012 and October 27, 2012;

Macy's Current Reports on Form 8-K filed on January 31, 2012, March 26, 2012, May 21, 2012, October 29, 2012, November 20, 2012 and November 28, 2012; and

Description of Macy's common stock, par value \$0.01 per share, contained in Macy's Registration Statement on Form 8-A filed on December 12, 1994.

You may obtain, free of charge, a copy of any of these documents (other than exhibits to these documents unless the exhibits are specifically incorporated by reference into these documents or referred to in this prospectus) by writing or calling us at the following address and telephone number:

Macy's, Inc.

7 West Seventh Street

Cincinnati, Ohio 45202

Attention: Investor Relations

(513) 579-7028

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FORWARD-LOOKING STATEMENTS

Some of the statements made and information contained in this prospectus and the documents we incorporate by reference, excluding historical information, are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995, the Securities Act and the Exchange Act. Such statements are based upon the beliefs and assumptions of, and on information available to, the management of the Company at the time such statements are made. The following are or may constitute forward-looking statements: (i) statements preceded by, followed by or that include the words may, will, could, should, believe, expect, future, potential, anticipate, intend, plan, think, estimate, or negative or other variations thereof, and (ii) statements regarding matters that are not historical facts. Such forward-looking statements are subject to various risks and uncertainties, including risks and uncertainties relating to:

the possible invalidity of the underlying beliefs and assumptions;

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

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

conditions to, or changes in the timing of, proposed transactions and changes in expected synergies, cost savings and non-recurring charges;

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

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

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

currency, interest and exchange rates and other capital market, economic and geopolitical conditions;

severe weather, natural disasters and changes in weather patterns;

possible outbreak of an epidemic or pandemic disease;

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

the possible inability of Macy's manufacturers to deliver products in a timely manner or meet quality standards;

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Macy's reliance on foreign sources of production, including risks related to the disruption of imports by labor disputes, regional health pandemics, and regional political and economic conditions;

duties, taxes, and other charges and quotas on imports; and

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

This list of factors is not exhaustive, and new factors may emerge or changes to these factors may occur that would impact our business. Additional information regarding these and other factors may be contained in Macy's filings with the SEC, especially on Forms 10-K, 10-Q and 8-K. All such risk factors are difficult to predict, contain material uncertainties that may affect actual results and may be beyond our control. No forward-looking statements should be relied upon as continuing to reflect the expectations of management or the current status of any matter referred to therein as of any date subsequent to the date on which such statements are made.

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DESCRIPTION OF DEBT SECURITIES

General

The debt securities that we may offer by this prospectus consist of unsecured notes, debentures, or other evidences of indebtedness of Macy's Holdings, a wholly owned subsidiary of Macy's, which securities we refer to as debt securities. Macy's Holdings may issue debt securities in one or more series under an indenture, dated as of January 13, 2012, among Macy's Holdings, as issuer, Macy's, as guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee. A copy of the indenture is filed as Exhibit 4.5 to the registration statement of which this prospectus is a part and is incorporated herein by reference. Except as otherwise defined in this prospectus, capitalized terms used in this prospectus have the meanings given to them in the indenture.

The provisions of the indenture will generally be applicable to all of the debt securities. Selected provisions of the indenture are described in this prospectus. Additional or different provisions that are applicable to a particular series of debt securities will, if material, be described in a prospectus supplement relating to the offering of debt securities of that series. These provisions may include, among other things and to the extent applicable, the following:

the title of the debt securities;

the extent, if any, to which the debt securities are subordinated in right of payment to other indebtedness of Macy's Holdings;

any limit on the aggregate principal amount of the debt securities;

any subordination provisions or other limitations applicable to guarantees of the debt securities;

the persons to whom any interest on the debt securities will be payable, if other than the registered holders thereof on the regular record date therefor;

the date or dates on which the principal of the debt securities will be payable;

the rate or rates at which the debt securities will bear interest, if any, and the date or dates from which interest will accrue;

the dates on which interest, if any, will be payable and the regular record dates for interest payment dates;

the place or places where the principal of and any premium and interest on the debt securities will be payable;

the period or periods, if any, within which, and the price or prices at which, the debt securities may be redeemed, in whole or in part, at the option of Macy's Holdings;

the obligation, if any, of Macy's Holdings to redeem or purchase the debt securities pursuant to sinking fund or similar provisions and the terms and conditions of any such redemption or purchase;

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the denominations in which the debt securities will be issuable, if other than denominations of \$1,000 and any integral multiple thereof;

the currency, currencies or currency units, if other than currency of the United States of America, in which payment of the principal of and any premium or interest on the debt securities will be payable, and the terms and conditions of any elections that may be made available with respect thereto;

any index or formula used to determine the amount of payments of principal of and any premium or interest on the debt securities;

whether the debt securities are to be issued in whole or in part in the form of one or more global securities and, if so, the identity of the depositary, if any, for the global securities;

the manner, if any, in which the debt securities will be exchangeable for the common stock or other securities of Macy's or any other person;

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the principal amount (or any portion of the principal amount) of the debt securities which will be payable upon any declaration of acceleration of the maturity of the debt securities pursuant to an event of default; and

the applicability to the debt securities of the provisions described under "Defeasance" below.

We may issue debt securities at a discount from their stated principal amount. Federal income tax considerations and other special considerations applicable to any debt security issued with original issue discount (an "original issue discount security") may be described in an applicable prospectus supplement.

If the purchase price of any series of the debt securities is payable in a foreign currency or currency unit or if the principal of or any premium or interest on any series of the debt securities is payable in a foreign currency or currency unit, the restrictions, elections, general tax considerations, specific terms, and other information with respect to the debt securities and the applicable foreign currency or currency unit will be set forth in an applicable prospectus supplement.

Unless otherwise indicated in an applicable prospectus supplement:

the debt securities will be issued only in fully registered form (without coupons) in denominations of \$1,000 or integral multiples thereof; and

payment of principal and any premium or interest on the debt securities will be payable, and the exchange and transfer of debt securities will be registrable, at Macy's Holdings' office or agency maintained for those purposes and at any other office or agency maintained for those purposes. No service charge will be made for any registration of transfer or exchange of the debt securities, but we may require payment of a sum sufficient to cover any tax or other governmental charge imposed in connection therewith.

Guarantees

Subject to the limitations described below and except as otherwise disclosed in the applicable prospectus supplement, Macy's will fully, unconditionally and irrevocably guarantee the full and punctual payment when due, whether at maturity, by acceleration, by redemption, by repurchase, or otherwise, of all payment obligations on the debt securities of a series, whether for principal of, or any premium or interest on, the debt securities or otherwise.

In the case of subordinated debt securities of any series, Macy's guarantee will be subordinated in right of payment to its senior debt on the same basis as the subordinated debt securities of each series are subordinated to Macy's Holdings' senior debt securities. No payment will be made by Macy's under its guarantee during any period in which payments by Macy's Holdings on any subordinated debt securities are suspended by the subordination provisions applicable to such series.

Macy's guarantee will be limited in a manner intended to assure that the amount thereof will not exceed the maximum amount that can be guaranteed by Macy's without rendering such guarantee voidable under applicable law relating to fraudulent conveyance or fraudulent transfer or similar laws affecting the rights of creditors generally.

Macy's guarantee will be a continuing guarantee and will:

(1) remain in full force and effect until either (a) payment in full of all the applicable debt securities (or such debt securities are otherwise satisfied and discharged in accordance with the provisions of the applicable indenture) or (b) released in connection with a redemption, if any;

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(2) be binding upon Macy's; and

(3) inure to the benefit of and be enforceable by the applicable trustee, the holders and their successors, transferees and assigns.

Global Securities

The debt securities of a series may be issued in whole or in part in the form of one or more global securities that will be deposited with, or on behalf of, a depository or its nominee identified in an applicable prospectus supplement. Unless and until it is exchanged in whole or in part for debt securities in registered form, a global security may not be registered for transfer or exchange except:

by the depository to a nominee of the depository;

by a nominee of the depository to the depository or another nominee of the depository;

by the depository or any nominee of the depository to a successor depository or a nominee of the successor depository; or

in any other circumstances described in an applicable prospectus supplement.

The specific terms of the depository arrangement with respect to any debt securities to be represented by a global security will be described in an applicable prospectus supplement. We expect that the following provisions will apply to depository arrangements.

Unless otherwise specified in an applicable prospectus supplement, any global security that represents debt securities will be registered in the name of the depository or its nominee. Upon the deposit of a global security with or on behalf of the depository for the global security, the depository will credit, on its book-entry registration and transfer system, the respective principal amounts of the debt securities represented by the global security to the accounts of institutions that are participants in such system. The accounts to be credited will be designated by the underwriters or agents of the debt securities or by Macy's Holdings, if the debt securities are offered and sold directly by Macy's Holdings.

Ownership of beneficial interests in debt securities represented by a global security will be limited to participants in the book-entry registration and transfer system of the applicable depository or persons that may hold interests through those participants. Ownership of those beneficial interests by participants will be shown on, and the transfer of ownership will be effected only through, records maintained by the depository or its nominee for such global security. Ownership of such beneficial interests by persons that hold through such participants will be shown on, and the transfer of such ownership will be effected only through, records maintained by the participants. The laws of some jurisdictions require that specified purchasers of securities take physical delivery of their securities in definitive form. These laws may impair your ability to transfer beneficial interests in a global security.

So long as the depository for a global security, or its nominee, is the registered owner of the global security, the depository or the nominee, as the case may be, will be considered the sole owner or holder of the debt securities represented by the global security for all purposes under the indenture. Unless otherwise specified in an applicable prospectus supplement, owners of beneficial interests in the global security will not be entitled to have any of the debt securities represented by the global security registered in their names, will not receive or be entitled to receive physical delivery of any such debt securities in certificated form, and will not be considered the owners or holders of the debt securities for any purpose under the indenture. Accordingly, each person owning a beneficial interest in debt securities represented by a global security must rely on the procedures of the applicable depository and, if the person is not a participant in the book-entry registration and transfer system of the applicable depository, on the procedures of the participant through which the person owns its interest, to exercise any rights of an owner or holder of debt securities under the indenture.

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We understand that, under existing industry practices, if an owner of a beneficial interest in debt securities represented by a global security desires to give any notice or take any action that an owner or holder of debt securities is entitled to give or take under the indenture:

the applicable depository would authorize its participants to give the notice or take the action; and

the participants would authorize persons owning the beneficial interests through the participants to give the notice or take the action or would otherwise act upon the instructions of the persons owning the beneficial interests.

Principal of and any premium and interest on debt securities represented by a global security will be payable in the manner described in an applicable prospectus supplement. Payment of principal of, and any premium or interest on, debt securities represented by a global security will be made to the applicable depository or its nominee, as the case may be, as the registered owner or the holder of the global security. None of us, the trustee, any paying agent, or the registrar for debt securities represented by a global security will have any responsibility or liability for any aspect of the records relating to or payments made on account of beneficial ownership interests in those debt securities or for maintaining, supervising, or reviewing any records relating to those beneficial ownership interests.

Certain Covenants of Macy's Holdings

Maintenance of Office or Agency. Macy's Holdings will be required to maintain an office or agency in each place of payment for each series of debt securities for notice and demand purposes and for the purposes of presenting or surrendering debt securities for payment, registration of transfer, or exchange.

Paying Agents, Etc. If Macy's Holdings acts as its own paying agent with respect to any series of debt securities, on or before each due date of the principal of or any premium or interest on any of the debt securities of that series, Macy's Holdings will be required to segregate and hold in trust for the benefit of the persons entitled to payment a sum sufficient to pay the amount due and to notify the trustee promptly of Macy's Holdings action or failure to act. If Macy's Holdings has one or more paying agents for any series of debt securities, prior to each due date of the principal of or any premium or interest on any debt securities of that series, Macy's Holdings will be required to deposit with a paying agent a sum sufficient to pay the amount due and, unless the paying agent is the trustee, to promptly notify the trustee of its action or failure to act. All moneys paid by Macy's Holdings to a paying agent for the payment of principal of or any premium or interest on any debt securities that remain unclaimed for two years after the principal or any premium or interest has become due and payable may be repaid to Macy's Holdings, and thereafter the holder of those debt securities may look only to Macy's Holdings for payment thereof.

