STAGE STORES INC
Form 10-Q
June 14, 2018

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

Form 10-Q

(Mark One)
þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended May 5, 2018

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

For the transition period from ______ to ______

Commission File Number 1-14035

Stage Stores, Inc.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| NEVADA | 91-1826900 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| | |
| 2425 West Loop South, Houston, Texas | 77027 |
| (Address of principal executive offices) | (Zip Code) |

(800) 579-2302
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer", "smaller reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

| | |
|---|---|
| Large accelerated filer o | Accelerated filer þ |
| Non-accelerated filer o (Do not check if a smaller reporting company) | Smaller reporting company o |
| | Emerging growth company o |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of June 7, 2018, there were 28,233,933 shares of the registrant’s common stock outstanding.

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
Stage Stores, Inc.
Condensed Consolidated Balance Sheets
(in thousands, except par value)
(Unaudited)

| | May 5, 2018 | February 3, 2018 As Adjusted | April 29, 2017 As Adjusted |
|---|---|---|---|
| ASSETS | | | |
| Cash and cash equivalents | $29,091 | $21,250 | $21,688 |
| Merchandise inventories, net | 477,562 | 438,377 | 475,048 |
| Prepaid expenses and other current assets | 48,762 | 52,407 | 48,195 |
| Total current assets | 555,415 | 512,034 | 544,931 |
| | | | |
| Property, equipment and leasehold improvements, net of accumulated depreciation of $713,867, $699,788 and $709,448, respectively | 244,214 | 252,788 | 277,285 |
| Intangible assets | 17,135 | 17,135 | 15,235 |
| Other non-current assets, net | 23,715 | 24,449 | 24,164 |
| Total assets | $840,479 | $806,406 | $861,615 |
| | | | |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | |
| Accounts payable | $128,883 | $145,991 | $137,289 |
| Accrued expenses and other current liabilities | 67,513 | 67,427 | 71,897 |
| Total current liabilities | 196,396 | 213,418 | 209,186 |
| | | | |
| Long-term debt obligations | 265,469 | 180,350 | 219,756 |
| Other long-term liabilities | 66,029 | 68,524 | 73,610 |
| Total liabilities | 527,894 | 462,292 | 502,552 |
| | | | |
| Commitments and contingencies | | | |
| | | | |
| Common stock, par value $0.01, 100,000 shares authorized, 33,111, 32,806 and 32,611 shares issued, respectively | 331 | 328 | 326 |
| Additional paid-in capital | 420,091 | 418,658 | 412,548 |
| Treasury stock, at cost, 5,175 shares, respectively | (43,339) | (43,298) | (43,347) |
| Accumulated other comprehensive loss | (4,978) | (5,177) | (5,517) |
| Accumulated deficit | (59,520) | (26,397) | (4,947) |
| Total stockholders' equity | 312,585 | 344,114 | 359,063 |
| Total liabilities and stockholders' equity | $840,479 | $806,406 | $861,615 |

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

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Stage Stores, Inc.
Condensed Consolidated Statements of Operations and Comprehensive Loss
(in thousands, except per share data)
(Unaudited)

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 As Adjusted |
| Net sales | $344,229 | $308,607 |
| Credit income | 15,514 | 12,928 |
| Total revenues | 359,743 | 321,535 |
| Cost of sales and related buying, occupancy and distribution expenses | 281,741 | 246,389 |
| Selling, general and administrative expenses | 107,277 | 101,437 |
| Interest expense | 2,253 | 1,586 |
| Loss before income tax | (31,528 ) | (27,877 ) |
| Income tax expense (benefit) | 150 | (8,890 ) |
| Net loss | $(31,678 ) | $(18,987 ) |
| | | |
| Other comprehensive income: | | |
| Amortization of employee benefit related costs, net of tax of $0 and $80, respectively | $199 | $131 |
| Total other comprehensive income | 199 | 131 |
| Comprehensive loss | $(31,479 ) | $(18,856 ) |
| | | |
| Basic loss per share data: | | |
| Basic loss per share | $(1.14 ) | $(0.70 ) |
| Basic weighted average shares outstanding | 27,765 | 27,268 |
| | | |
| Diluted loss per share data: | | |
| Diluted loss earnings per share | $(1.14 ) | $(0.70 ) |
| Diluted weighted average shares outstanding | 27,765 | 27,268 |

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

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Stage Stores, Inc.
Condensed Consolidated Statements of Cash Flows
(in thousands)
(Unaudited)

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 As Adjusted |
| Cash flows from operating activities: | | |
| Net loss | $(31,678) | $(18,987) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation and amortization of long-lived assets | 15,151 | 16,377 |
| Gain on retirements of property, equipment and leasehold improvements | (30) | (452) |
| Deferred income taxes | — | (1,117) |
| Stock-based compensation expense | 1,558 | 2,182 |
| Amortization of debt issuance costs | 74 | 72 |
| Deferred compensation obligation | 41 | 61 |
| Amortization of employee benefit related costs | 199 | 211 |
| Construction allowances from landlords | — | 998 |
| Other changes in operating assets and liabilities: | | |
| Increase in merchandise inventories | (39,185) | (31,999) |
| Decrease (increase) in other assets | 4,303 | (7,193) |
| (Decrease) increase in accounts payable and other liabilities | (19,088) | 39,534 |
| Net cash used in operating activities | (68,655) | (313) |
| | | |
| Cash flows from investing activities: | | |
| Additions to property, equipment and leasehold improvements | (6,930) | (7,359) |
| Proceeds from insurance and disposal of assets | 45 | 1,223 |
| Business acquisition | — | (33,843) |
| Net cash used in investing activities | (6,885) | (39,979) |
| | | |
| Cash flows from financing activities: | | |
| Proceeds from revolving credit facility borrowings | 164,071 | 153,311 |
| Payments of revolving credit facility borrowings | (78,310) | (96,559) |
| Payments of long-term debt obligations | (731) | (4,083) |
| Payments of debt issuance costs | — | (8) |
| Payments for stock related compensation | (204) | (257) |
| Cash dividends paid | (1,445) | (4,227) |
| Net cash provided by financing activities | 83,381 | 48,177 |
| Net increase in cash and cash equivalents | 7,841 | 7,885 |
| | | |
| Cash and cash equivalents: | | |
| Beginning of period | 21,250 | 13,803 |
| End of period | $29,091 | $21,688 |
| | | |
| Supplemental disclosures including non-cash investing and financing activities: | | |
| Interest paid | $2,116 | $1,525 |
| Income taxes refunded | $(180) | $(437) |

| | | |
|---|---|---|
| Unpaid liabilities for capital expenditures | $2,597 | $6,156 |

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

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Stage Stores, Inc.
Condensed Consolidated Statement of Stockholders’ Equity
For the Three Months Ended May 5, 2018
(in thousands, except per share data)
(Unaudited)

| | Common Stock | | Additional Paid-in Capital | Treasury Stock | | Accumulated Other Comprehensive Loss | Accumulated Deficit | Total |
|---|---|---|---|---|---|---|---|---|
| | Shares | Amount | | Shares | Amount | | | |
| Balance at February 3, 2018 | 32,806 | $ 328 | $418,658 | (5,175) | $(43,298) | $ (5,177) | $ (26,397) | $344,114 |
| Net loss | — | — | — | — | — | — | (31,678) | (31,678) |
| Other comprehensive income | — | — | — | — | — | 199 | — | 199 |
| Dividends on common stock, $0.05 per share | — | — | — | — | — | — | (1,445) | (1,445) |
| Deferred compensation | — | — | 41 | — | (41) | — | — | — |
| Issuance of equity awards, net | 305 | 3 | (3) | — | — | — | — | — |
| Tax withholdings paid for net settlement of stock awards | — | — | (163) | — | — | — | — | (163) |
| Stock-based compensation expense | — | — | 1,558 | — | — | — | — | 1,558 |
| Balance at May 5, 2018 | 33,111 | $ 331 | $420,091 | (5,175) | $(43,339) | $ (4,978) | $ (59,520) | $312,585 |

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

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Stage Stores, Inc.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

NOTE 1 - BASIS OF PRESENTATION

The accompanying condensed consolidated financial statements of Stage Stores, Inc. and its subsidiary (“we,” “us” or “our”) have been prepared in accordance with the requirements of the U.S. Securities and Exchange Commission (“SEC”) for interim financial information and do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (“GAAP”) for complete financial statements. Those adjustments that are, in the opinion of management, necessary for a fair presentation of the results of the interim periods have been made. Results of operations for such interim periods are not necessarily indicative of the results of operations for a full year due to seasonality and other factors. The condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto filed with our Annual Report on Form 10-K for the year ended February 3, 2018 (“Form 10-K”).

