

Value City
1st Quarter Earnings
Conference Call

June 8, 2004
8:30 AM ET

Operator (Connie)

Thank you for holding, ladies and gentlemen, and welcome to the Retail Ventures, Inc. 1st Quarter Operating Results Conference Call. At this time, all lines are in a listen-only mode. There will be an opportunity to ask questions at the end of today's conference. Instructions for asking questions will be given at a later time. I thank you for your attention, and now turn the time over to our host, Mr. John Rossler. Please go ahead.

John Rossler, President and CEO

Thank you, Connie. Good morning and welcome to Retail Ventures, Inc.'s first quarter fiscal 2004 conference call. I'm John Rossler, President and CEO. With me today is Ed Kozlowski, our Chief Operating Officer, and Jim McGrady, our Chief Financial Officer. Before proceeding, I would like to restate for you the company's policy with respect to forward-looking information, pursuant to the Private Securities Litigation Reform Act of 1995. Statements made in the course of this call that are not purely historical, such as statements regarding the company's or management's

intentions, expectations, or projections of the future, are forward-looking statements. Actual results could materially differ from the forward-looking statements. Factors that could cause or contribute to such differences include but are not limited to the factors and risks discussed in the company's annual report on Form 10-K for the period ended January 31, 2004, and the other reports filed from time to time by the company with the Securities and Exchange Commission. Any forward-looking statements made during this call are based upon information presently available to the company, and the company assumes no obligation to update any such forward-looking statements.

A little over two years ago, our company embarked on a turnaround strategy. Our goal at the time was not just to return to profitability but to build a strong foundation that could support and sustain a health growing and prosperous company for many years to come. It was anticipated that this turnaround effort would take three years. RVI appears to have turned the corner and is on a path to complete the turnaround within the anticipated time frame.

Yesterday, we announced the RVI first quarter 2004 operating results. The first quarter was successful and exceeded expectations. This was the third quarter in a row with substantially improved sales and profitability over the prior year. Progress is being achieved in all three retail divisions across numerous financial metrics. This is a positive sign that the strategic, financial, organizational and human capital investments RVI has made over the last two years are beginning to pay off. Highlighting some of the specific performance measures of Q1 2004 compared to 2003, total sales were up 9.8 percent.

Gross profit as a percentage to sales increased 330 basis points. Operating profit increased \$18.6 million. Jim will discuss more of the financial results a little later.

Regarding our individual business segments, at the corporate level, RVI has spent the last six months strengthening its retail support expertise. These upfront investments will ultimately lead to increased productivity across the entire portfolio. In the Value City Department Store business segment, our financial performance for Q1 continued the trend of improved operations that began in the third quarter of last year. In the first half of 2003, Value City had focused efforts on increasing traffic. Although this effort was successful in increasing transactions, it created lower than anticipated average unit retail prices. Beginning around six months ago, Value City took a more balanced approach to its recovery. Rather than single-mindedly chasing sales with promotional pricing reductions, we have moved our strategy towards building a more sustainable profit model. This new model is based on reducing inventories and raising average unit retails, while still maintaining our extreme value position with the customer. The combination of lower costs and higher AUR will provide a solid foundation to fund future top-line growth initiatives.

We have not yet fully completed this transformation. Due to the length of our buying cycles, it is anticipated that the full impact on prices will not be felt until we reach the back-to-school season. Even so, Q1 for Value City saw a meaningful improvement in both IMU and gross margin percent. Value City is contributing positive cash flow. The

momentum is in place to achieve our higher AUR goals in the coming fall season. We're clearly moving in the proper direction.