Existence. Macy's Holdings will be required to, and will be required to cause its subsidiaries to, preserve and keep in full force and effect its and their existence, charter rights, statutory rights, and franchises, except to the extent that the failure to do so would not have a material adverse effect.

Restrictive Covenants. Any restrictive covenants applicable to any series of debt securities will be described in an applicable prospectus supplement.

Events of Default

The following are Events of Default under the indenture with respect to debt securities of any series:

- (1) failure to pay any interest on any debt security of that series when due, which failure continues for 30 calendar days;
- (2) failure to pay principal of or premium, if any, on any debt security of that series when due and payable;

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- (3) failure to make any sinking fund payment in respect of any debt security of that series when it becomes due and payable;
- (4) failure to perform, or breach of, any other of Macy's Holdings' covenants in the indenture (other than a covenant included in the indenture solely for the benefit of a series of debt securities other than that series), which failure or breach continues for 60 calendar days after written notice thereof has been given to Macy's Holdings as provided in the indenture;
- (5) any nonpayment at maturity or other default (beyond any applicable grace period) under any agreement or instrument relating to any other indebtedness of Macy's Holdings, the unpaid principal amount of which is not less than \$100 million, which default results in the acceleration of the maturity of the indebtedness prior to its stated maturity or occurs at the final maturity thereof;
- (6) any guarantee of the debt securities of that series ceases to be in full force and effect (except as contemplated by the terms of the indenture) or is declared in a judicial proceeding to be null and void, or Macy's denies or disaffirms in writing its obligations under its guarantee;
- (7) specified events of bankruptcy, insolvency, or reorganization involving Macy's Holdings or Macy's; and
- (8) any other Event of Default provided with respect to debt securities of that series.

Pursuant to the Trust Indenture Act of 1939, the trustee is required, within 90 calendar days after the occurrence of a default in respect of any series of debt securities, to give to the holders of the debt securities of that series notice of all uncured defaults known to it, except that:

in the case of a default in the performance of any covenant of the character contemplated in clause (4) above, no notice will be given until at least 30 calendar days after the occurrence of the default; and

other than in the case of a default of the character contemplated in clause (1), (2) or (3) above, the trustee may withhold notice if and so long as it in good faith determines that the withholding of notice is in the interests of the holders of the debt securities of that series.

If an Event of Default described in clause (7) above occurs, the principal of, and any premium and accrued interest on the debt securities of that series will become immediately due and payable without any declaration or other act on the part of the trustee or any holder of the debt securities of that series. If any other Event of Default with respect to debt securities of any series occurs and is continuing, either the trustee or the holders of at least 25% in principal amount of the outstanding debt securities of that series may declare the principal amount of all debt securities of that series to be due and payable immediately. However, at any time after a declaration of acceleration with respect to debt securities of any series has been made, but before a judgment or decree based on such acceleration has been obtained, the holders of a majority in principal amount of the outstanding debt securities of that series may, under specified circumstances, rescind and annul such acceleration. See [Modification and Waiver](#) below.

Subject to the duty of the trustee to act with the required standard of care during an Event of Default, the trustee will have no obligation to exercise any of its rights or powers under the indenture at the request or direction of the holders of debt securities, unless holders of debt securities shall have offered to the trustee reasonable security or indemnity. Subject to the provisions of the indenture, including those requiring security or indemnification of the trustee, the holders of a majority in principal amount of the debt securities of any series will have the right to direct the time, method, and place of conducting any proceeding for any remedy available to the trustee, or exercising any trust or power conferred on the trustee, with respect to the debt securities of that series.

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No holder of a debt security of any series will have any right to institute any proceeding with respect to the indenture or for any remedy thereunder unless:

the holder has previously given to the trustee written notice of a continuing Event of Default with respect to the debt securities of that series;

the holders of at least 25% in aggregate principal amount of the outstanding debt securities of that series have requested in writing that the trustee institute a proceeding as trustee in respect of the Event of Default;

the holder or holders have offered reasonable indemnity to the trustee to institute the proceeding as trustee;

the trustee has not received from the holders of a majority in principal amount of the outstanding debt securities of that series a direction inconsistent with the written request; and

the trustee has failed to institute the proceeding within 60 calendar days after receipt of the written request.

However, the limitations described above do not apply to a suit instituted by a holder of a debt security for enforcement of payment of the principal of and any premium or interest on such debt security on or after the applicable due dates for the payment of such obligations.

Macy's Holdings is required to furnish to the trustee annually a statement as to the performance of its obligations under the indenture and as to any default in its performance.

Any additional Events of Default with respect to any series of debt securities, and any variations from the foregoing Events of Default applicable to any series of debt securities, will be described in an applicable prospectus supplement.

Modification and Waiver

In general, modifications and amendments of the indenture may be made by Macy's Holdings, Macy's and the trustee with the consent of the holders of not less than a majority in principal amount of the outstanding debt securities of each series affected thereby. However, no modification or amendment of the indenture may, without the consent of the holder of each outstanding debt security affected thereby:

change the stated maturity of, or any installment of principal of, or interest on, any debt security;

reduce the principal amount of, the rate of interest on, or the premium, if any, payable upon the redemption of, any debt security;

reduce the amount of principal of an original issue discount security payable upon acceleration of the maturity thereof;

change the place or currency of payment of principal of, and any premium or interest on, any debt security;

impair the right to institute suit for the enforcement of any payment on or with respect to any debt security on or after the stated maturity or prepayment date thereof; or

reduce the percentage in principal amount of outstanding debt securities of any series required for modification or amendment of the indenture or for waiver of compliance with certain provisions of the indenture or for waiver of certain defaults.

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The holders of at least a majority in principal amount of the outstanding debt securities of any series may, on behalf of the holders of all debt securities of that series, waive Macy's Holdings' compliance with specified covenants of the indenture. The holders of at least a majority in principal amount of the outstanding debt securities of any series may, on behalf of the holders of all debt securities of that series, waive any past default under the indenture with respect to that series, except:

a default in the payment of the principal of, any premium or interest on, any debt security of that series; or

a default of a provision of the indenture that cannot be modified or amended without the consent of the holder of each outstanding debt security of that series.

Defeasance

Unless otherwise specified in a prospectus supplement applicable to a particular series of debt securities and except as described below, upon compliance with the applicable requirements described below, Macy's Holdings:

(1) will be deemed to have been discharged from its obligations with respect to the outstanding debt securities of that series; or

(2) will be released from its obligations to comply with certain covenants described under Certain Covenants of Macy's Holdings above and from certain prohibitions against consolidations, mergers, and the transfer of its assets described under Limitations on Merger and Other Transactions below with respect to the outstanding debt securities of that series, and the occurrence of an event described in any of clauses (3), (4), (5) and (8) under Events of Default above will no longer be an Event of Default with respect to the debt securities of that series except to the limited extent described below.

Following any defeasance described in clause (1) or (2) above, Macy's Holdings will continue to have specified obligations under the indenture, including obligations to register the transfer or exchange of debt securities of the applicable series; replace destroyed, stolen, lost, or mutilated debt securities of the applicable series; maintain an office or agency in respect of the debt securities of the applicable series; and hold funds for payment to holders of debt securities of the applicable series in trust. In the case of any defeasance described in clause (2) above, any failure by Macy's Holdings to comply with its continuing obligations may constitute an Event of Default with respect to the debt securities of the applicable series as described in clause (4) under Events of Defaults above.

In order to effect any defeasance described in clause (1) or (2) above, Macy's Holdings must irrevocably deposit with the trustee, in trust, money or specified government obligations (or depositary receipts therefor), or a combination thereof, that through the scheduled payment of principal and interest in accordance with their terms will provide, without reinvestment, money in an amount sufficient to pay all of the principal and any premium and interest on the debt securities of such series on the dates such payments are due in accordance with the terms of such debt securities. In addition, among other things:

no Event of Default or event which with the giving of notice or lapse of time, or both, would become an Event of Default under the indenture shall have occurred and be continuing on the date of such deposit;

in the event of any defeasance described in clause (1) above, Macy's Holdings shall have delivered to the trustee an opinion of outside counsel, stating that (a) it has received from, or there has been published by, the United States Internal Revenue Service a ruling or (b) there has been a change in applicable federal income tax law, in either case to the effect that, among other things, the holders of the outstanding debt securities of such series will not recognize gain or loss for United States federal income tax purposes as a result of such deposit or defeasance and will be subject to United States federal income tax in the same manner as if such deposit or defeasance had not occurred;

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in the event of any defeasance described in clause (2) above, Macy's Holdings shall have delivered to the trustee an opinion of outside counsel to the effect that, among other things, the holders of the outstanding debt securities of such series will not recognize gain or loss for United States federal income tax purposes as a result of such deposit or defeasance and will be subject to United States federal income tax in the same manner as if such deposit or defeasance had not occurred;

Macy's Holdings shall have delivered to the trustee an officer's certificate to the effect that (a) the debt securities of such series, if then listed on any securities exchange, will not be delisted solely as a result of such deposit and (b) any defeasance described in clause (1) or (2) above shall not result in a breach or violation of, or constitute a default under, any agreement to which Macy's Holdings is a party or violate any law to which Macy's Holdings is subject;

Macy's Holdings shall have delivered to the trustee a certificate from a nationally recognized firm of independent accountants or other person acceptable to the trustee expressing their opinion that the payments of principal and interest when due on the deposited government obligations plus any deposited money will provide the cash at such times and in such amounts as will be sufficient to pay the principal of and any premium and interest when due on the debt securities of such series on the respective maturities or on any earlier date or dates on which the debt securities of such series shall be subject to redemption at the option of the holder thereof;

any defeasance described in clause (1) or (2) above will not cause the trustee to have a conflicting interest within the meaning of the Trust Indenture Act (assuming all applicable debt securities are in default within the meaning of the Trust Indenture Act);

Macy's Holdings shall have delivered to the trustee an officer's certificate and an opinion of counsel, each stating that all conditions precedent with respect to any defeasance described in clause (1) or (2) above have been complied with; and

any defeasance described in clause (1) or (2) above will not result in the trust arising from such deposit constituting an investment company within the meaning of the Investment Company Act unless such trust will be qualified under the Investment Company Act or will be exempt from regulation thereunder.

If Macy's Holdings fails to comply with its remaining obligations under the indenture with respect to the debt securities of the applicable series following a defeasance described in clause (2) above and the debt securities of that series are declared due and payable because of the occurrence of any undefeased Event of Default, the amount of money and government obligations on deposit with the trustee may be insufficient to pay amounts due on the debt securities of that series at the time of the acceleration resulting from such Event of Default. However, Macy's Holdings will remain liable in respect of such payments.

Satisfaction and Discharge

Macy's Holdings, at its option, may satisfy and discharge the indenture (except for specified obligations of Macy's Holdings and the trustee, including, among others, the obligations to apply money held in trust) when:

either:

(1) all of the debt securities previously authenticated and delivered under the indenture (subject to specified exceptions relating to debt securities that have otherwise been satisfied or provided for) have been delivered to the trustee for cancellation; or

(2) all of the debt securities not previously delivered to the trustee for cancellation have become due and payable, will become due and payable at their stated maturity within one year, or are to be called for redemption within one year under arrangements satisfactory to the trustee for the giving of notice of redemption by the trustee, and Macy's Holdings has deposited or caused to be deposited with the trustee as trust funds for such

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purpose an amount sufficient to pay and discharge the entire indebtedness on such debt securities, for principal and any premium and interest to the date of such deposit (in the case of debt securities which have become due and payable) or to the stated maturity or redemption date, as the case may be;

Macy's Holdings has paid or caused to be paid all other sums payable by it under the indenture; and

Macy's Holdings has delivered to the trustee an officer's certificate and an opinion of counsel, each to the effect that all conditions precedent relating to the satisfaction and discharge of the indenture have been satisfied.