We are a retailer of trend-right, moderately priced, name-brand apparel, accessories, cosmetics, footwear and home goods. As of May 5, 2018, we operated in 42 states through 773 BEALLS, GOODY’S, PALAIS ROYAL, PEEBLES and STAGE specialty department stores and 59 GORDMANS off-price stores, as well as an e-commerce website. Our department stores are predominantly located in small towns and rural communities. Our off-price stores are predominantly located in mid-sized, non-rural Midwest markets.

References to a particular year are to our fiscal year, which is the 52- or 53-week period ending on the Saturday closest to January 31st of the following calendar year. For example, a reference to “2018” is a reference to the fiscal year ending February 2, 2019, and “2017” is a reference to the fiscal year ended February 3, 2018. Fiscal years 2018 and 2017 are comprised of 52 weeks and 53 weeks, respectively. References to the “three months ended May 5, 2018” and “three months ended April 29, 2017” are for the respective 13-week fiscal quarters. References to quarters relate to our fiscal quarters.

On April 7, 2017, we acquired select assets of Gordmans Stores, Inc. and its subsidiaries through a bankruptcy auction (“Gordmans Acquisition”). The results of the Gordmans branded stores that we operated since the Gordmans Acquisition are included in our condensed consolidated statements of operations (see Note 9).

Recently Adopted Accounting Pronouncements. In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, Revenue from Contracts with Customers (Topic 606), and subsequently issued related ASUs, which were incorporated into Topic 606. Under Topic 606, revenue is recognized when a customer obtains control of promised goods or services in an amount that reflects the consideration the entity expects to be entitled to in exchange for those goods or services. The standard establishes a five-step revenue recognition model, which includes (i) identifying the contract with the customer, (ii) identifying the separate performance obligations in the contract, (iii) determining the transaction price, (iv) allocating the transaction price to the separate performance obligations, and (v) recognizing revenue when each performance obligation is satisfied. The standard also requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. To determine the impact of the new standard on our financial statements, we reviewed representative transactions across our revenue streams and compared our historical accounting practices to the new standard. On February 4, 2018, we adopted the new standard using the full retrospective method. As a result of the adoption of ASU 2014-09, the condensed consolidated statements of operations reflect the reclassification of credit income related to our private label credit card program from selling, general and administrative expenses to revenue. In addition, the condensed consolidated balance sheets and condensed consolidated statement of cash flows reflect the reclassification of the asset for the right to recover merchandise returned from merchandise inventories to prepaid expenses and other current assets. The tables that follow depict the impact of the reclassification adjustments on the prior period financial statement presentations.

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The condensed consolidated balance sheets reflect the reclassification of the asset for the right to recover merchandise returned from merchandise inventories to prepaid expenses and other current assets.

Condensed Consolidated Balance Sheets (in thousands)

| | February 3, 2018 As previously reported | ASU 2014-09 Adjustments | February 3, 2018 As adjusted |
|---|---|---|---|
| Assets: | | | |
| Merchandise inventories, net | $ 439,735 | $ (1,358 ) | $ 438,377 |
| Prepaid expenses and other current assets | 51,049 | 1,358 | 52,407 |

| | April 29, 2017 As previously reported | ASU 2014-09 Adjustments | April 29, 2017 As adjusted |
|---|---|---|---|
| Assets: | | | |
| Merchandise inventories, net | $ 477,189 | $ (2,141 ) | $ 475,048 |
| Prepaid expenses and other current assets | 46,054 | 2,141 | 48,195 |

The condensed consolidated statement of operations reflects the reclassification of credit income from selling, general and administrative expenses to revenue.

Condensed Consolidated Statement of Operations and Comprehensive Loss (in thousands)

| | Three Months Ended April 29, 2017 As previously reported | ASU 2014-09 Adjustments | Three Months Ended April 29, 2017 As adjusted |
|---|---|---|---|
| Net sales | $ 308,607 | $ — | $ 308,607 |
| Credit income | — | 12,928 | 12,928 |
| Total revenues | 308,607 | 12,928 | 321,535 |
| Selling, general and administrative expenses | 88,509 | 12,928 | 101,437 |

The condensed consolidated statement of cash flows reflects the reclassification of the asset for the right to recover merchandise returned from merchandise inventories to prepaid expenses and other current assets.

Condensed Consolidated Statement of Cash Flows (in thousands)

| | Three Months Ended | | Three Months Ended |
|---|---|---|---|

| | April 29, 2017 As previously reported | ASU 2014-09 Adjustments | April 29, 2017 As adjusted |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Increase in merchandise inventories | $ (33,106 ) | $ 1,107 | $ (31,999 ) |
| Increase in other assets | (6,086 ) | (1,107 ) | (7,193 ) |

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In March 2017, the FASB issued ASU 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, which requires the service cost component of net periodic benefit cost to be presented in the same income statement line item as other employee compensation costs arising from services rendered during the period. If a subtotal for operating income is shown on the income statement, then the other components of the net periodic benefit cost must be presented separately from the line item that includes the service cost and outside of any subtotal of operating income. The new standard also requires disclosure of the line item(s) in the income statement that include net periodic benefit costs. Additionally, only the service cost component of the net periodic benefit cost is eligible for capitalization. The change in presentation of service cost must be applied retrospectively, while the capitalization of service cost must be applied on a prospective basis. On February 4, 2018, we adopted ASU 2017-07. The pension plan that we sponsor is frozen, and therefore, service costs no longer accrue under the plan. The adoption of the new standard did not change the presentation of our condensed consolidated statements of operations.

Recent Accounting Pronouncements Not Yet Adopted. In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The guidance in this ASU supersedes the leasing guidance in Topic 840, Leases. The new standard requires lessees to recognize a right-of-use asset and lease liability on the balance sheet for all leases with terms longer than 12 months. We plan to make a policy election that will keep leases with an initial term of 12 months or less off the balance sheet and will result in recognizing those lease payments in the consolidated statements of operations on a straight-line basis over the lease term. Consistent with current GAAP, the recognition, measurement and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a financing or operating lease. However, unlike current GAAP, which requires only capital leases to be recognized on the balance sheet, ASU 2016-02 will require both types of leases to be recognized on the balance sheet. As a result, lessees will be required to put most leases on their balance sheets while recognizing expense on their income statements in a manner similar to current accounting. In addition, this guidance requires disclosures about the amount, timing and uncertainty of cash flows arising from leases. The new standard will be effective for us in the first quarter of fiscal 2019, which begins on February 3, 2019. A modified retrospective transition approach is required for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. We continue to evaluate the impact that the adoption of this ASU will have on our consolidated financial statements and disclosures, including the effect of certain optional practical expedients permitted under the transition guidance. Based on our assessment to date, we expect the adoption of ASU 2016-02 will result in a significant increase in lease-related assets and liabilities on our consolidated balance sheets. The ultimate impact of adopting the new standard will depend on our lease portfolio as of the adoption date.