The DSW segment continues to show strong improvement as a growth retailer. In Q1, DSW continued its strong comp store sales growth and opened nine new stores. In spite of the costs and efforts associated with that many successful new openings, DSW produced a substantially improved operating performance. DSW has been successful in converting its strong top-line growth into even greater bottom-line growth by leveraging its costs over the increased volume. At the same time, DSW has been making long-term investments in both people and technology to improve the management of the entire supply chain. These investments will allow DSW to support its growth and continue improving productivity. As we move into the remainder of fiscal 2004, DSW will be facing stronger comp store sales and margin comparisons with 2003. Although this will increase the challenge, we anticipate that our frontloaded investments, in combination with increased efficiencies, will allow us to continue our year-over-year improvements at DSW. In total, we plan on opening 35 new DSW stores in 2004.

Filene's Basement used the year 2003 as a strategic recalibration year, returning to its legendary roots by increasing the quality of the fashion brand mix and shifting promotions to event-based marketing. The favorable results of Q1 indicated that these efforts are already having a positive impact on the top line. Comp store sales growth for Filene's Basement was quite strong. AUR and IMU also increased during the quarter. Although there was a slight decline in operating profits, this was entirely due to the cost

associated with the opening of three new Filene's Basement stores during the quarter. Pre-opening expenses for Filene's Basement during Q1 were \$1.3 million. Excluding this cost, operating profits for Filene's Basement would have improved nearly a half a million dollars. We anticipate that one additional Filene's Basement store will be opened in the fall season.

In summary, with the completion of the first quarter, RVI has now posted three consecutive quarters of improved performance. Every brand is showing improvement. The change initiatives implemented over the past two years are beginning to positively impact operating results. Although the transformation from a struggling company to a solid growth-oriented enterprise is not yet complete, we are on the upswing, and we have momentum in our favor. Our goal for the remainder of the year will be to continue this trend by maintaining our focus on increasing sales, improving margins, and reducing costs.

As a final note, two years ago, to fund the turnaround effort, RVI restructured its debt. At the time, it was anticipated that this additional debt would be temporary and that it would be reduced and restructured again by the end of three years. This is still our intent. We are currently exploring our alternatives and expect to have this matter resolved during the year.

Thank you. I will now ask Jim McGrady, our Chief Financial Officer, to proceed with our financial review.

Jim McGrady, Chief Financial Officer

Thank you, John. Good morning, everyone. Yesterday, as John said, we announced a net loss for the first quarter of \$1.5 million, or five cents a share, versus a loss of \$13.2 million, or 39 cents a share, in the prior year. Total sales for the first quarter increased \$57.8 million, or 9.8 percent, to \$646.3 million from \$588.5 million. Comparable store sales for the quarter increased 4.2 percent as compared to the prior year decline of 4.4 percent. Our comp store sales by business segment were: Value City Department Stores had a decline of 1.1; DSW increased 10.6; and Filene's Basement improved 15.8 percent.

Our Value City segment sales decreased \$3.8 million or as mentioned earlier 1.1 percent to \$339.1 million and, as previously mentioned, had a negative comp of 1.1. The decrease in comp sales is comprised of a decrease in non-apparel hard lines of eight-tenths of a percent, a decrease in apparel of 1.8 percent, and an increase in jewelry sales of 0.9 percent. The apparel divisions of men's and ladies had decreases of 1.8 and 4.9 percent, respectively, while children's increased 7.1 percent. Shoe sales in the Value City segment were a positive 0.5 percent during the quarter.

DSW sales were \$227.3 million, which is a 24.2 percent increase in the quarter. This includes a net increase of 22 stores from a year ago, along with the quarter's comp store sales increase of 10.6 percent. The categories of women's dress, casual and sandals, and accessories had favorable increases during the period. During the quarter, we had a net decrease in the leased shoe department operations of 10, due to store reductions.

Filene's Basement sales increased 27.7 percent in the quarter to \$79.9 million. This includes a net increase of four stores during the comparable periods and a comp store increase of 15.8 percent. The merchandise categories of men's, ladies, and children's all had comp sales increases of 15.5 percent, 10.3 percent, and 37.4 percent, respectively. Other categories such as jewelry, shoes and home also showed improvements.