Limitations on Merger and Other Transactions

Prior to the satisfaction and discharge of the indenture, Macy's Holdings may not consolidate with or merge with or into any other person, or transfer all or substantially all of its properties and assets to another person unless:

either

(1) Macy's Holdings is the continuing or surviving person in the consolidation or merger; or

(2) the person (if other than Macy's Holdings) formed by the consolidation or into which Macy's Holdings is merged or to which all or substantially all of the properties and assets of Macy's Holdings are transferred is a corporation, partnership, limited liability company, business trust, trust or other legal entity organized and validly existing under the laws of the United States, any State thereof, or the District of Columbia, and expressly assumes, by a supplemental indenture, all of Macy's Holdings' obligations under the debt securities and the indenture;

immediately after the transaction and the incurrence or anticipated incurrence of any indebtedness to be incurred in connection therewith, no Default exists; and

an officer's certificate is delivered to the trustee to the effect that both of the conditions set forth above have been satisfied and an opinion of outside counsel has been delivered to the trustee to the effect that the first condition set forth above has been satisfied.

The continuing, surviving, or successor person will succeed to and be substituted for Macy's Holdings with the same effect as if it had been named in the indenture as a party thereto, and thereafter the predecessor person will be relieved of all obligations and covenants under the indenture and the debt securities.

Governing Law

The indenture is, and the debt securities will be, governed by, and construed in accordance with, the laws of the State of New York.

Regarding the Trustee

The indenture and the Trust Indenture Act contain specified limitations on the right of the trustee, should it become a creditor of Macy's Holdings within three months of, or subsequent to, a default by Macy's Holdings to make payment in full of principal of or interest on any series of debt securities issued pursuant to the indenture when and as the same becomes due and payable, to obtain payment of claims, or to realize for its own account on property received in respect of any such claim as security or otherwise, unless and until such default is cured. However, the trustee's rights as a creditor of Macy's Holdings will not be limited if the creditor relationship arises from, among other things:

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the ownership or acquisition of securities issued under any indenture or having a maturity of one year or more at the time of acquisition by the trustee;

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specified advances authorized by a receivership or bankruptcy court of competent jurisdiction or by the indenture;

disbursements made in the ordinary course of business in its capacity as indenture trustee, transfer agent, registrar, custodian, or paying agent or in any other similar capacity;

indebtedness created as a result of goods or securities sold in a cash transaction or services rendered or premises rented; or

the acquisition, ownership, acceptance, or negotiation of specified drafts, bills of exchange, acceptances, or other obligations.

The indenture does not prohibit the trustee from serving as trustee under any other indenture to which Macy's Holdings may be a party from time to time or from engaging in other transactions with Macy's Holdings. If the trustee acquires any conflicting interest within the meaning of the Trust Indenture Act and there is an Event of Default with respect to any series of debt securities, the trustee must eliminate the conflict or resign.

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DESCRIPTION OF MACY S CAPITAL STOCK

Authorized Capital Stock

Macy s is authorized to issue 1,125 million shares of capital stock, consisting of 1,000 million shares of common stock, par value \$0.01 per share, and 125 million shares of preferred stock, par value \$0.01 per share.

Common Stock

Holders of Macy s common stock are entitled to one vote for each share held of record on all matters submitted to a vote of stockholders. Upon satisfaction of Macy s obligations to preferred stockholders, holders of Macy s common stock may receive dividends when declared by the Macy s board of directors. If Macy s liquidates, dissolves or winds-up its business, holders of Macy s common stock will share equally in the assets remaining after Macy s pays all of its creditors and satisfies all of its obligations to preferred stockholders. Holders of Macy s common stock have no conversion, preemptive, subscription or redemption rights. Macy s common stock is traded on the New York Stock Exchange under the symbol M. The registrar and transfer agent for the comm/TR>

Balance at January 1, 2008

\$18,091

Less reinsurance recoverables

(2,692)

Net balance at January 1, 2008

15,399

Incurred related to:

Current Year

65,314

Prior Year

840

Total incurred

66,154

Payments related to:

Current Year

(48,812)

Prior Year

(6,998)

Total payments

(55,810)

Net balance at September 30, 2008

25,743

Plus reinsurance recoverables

104,567

Balance at September 30, 2008

\$130,310

HILLTOP HOLDINGS INC.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****SEPTEMBER 30, 2008****(unaudited)****6. Reserve for Unpaid Losses and Loss Adjustment Expenses (Continued)**

The reserve for losses and loss adjustment expenses includes amounts that may be due to, or payable by, the sellers of NLASCO by January 2010 based on actual losses incurred as compared to the reserve as of the acquisition date. Prior year losses and payments include amounts back to the purchase of NLASCO on January 31, 2007 only, as all other prior losses and payments are the responsibility of the sellers.

7. Reinsurance Activity

NLASCO limits the maximum net loss that can arise from large risks or risks in concentrated areas of exposure by reinsuring (ceding) certain levels of risk. Substantial amounts of business are ceded; however, these reinsurance contracts do not relieve NLASCO from its obligations to policyholders. Such reinsurance includes quota share, excess of loss, catastrophe, and other forms of reinsurance on essentially all property and casualty lines of insurance. Failure of reinsurers to honor their obligations could result in losses to NLASCO; consequently, allowances are established for amounts deemed uncollectible. NLASCO evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurer insolvencies. At September 30, 2008, we had reinsurance receivables with no allowance of approximately \$104.6 million.

The effect of reinsurance on premiums written and earned for the three and nine months ended September 30, 2008 and 2007 is as follows (in thousands):

	Three Months Ended				Nine Months Ended			
	September 30, 2008		September 30, 2007		September 30, 2008		September 30, 2007	
	Written	Earned	Written	Earned	Written	Earned	Written	Earned
Premiums from direct business	\$ 31,430	\$ 33,984	\$32,427	\$30,776	\$ 98,725	\$ 98,444	\$ 92,012	\$73,277
Reinsurance assumed	1,365	1,402	1,637	1,264	4,134	4,574	5,369	2,373
Reinsurance ceded	(11,347)	(12,641)	(4,531)	(5,775)	(17,989)	(20,001)	(10,992)	(6,188)
Net premiums	\$ 21,448	\$ 22,745	\$29,533	\$26,265	\$ 84,870	\$ 83,017	\$ 86,389	\$69,462

The effect of reinsurance incurred losses was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2008	September 30, 2007	September 30, 2008	September 30, 2007
Loss and loss adjustment expense (LAE) incurred	\$ 123,850	\$14,532	\$ 164,662	\$42,991
Reinsurance recoverables	(96,978)	(760)	(98,508)	(1,702)
Net loss and LAE incurred	\$ 26,872	\$13,772	\$ 66,154	\$41,289

HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2008

(unaudited)

7. Reinsurance Activity (Continued)

Multi-line excess of loss coverage

For all lines of business, ASIC's retention on any one risk for 2008 is \$200,000 and NLIC's is \$200,000.

Catastrophic coverage

NLASCO has five levels of catastrophic excess of loss reinsurance providing for coverage up to \$200 million in 2008 above \$1.0 million in retention for ASIC and \$6.0 million for NLIC. NLASCO has an automatic reinstatement provision after the first loss for each layer to provide coverage in the event of subsequent catastrophes during the year. Coverage will lapse after the second or third event depending on the coverage layer, in which case NLASCO will evaluate the need for a new contract for the remainder of the year. During 2008, the first three layers can be reinstated twice for 100% of the original premium each time and the next two layers can be reinstated one time for 100% of the original premium.

For the quarter ended September 30, 2008, the Company experienced three significant catastrophes that resulted in losses in excess of retention. As of September 30, 2008, the total loss and loss adjustment expenses incurred associated with Hurricane Dolly was \$6.4 million, however, since the losses exceeded retention, net exposure to the Company was \$6.0 million retention and \$14,000 in reinstatement premiums. Total loss and loss adjustment expenses incurred associated with Hurricane Gustav was \$3.9 million, however, since the losses exceeded retention, net exposure to the Company was \$1.0 million retention and \$36,000 in reinstatement premiums. Total loss and loss adjustment expenses incurred associated with Hurricane Ike was \$98.0 million, however, since the losses exceeded retention, net exposure to the Company was \$7.0 million retention and \$8.2 million in reinstatement premiums.

8. Income Taxes

At September 30, 2008, the Company had net operating loss carry-forwards for Federal income tax purposes, subject to certain limitations, of approximately \$47.7 million and \$49.0 million for regular income tax and alternative minimum tax, respectively. These net operating loss carry-forwards expire in 2018 through 2024. The net operating loss carry-forwards for alternative minimum Federal income taxes generally are limited to offsetting 90% of the alternative minimum taxable earnings for a given period.

In conjunction with the sale of the Company's manufactured housing business lines that closed on July 31, 2007, approximately \$282.6 million of the Company's net operating loss carry forwards were utilized and \$175.2 million of temporary taxable differences were recognized.

As of September 30, 2008, we had a deferred tax asset, net of liabilities, of \$16.3 million. Our 35% rate reflects a change from the 40% rate utilized prior to the July 31, 2007 sale transaction as future taxable income of our insurance business will primarily be subject to Federal but not state income taxes. Insurance companies are generally not taxed in most states on income taxes, as they pay premium taxes in states where they generate premium revenue.

HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2008

(unaudited)

8. Income Taxes (Continued)

As a result of the allocation of the purchase price for the real estate assets we sold in 2007 by the purchaser, we reallocated \$34.1 million of gain recognized to those assets in the quarter ended September 30, 2008, the period in which the purchase price allocation was finalized. This reallocation allowed us to utilize \$34.1 million of our net operating loss carry forwards, which reduced our deferred tax asset by \$11.9 million and increased our income tax receivable by the same amount. In addition, we were able to utilize \$13.2 million of net operating losses that previously were limited under special IRS rules (the "Section 382 Limitations"), resulting in a deferred tax benefit of \$4.6 million.

We allocate income taxes between continuing and discontinued operations in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes ("SFAS No. 109"), particularly paragraph 140. We recognize income tax benefits in continuing operations on the effective rate method and income tax expense in discontinued operations without such pro-ration in accordance with Accounting Principles Board Opinion 28 and ASB Interpretation No. 18.

Effective January 1, 2007, we adopted FASB Interpretation No. 48, which required the measurement of unrecognized tax benefits. Unrecognized tax benefits are the difference between a tax position taken, or expected to be taken, in a tax return and the benefit recognized for accounting purposes. For the period ending September 30, 2008 we had no unrecognized tax benefits.

We file tax returns as prescribed by the tax laws of the jurisdictions in which we operate. We are subject to tax audits in numerous jurisdictions in the U.S. until the applicable statute of limitations expires. The following is a summary of the tax years open to examination:

U.S. Federal 2005 through 2007
U.S. States 2004 through 2007

As of September 30, 2008, there are no Federal or State tax audits.

Under special IRS rules (the "Section 382 Limitation"), cumulative stock purchases by 5% shareholders exceeding 50% during a three year period can limit a company's future use of net operating losses (NOL's). We had a Section 382 ownership change in February 2004 at the time of the IPO.