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NOTE 2 - DEBT OBLIGATIONS

Debt obligations for each period presented consisted of the following (in thousands):

| | May 5, 2018 | February 3, 2018 | April 29, 2017 |
|---|---|---|---|
| Revolving Credit Facility | $265,049 | $ 179,288 | $216,454 |
| Finance obligations | 1,310 | 1,549 | 2,429 |
| Other financing | 2,006 | 2,498 | 3,949 |
| Total debt obligations | 268,365 | 183,335 | 222,832 |
| Less: Current portion of debt obligations | 2,896 | 2,985 | 3,076 |
| Long-term debt obligations | $265,469 | $ 180,350 | $219,756 |

We have a $400.0 million senior secured revolving credit facility (“Revolving Credit Facility”) with a seasonal increase to $450.0 million and a $25.0 million letter of credit sublimit. The Revolving Credit Facility matures on December 16, 2021.

We use the Revolving Credit Facility to provide financing for working capital and general corporate purposes, as well as to finance capital expenditures and to support our letter of credit requirements. Borrowings are limited to the availability under a borrowing base that is determined principally on eligible inventory as defined by the Revolving Credit Facility agreement. Inventory, cash and cash equivalents are pledged as collateral. The daily interest rates are determined by a prime rate or LIBOR, plus an applicable margin, as set forth in the Revolving Credit Facility agreement. For the three months ended May 5, 2018, the weighted average interest rate on outstanding borrowings and the average daily borrowings were 3.15% and $247.5 million, respectively.

Letters of credit issued under the Revolving Credit Facility support certain merchandise purchases and collateralize retained risks and deductibles under various insurance programs. At May 5, 2018, outstanding letters of credit totaled approximately $6.2 million. These letters of credit expire within 12 months of issuance, but may be renewed. Excess availability under the Revolving Credit Facility at May 5, 2018 was $67.2 million.

The Revolving Credit Facility agreement contains covenants which, among other things, restrict, based on required levels of excess availability, (i) the amount of additional debt or capital lease obligations, (ii) the payment of dividends to $30 million in a fiscal year, and (iii) the repurchase of common stock under certain circumstances. The agreement also contains a fixed charge coverage ratio covenant in the event excess availability is below a defined threshold or an event of default has occurred. At May 5, 2018, we were in compliance with the debt covenants of the Revolving Credit Facility agreement and we expect to remain in compliance.

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NOTE 3 - REVENUE

Net Sales

We recognize revenue for merchandise sales, net of expected returns and sales tax, at the time the guest takes possession of the merchandise. When merchandise is shipped to our guests, we estimate receipt based on historical experience. The liability for sales returns is estimated based on historical return rates and sales for the return period. We recognize a return asset and corresponding adjustment to cost of sales for our right to recover returned merchandise. At each financial reporting date, we assess our estimates of expected returns, refund liabilities and return assets. For merchandise sold in our stores and online, tender is accepted at the point of sale. When we receive payment before the guest has taken possession of the merchandise, the amount received is recorded as deferred revenue until the transaction is complete. Performance obligations for unfulfilled merchandise orders are typically satisfied within one week. Shipping and handling fees charged to guests relate to fulfillment activities and are included in net sales with the corresponding costs recorded in cost of sales.

We record deferred revenue for the sale of gift cards and merchandise credits issued for returned merchandise, and we recognize revenue in net sales upon redemption. Gift card and merchandise credit redemptions typically occur within 12 months of the date of issuance with the majority redeemed within the first three months. Our gift cards and merchandise credits do not expire. Based on historical redemption rates, a small percentage of gift cards and merchandise credits will never be redeemed. We recognize estimated breakage income for gift cards and merchandise credits that will never be redeemed in proportion to actual historical redemption patterns.

Under our loyalty programs, members can accumulate points, based on their spending levels, toward earning a reward certificate that can be redeemed for future merchandise purchases. Points earned by loyalty members reset to zero at the end of each calendar year. Reward certificates expire 30 days and 60 days after the date of issuance for our department stores and off-price stores, respectively. We allocate and defer a portion of our sales to reward certificates expected to be earned, based on the relative stand-alone sales transaction price and reward certificate value, and then recognize the reward certificate as a net sale when it is redeemed.

The following table sets forth the composition of net sales by merchandise category for each period presented (in thousands):

| | Three Months Ended | | | | | |
|---|---|---|---|---|---|---|
| | May 5, 2018 | | | April 29, 2017 | | |
| Merchandise Category | Department Stores | Off-price Stores | Total Company | Department Stores | Off-price Stores | Total Company |
| Women’s | $103,487 | $19,967 | $123,454 | $113,392 | $5,104 | $118,496 |
| Men’s | 41,336 | 7,545 | 48,881 | 42,472 | 2,069 | 44,541 |
| Children's | 29,078 | 8,096 | 37,174 | 32,688 | 1,933 | 34,621 |
| Apparel | 173,901 | 35,608 | 209,509 | 188,552 | 9,106 | 197,658 |
| | | | | | | |
| Footwear | 44,483 | 4,819 | 49,302 | 45,643 | 405 | 46,048 |
| Accessories | 18,872 | 4,366 | 23,238 | 20,262 | 1,595 | 21,857 |
| Cosmetics/Fragrances | 31,186 | 2,482 | 33,668 | 28,937 | 727 | 29,664 |
| Home/Gifts/Other | 12,809 | 18,507 | 31,316 | 10,916 | 4,987 | 15,903 |
| Non-apparel | 107,350 | 30,174 | 137,524 | 105,758 | 7,714 | 113,472 |
| | | | | | | |
| Revenue adjustments not allocated [(a)] | (2,888) | 84 | (2,804) | (2,005) | (518) | (2,523) |
| | | | | | | |
| Net sales | $278,363 | $65,866 | $344,229 | $292,305 | $16,302 | $308,607 |

(a) Includes adjustments related to deferred revenue, estimated sales returns, breakage income, shipping and miscellaneous revenues, which are not allocated to merchandise categories.

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Credit Income

The portfolio for our private label credit card is owned and serviced by Comenity Bank, an affiliate of Alliance Data Systems Corporation. Comenity Bank manages the account activation, receivables funding, card authorization, card issuance, statement generation, remittance processing and guest service functions for our private label credit card program. We perform certain duties, including electronic processing and transmitting of transaction records, and executing marketing promotions designed to increase card usage. We also accept payments in our stores from cardholders on behalf of Comenity Bank. We receive a monthly net portfolio yield payment from Comenity Bank, and can potentially earn an annual bonus based upon the performance of the private label credit card portfolio. The receivable for credit income, which is recorded in prepaid expenses and other current assets, was $4.7 million, $5.8 million, $4.1 million and $4.9 million as of May 5, 2018, February 3, 2018, April 29, 2017 and January 28, 2017, respectively.

Contract Liabilities

Contract liabilities reflect performance obligations related to gift cards, merchandise credits, loyalty program rewards and unfulfilled merchandise orders that have not been satisfied as of a given date. Contract liabilities are recorded in accrued expenses and other current liabilities. Contract liabilities for each period presented were as follows (in thousands):

| | May 5, 2018 | February 3, 2018 | April 29, 2017 |
|---|---|---|---|
| Gift cards and merchandise credits, net | $10,159 | $ 12,122 | $8,964 |
| Loyalty program rewards, net | 3,081 | 1,118 | 1,759 |
| Merchandise fulfillment liability | 788 | 234 | 580 |
| Total contract liabilities | $14,028 | $ 13,474 | $11,303 |

The following table summarizes contract liability activity for each period presented (in thousands):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Beginning balance | $13,474 | $11,669 |
| Net sales recognized during the period from amounts included in contract liability balances at the beginning of the period | (4,669 ) | (2,909 ) |
| Current period additions to contract liability balances included in contract liability balances at the end of the period | 5,223 | 2,543 |
| Ending balance | $14,028 | $11,303 |

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NOTE 4 - STOCK-BASED COMPENSATION

Stock-based compensation expense by type of grant for each period presented was as follows (in thousands):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Non-vested stock | $1,187 | $1,508 |
| Restricted stock units | 492 | 73 |
| Stock-settled performance share units | 371 | 674 |
| Cash-settled performance share units | 54 | — |
| Total compensation expense | 2,104 | 2,255 |
| Related tax benefit | — | (848 ) |
| Stock-based compensation expense, net of tax | $2,104 | $1,407 |

As of May 5, 2018, we have estimated unrecognized compensation cost of $16.6 million related to stock-based compensation awards granted, which is expected to be recognized over a weighted average period of 2.7 years.