As you may recall, our business units during last year were negatively impacted by some weather conditions that occurred throughout most of the markets where we operate, just putting that out there as a reminder to everybody. In the first quarter, our gross profit as a percent of sales increased 330 basis points to 40.1 percent, compared to 36.8 percent for the prior year. The increase in our margin is attributable to higher initial markups in all three of our operating divisions. The sales improvement is driven by strong comps in DSW and Filene's and a focus, as John mentioned, as we get back to higher average unit retails in the Value City unit. All of these contributed to lower markdowns during the quarter, particularly in POS markdowns. This again was across all segments. Total gross profit increased 42.7 million to 259.4 million as a result of this. As a percent of sales by segment, gross profit in the first quarter was Value City Department Stores, 39 percent, DSW 43.5 percent, Filene's Basement 35.4 percent and again, overall, 40.1 percent.

Total selling, general, and administrative expenses for the quarter increased by \$24.2 million to 255.3 million. As a percent of sales, SG&A was 39.5 compared to 39.3 in the first quarter of the prior year. Pre-opening expenses for stores opening since

the fiscal yearend increased \$3.6 million over the prior year's quarters. We opened a total of 12 new stores during the first quarter, nine DSW and three of Filene's Basement. Total SG&A expenses associated with these stores open subsequent to May 3 of the prior year, through May 1 of 2004 was \$13.3 million and represents approximately 55 percent of our SG&A expense increase. Other costs that increased during the year include employee health and welfare and retirement. Our SG&A as a percent of sales by segment in the first quarter was comprised of Value City Department Stores 40.6 percent, DSW was at 37.8, Filene's Basement 39.5, for a total of 39.5 percent overall.

Operating profit for the quarter was a \$5.7 million profit, an increase of \$18.5 million from the prior year's operating loss of \$12.8 million. This is about nine-tenths of sales for the quarter versus a negative 2.2 for the prior year. Operating profit by segment was at Value City Department Stores a loss of 4.4 million, at DSW an operating profit of 12.9, actually 13 million, and an operating loss of 2.9 million at Filene's Basement, overall again \$5.7 million. Our net interest and expense for the quarter decreased \$1.2 million to \$8.3 million. This decrease is attributable to a decrease of approximately one full percentage point in our weighted average borrowing rate, offset by about \$33.6 million in an increase in weighted average borrowing. Effective tax rate for the quarter is 40.7 percent versus 41.2 percent for the prior year.

As I turn to our balance sheet, our inventory totaled \$469 million at May 1, 2004. In contrast, it was \$452.9 million last year. This is an increase of about 3.6 percent and \$16.1 million. The increase of the 22 new DSW stores and four new Filene's Basement

stores and a net reduction in leased locations account for the net change of about \$24 million. Net working capital was \$248 million and \$242.5 million at May 1, 2004 and May 3, 2003 respectively. A current ratio of both of those dates was 1.8 percent. Net cash provided by operations was about \$600,000 in the year to date fiscal 2004 period, and this is in contrast to a use of \$38.1 million in the prior year first quarter.

Net cash used for capital expenditures was \$14 million and \$10.8 million for the comparable two periods. During the three months ended May 1 of this year, CAPEX included \$7.4 million for new stores, \$4.2 million for improvements to existing stores, and \$2.4 million for technology equipment upgrades and new systems. In addition to the capital expenditures during the first quarter of this year, we also acquired the Leslie Fay trade name for approximately \$4 million.

EBITDA in the first quarter was \$19 million. Availability under a revolving credit agreement was \$160.8 million, and direct borrowings aggregated \$140 million plus \$13.9 million of letters of credit were issued during that period.