HILLTOP HOLDINGS INC.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****SEPTEMBER 30, 2008****(unaudited)****8. Income Taxes (Continued)**

The significant components of the provision for income taxes are as follows (in thousands):

	Three Months Ended September 30, 2008			Nine Months Ended September 30, 2008		
	Continuing Operations	Discontinued Operations	Total	Continuing Operations	Discontinued Operations	Total
Current tax benefit	\$ 17,303	\$ 11,919	\$ 29,222	\$ 16,581	\$ 11,919	\$ 28,500
Deferred tax expense	(12,814)	(11,919)	(24,733)	434	(11,919)	(11,485)
Allowance	4,603		4,603	4,603		4,603
Income tax benefit	\$ 9,092	\$	\$ 9,092	\$ 21,618	\$	\$ 21,618

	Three Months Ended September 30, 2007			Nine Months Ended September 30, 2007		
	Continuing Operations	Discontinued Operations	Total	Continuing Operations	Discontinued Operations	Total
Current tax expense	\$ (5,353)	\$ (74,234)	\$ (79,587)	\$ (3,124)	\$ (76,563)	\$ (79,687)
Deferred tax benefit (expense)	1,964	(59,930)	(57,966)	1,121	(43,402)	(42,281)
Allowance		59,930	59,930		43,402	43,402
Income tax expense	\$ (3,389)	\$ (74,234)	\$ (77,623)	\$ (2,003)	\$ (76,563)	\$ (78,566)

[Table of Contents](#)**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****SEPTEMBER 30, 2008****(unaudited)****8. Income Taxes (Continued)**

The provision for income taxes differs from the amount that would be computed by applying the statutory Federal income tax rate of 35% to income before income taxes as a result of the following (in thousands):

	Three Months Ended September 30, 2008			Nine Months Ended September 30, 2008		
	Continuing Operations	Discontinued Operations	Total	Continuing Operations	Discontinued Operations	Total
Tax at statutory rate	\$ 4,465	\$	\$ 4,465	\$ 17,007	\$	\$ 17,007
Permanent differences	24		24	8		8
Decrease in valuation allowance	4,603		4,603	4,603		4,603
Income tax benefit	\$ 9,092	\$	\$ 9,092	\$ 21,618	\$	\$ 21,618

	Three Months Ended September 30, 2007			Nine Months Ended September 30, 2007		
	Continuing Operations	Discontinued Operations	Total	Continuing Operations	Discontinued Operations	Total
Tax at statutory rate	\$ (3,381)	\$ (126,741)	\$ (130,122)	\$ (1,983)	\$ (123,474)	\$ (125,457)
Permanent differences	(8)	9,857	9,849	(20)	21,148	21,128
State taxes		(17,280)	(17,280)		(17,639)	(17,639)
Decrease in valuation allowance		59,930	59,930		43,402	43,402
Income tax expense	\$ (3,389)	\$ (74,234)	\$ (77,623)	\$ (2,003)	\$ (76,563)	\$ (78,566)

HILLTOP HOLDINGS INC.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****SEPTEMBER 30, 2008****(unaudited)****8. Income Taxes (Continued)**

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amount of the assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The tax effects of significant temporary differences that give rise to the net deferred tax assets and liabilities are as follows (in thousands):

	September 30, 2008	December 31, 2007
Deferred Tax Assets:		
Net operating loss carryforwards	\$ 16,680	\$ 28,600
Accrued liabilities and other	874	2,180
Loss and loss adjustment expense discounting	652	708
Securities available for sale	1,827	542
Unearned premiums	6,985	4,665
Loan origination costs	413	436
AMT credit carryforward	256	256
Valuation allowance		(4,603)
 Total gross deferred tax assets	 \$ 27,687	 \$ 32,784
Deferred Tax Liabilities:		
Rental and other property, net	\$ 21	\$ 14
Intangible assets	5,015	5,558
Goodwill	146	171
Deferred policy acquisition costs	6,227	4,822
 Total gross deferred tax liabilities	 \$ 11,409	 \$ 10,565
 Net Deferred Tax Asset	 \$ 16,278	 \$ 22,219

9. Statutory Net Income and Capital and Surplus

The Company's insurance subsidiaries, which are domiciled in the State of Texas, prepare their statutory financial statements in accordance with accounting principles and practices prescribed or permitted by the Texas Department of Insurance, which Texas recognizes for determining solvency under Texas State Insurance Law. The Commissioner of the Texas Department of Insurance has the right to permit other practices that may deviate from prescribed practices. Prescribed statutory accounting practices are those practices that are incorporated directly or by reference in state laws, regulations, and general administrative rules applicable to all insurance enterprises domiciled in Texas. Permitted statutory accounting practices encompass all accounting practices that are not prescribed; such practices differ from state to state, may differ from company to company within a state, and may change in the future. The Company's insurance subsidiaries have no such permitted statutory accounting practices.

The Company's insurance subsidiaries' statutory financial statements are presented on the basis of accounting practices prescribed or permitted by the Texas Department of Insurance. Texas had adopted the National Association of Insurance Commissioners' (NAIC) statutory accounting practices as the

HILLTOP HOLDINGS INC.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****SEPTEMBER 30, 2008****(unaudited)****9. Statutory Net Income and Capital and Surplus (Continued)**

basis of its statutory accounting practices with certain differences, which are not significant to the companies' statutory equity.

Following is a summary of statutory capital and surplus and statutory net income of each insurance subsidiary for the three and nine months ended September 30, 2008 and 2007 (in thousands).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
National Lloyds Insurance Company				
Capital and surplus	\$81,667	\$92,300	\$81,667	\$92,300
Statutory net (loss) income	\$ (6,929)	\$ 3,184	\$ (6,445)	\$ 9,419
American Summit Insurance Company				
Capital and surplus	\$23,212	\$24,490	\$23,212	\$24,490
Statutory net (loss) income	\$ (837)	\$ 1,386	\$ 602	\$ 2,804

10. Capital and Dividend Restrictions

The funding of the cash requirements (including debt service) of NLASCO is primarily provided by cash dividends from NLASCO's wholly-owned insurance subsidiaries. Dividends paid by the insurance subsidiaries are restricted by regulatory requirements of the Texas Department of Insurance. Under Texas State Insurance Law for property and casualty companies, all dividends must be distributed out of earned surplus only. Furthermore, without the prior approval of the Commissioner, dividends cannot be declared or distributed which exceed the greater of ten percent of NLASCO's surplus, as shown by its last statement on file with the Commissioner, or 100% of net income for such period. The subsidiaries paid \$14.0 million in dividends to NLASCO in March 2008. At September 30, 2008, the maximum dividend that may be paid to NLASCO in 2008 without regulatory approval is an additional \$7.3 million.

Regulations of the Texas Department of Insurance require insurance companies to maintain minimum levels of statutory surplus to ensure their ability to meet their obligations to policyholders. At September 30, 2008, the Company's insurance subsidiaries had statutory surplus in excess of the minimum required.

Also, the NAIC has adopted the risk based calculation formula for insurance companies that establishes minimum capital requirements relating to insurance risk, asset credit risk (RBC ratio), interest rate risk and business risk. The formula is used by the NAIC and certain state insurance regulators as an early warning tool to identify companies that require additional scrutiny or regulatory action. At September 30, 2008, the Company's insurance subsidiaries' RBC ratio exceeded the level at which regulatory action would be required.

HILLTOP HOLDINGS INC.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****SEPTEMBER 30, 2008****(unaudited)****11. Equity and Loss per share**

The following reflects the calculation of loss per share on a basic and diluted basis (in thousands, except per share information).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Income (Loss) per share from continuing operations:				
(Loss) Income from continuing operations	\$ (3,664)	\$ 6,260	\$ (26,975)	\$ 3,776
Preferred stock dividends	(2,579)	(2,577)	(7,735)	(7,734)
(Loss) Income from continuing operations	\$ (6,243)	\$ 3,683	\$ (34,710)	\$ (3,958)
Basic (loss) income per share from continuing operations	\$ (0.11)	\$ 0.07	\$ (0.61)	\$ (0.07)
Diluted (loss) income per share from continuing operations	\$ (0.11)	\$ 0.06	\$ (0.61)	\$ (0.07)
Income per share from discontinued operations:				
Loss from discontinued operations	\$	\$ (2,212)	\$	\$ (11,125)
Gain on sale of discontinued operations		364,330		363,907
Income tax expense from discontinuing operations		(74,234)		(76,563)
Minority interest in discontinued operations		86		494
Income from discontinued operations	\$	\$ 287,970	\$	\$ 276,713
Basic income per share from discontinued operations	\$	\$ 5.10	\$	\$ 5.02
Diluted income per share from discontinued operations	\$	\$ 5.06	\$	\$ 4.92
Income (Loss) per share available to common stockholders:				
(Loss) Income available to common stockholders	\$ (6,243)	\$ 291,653	\$ (34,710)	\$ 272,755
Basic (loss) income per share available to common stockholders	\$ (0.11)	\$ 5.17	\$ (0.61)	\$ 4.95
Diluted (loss) income per share available to common stockholders	\$ (0.11)	\$ 5.12	\$ (0.61)	\$ 4.85
Weighted average share information:				
Basic shares outstanding	56,452	56,446	56,452	55,071
Diluted shares outstanding	56,452	56,961	56,452	56,271

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Weighted average equivalent shares excluded from diluted loss per share because they would be anti-dilutive:

Operating partnership units(a)				
Stock warrants(b)	1	937	1	937
Senior exchangeable Notes	6,718	6,718	6,718	6,718
Stock options	541		541	
Total	7,260	7,655	7,260	7,655

-
- (a) From June 30, 2006 through June 30, 2007, we redeemed approximately 94,000 OP units. In July 2007, the remaining OP units were redeemed.
- (b) On August 11, 2008, the Company retired 936,745 warrants for total cost of \$215,451.

HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2008

(unaudited)

11. Equity and Loss per share (Continued)

On September 11, 2008, the board of directors declared a quarterly cash dividend of \$0.515625 per share on the Company's Series A Cumulative Redeemable Preferred Stock. The dividend was paid on October 30, 2008 to shareholders of record on October 15, 2008. The Board reviews the payment of dividends on a quarterly basis.

12. Commitments and Contingencies

Liabilities for loss contingencies arising from claims, assessments, litigation, fines and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated.

We are a party to various legal actions resulting from our operating activities. These actions consist of litigation and administrative proceedings arising in the ordinary course of business, some of which are covered by liability insurance, and none of which is expected to have a material adverse effect on our consolidated financial condition, results of operations or cash flows taken as a whole.

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

The following discussion should be read in conjunction with the consolidated historical financial statements and notes appearing elsewhere in this quarterly report on Form 10-Q and the financial information set forth in the tables below.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, as amended by the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical fact, included in this report that address results or developments that we expect or anticipate will or may occur in the future, that are preceded by, followed by or include the words "believes," "expects," "may," "will," "would," "could," "should," "seeks," "approximately," "intends," "plans," "projects," "estimates" or "anticipates" or the negative of these words and phrases or similar words or phrases, including such things as our business strategy, our financial condition, our litigation, our efforts to make strategic acquisitions, our liquidity and sources of funding, our capital expenditures, our products, market trends, operations and business, are forward-looking statements. These forward-looking statements are based on our beliefs, assumptions and expectations of our future performance taking into account all information currently available to us. These beliefs, assumptions and expectations are subject to risks and uncertainties and can change as a result of many possible events or factors, not all of which are known to us. If an event occurs or further changes, our business, business plan, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. Certain factors that could cause actual results to differ include, among others:

changes in the acquisition market;

our ability to find and complete strategic acquisitions with suitable merger or acquisition candidates or find other suitable ways in which to invest our capital;

the adverse impact of external factors, such as changes in interest rates, inflation and consumer confidence;

our corporate debt ratings;

the condition of capital markets;

actual outcome of the resolution of any conflict;

our ability to use net operating loss carryforwards to reduce future tax payments;

the impact of the tax code and rules on our financial statements;

failure of NLASCO, Inc.'s insurance subsidiaries to maintain their respective A.M. Best ratings;

failure to maintain NLASCO, Inc.'s current agents;

lack of demand for insurance products;

cost or availability of adequate reinsurance;

changes in key management;

severe catastrophic events in our geographic area;

failure of NLASCO, Inc.'s reinsurers to pay obligations under reinsurance contracts;

failure of NLASCO, Inc. to maintain sufficient reserves for losses on insurance policies; and

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failure of NLASCO, Inc. to maintain appropriate insurance licenses.