Non-vested Stock

We grant shares of non-vested stock to our employees and non-employee directors. Shares of non-vested stock awarded to employees vest 25% annually over a four-year period from the grant date. Shares of non-vested stock awarded to non-employee directors cliff vests after one year. At the end of the vesting period, shares of non-vested stock convert one-for-one to common stock. Certain non-vested stock awards have shareholder rights, including the right to vote and to receive dividends. The fair value of non-vested stock awards with dividend rights is based on the closing share price of our common stock on the grant date. The fair value of non-vested stock awards that do not have dividend rights is discounted for the present value of expected dividends during the vesting period. Compensation expense is recognized ratably over the vesting period.

The following table summarizes non-vested stock activity for the three months ended May 5, 2018:

| Non-vested Stock | Number of Shares | Weighted Average Grant Date Fair Value |
|---|---|---|
| Outstanding at February 3, 2018 | 1,637,037 | $ 6.67 |
| Granted | 420,000 | 2.19 |
| Vested | (379,170 ) | 10.87 |
| Forfeited | (47,743 ) | 2.73 |
| Outstanding at May 5, 2018 | 1,630,124 | 4.65 |

The weighted-average grant date fair value for non-vested stock granted during the three months ended May 5, 2018 and April 29, 2017 was $2.19 and $2.09, respectively. The aggregate intrinsic value of non-vested stock that vested during the three months ended May 5, 2018 and April 29, 2017 was $0.8 million for each respective period. The payment of the employees' tax liability for a portion of the vested shares was satisfied by withholding shares with a fair value equal to the tax liability. As a result, the actual number of shares issued during three months ended May 5, 2018 was 305,620.

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Restricted Stock Units ("RSUs")

We grant RSUs to our employees, which vest 25% annually over a four-year period from the grant date. Each vested RSU is settled in cash in an amount equal to the fair market value of one share of our common stock on the vesting date, not to exceed five times the per share fair market value of our common stock on the grant date. Unvested RSUs have the right to receive a dividend equivalent payment equal to cash dividends paid on our common stock. RSUs are accounted for as a liability in accordance with accounting guidance for cash settled stock awards. The liability for RSUs is remeasured based on the closing share price of our common stock at each reporting period until the award vests. Compensation expense is recognized ratably over the vesting period and adjusted with changes in the fair value of the liability.

The following table summarizes RSU activity for the three months ended May 5, 2018:

| Restricted Stock Units | Number of Units | Weighted Average Grant Date Fair Value |
|---|---|---|
| Outstanding at February 3, 2018 | 1,283,750 | $ 2.14 |
| Granted | 1,375,000 | 2.19 |
| Vested | (277,186 ) | 2.12 |
| Outstanding at May 5, 2018 | 2,381,564 | 2.17 |

Stock-settled Performance Share Units ("Stock-settled PSUs")

We grant stock-settled PSUs as a means of rewarding management for our long-term performance based on total shareholder return relative to a specific group of companies over a three-year performance cycle. These PSUs cliff vest following a three-year performance cycle, and if earned, are settled in shares of our common stock, unless otherwise determined by our Board of Directors ("Board"), or its Compensation Committee. The actual number of shares of our common stock that may be earned ranges from zero to a maximum of twice the number of target units awarded to the recipient. Grant recipients do not have any shareholder rights on unvested or unearned stock-settled PSUs. The fair value of these PSUs is estimated using a Monte Carlo simulation, based on the expected term of the award, a risk-free rate, expected dividends, expected volatility, and share price of our common stock and the specified peer group. The expected term is estimated based on the vesting period of the awards, the risk-free rate is based on the yield on U.S. Treasury securities matching the vesting period, and the volatility is based on the historical volatility over the expected term. Compensation expense is recognized ratably over the corresponding vesting period for stock-settled PSUs.

The following table summarizes stock-settled PSU activity for the three months ended May 5, 2018:

| Period Granted | Target PSUs Outstanding at February 3, 2018 | Target PSUs Granted | Target PSUs Outstanding at May 5, 2018 | Weighted Average Grant Date Fair Value |
|---|---|---|---|---|

| | | | | per Target PSU |
|---|---|---|---|---|
| 2016 | 321,706 | — | 321,706 | $ 8.69 |
| 2017 | 600,000 | — | 600,000 | 1.80 |
| 2018 | — | 280,000 | 280,000 | 3.05 |
| Total | 921,706 | 280,000 | 1,201,706 | 3.94 |

The weighted-average grant date fair value for stock-settled PSUs granted during the three months ended May 5, 2018 and April 29, 2017 was $3.05 and $1.80, respectively. No stock-settled PSUs vested during the three months ended May 5, 2018 and April 29, 2017, respectively.

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Cash-settled Performance Share Units (“Cash-settled PSUs”)

We grant cash-settled PSUs as a means of rewarding management for our long-term performance based on total shareholder return relative to a specific group of companies over a three-year performance cycle. These PSUs cliff vest following a three-year performance cycle, and if earned, are settled in cash. The amount of settlement ranges from zero to a maximum of twice the number of target units awarded multiplied by the fair market value of one share of our common stock on the vesting date. Grant recipients do not have any shareholder rights on unvested or unearned cash-settled PSUs. Cash-settled PSUs are accounted for as a liability in accordance with accounting guidance for cash settled stock awards. The liability for cash-settled PSUs is remeasured based on their fair value at each reporting period until the award vests, which is estimated using a Monte Carlo simulation. Assumptions used in the valuation include the expected term of the award, a risk-free rate, expected dividends, expected volatility, and share price of our common stock and the specified peer group. The expected term is estimated based on the vesting period of the awards, the risk-free rate is based on the yield on U.S. Treasury securities matching the vesting period, and the volatility is based on the historical volatility over the expected term. Compensation expense is recognized ratably over the corresponding vesting period and adjusted with changes in the fair value of the liability.

The following table summarizes cash-settled PSU activity three months ended May 5, 2018:

| Period Granted | Target PSUs Outstanding at February 3, 2018 | Target PSUs Granted | Target PSUs Outstanding at May 5, 2018 | Weighted Average Grant Date Fair Value per Target PSU |
|---|---|---|---|---|
| 2018 | — | 460,000 | 460,000 | $ 3.05 |

Stock Appreciation Rights (“SARs”)

Prior to 2012, we granted SARs to our employees, which generally vested 25% annually over a four-year period from the grant date. Outstanding SARs expire, if not exercised or forfeited, within seven years from the grant date. Exercised SARs are settled by the issuance of common stock in an amount equal to the increase in share price of our common stock between the grant date and the exercise date.

The following table summarizes SARs activity for the three months ended May 5, 2018:

| Stock Appreciation Rights | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (years) | Aggregate Intrinsic Value (in thousands) |
|---|---|---|---|---|
| Outstanding, vested and exercisable at February 3, 2018 | 97,900 | $ 18.83 | | |
| Expired | (97,700) | 18.84 | | |
| Outstanding, vested and exercisable at May 5, 2018 | 200 | $ 16.10 | 0.05 | $ — |

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NOTE 5 - EARNINGS PER SHARE

The following tables show the computation of basic and diluted loss per common share for each period presented (in thousands, except per share amounts):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Basic: | | |
| Net loss | $(31,678) | $(18,987) |
| Less: Allocation of earnings to participating securities | — | — |
| Net loss allocated to common shares | (31,678) | (18,987) |
| | | |
| Basic weighted average shares outstanding | 27,765 | 27,268 |
| Basic loss per share | $(1.14) | $(0.70) |

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Diluted: | | |
| Net loss | $(31,678) | $(18,987) |
| Less: Allocation of earnings to participating securities | — | — |
| Net loss allocated to common shares | (31,678) | (18,987) |
| | | |
| Basic weighted average shares outstanding | 27,765 | 27,268 |
| Add: Dilutive effect of stock awards | — | — |
| Diluted weighted average shares outstanding | 27,765 | 27,268 |
| Diluted loss per share | $(1.14) | $(0.70) |

The number of shares attributable to SARs and non-vested stock grants that would have been considered dilutive securities, but were excluded from the calculation of diluted loss per common share because the effect was anti-dilutive were as follows (in thousands):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Number of anti-dilutive shares due to net loss for the period | — | — |
| Number of anti-dilutive SARs due to exercise price greater than average market price of our common stock | 57 | 156 |

NOTE 6 - STOCKHOLDERS' EQUITY

During the first quarter 2018, we paid $1.4 million in cash dividends. On May 24, 2018, our Board declared a quarterly cash dividend of $0.05 per share of common stock, payable on June 20, 2018 to shareholders of record at the close of business on June 5, 2018.