For a further discussion of these and other risks and uncertainties that could cause actual results to differ materially from those contained in our forward-looking statements, please refer to "Risk Factors" in Part II, Item 1A of this report and our Annual Report on Form 10-K, which was filed with the Securities and Exchange Commission on March 17, 2008. Consequently, all of the forward-looking statements made in this report are qualified by these cautionary statements and those risk factors, and there can be no assurance that the actual results or developments anticipated by us will be realized, or even substantially realized, and that they will have the expected consequences to, or effects on, us and our business or operations. Forward-looking statements made in this report speak as of the date of this report or as of the date specifically referenced in any such statement set forth in this report. We undertake no obligation to update or revise any forward-looking statements in this report.

Unless the context otherwise indicates, the words "we," "our," "ours," "us," "HTH" and the "Company" refer to Hilltop Holdings Inc., or Hilltop, and its subsidiaries, collectively.

GENERAL STRUCTURE OF THE COMPANY

We are a holding company that is endeavoring to make opportunistic acquisitions or a business combination. In connection with that strategy, we are identifying and evaluating potential targets on an ongoing basis. At September 30, 2008, Hilltop and its operating partnership, Affordable Residential Communities LP, had approximately \$717 million of available cash and cash equivalents that could be used for this purpose. No assurances, however, can be given that we will be able to identify suitable targets, consummate acquisitions or a combination or, if consummated, successfully integrate or operate the acquired business.

Hilltop indirectly owns all of the outstanding shares of NLASCO, Inc., or NLASCO. NLASCO, in turn, owns National Lloyds Insurance Company, or NLIC, and American Summit Insurance Company, or ASIC, both of which are licensed property and casualty insurers operating in multiple states. In addition, NLASCO also owns the NALICO General Agency that operates in Texas. NLIC commenced business in 1949 and currently operates in 15 states with its largest market being the state of Texas. NLIC carries a financial strength rating of "A" (Excellent) by A.M. Best. ASIC was formed in 1955 and currently operates in 13 states, its largest market being the state of Arizona. ASIC carries a financial strength rating of "A-"(Excellent) by A.M. Best. Both of these companies are regulated by the Texas Department of Insurance.

Our common stock is listed on the New York Stock Exchange, or the NYSE, under the symbol "HTH". Our Series A Cumulative Redeemable Preferred Stock is listed on the NYSE under the symbol "HTH-PA".

OVERVIEW OF RESULTS

For the nine months ended September 30, 2008, net loss attributable to common stockholders was \$34.7 million, or \$0.61 per share, as compared to net income of \$272.8 million, or \$4.95 per share, for the same period in 2007. Continuing operations accounted for \$27.0 million of the net loss for the nine months ended September 30, 2008, compared to \$3.8 million of the net income for the nine months ended September 30, 2007. Net loss from continuing operations increased by \$30.8 million for the nine months ended September 30, 2008, as compared to the same period in 2007, primarily due to the loss on investment of \$41.9 million (\$27.2 million net of tax) recorded for equity securities held at HTH and \$1.4 million of costs associated with acquisition activities being expensed due to the determination that HTH would no longer pursue such target during the second quarter of 2008. Additionally, the net loss increased due to increase in loss and loss adjustment expenses related to Hurricane Dolly, Gustav and Ike of approximately \$14.0 million, net of reinsurance recoveries, and the decrease in net premiums earned due to reinstatement premiums related to Hurricane Dolly, Ike and Gustav of

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\$8.2 million. Those losses and expenses were partially offset by additional interest income generated on the cash from the sale of the assets related to the manufactured housing business segment that closed on July 31, 2007 and the fact that NLASCO had nine months of revenue in 2008, as compared to eight months in 2007.

BUSINESS OBJECTIVES AND OPERATING STRATEGIES

Strategic Acquisitions. Hilltop is seeking to make opportunistic acquisitions with certain of the proceeds from the sale of the manufactured home business and, if necessary or appropriate, from additional equity or debt financing sources.

Insurance Operations. NLASCO specializes in providing fire and homeowners insurance for low value dwellings and manufactured homes, primarily in Texas and other areas of the south, southeastern and southwestern United States. NLASCO targets underserved markets that require underwriting expertise that many larger carriers have been unwilling to develop given the relatively small volume of premiums produced by local agents. Within these markets, NLASCO capitalizes on its superior local knowledge to identify profitable underwriting opportunities. NLASCO believes that it distinguishes itself from competitors by delivering products that are not provided by many larger carriers, providing a high level of customer service and responding quickly to the needs of its agents and policyholders. NLASCO applies a high level of selectivity in the risks it underwrites and uses a risk-adjusted return approach to capital allocation, which NLASCO believes allows it to consistently generate underwriting profits.

Many insurance buyers, agents and brokers use the ratings assigned by A.M. Best and other rating agencies to assist them in assessing the financial strength and overall quality of the companies from which they purchase insurance. A.M. Best assigned NLIC a financial strength rating of "A" (Excellent) and ASIC a rating of "A-" (Excellent). An "A" rating is the third highest of 15 rating categories used by A.M. Best, and an "A-" rating is the fourth highest of 15 rating categories. In evaluating a company's financial and operating performance, A.M. Best reviews a company's profitability, leverage and liquidity, as well as its book of business, the adequacy and soundness of its reinsurance, the quality and estimated market value of its assets, the adequacy of its liabilities for losses and LAE, the adequacy of its surplus, its capital structure, the experience and competence of its management and its market presence. This rating is intended to provide an independent opinion of an insurer's ability to meet its obligations to policyholders and is not an evaluation directed at investors. This rating assignment is subject to the ability to meet A.M. Best's expectations as to performance and capitalization on an ongoing basis, including with respect to management of liabilities for losses and LAE, and is subject to revocation or revision at any time at the sole discretion of A.M. Best. NLASCO cannot ensure that NLIC and ASIC will maintain their present ratings.

Critical Accounting Policies and Estimates

The Company has prepared its consolidated financial statements in accordance with generally accepted accounting principles, or GAAP, which require certain estimates and assumptions that affect the recorded amount of assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results may differ from these estimates. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP, however, have been condensed or omitted pursuant to Article 10 of Regulation S-X. A summary of HTH's significant accounting policies has been provided in its Form 10-K for the year ended December 31, 2007. Summarized below are those accounting policies that require the most difficult, subjective or complex judgments and that have the most significant impact on HTH's financial condition and results of operations. Management evaluates these estimates on an ongoing basis. These estimates are based on information currently available to management and on various other assumptions management believes are reasonable.

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Losses and Loss Adjustment Expenses. The liability for losses and loss adjustment expenses represents estimates of the ultimate unpaid cost of all losses incurred, including losses for claims that have not yet been reported. The amount of loss reserves for reported claims is based primarily on a case-by-case evaluation of the type of risk involved, knowledge of the circumstances surrounding each claim and the insurance policy provisions relating to the type of loss. The amounts of loss reserves for unreported claims and loss adjustment expenses are determined using historical information as adjusted to current conditions.

When a claim is reported, a "case reserve" is established for the estimated amount of the ultimate payment. This estimate reflects an informed judgment based upon general insurance reserving practices and the experience and knowledge of the Company. The estimate considers the nature and value of the specific claim, the severity of injury or damage, and the policy provisions relating to the type of loss. Case reserves are adjusted as more information becomes available.

We maintain incurred but not reported, or IBNR, reserves to provide for already incurred claims that have not yet been reported and developments on reported claims. The IBNR reserve is estimated based on the volume of premiums written and is reviewed quarterly by our actuaries.

Such liabilities are necessarily based on estimates and, while management believes that the amount is adequate, the ultimate liability may be in excess of or less than the amounts provided. The methods for making such estimates and for establishing the resulting liability are continually reviewed, and any adjustments are reflected in earnings currently. The liability for losses and loss adjustment expenses has not been reduced for reinsurance recoverables.

Investment Securities. Investment securities consist of U.S. Government, mortgage-backed, corporate debt and equity securities. We classify our fixed maturities in one of three categories: trading, available-for-sale or held-to-maturity; and our equity securities are classified as trading or available-for-sale. Trading securities are bought and held principally for the purpose of selling them in the near term. Held-to-maturity debt securities are those securities in which we have the ability and intent to hold the security until maturity. All securities not included in trading or held-to-maturity are classified as available-for-sale. Trading and available-for-sale securities are recorded at fair value. Held-to-maturity debt securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums or discounts. Unrealized holding gains and losses on trading securities are included in earnings. Unrealized holding gains and losses, net of the related tax effect, on available-for-sale securities are excluded from earnings and are reported as a separate component of other comprehensive income until realized. Realized gains and losses from the sale of trading and available-for-sale securities are determined on a specific identification basis. We regularly review our investment securities to assess whether the amortized cost is impaired and if impairment is other than temporary. A decline in the market value of any available-for-sale or held-to-maturity security below cost that is deemed to be other-than-temporary results in a reduction in carrying amount to fair value. The impairment is charged to earnings and a new cost basis for the security is established. To determine whether impairment is other-than-temporary, we consider whether we have the ability and intent to hold the investment until a market price recovery and consider whether evidence indicating the cost of the investment is recoverable outweighs evidence to the contrary. Evidence considered in this assessment includes the reasons for the impairment, the severity and duration of the impairment, changes in value subsequent to year-end, and forecasted performance of the investee. Premiums and discounts are amortized or accreted over the life of the related held-to-maturity or available-for-sale security as an adjustment to yield using the effective-interest method. Dividend and interest income are recognized when earned.

Deferred Acquisition Costs. Commissions and other costs of acquiring insurance that vary with, and are primarily related to, the production of new and renewal business are deferred and amortized over the terms of the policies or reinsurance treaties to which they relate. Proceeds from reinsurance

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transactions that represent recovery of acquisition costs reduce applicable unamortized acquisition costs in such a manner that net acquisition costs are capitalized and charged to expense in proportion to net revenue recognized. Future investment income is considered in determining the recoverability of deferred acquisition costs. We regularly review the categories of acquisition costs that are deferred and assess the recoverability of this asset. A premium deficiency and a corresponding charge to income is recognized if the sum of the expected loss and loss adjustment expenses, unamortized acquisition costs and maintenance costs exceeds related unearned premiums and anticipated investment income.

Revenue Recognition. Property and liability premiums are recognized as revenue on a pro rata basis over the policy term. The portion of premiums that will be earned in the future are deferred and reported as unearned premiums. We routinely evaluate the premium receivable balance to determine if an allowance for uncollectible accounts is necessary.

Other income consists of premium installment charges, which are recognized when earned, and other miscellaneous income.

Reinsurance. In the normal course of business, NLASCO seeks to reduce losses that may arise from catastrophes or other events that cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. Net premiums earned, losses and LAE and policy acquisition and other underwriting expenses are reported net of the amounts related to reinsurance ceded to other companies. Amounts recoverable from reinsurers related to the portions of the liability for losses and LAE are reported as assets. Amounts recoverable from reinsurers are estimated in a manner consistent with the reinsured policy.

The Company accounts for reinsurance contracts under the provisions of Statement of Financial Accounting Standards ("SFAS"), No. 113, "Accounting and Reporting for Reinsurance on Short-Duration and Long-Duration Contracts." Amounts recoverable from reinsurers related to the portions of the liability for losses and LAE and unearned premiums ceded to them are reported as assets. Reinsurance assumed from other companies, including assumed premiums written and earned and losses and LAE, is accounted for in the same manner as direct insurance written.

Income Taxes. Effective January 1, 2007, we adopted FASB Interpretation No. ("FIN") 48, Accounting for Uncertainty in Income Taxes. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. 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. FIN 48 requires that we determine whether the benefits of our tax positions are more likely than not of being sustained upon audit based on the technical merits of the tax position. For tax positions that are more likely than not of being sustained upon audit, we recognize the largest amount of the benefit that is more likely than not of being sustained in our consolidated financial statements. For tax positions that are not likely of being sustained upon audit, we do not recognize any portion of the benefits in our consolidated financial statements. The provisions of FIN 48 also provide guidance on derecognition, classification, interest and penalties, accounting in interim periods, and disclosure.