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NOTE 7 - PENSION PLAN

We sponsor a frozen defined benefit pension plan. The components of net periodic pension cost, which were recognized in selling, general and administrative expenses, were as follows (in thousands):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Employer service cost | $ 123 | $ 125 |
| Interest cost on pension benefit obligation | 358 | 364 |
| Expected return on plan assets | (414 ) | (403 ) |
| Amortization of net loss | 199 | 211 |
| Net periodic pension cost | $ 266 | $ 297 |

Our funding policy is to make contributions to maintain the minimum funding requirements for our pension obligations in accordance with the Employee Retirement Income Security Act. We may elect to contribute additional amounts to maintain a level of funding to minimize the Pension Benefit Guaranty Corporation premium costs or to cover the short-term liquidity needs of the plan in order to maintain current invested positions. We contributed $0.2 million during the three months ended May 5, 2018, and we expect to contribute an additional $1.0 million in 2018.

NOTE 8 - FAIR VALUE MEASUREMENTS

We recognize or disclose the fair value of our financial and non-financial assets and liabilities on a recurring and non-recurring basis. Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities which are required to be recorded at fair value, we assume the highest and best use of the asset by market participants in which we would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability.

We apply the following fair value hierarchy, which prioritizes the inputs used to measure fair value into three levels, and base the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

| | |
|---|---|
| Level 1 – | Quoted prices in active markets for identical assets or liabilities. |
| Level 2 – | Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. |
| Level 3 – | Inputs that are both unobservable and significant to the overall fair value measurement reflect our estimates of assumptions that market participants would use in pricing the asset or liability. |

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Financial assets and liabilities measured at fair value on a recurring basis were as follows (in thousands):

| | May 5, 2018 | | | |
|---|---|---|---|---|
| | Balance | Quoted Prices in Active Markets for Identical Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Other assets: | | | | |
| Securities held in grantor trust for deferred compensation plans [(a)(b)] | $19,606 | $ 19,606 | $ — | $ — |

| | February 3, 2018 | | | |
|---|---|---|---|---|
| | Balance | Quoted Prices in Active Markets for Identical Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Other assets: | | | | |
| Securities held in grantor trust for deferred compensation plans [(a)(b)] | $20,293 | $ 20,293 | $ — | $ — |

| | April 29, 2017 | | | |
|---|---|---|---|---|
| | Balance | Quoted Prices in Active Markets for Identical Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Other assets: | | | | |
| Securities held in grantor trust for deferred compensation plans [(a)(b)] | $19,072 | $ 19,072 | $ — | $ — |

[(a)] The liability for the amount due to participants corresponding in value to the securities held in the grantor trust is recorded in other long-term liabilities.
[(b)] Using the market approach, the fair values of these items represent quoted market prices multiplied by the quantities held. Net gains and losses related to the changes in fair value in the assets and liabilities under the various deferred compensation plans are recorded in selling, general and administrative expenses and were nil for the three months ended May 5, 2018 and for the fiscal year ended February 3, 2018.

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Non-financial assets measured at fair value on a nonrecurring basis were as follows (in thousands):

| | February 3, 2018 | | | |
|---|---|---|---|---|
| | Balance | Quoted Prices in Active Markets for Identical Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Assets: | | | | |
| Store property, equipment and leasehold improvements [a] | $778 | $ — | $ — | $ 778 |

[a] Using an undiscounted cash flow model, we evaluate the cash flow trends of our stores at least annually and when events or changes in circumstances, such as a store closure, indicate that property, equipment and leasehold improvements may not be fully recoverable. When a store's projected undiscounted cash flows indicate its carrying value may not be recoverable, we use a discounted cash flow model, with a 10% discount rate, to estimate the fair value of the underlying long-lived assets. An impairment write-down is recorded if the carrying value of a long-lived asset exceeds its fair value. Key assumptions in estimating future cash flows include, among other things, expected future operating performance, including expected closure date and lease term, and changes in economic conditions. We believe estimated future cash flows are sufficient to support the carrying value of our long-lived assets. Significant changes in the key assumptions used in our cash flow projections may result in additional asset impairments. There were no impairments of long-lived assets recognized for the three months ended May 5, 2018 and April 29, 2017, respectively. We recognized impairment charges of $1.7 million during fiscal year 2017. Impairment charges are recorded in cost of sales and related buying, occupancy and distribution expenses.

Due to the short-term nature of cash and cash equivalents, payables and short-term debt obligations, the carrying value approximates the fair value of these instruments. In addition, we believe that the Revolving Credit Facility obligation approximates its fair value because interest rates are adjusted daily based on current market rates.

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NOTE 9 - GORDMANS ACQUISITION

On April 7, 2017, we acquired select assets of Gordmans Stores, Inc. and its subsidiaries (collectively, the "Sellers") through a bankruptcy auction. The terms of the transaction agreement required us to take assignment of a minimum of 50 of the Sellers' store leases, with rights to take assignment of the leases for an additional seven stores and a distribution center. We also acquired all of the Sellers' inventory, furniture, fixtures and equipment at the 57 store locations and distribution center, as well as the trademarks and other intellectual property of the Sellers. The Gordmans stores, which we operate as an off-price concept, add scale to our business, while allowing us to leverage strategic synergies and our current infrastructure. The acquisition also brings beneficial geographic and guest diversification.

The purchase price for the inventory and other assets acquired from the Sellers was approximately $36.1 million, all of which was paid by the end of the second quarter 2017 using existing cash and availability under the Revolving Credit Facility. We took assignment of 55 of the 57 store locations and the distribution center, and we renegotiated the terms of many of those leases. We also entered into new leases for three former Gordmans store locations, two of which opened in the second quarter 2017, and one opened in the third quarter 2017.

The estimated fair values of the assets acquired at the acquisition date were as follows (in thousands):

| | April 7, 2017 |
|---|---|
| Inventory | $31,770 |
| Property, plant and equipment and other assets | 4,374 |
| Total | $36,144 |

Acquisition and integration related costs were recognized in selling, general and administrative expenses and were $6.3 million for the three months ended April 29, 2017.

Net sales included in our condensed consolidated statements of operations from Gordmans stores that we operated beginning on April 7, 2017, were as follows for each period presented (in thousands):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Net sales | $65,866 | $16,302 |

Pro forma net sales and earnings for the three months ended April 29, 2017 are not presented due to the impracticability in substantiating this information as the Gordmans Acquisition was limited to select assets and assignment of leases acquired through a bankruptcy auction. Furthermore, the results of operations may have been impacted by the Sellers' liquidation and may not be indicative of future performance.

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

Cautionary Statement Concerning Forward-Looking Statements for Purposes of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995

The Private Securities Litigation Reform Act of 1995 ("Act") provides a safe harbor for forward-looking statements to encourage companies to provide prospective information, so long as those statements are identified as forward-looking and are accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those discussed in the statements. We wish to take advantage of the "safe harbor" provisions of the Act.

Certain statements in this report are forward-looking statements within the meaning of the Act, and such statements are intended to qualify for the protection of the safe harbor provided by the Act. The words "anticipate," "estimate," "expect," "objective," "goal," "project," "intend," "plan," "believe," "will," "should," "may," "target," "forecast," "guidance," expressions generally identify forward-looking statements. Similarly, descriptions of our objectives, strategies, plans, goals or targets are also forward-looking statements. Forward-looking statements relate to the expectations of management as to future occurrences and trends, including statements expressing optimism or pessimism about future operating results or events and projected sales, earnings, capital expenditures and business strategy.

Forward-looking statements are based upon a number of assumptions and factors concerning future conditions that may ultimately prove to be inaccurate and could cause actual results to differ materially from those in the forward-looking statements. Forward-looking statements that are made herein and in other reports and releases are not guarantees of future performance and actual results may differ materially from those discussed in such forward-looking statements as a result of various factors. These factors include, but are not limited to, the ability for us to maintain normal trade terms with vendors, the ability for us to comply with the various covenant requirements contained in the Revolving Credit Facility agreement, the demand for apparel, and other factors. The demand for apparel and sales volume can be affected by significant changes in economic conditions, including an economic downturn, employment levels in our markets, consumer confidence, energy and gasoline prices, the value of the Mexican peso, and other factors influencing discretionary consumer spending. Other factors affecting the demand for apparel and sales volume include unusual weather patterns, an increase in the level of competition in our market areas, competitors' marketing strategies, changes in fashion trends, changes in the average cost of merchandise purchased for resale, availability of product on normal payment terms and the failure to achieve the expected results of our merchandising and marketing plans as well as our store opening or relocation plans. Additional assumptions, factors and risks concerning future conditions are discussed in the Risk Factors section of the Form 10-K, and may be discussed from time to time in our other filings with the SEC, including Quarterly Reports on Form 10-Q and Current Reports on Form 8-K. Most of these factors are difficult to predict accurately and are generally beyond our control.

Forward-looking statements are and will be based upon management's then-current views and assumptions regarding future events and operating performance, and are applicable only as of the dates of such statements. Although management believes the expectations expressed in forward-looking statements are based on reasonable assumptions within the bounds of our knowledge, forward-looking statements, by their nature, involve risks, uncertainties and other factors, any one or a combination of which could materially affect our business, financial condition, results of operations or liquidity.

Readers should carefully review the Form 10-K in its entirety including, but not limited to, our financial statements and the notes thereto and the risks and uncertainties described in Part I, Item 1A (Risk Factors) of the Form 10-K. This report should be read in conjunction with the Form 10-K, and you should consider all of these risks, uncertainties and other factors carefully in evaluating forward-looking statements.

Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date they are made. We undertake no obligation to publicly update forward-looking statements whether as a result of new information, future events or otherwise. Readers are advised, however, to consult any further disclosures we make on related subjects in our public announcements and SEC filings.

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For purposes of the following discussion, all references to the “first quarter 2018” and the “first quarter 2017” are for the 13-week fiscal periods ended May 5, 2018 and April 29, 2017, respectively.

The financial information, discussion and analysis that follow should be read in conjunction with our consolidated financial statements and the related notes included in this Form 10-Q as well as the financial and other information included in the Form 10-K.

Our Business

We are a retailer of trend-right, moderately priced, name-brand apparel, accessories, cosmetics, footwear and home goods. As of May 5, 2018, we operated in 42 states through 773 BEALLS, GOODY’S, PALAIS ROYAL, PEEBLES and STAGE specialty department stores and 59 GORDMANS off-price stores, as well as an e-commerce website. Our department stores are predominantly located in small towns and rural communities. Our off-price stores are predominantly located in mid-sized, non-rural Midwest markets.

Results of Operations

Select financial results for the first quarter 2018 were as follows (comparisons are to the first quarter 2017):

- Net sales increased $35.6 million, or 11.5%, including a $49.6 million increase in sales from our Gordmans off-price stores.
- Comparable sales decreased 2.8%. Comparable sales consist of store sales after a store has been in operation for 14 full months and e-commerce sales.
- Net loss was $31.7 million compared to $19.0 million.
- Loss per common share was $1.14, compared to a loss per common share of $0.70.
- EBIT was $(29.3) million compared to $(26.3) million.
- Cash dividends of $1.4 million, or $0.05 per common share, were paid.

2018 Outlook and Strategy

The first quarter 2018 had a strong start as the momentum from the fourth quarter 2017 continued. This positive trend was disrupted by cold weather that spread across our geography in late March and early April during the Easter holiday shopping season, contributing to negative comparable sales of 2.8% for the quarter. Comparable sales turned positive again for the second half of April and May as temperatures normalized. Comparable sales for our department stores in Texas, Louisiana, Oklahoma and New Mexico, which are in markets that are dependent on the oil and gas industry, have outperformed the balance of the chain each quarter since the first quarter 2017. Our e-commerce business continues to grow and had a double-digit sales increase for the first quarter 2018 compared to the first quarter 2017.

During the first quarter 2018, we closed four department stores, and we expect to close approximately 30 to 35 department stores in total in 2018, as part of our multi-year plan to exit stores that do not meet our sales productivity and profitability standards. Store counts at the end of the first quarter 2018 and first quarter 2017 were as follows:

| | May 5, 2018 | April 29, 2017 |
|---|---|---|
| Department stores | 773 | 800 |
| Off-price stores | 59 | 50 |
| Total stores | 832 | 850 |

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Our 2018 strategic initiatives are focused on:

- Off-Price Growth - During the first quarter 2018, we completed the conversion of one of our department stores to a Gordmans store. We plan to open one new Gordmans store and convert five to ten department stores to Gordmans stores in 2018. We continue to refine our off-price business model and seek opportunities to open additional Gordmans stores in 2019 and beyond.

- Differentiation - We are differentiating both our department stores and Gordmans stores from the competition by growing the outperforming areas of their respective businesses. Beauty is a core strength in our department stores, and we are leveraging this strength to drive beauty and fragrance sales growth in our Gordmans stores. In our department stores, we expanded our Beauty Bar concept to 136 stores during the first quarter 2018, and we plan to expand to 350 stores in total during 2018. By year end, we will have Beauty Bar in 500 stores. In Gordmans, home is a core strength representing nearly 30% of sales, and we are leveraging this strength to drive more value and new categories into our department store home business. In addition, we are focused on accelerating the positive sales trends in athletic and outdoor by adding new brands and expanded assortments in these categories.

- Guest Acquisition and Retention - Our marketing efforts are positioned to more efficiently retain our existing guests, while redeploying funds to acquire new guests. We have shifted from print into digital, broadcast, and social marketing initiatives, which enables us to reach more guests and be more nimble and targeted with our promotional efforts. Our private label credit card and loyalty programs are designed to promote guest loyalty. In 2018, we expect our private label credit card sales penetration to reach 50% in our department stores. In our off-price stores, we have set a long-term goal for our private label credit card sales penetration to reach 25%. Our Style Circle Rewards® program has nearly 8 million members, and we enrolled our 1 millionth gRewards® member during the first quarter 2018.

- Guest Experience - We are enhancing the guest experience in our stores by refocusing on service and a selling culture and maintaining an ongoing flow of new merchandise offerings. In addition, we are dedicated to providing our guests with a seamless omni-channel experience through our Web @ POS and Buy Online, Ship-to-Store programs. Web @ POS, which offers in-store guests access to our full online assortment, delivered a sales increase of more than 40% in the first quarter 2018 as compared to our previous program for shipping merchandise direct to guests from our stores in the first quarter 2017. Our Buy Online, Ship-to-Store orders are now more than 25% of total e-commerce orders, with 30% of those guests buying additional items when they visit the store to pick up their orders.