Goodwill and Other Indefinite Lived Intangible Assets. Goodwill represents the excess of the cost over fair value of assets or businesses acquired. Goodwill is tested annually for impairment and is tested more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. For goodwill, the impairment determination is made at the reporting unit level and consists of two steps. First, we determine the fair value of a reporting unit and compare it to its carrying amount. Second, if the carrying amount of a reporting unit exceeds its fair value, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting

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unit in a manner similar to a purchase price allocation, in accordance with FASB Statement No. 141, Business Combinations. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill. Other indefinite lived intangible assets consist of \$3.0 million, which is estimated fair value of state licenses acquired in the NLASCO purchase.

Fair Value. The Company's estimates of fair value for financial assets and financial liabilities are based on the framework established in Statement of Financial Accounting Standards No. 157, "Fair Value Measurements", or SFAS 157. The framework is based on the inputs used in valuation and requires that observable inputs be used in the valuations when available. The disclosure of fair value estimates in the SFAS 157 hierarchy is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the Company's significant market assumptions. The three levels of the hierarchy are as follows: Level 1 Unadjusted quoted market prices for identical assets or liabilities in active markets that the Company has the ability to access. Level 2 Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; or valuations based on models where the significant inputs are observable (e.g., interest rates, yield curves, prepayment speeds, default rates, loss severities, etc.) or can be corroborated by observable market data. Level 3 Valuations based on models where significant inputs are not observable. The unobservable inputs reflect the Company's own assumptions about the assumptions that market participants would use.

RESULTS OF OPERATIONS

Overview. For the quarter ended September 30, 2008, the Company experienced three significant catastrophes that resulted in losses in excess of retention. As of September 30, 2008, the total loss and loss adjustment expenses incurred associated with Hurricane Dolly was \$6.4 million, however, since the losses exceeded retention, net exposure to the Company was \$6.0 million retention and \$14,000 in reinstatement premiums. Total loss and loss adjustment expenses incurred associated with Hurricane Gustav was \$3.9 million, however, since the losses exceeded retention, net exposure to the Company was \$1.0 million retention and \$36,000 in reinstatement premiums. Total loss and loss adjustment expenses incurred associated with Hurricane Ike was \$98.0 million, however, since the losses exceeded retention, net exposure to the Company was \$7.0 million retention and \$8.2 million in reinstatement premiums. Additionally, the Company wrote down securities owned by NLASCO, Inc. of \$1.1 million.

As a result of the allocation of the purchase price for the real estate assets we sold in 2007 by the purchaser, we reallocated \$34.1 million of gain recognized to those assets in the quarter ended September 30, 2008, the period in which the purchase price allocation was finalized. This reallocation allowed us to utilize \$34.1 million of our net operating loss carry forwards, which reduced our deferred tax asset by \$11.9 million and increased our income tax receivable by the same amount. In addition, we were able to utilize \$13.2 million of net operating losses that previously were limited under special IRS rules (the "Section 382 Limitations"), resulting in a deferred tax benefit of \$4.6 million.

Comparison of the Three Months Ended September 30, 2008 to the Three Months Ended September 30, 2007

Revenue. Revenue for the three months ended September 30, 2008 was \$29.8 million, as compared to \$38.0 million for the same period in 2007. Net premiums earned were \$22.7 million for the third quarter in 2008, as compared to \$26.3 million for 2007. Net investment income was \$6.7 million for the third quarter of 2008, as compared to \$10.0 million for the same period in 2007, primarily due to higher cash balances and higher yield in 2007. We had a net realized loss on investments of \$1.2 million in the third quarter of 2008, due to the write down of securities owned by NLASCO, Inc. Other income was \$1.5 million for the third quarter in 2008, as compared to \$1.8 million for 2007. Revenues related to the manufactured housing business lines have been

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reclassified to discontinued operations and are presented net in the caption "Loss from discontinued operations."

Underwriting Results. The following table shows the components of the Company's underwriting (loss) gain for the three months ended September 30, 2008 and 2007. The Company's underwriting gain or loss consists of net premiums earned, less loss and LAE and policy acquisition and other underwriting expenses. The underwriting results are discussed below (in thousands).

	Three Months Ended September 30,			% Change
	2008	2007	Change	
Direct premiums written	\$ 31,430	\$32,427	\$ (997)	-3.1%
Net premiums written	\$ 21,448	\$29,533	\$ (8,085)	-27.4%
Net premiums earned	\$ 22,745	\$26,265	\$ (3,520)	-13.4%
Loss and LAE	26,872	13,772	13,100	95.1%
Policy acquisition and other underwriting expenses	10,736	8,949	1,787	20.0%
Underwriting (loss) gain	\$(14,863)	\$ 3,544	\$(18,407)	-519.4%
Loss and LAE ratio	118.1%	52.4%	65.7%	
Policy acquisition and other underwriting expense ratio	44.1%	31.0%	13.1%	
Combined ratio	162.2%	83.4%	78.8%	

The Company seeks to operate at a combined ratio of no greater than 85.0%. Loss ratios are ratios that express the relationship of losses to premiums. Loss and LAE ratio is loss and LAE expenses divided by net premiums earned for the same period. Policy acquisition and other underwriting expense ratio is policy acquisition and other underwriting expense divided by net premiums earned for the same period. Combined ratio gives you the sum of both previous ratios. The increase in policy acquisition and other underwriting expenses is due to the benefit received in 2007 related to the purchase accounting of \$4.3 million.

Premiums. The property and casualty insurance industry is affected by soft and hard market business cycles. During a soft market, price competition tends to increase as insurers are willing to reduce premium rates in order to maintain growth in premium volume. The soft market makes it more difficult to attract new business, as well as retain exposures which are adequately priced. Although we recognize the need to remain competitive in the marketplace, the Company remains committed to its disciplined underwriting philosophy accepting only risks that are appropriately priced, while declining risks which are underpriced for the level of coverage provided.

Direct premiums written by major product line for the three months ended September 30, 2008 and 2007, are presented in the table below (in thousands):

	Three Months Ended September 30,			% Change
	2008	2007	Change	
Direct Premiums Written:				
Homeowners	\$ 13,203	\$ 14,244	\$ (1,041)	-7.3%
Fire	12,059	12,645	(586)	-4.6%
Mobile Home	4,498	3,842	656	17.1%
Commercial	1,533	1,563	(30)	-1.9%
Other	137	133	4	3.0%
	\$31,430	\$32,427	\$ (997)	-3.1%

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Total direct premiums written decreased for the three months ended September 30, 2008 for all of the insurance products, except mobile home and other lines, due to the overall soft insurance market.

Net premiums written by major product line for the three months ended September 30, 2008 and 2007, are presented in the table below (in thousands):

	Three Months Ended September 30,			%
	2008	2007	Change	Change
Net Premiums Written				
Homeowners	\$ 9,010	\$ 13,927	\$(4,917)	-35.3%
Fire	8,229	10,900	(2,671)	-24.5%
Mobile Home	3,069	3,238	(169)	-5.2%
Commercial	1,046	1,352	(306)	-22.6%
Other	94	116	(22)	-19.0%
	\$21,448	\$29,533	\$(8,085)	-27.4%

Total net premiums written decreased for the three months ended September 30, 2008 for all insurance products due to the reinstatement premiums related to Hurricane Dolly, Gustav, and Ike totaling \$8.2 million.

Net premiums earned by major product line for the three months ended September 30, 2008 and 2007, are presented in the table below (in thousands):

	Three Months Ended September 30,			%
	2008	2007	Change	Change
Net Premiums Earned:				
Homeowners	\$ 9,555	\$ 11,472	\$(1,917)	-16.7%
Fire	8,727	9,873	(1,146)	-11.6%
Mobile Home	3,255	3,659	(404)	-11.0%
Commercial	1,109	1,166	(57)	-4.9%
Other	99	95	4	4.2%
	\$22,745	\$26,265	\$(3,520)	-13.4%

Net premiums earned for the three months ended September 30, 2008 were down as compared to 2007. The decrease in earned premium is primarily due to the reinstatement premiums related to Hurricane Dolly, Gustav, and Ike totaling \$8.2 million. Additionally, net premiums earned for the three months ended September 30, 2007 were reduced by \$4.5 million related to purchase accounting. The premium revenue is earned over the life of the policies, generally twelve months. On the date NLASCO was acquired by Hilltop, the unearned premium balance was adjusted to fair market value as required under GAAP.

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Policy Acquisition and Other Underwriting Expenses. Policy acquisition and other underwriting expenses for the three months ended September 30, 2008 and 2007 were as follows (in thousands):

	Three Months Ended September 30,			%
	2008	2007	Change	
Deferral and amortization of deferred policy acquisition costs	\$ 207	\$ (4,204)	\$ 4,411	-104.9%
Other underwriting expenses	10,529	13,153	(2,624)	-19.9%
Total policy acquisition and other underwriting expenses	10,736	8,949	1,787	20.0%
Other income excluding commission income	(706)	(813)	107	-13.2%
Total policy acquisition and other underwriting expenses including other income	\$ 10,030	\$ 8,136	\$ 1,894	23.3%
Net premiums earned	\$22,745	\$26,265	\$(3,520)	-13.4%
Expense ratio	44.1%	31.0%	13.1%	

Loss and Loss Adjustment Expenses. Loss and LAE are recognized based on formula and case basis estimates for losses reported with respect to direct business, estimates of unreported losses based on past experience and deduction of amounts for reinsurance placed with reinsurers. The loss and LAE ratio is calculated by taking the ratio of incurred losses and LAE to net premiums earned. The loss and LAE ratio for the three months ended September 30, 2008 and 2007 of 118.1% and 52.4%, respectively, has been adjusted to remove the effect of losses attributable to the prior owner. The increase in the loss and LAE ratio is due to several hurricanes that occurred in July and September 2008. The actual loss related to Hurricane Dolly, Gustav and Ike excluding reinstatement premium is \$14.0 million.

General and Administrative Expense. General and administrative expense for the three months ended September 30, 2008 was \$1.8 million, as compared to \$2.2 million for the three months ended September 30, 2007, a decrease of \$0.4 million, or 18%. This decrease was mainly due to decreases in salaries, benefits and travel costs, which were partially offset by an increase in related party management fees.

Depreciation and Amortization Expense. Depreciation and amortization expense for the three months ended September 30, 2008 was \$0.5 million, as compared to \$0.6 million for the three months ended September 30, 2007, a decrease of 17%.

Interest Expense. Interest expense for the three months ended September 30, 2008 was \$2.6 million, as compared to \$2.9 million for the three months ended September 30, 2007, a decrease of \$0.3 million, or 10%. The decrease in interest expense is due to the pay down of debt in the first quarter of 2008 and lower rates on our variable rate debt.

Minority Interest. Minority interest for the three months ended September 30, 2007 was \$0.01 million. Minority interest only affected 2007, as all minority interest holders were eliminated in conjunction with the closing of the asset sale on July 31, 2007.

Income Taxes. The Company had a \$9.1 million income tax benefit for the three months ended September 30, 2008, compared to \$77.6 million expense for the same period in 2007. The benefit in 2008 is primarily due to the tax benefit recorded as a result of operating losses of NLASCO and recognizing losses on the impairment of \$0.4 million on securities. The expense in 2007 is primarily due to the tax expense related to the gain on sale of discontinued operations of \$74.2 million.

Discontinued Operations. On July 31, 2007, the Company closed the sale of certain of its assets, including the operating assets of the Company's manufactured home businesses to American

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Residential Communities LLC, an affiliate of Farallon Capital Management, L.L.C., Helix Funds LLC, and GEM Realty Capital, Inc. The Company reclassified all operations included in this sale to discontinued operations and, for the third quarter of 2007, the discontinued loss was \$2.2 million and the gain on sale of discontinued operations was \$364.3 million.

Preferred Stock Dividend. On September 11, 2008, the HTH board of directors declared a quarterly cash dividend of \$0.5156 per share on each of the 5,000,000 outstanding shares of our Series A Preferred Stock, payable October 30, 2008, amounting to \$2.6 million. For the quarter ended September 30, 2007, the dividend declared also was \$0.5156 per share, or \$2.6 million.

Net Loss Attributable to Common Stockholders. As a result of the foregoing, our net loss attributable to common stockholders was \$6.2 million for the three months ended September 30, 2008, as compared to net income of \$291.7 million for the three months ended September 30, 2007. The principal reason for the loss in the third quarter of 2008 is due to an increase in loss and loss adjustment expense of \$14.0 million and \$8.2 million in reinstatement premium related to Hurricane Dolly, Gustav, and Ike. The principal reason for the income in the third quarter of 2007 is due to the sale of discontinued operations.

Comparison of the Nine Months Ended September 30, 2008 to the Nine Months Ended September 30, 2007

Revenue. Revenue for the nine months ended September 30, 2008 was \$66.7 million, as compared to \$87.7 million for the same period in 2007. Net premiums earned were \$83.0 million for the first nine months in 2008, as compared to \$69.5 million for 2007, such increase is primarily due to the fact that 2007 only included eight months of income from NLASCO. Net investment income was \$21.9 million for the first nine months of 2008, as compared to \$13.3 million for the same period in 2007, such increase is primarily due to the income generated on the net proceeds received from the sale of our manufactured housing businesses. We had a net realized loss on investments of \$42.9 million in the first nine months of 2008, due to the write down and subsequent sale of securities primarily owned by HTH. Other income was \$4.7 million for the first nine months in 2008, as compared to \$4.8 million for 2007, primarily due to the decrease in service revenue due to a soft insurance market, which was partially offset by the fact that 2007 only included eight months of income from NLASCO. Revenues related to the manufactured housing business lines have been reclassified to discontinued operations and are presented net in the caption "Loss from discontinued operations."

Underwriting Results. The following table shows the components of the Company's underwriting (loss) gain for the nine months ended September 30, 2008 and 2007. The Company's underwriting gain

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or loss consists of net premiums earned, less loss and LAE and policy acquisition and other underwriting expenses. The underwriting results are discussed below (in thousands).

	Nine Months Ended September 30,			% Change
	2008	2007	Change	
Direct premiums written	\$ 98,725	\$ 92,012	\$ 6,713	7.3%
Net premiums written	\$ 84,870	\$ 86,389	\$ (1,519)	-1.8%
Net premiums earned	\$ 83,017	\$ 69,462	\$ 13,555	19.5%
Loss and LAE	66,154	41,289	24,865	60.2%
Policy acquisition and other underwriting expenses	32,350	23,472	8,878	37.8%
Underwriting (loss) gain	\$(15,487)	\$ 4,701	\$(20,188)	-429.4%
Loss and LAE ratio	79.7%	59.4%	20.3%	
Policy acquisition and other underwriting expense ratio	36.4%	30.8%	5.6%	
Combined ratio	116.1%	90.2%	25.9%	

The Company seeks to operate at a combined ratio of no greater than 85.0%. Loss ratios are ratios that express the relationship of losses to premiums. Loss and LAE ratio is loss and LAE expenses divided by net premiums earned for the same period. Policy acquisition and other underwriting expense ratio is policy acquisition and other underwriting expense divided by net premiums earned for the same period. Combined ratio gives you the sum of both previous ratios. The increase in policy acquisition and other underwriting expenses is due to the benefit received in 2007 related to the purchase accounting of \$11.8 million.

Premiums. The property and casualty insurance industry is affected by soft and hard market business cycles. During a soft market, price competition tends to increase as insurers are willing to reduce premium rates in order to maintain growth in premium volume. The soft market makes it more difficult to attract new business, as well as retain exposures which are adequately priced. Although we recognize the need to remain competitive in the marketplace, the Company remains committed to its disciplined underwriting philosophy accepting only risks that are appropriately priced, while declining risks which are underpriced for the level of coverage provided.

Direct premiums written by major product line for the nine months ended September 30, 2008 and 2007, are presented in the table below (in thousands):

	Nine Months Ended September 30,			% Change
	2008	2007	Change	
Direct Premiums Written:				
Homeowners	\$41,537	\$40,788	\$ 749	1.8%
Fire	37,429	35,345	2,084	5.9%
Mobile Home	14,851	11,242	3,609	32.1%
Commercial	4,562	4,321	241	5.6%
Other	346	316	30	9.5%
	\$98,725	\$92,012	\$ 6,713	7.3%

Total direct premiums written increased for the nine months ended September 30, 2008 for all of the insurance products, due to the fact that 2007 only includes eight months. Direct premiums are down slightly over the same quarter last year, due to the overall soft insurance market.

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Net premiums written by major product line for the nine months ended September 30, 2008 and 2007, are presented in the table below (in thousands):

	Nine Months Ended September 30,			%
	2008	2007	Change	Change
Net Premiums Written				
Homeowners	\$35,708	\$41,334	\$(5,626)	-13.6%
Fire	32,176	31,336	840	2.7%
Mobile Home	12,766	9,590	3,176	33.1%
Commercial	3,921	3,847	74	1.9%
Other	299	282	17	6.0%
	\$84,870	\$86,389	\$(1,519)	-1.8%

Total net premiums written decreased for the nine months ended September 30, 2008 for the homeowners line of business due to the reinstatement premiums related to Hurricane Dolly, Gustav, and Ike totaling \$8.2 million. Net written premiums are down slightly over the same period last year, due to the overall soft insurance market.

Net premiums earned by major product line for the nine months ended September 30, 2008 and 2007, are presented in the table below (in thousands):

	Nine Months Ended September 30,			%
	2008	2007	Change	Change
Net Premiums Earned:				
Homeowners	\$34,929	\$30,629	\$ 4,300	14.0%
Fire	31,474	26,029	5,445	20.9%
Mobile Home	12,488	9,563	2,925	30.6%
Commercial	3,836	3,038	798	26.3%
Other	290	203	87	42.9%
	\$83,017	\$69,462	\$13,555	19.5%

Net premiums earned for the nine months ended September 30, 2008 were up as compared to 2007 due to the fact that 2007 only included eight months of income from NLASCO compared to nine months of income in 2008. The premium revenue is earned over the life of the policies, generally twelve months. On the date NLASCO was acquired by Hilltop, the unearned premium balance was adjusted to fair market value as required under GAAP.

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Policy Acquisition and Other Underwriting Expenses. Policy acquisition and other underwriting expenses for the nine months ended September 30, 2008 and 2007 were as follows (in thousands):

	Nine Months Ended September 30,			%
	2008	2007	Change	
Deferral and amortization of deferred policy acquisition costs	\$ (2,366)	\$ (7,288)	\$ 4,922	-67.5%
Other underwriting expenses	34,716	30,760	3,956	12.9%
Total policy acquisition and other underwriting expenses	32,350	23,472	8,878	37.8%
Other income excluding commission income	(2,173)	(2,074)	(99)	4.8%
Total policy acquisition and other underwriting expenses including other income	\$ 30,177	\$ 21,398	\$ 8,779	41.0%
Net premiums earned	\$ 83,017	\$ 69,462	\$ 13,555	19.5%
Expense ratio	36.4%	30.8%	5.5%	

Loss and Loss Adjustment Expenses. Loss and LAE are recognized based on formula and case basis estimates for losses reported with respect to direct business, estimates of unreported losses based on past experience and deduction of amounts for reinsurance placed with reinsurers. The loss and LAE ratio is calculated by taking the ratio of incurred losses and LAE to net premiums earned. The loss and LAE ratio for the nine months ended September 30, 2008 and 2007 of 79.7% and 59.4%, respectively, has been adjusted to remove the effect of losses attributable to the prior owner. The increase in the loss and LAE ratio is due to several severe spring storms and several hurricanes that occurred in July and September 2008. The actual loss related to Hurricane Dolly, Gustav and Ike, excluding reinstatement premium, was \$14.0 million.

General and Administrative Expense. General and administrative expense for the nine months ended September 30, 2008 was \$7.2 million, as compared to \$7.4 million for the nine months ended September 30, 2007, a decrease of \$0.2 million, or 3%. This decrease was mainly due to a decrease in salaries, benefits, and professional fees, which were offset by \$1.4 million in acquisition costs expensed in 2008. The acquisition costs related to expenses incurred in connection with a possible transaction, that, as of the end of second quarter of 2008, we determined no longer to pursue.

Depreciation and Amortization Expense. Depreciation and amortization expense was \$1.6 million for the nine months ended September 30, 2008 and 2007.

Interest Expense. Interest expense for the nine months ended September 30, 2008 was \$7.9 million, as compared to \$8.2 million for the nine months ended September 30, 2007, a decrease of \$0.3 million, or 4%. The decrease in interest expense is due to the pay down of debt in the first quarter of 2008 and lower rates on variable rate debt, partially offset by only eight months of interest expense on the debt of NLASCO.

Minority Interest. Minority interest for the nine months ended September 30, 2007 was \$0.1 million. Minority interest only affected 2007, as all minority interest holders were eliminated in conjunction with the closing of the asset sale on July 31, 2007.

Income Taxes. The Company had a \$21.6 million income tax benefit for the nine months ended September 30, 2008, compared to \$78.6 million expense for the same period in 2007. The benefit in 2008 is primarily due to the tax benefit recorded as a result of recognizing losses on the impairment of \$15.0 million on securities and operating losses of NLASCO. The expense in 2007 is primarily due to the tax expense related to the gain on sale of discontinued operations of \$76.6 million.

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Discontinued Operations. On July 31, 2007, the Company closed the sale of certain of its assets, including the operating assets of the Company's manufactured home businesses to American Residential Communities LLC, an affiliate of Farallon Capital Management, L.L.C., Helix Funds LLC, and GEM Realty Capital, Inc. The Company reclassified all operations included in this sale to discontinued operations and, for 2007, the discontinued loss was \$11.1 million and the gain on sale of discontinued operations was \$363.9 million.

Preferred Stock Dividend. On April 9, 2008, the HTH board of directors declared a quarterly cash dividend of \$0.5156 per share on each of the 5,000,000 outstanding shares of our Series A Preferred Stock, payable April 30, 2008, amounting to \$2.6 million. On June 12, 2008, the HTH board of directors declared a quarterly cash dividend of 0.5156 per share on each of the 5,000,000 outstanding shares of our Series A Preferred Stock, payable July 30, 2008, amounting to \$2.6 million. On September 11, 2008, the HTH board of directors declared a quarterly cash dividend of 0.5156 per share on each of the 5,000,000 outstanding shares of our Series A Preferred Stock, payable October 30, 2008, amounting to \$2.6 million. For the nine months ended September 30, 2007, the dividends declared were also \$1.5468 per share, or \$7.7 million.

Net Loss Attributable to Common Stockholders. As a result of the foregoing, our net loss attributable to common stockholders was \$34.7 million for the nine months ended September 30, 2008, as compared to \$272.8 million of net income for the nine months ended September 30, 2007. The principal reason for the loss in the first nine months of 2008 is the write down and subsequent sale of stock held by HTH of \$41.9 million, hurricane losses of \$14.0 million, and reinstatement premium of \$8.2 million, which was partially offset by the additional month of income generated by NLASCO in 2008.