Non-GAAP Financial Measures

The following table presents earnings before interest and taxes (EBIT), a non-GAAP financial measure. We believe the presentation of this supplemental non-GAAP financial measure enhances an investor's understanding of our financial performance. In addition, management uses this non-GAAP financial measure to assess the results of our operations. Non-GAAP financial information should not be considered in isolation or viewed as a substitute for net income, cash flow from operations, diluted earnings per common share or other measures of performance as defined by GAAP. Moreover, the inclusion of non-GAAP financial information as used herein is not necessarily comparable to other similarly titled measures of other companies due to the potential inconsistencies in the method of presentation and items considered. The following table sets forth the supplemental financial information and the reconciliation of GAAP disclosures to non-GAAP financial measures (in thousands):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Net loss (GAAP) | $(31,678) | $(18,987) |

| | | |
|---|---|---|
| Interest expense | 2,253 | 1,586 |
| Income tax expense (benefit) | 150 | (8,890 ) |
| EBIT (non-GAAP) | $(29,275 ) | $(26,291 ) |

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First Quarter 2018 Compared to First Quarter 2017

The following table sets forth the results of operations for the periods presented (in thousands, except percentages):

| | Three Months Ended | | | | | |
|---|---|---|---|---|---|---|
| | May 5, 2018 | | April 29, 2017 | | Change | |
| | Amount | % to Sales [a] | Amount | % to Sales [a] | Amount | % |
| Net sales | $344,229 | 100.0 % | $308,607 | 100.0 % | $35,622 | 11.5% |
| Credit income | 15,514 | 4.5 % | 12,928 | 4.2 % | 2,586 | 20.0% |
| Total revenues | 359,743 | 104.5 % | 321,535 | 104.2 % | 38,208 | 11.9% |
| Cost of sales and related buying, occupancy and distribution expenses | 281,741 | 81.8 % | 246,389 | 79.8 % | 35,352 | 14.3% |
| Selling, general and administrative expenses | 107,277 | 31.2 % | 101,437 | 32.9 % | 5,840 | 5.8 % |
| Interest expense | 2,253 | 0.7 % | 1,586 | 0.5 % | 667 | |
| Loss before income tax | (31,528 ) | (9.2 )% | (27,877 ) | (9.0 )% | (3,651 ) | |
| Income tax expense (benefit) | 150 | — % | (8,890 ) | (2.9 )% | 9,040 | |
| Net loss | $(31,678 ) | (9.2 )% | $(18,987 ) | (6.2 )% | $(12,691) | |

[a] Percentages may not foot due to rounding.

Net Sales

Sales increased $35.6 million, or 11.5%, to $344.2 million for the first quarter 2018 from $308.6 million for the first quarter 2017, primarily due to a $49.6 million increase in our Gordmans store sales, partially offset by a decrease in our department store sales. The decrease in our department store sales in first quarter 2018 as compared to the first quarter 2017, was driven by store closures and a 2.8% decrease in comparable sales. Comparable sales reflect a 2.8% decrease in the number of transactions and a flat average transaction value. Comparable sales for the first quarter 2018 were negatively impacted by cold weather that spread across our geography in late March and early April during the Easter holiday shopping season.

Comparable sales for our stores in Texas, Louisiana, Oklahoma and New Mexico, where the economies are generally impacted by the oil and gas industry, outperformed the balance of our chain in the first quarter 2018 compared to the first quarter 2017. Comparable sales in these four states were down 1.4%, while comparable sales in the balance of our chain were down 4.5%.

Our non-apparel categories outperformed our apparel categories. Non-apparel comparable sales increased 3.4% and apparel comparable sales decreased 6.4%. Home, gifts, cosmetics, handbags, men’s and footwear were our best performing merchandise categories. Our best performing apparel areas were activewear and denim.

Credit Income

Credit income earned from our private label credit card program increased $2.6 million, or 20.0%, to $15.5 million for the first quarter 2018 from $12.9 million for the first quarter 2017, primarily due to incremental credit income from our Gordmans stores.

Cost of Sales

Cost of sales increased $35.4 million, or 14.3%, to $281.7 million for the first quarter 2018 from $246.4 million for the first quarter 2017. Cost of sales as a percent of sales increased 200 basis points to 81.8% for the first quarter 2018 from 79.8% for the first quarter 2017. The increase in the cost of sales rate reflects an increase of 170 basis points in the merchandise costs of sales rate due to added promotional activities in response to the challenging mid-quarter sales environment, and an increase of 30 basis points in the buying, occupancy and distribution expenses rate.

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Selling, General and Administrative Expenses (“SG&A”)

SG&A expenses for the first quarter 2018 increased $5.8 million to $107.3 million from $101.4 million for the first quarter 2017. The increase in SG&A expenses is primarily attributable to higher store expenses from the addition of our Gordmans stores. As a percent of sales, SG&A expenses decreased to 31.2% for the first quarter 2018 from 32.9% for the first quarter 2017.

Interest Expense

Net interest expense was $2.3 million for the first quarter 2018, compared to $1.6 million for the first quarter 2017. Interest expense is primarily comprised of interest on borrowings under the Revolving Credit Facility, related letters of credit and commitment fees, amortization of debt issuance costs and interest on finance obligations. The increase in interest expense is primarily due to an increase in average borrowings and higher interest rates under the Revolving Credit Facility for the first quarter 2018 compared to the first quarter 2017. For the first quarter 2018, the weighted average interest rate on outstanding borrowings and the average daily borrowings were 3.15% and $247.5 million, respectively, as compared to 2.43% and $192.3 million for the first quarter 2017.

Income Taxes

Our effective income tax rate for the first quarter 2018 was 0.5%, resulting in an estimated tax expense of $0.2 million. This compares to an effective tax rate of 31.9% and an income tax benefit of $8.9 million for the first quarter 2017. The lower effective income tax rate in the first quarter 2018 compared to the first quarter 2017 is primarily due to the valuation of all tax benefits due to the uncertainty of realization, which is dependent upon generation of taxable income.

Seasonality and Inflation

Our business, like many other retailers, is subject to seasonal influences, with a significant portion of sales and income typically realized during the last quarter of our fiscal year. Working capital requirements fluctuate during the year and generally reach their highest levels during the third and fourth quarters. Because of the seasonality of our business, results from any quarter are not necessarily indicative of the results that may be achieved for a full fiscal year.

We do not believe that inflation has had a material effect on our results of operations. However, there can be no assurance that our business will not be affected by inflation in the future.

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Liquidity and Capital Resources

Our liquidity is currently provided by (i) existing cash balances, (ii) operating cash flows, (iii) trade credit terms from our vendors and their factors and (iv) the Revolving Credit Facility. Our primary cash requirements are for operational needs, including rent and salaries, inventory purchases, and capital investments in our stores, e-commerce and information technology. We also have used our cash flows and other liquidity sources to pay quarterly cash dividends. Our cash requirements for 2017 included the Gordmans Acquisition and additional investments required to support the integration of the Gordmans operations into our infrastructure.

We believe that our sources of liquidity will be sufficient to cover working capital needs, planned capital expenditures and debt service requirements for the remainder of 2018 and the foreseeable future.

Key components of our cash flow are summarized below (in thousands):

| | Three Months Ended | |
|---|---|---|
| | May 5, 2018 | April 29, 2017 |
| Net cash (used in) provided by: | | |
| Operating activities | $(68,655) | $ (313 ) |
| Investing activities | (6,885 ) | (39,979) |
| Financing activities | 83,381 | 48,177 |

Operating Activities

During the first quarter 2018, we used $68.7 million in cash from operating activities. Net loss, adjusted for non-cash expenses, used cash of approximately $14.7 million. Changes in operating assets and liabilities used net cash of approximately $54.0 million, which included a $39.2 million increase in merchandise inventories, primarily due to the seasonal build of inventories, partially offset by a $4.3 million decrease in other assets and a $19.1 million decrease in accounts payable and other liabilities.

During the first quarter 2017, we used $0.3 million in cash from operating activities. Net loss, adjusted for non-cash expenses, used cash of approximately $1.7 million. Changes in operating assets and liabilities provided net cash of approximately $0.3 million, which included a $32.0 million increase in merchandise inventories primarily due to the seasonal build of inventories, an increase in other assets of $7.2 million and an increase in accounts payable and other liabilities of $39.5 million. Additionally, cash flows from operating activities included construction allowances from landlords of $1.0 million, which funded a portion of the capital expenditures related to store leasehold improvements in relocated, expanded and remodeled stores.