LIQUIDITY AND CAPITAL RESOURCES

General

Hilltop is a holding company whose assets primarily consist of the stock of its subsidiaries and invested assets with a combined value of \$1,150 million at September 30, 2008. On July 31, 2007, the Company closed the sale of substantially all of its assets, including the operating assets used in the Company's manufactured home communities business and its manufactured home retail sales and financing businesses, and received gross proceeds of \$889.3 million in cash. Of this amount, as of September 30, 2008, the Company had invested approximately \$735 million in overnight deposits at JP Morgan Chase, Bank of America, and Wells Fargo. These investments are in excess of the Federal Deposit Insurance Corporation insurance limit, however, the Company does not believe that it is exposed to any significant credit risk on cash.

Hilltop is seeking to make opportunistic acquisitions with its available cash and, if necessary or appropriate, from additional equity or debt financing sources.

At September 30, 2008, we had approximately \$769.1 million of cash and cash equivalents and \$143.7 million of investments, as compared to \$783.0 million of cash and cash equivalents and \$191.0 million of investments as of December 31, 2007.

As of September 30, 2008, our short-term liquidity needs included (a) funds for dividend payments on our \$125 million Series A cumulative redeemable preferred stock bearing a dividend rate of 8.25% per annum (approximately \$10.3 million annually), (b) funds to pay our insurance claims and (c) funds to service our debt.

Restrictions on Dividends and Distributions

Aside from investment income on Hilltop's invested assets, as a holding company, Hilltop relies on dividends and other permitted distributions from its subsidiaries. The payment of dividends from

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Hilltop's insurance subsidiaries, NLIC and ASIC, are subject to significant limitations under debt agreements, which limit their ability to declare and pay dividends in the event of a default.

Additionally, under Texas State Insurance Law for property and casualty companies, all dividends must be distributed out of earned surplus only. Furthermore, without the prior approval of the Commissioner of Texas Department of Insurance, dividends cannot be declared or distributed that exceed the greater of ten percent of the company's surplus, as shown by its last statement on file with the Commissioner, or 100% of net income for such period. NLIC and ASIC paid dividends totaling \$14.0 million to NLASCO in March 2008. At September 30, 2008, the maximum additional dividends that may be paid to NLASCO in 2008 without regulatory approval is approximately \$7.3 million.

Regulations of the Texas Department of Insurance require insurance companies to maintain minimum levels of statutory surplus to ensure their ability to meet their obligations to policyholders. At September 30, 2008, the Company's insurance subsidiaries had statutory surplus in excess of the minimum required.

Also, the National Association of Insurance Commissioners, or NAIC, has adopted risk-based capital, or "RBC", requirements for insurance companies that establish minimum capital requirements relating to insurance risk, assesses credit risk, interest rate risk and business risk. The formula is used by the NAIC and certain state insurance regulators as an early warning tool to identify companies that require additional scrutiny or regulatory action. At September 30, 2008, the Company's insurance subsidiaries' RBC ratio exceeded the level at which regulatory action would be required.

We believe that restrictions on liquidity resulting from restrictions on the payments of dividends by our subsidiary companies will not have a material impact on our ability to carry out our normal business activities, including dividend payments on our Series A cumulative redeemable preferred stock and debt payments on our senior exchangeable notes.

Sources and Uses of Funds

Our liquidity requirements are met primarily by positive cash flow from our normal operations and investment activity. Primary sources of cash from insurance operations are premiums and other considerations, net investment income and investment sales and maturities. Primary uses of cash include payments of benefits, operating expenses and income taxes and purchases of investments.

Our primary investment objectives are to preserve capital and manage for a total rate of return in excess of a specified benchmark portfolio. Our strategy is to purchase securities in sectors that represent the most attractive relative value. Bonds, cash and short-term investments constitute \$904.6 million, or 99.1%, of our cash and investments at September 30, 2008. Although there is no intent to dispose of these investments at this time, our bonds are substantially in readily marketable securities.

Our investment committee meets regularly to review the portfolio performance and investment markets in general. Our management generally meets monthly to review the performance of investments and monitor market conditions for investments that would warrant any revision to investment guidelines.

Cash used in operations was \$3.4 million for the nine months ended September 30, 2008, primarily due to payment of \$10.1 million in state income taxes. Cash provided by operations was \$9.7 million for the nine months ended September 30, 2007, due to the adjustments related to discontinued operations of \$277.8 million, which was partially offset by the increase in unearned premiums at NLASCO of \$18.1 million.

Cash used in investing activities was \$17.3 million in the nine months ended September 30, 2008, compared with cash provided by investing activities of \$795.1 million in the same period in 2007. The

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cash used in investing activities for the nine months ended September 30, 2008 is primarily due to the designation of \$18.5 million as restricted cash. This amount was designated as restricted because of a guaranty provided by us with respect to a third-party loan made to a target we were pursuing. The loan matures in February 2009 and is secured by auction rate securities pledged by the target. We, however, are no longer pursuing this target. Cash provided by investing activities for the nine months ended September 30, 2008 is due to proceeds from the sale of assets related to discontinued operations.

Cash used in financing activities was \$11.7 million for the nine months ended September 30, 2008, compared with cash provided by financing activities of \$61.4 million in the same period in 2007. The decrease in cash from financing activities for 2008 was due primarily to the repayment of \$4.0 million in debt and payment of \$7.7 million in preferred dividends. The cash generated in the first nine months of 2007 was due to proceeds received from our common stock rights offering and stock issuances in connection with the NLASCO acquisition.

We believe that existing cash and investment balances, when combined with anticipated cash flows from operations and dividends from our insurance companies, will be adequate to meet our expected liquidity needs for the reasonably foreseeable future. We will continue to pursue and investigate possible strategic investments. In regards to strategic acquisitions, we may need to secure external financing. We cannot assure you that we will be successful in obtaining any such financing or in the implementation of our business plan.

Inflation

Inflation in the U.S. has been relatively low in recent years and did not have a material impact on our results of operations for the nine months ended September 30, 2008 and 2007. Although the impact of inflation has been relatively insignificant in recent years, it remains a factor in the United States economy and may increase the cost of acquiring or replacing property and equipment and the costs of labor and utilities.

COMMITMENTS

NLASCO's loss reserves do not have contractual maturity dates. However, based on historical payment patterns, the following table estimates when management expects the loss reserves to be paid. The timing of claim payments is subject to significant uncertainty. NLASCO maintains a portfolio of investments with varying maturities to provide adequate cash flows for the payment of claims.

	Reserves (in thousands)
2008	\$ 82,096
2009	39,093
2010	5,212
2011	1,303
2012	1,303
Thereafter	1,303
	\$ 130,310

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Our future income, cash flows and fair values relevant to financial instruments are dependent upon market interest rates. Market risk relates to the risk of loss from adverse changes in market prices and interest rates. We may use some derivative financial instruments to manage, or hedge, interest rate risks related to our borrowings from time to time. We do not use derivatives for trading or speculative purposes and only enter into contracts with major financial institutions based on their credit rating and other factors. As of September 30, 2008, we had no derivative financial instruments.

As of September 30, 2008, our total debt outstanding was approximately \$138.4 million, comprised of approximately \$90.9 million, or 65.7%, of indebtedness subject to fixed interest rates and approximately \$47.5 million, or 34.3% of our total consolidated debt, subject to variable interest rates.

If LIBOR and the prime rate were to increase by one eighth of one percent (0.125%), the increase in interest expense on the variable rate debt would decrease future earnings and cash flows by approximately \$59,000 annually.

Interest risk amounts were determined by considering the impact of hypothetical interest rates on our financial instruments. These analyses do not consider the effect of any change in overall economic activity that could occur in that environment. Further, in the event of a change of that magnitude, we may take actions to further mitigate our exposure to the change. However, due to the uncertainty of the specific actions that would be taken and their possible effects, these analyses assume no changes in our financial structure.

The fair value of debt outstanding as of September 30, 2008 was approximately \$151.3 million.

The following table sets forth certain information with respect to our indebtedness outstanding as of September 30, 2008 (in thousands).

	Principal Commitments		
	Fixed	Variable	Total
2008	\$	\$ 18	\$ 18
2013 and Thereafter	90,850	47,500	138,350
Commitments	\$90,850	\$47,518	\$138,368

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ITEM 4. CONTROLS AND PROCEDURES

(a)

Disclosure Controls and Procedures. The Company's management, with the participation of the Company's Chief Executive Officer and Chief Accounting Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based on such evaluation, the Company's Chief Executive Officer and Chief Accounting Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act and are effective in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Accounting Officer, as appropriate to allow timely decisions regarding required disclosure.

(b)

Changes in internal control over financial reporting. There have not been any changes in our internal control over financial reporting (as defined in Rule 13a-15(f) promulgated under the Securities Exchange Act of 1934) during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the risk factors discussed in our Annual Report on Form 10-K for the year ended December 31, 2007, which could materially affect our business, financial condition or future results. The risks described in this report and in our Annual Report on Form 10-K are not the only risks facing us. 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 or future results.

Difficult market conditions may adversely affect our investments and business. The capital and credit markets have been experiencing volatility and disruption for more than 12 months. Recently, the volatility and disruption has reached unprecedented levels, resulting in dramatic declines. This downward pressure has negatively affected the performance of our investments, which has resulted in the write-down of those investments. These write-downs, when determined to be other than temporary, reduce our earnings for that period. If current levels of market disruption and volatility continue or worsen, there can be no assurance that we will not experience additional losses on our investments and reductions to earnings.

In addition, falling housing prices, increasing home foreclosures, unemployment and under-employment may negatively affect our insurance operations. Combined with the market turmoil described above, these conditions have led to increased levels of commercial and consumer delinquencies, lack of consumer confidence and a widespread reduction of business and consumer activity generally. Resulting effects of these and other conditions may include a decrease in the number of new policies and renewals written or changes in payment patterns or increases in delinquencies or defaults on existing policies. If these conditions continue or worsen, our business and results of operations may be adversely affected.

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Hilltop Holdings Inc. held its 2008 Annual Meeting of Stockholders, or Annual Meeting, on July 9, 2008. At the Annual Meeting, the stockholders of Hilltop Holdings Inc. elected Rhodes Bobbitt, W. Joris Brinkerhoff, Charles R. Cummings, Gerald J. Ford, J. Markham Green, William T. Hill, Jr., W. Robert Nichols, C. Clifton Robinson, James R. Staff, Carl B. Webb and Larry D. Willard to serve until our 2009 Annual Meeting.

The total number of shares entitled to vote at our Annual Meeting was 56,448,098 shares of common stock. A total of 44,969,714 shares of common stock were represented in person or by proxy at the Annual Meeting. The following table sets forth, with respect to each of the directors elected, the number of votes cast for or withheld with respect to his election.

Nominee	Votes	
	Votes For	Withheld
Rhodes Bobbitt	44,666,915	302,799
W. Joris Brinkerhoff	44,606,543	303,171
Charles R. Cummings	44,666,249	303,465
Gerald J. Ford	42,951,274	2,018,440
J. Markham Green	44,666,895	302,819
William T. Hill, Jr.	44,665,915	303,799
W. Robert Nichols	44,666,915	302,799
C. Clifton Robinson	44,649,190	320,524
James R. Staff	42,968,859	2,000,855
Carl B. Webb	44,649,218	320,496
Larry D. Willard	44,647,684	322,030

Our stockholders also ratified the selection of PricewaterhouseCoopers LLP as our independent registered public accounting firm. There were 44,921,535 votes cast for ratification, 16,755 votes against and 31,424 shares abstained from voting. There were no broker non-votes on this matter.

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ITEM 6. EXHIBITS

- (a) Exhibits:
See Exhibit Index

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SIGNATURES

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

HILLTOP HOLDINGS INC.

Date: November 10, 2008

By: /s/ DARREN PARMENTER

Darren Parmenter
Senior Vice President and Chief Accounting Officer
(Principal financial and accounting officer and duly
authorized officer)

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EXHIBIT INDEX

Exhibit Number	Exhibit Title
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended.
31.2	Certification of Chief Accounting Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended.
32.1	Certification of Chief Executive Officer of Hilltop Holdings Inc., pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Accounting Officer of Hilltop Holdings Inc., pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.