The increase in cash used in operating activities in the first quarter 2018 compared to the first quarter 2017 reflects a shift in the timing of payments due to earlier merchandise receipts and a higher payables balance at the end of 2017 compared to 2016.

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Investing Activities

Net cash used in investing activities was $6.9 million for the first quarter 2018, compared to $40.0 million for the first quarter 2017. Investing activities for the first quarter 2017 included $33.8 million paid for the Gordmans Acquisition, which was funded with existing cash and availability under the Revolving Credit Facility, and was predominately for inventory acquired.

Capital expenditures were $6.9 million for the first quarter 2018, compared to $7.4 million for the first quarter 2017, reflecting a decrease in store expansions and remodels. We received construction allowances from landlords of $1.0 million in the first quarter 2017 to fund a portion of the capital expenditures related to store leasehold improvements. These funds are recorded as a deferred rent credit on the balance sheet and are recognized as an offset to rent expense over the lease term commencing with the date the allowances are earned.

We estimate that capital expenditures in 2018, net of construction allowances to be received from landlords, will be approximately $30.0 million to $35.0 million. The expenditures will principally be for investments in our stores, technology, omni-channel and supply-chain.

Financing Activities

Net cash provided by financing activities for the first quarter 2018 was $83.4 million, compared to $48.2 million for the first quarter 2017. The change is primarily due to increased net borrowings under the Revolving Credit Facility.

We use the Revolving Credit Facility to provide financing for working capital and general corporate purposes, as well as to finance capital expenditures and to support our letter of credit requirements. Borrowings are limited to the availability under a borrowing base that is determined principally on eligible inventory as defined by the Revolving Credit Facility agreement. Inventory, cash and cash equivalents are pledged as collateral. The daily interest rates are determined by a prime rate or LIBOR, plus an applicable margin, as set forth in the Revolving Credit Facility agreement. For the first quarter 2018, the weighted average interest rate on outstanding borrowings and the average daily borrowings were 3.15% and $247.5 million, respectively, compared to 2.43% and $192.3 million for the first quarter 2017.

Letters of credit issued under the Revolving Credit Facility support certain merchandise purchases and collateralize retained risks and deductibles under various insurance programs. At May 5, 2018, outstanding letters of credit totaled approximately $6.2 million. These letters of credit expire within 12 months of issuance, but may be renewed. Excess borrowing availability under the Revolving Credit Facility at May 5, 2018 was $67.2 million, improving to $80.4 million at June 2, 2018.

The Revolving Credit Facility agreement contains covenants which, among other things, restrict, based on required levels of excess availability, (i) the amount of additional debt or capital lease obligations, (ii) the payment of dividends to $30.0 million in a fiscal year, and (iii) the repurchase of common stock under certain circumstances. The agreement also contains a fixed charge coverage ratio covenant in the event excess availability is below a defined threshold or an event of default has occurred. At May 5, 2018, we were in compliance with the debt covenants of the agreement and we expect to remain in compliance.

During the first quarter 2018, we paid $1.4 million in cash dividends. On May 24, 2018, our Board declared a quarterly cash dividend of $0.05 per share of common stock, payable on June 20, 2018 to shareholders of record at the close of business on June 5, 2018.

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Recent Accounting Standards

Disclosure concerning recent accounting standards is incorporated by reference to Note 1 of our Condensed Consolidated Financial Statements (Unaudited) contained in this Form 10-Q.

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

We are subject to market risk from exposure to changes in interest rates on borrowings under the Revolving Credit Facility. An increase or decrease of 10% in interest rates would not have a material effect on our financial condition, results of operations, or liquidity.

## ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures, as that term is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended ("Exchange Act"), as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have each concluded that such disclosure controls and procedures were effective as of the end of the period covered by this report.

Internal Control Over Financial Reporting

As defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act, the term "internal control over financial reporting" means a process designed by, or under the supervision of, the issuer's principal executive and principal financial officers, or persons performing similar functions, and effected by the issuer's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

(1) Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer;

(2) Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer; and

(3) Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the issuer's assets that could have a material adverse effect on the financial statements.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. There were no changes in our internal control over financial reporting during the three months ended May 5, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

# PART II – OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

No response is required under Item 103 of Regulation S-K.

## ITEM 1A. RISK FACTORS

There have not been any material changes from the risk factors as previously disclosed in the Form 10-K.

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

On March 7, 2011, our Board approved a stock repurchase program ("2011 Stock Repurchase Program"), which authorized us to repurchase up to $200.0 million of our outstanding common stock. The 2011 Stock Repurchase Program will expire when we have exhausted the authorization, unless terminated earlier by our Board. Through May 5, 2018, we repurchased approximately $141.6 million of our outstanding common shares under the 2011 Stock Repurchase Program. Also in March 2011, our Board authorized us to repurchase shares of our outstanding common stock equal to the amount of the proceeds and related tax benefits from the exercise of stock options, stock appreciation rights and other equity grants. Purchases of shares of our common stock may be made from time to time, either on the open market or through privately negotiated transactions and are financed by our existing cash, cash flow and other liquidity sources, as appropriate.

The table below sets forth information regarding our repurchases of common stock during the three months ended May 5, 2018:

ISSUER PURCHASES OF EQUITY SECURITIES

| Period | Total Number of Shares Purchased [(a)] | Average Price Paid Per Share [(a)] | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs [(b)] |
|---|---|---|---|---|
| February 4, 2018 to March 3, 2018 | 5,347 | $ 1.92 | — | $58,351,202 |
| March 4, 2018 to April 7, 2018 | 81,763 | 2.20 | — | $58,351,202 |
| April 8, 2018 to May 5, 2018 | 4,757 | 2.98 | — | $58,351,202 |
| Total | 91,867 | $ 2.23 | — | |

[(a)] Although we did not repurchase any of our common stock during the three months ended May 5, 2018 under the 2011 Stock Repurchase Program:

- We reacquired 73,550 shares of common stock from certain employees to cover tax withholding obligations from the vesting of restricted stock at a weighted average acquisition price of $2.22 per common share; and
- The trustee of the grantor trust established by us for the purpose of holding assets under our deferred compensation plan purchased an aggregate of 18,317 shares of our common stock in the open market at a weighted average price of $2.27 in connection with the option to invest in our stock under the deferred compensation plan and reinvestment of dividends paid on our common stock held in trust in the deferred compensation plan.

[(b)] Reflects the $200.0 million authorized under the 2011 Stock Purchase Program, less the $141.6 million repurchased as of May 5, 2018 using our existing cash, cash flow and other liquidity sources since March 2011.

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## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 4. MINE SAFETY DISCLOSURES

None.

## ITEM 5. OTHER INFORMATION

None.

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ITEM 6. EXHIBITS

The following documents are the exhibits to this Form 10-Q. For convenient reference, each exhibit is listed according to the Exhibit Table of Item 601 of Regulation S-K.

| Exhibit Number | Description |
|---|---|
| 10.1† | Form of Stage Stores Incentive Award Agreement is incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on March 23, 2018. |
| 10.2† | Form of Stage Stores Performance Unit Award Agreement under the Stage Stores 2017 Long-Term Incentive Plan is incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K filed on March 23, 2018. |
| 31.1* | Certification of Chief Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2* | Certification of Chief Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32* | Certification Pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

* Filed electronically herewith.
† Management contract or compensatory plan or arrangement.

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SIGNATURES

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

| | |
|---|---|
| | STAGE STORES, INC. |
| Dated: June 14, 2018 | /s/ Michael L. Glazer<br>Michael L. Glazer<br>President and Chief Executive Officer<br>(Principal Executive Officer) |
| Dated: June 14, 2018 | /s/ Oded Shein<br>Oded Shein<br>Executive Vice President, Chief Financial Officer and Treasurer<br>(Principal Financial Officer) |