This concludes the review of the first quarter. As we take a look forward with respect to the remainder of fiscal 2004, we are optimistic yet cautious with our projections for comp store sales volume for the second quarter and for the balance of the year. Our expectations are in the low single digit range for the second quarter and throughout the balance of 2004. As John mentioned earlier, we're committed and focused to controlling our costs in all of our operations and support areas. Our efforts to

improve margin rates in our businesses, particularly at Value City and Filene's, will continue to be a focus of those enterprises throughout the balance of the year

Our EPS expectation for the year is in the range of 42 to 47 cents per diluted share. By quarter, we would expect EPS to be around breakeven in the second quarter and earnings of 15 to 20 cents in the third quarter and 25 to 30 cents in the fourth quarter. We expect our gross margin rate, as we had mentioned in the fourth quarter call of last year, to improve by about 25 to 30 basis points compared to the prior year, and this improvement will result from the improved IMUs and AURs at Value City, plus the full-year effect of our market repositioning at Filene's Basement. The expectation for DSW is that we'll probably maintain that 2003 margin rate. The SG&A expense rate overall is expected to decline by around 10 basis points versus the prior year. This includes the impact of the pre-opening expenses for our store program. The company expects the interest expense this year in 2004 again to be about 33 to \$35 million, and our tax rate will be somewhere in the range of 40 to 41 percent as we approach year-end.

That concludes the financial review, and at this time, I would like to ask Connie if she would be kind enough to open up the lines to questions.

Operator

Thank you. To ask a question, please press a "1" followed by a "4" on your touchtone phone. If for any reason you need to retract your question, you can press a "1" followed by a "3". All questions will be taken in the order they are received. And it

looks like our first question is from Mr. David Mann with Johnson Rice. Go ahead please.

David Mann, Johnson Rice

Yes, good morning, gentlemen. John, can you talk a little bit about the DSW business? That margin and SG&A performance seemed fairly impressive. What in addition to the comp leverage is going on there, and should we expect that to continue going forward, notwithstanding your comments on the tough compares?

John Rossler, President and CEO

Good morning, David. From a high level, the first thing that happened for us was it was an extremely great boot season last fall/winter, and it drove people in the stores, had great full sales, cleaned the merchandise, the fall/winter goods out, and we were able to get into the stores our spring/summer merchandise really early. As Mother Nature had it, she blessed us with some early good weather compared to last year, and the industry itself was a very colorful season. The spring/summer season is about colors. So the fact that we were able to bring the new colors of the season in early, the weather gave us a lift, got early full-price sales, helped the top line and helped our margin, also. We were able to, with focus from our Operations Group, leverage those sales increases, you know, by pounding the expenses down. The margins just pretty much happened to flow with the fact that you clean inventories and a fresh season of color.

David Mann, Johnson Rice

In terms of the Value City gross margin, I guess last year, you implemented a planning and allocation system. Is that one of the drivers that's helped out the increased margin in the first quarter?

Ed Kozlowski, Chief Operating Officer

This is Ed Kozlowski. Actually, David, the new planning and allocation was introduced into DSW in the fall, and we really did not anticipate and do not anticipate that we'll really start receiving benefits from that until fall of this year. We get really fully integrated and really understand that planning and allocation. Value City's gross margin drivers were really from the fact that as we talked about in the third quarter conference call, I believe, that we had average unit retail issues that we started to address. As a result of addressing these average unit retail issues, we've been able to improve the IMU and make sure that we're still giving the consumer the bargain prices they want and deserve. But that's really been the fundamental driver. Also, being more inventory conscious and more control-oriented, we were able to buy right, buy smarter, and the sell-throughs are better and, as a result, our markdown percentage is lower in the first quarter for Value City. So those were the two principal drivers of the increased gross margin at Value City – IMU and control markdowns.

David Mann, Johnson Rice

Okay. And then, John, you talked about your turnaround schedule. Does that suggest that you're still believing that you can get back to sort of that two percent net margin by the end of that timetable?

John Rossler, President and CEO

Yes, David, that's right. I think probably the three things that are still hanging out on the turnaround the most, one is information technology. We're two years into renovating the systems for Value City, and we're probably somewhere in the neighborhood of two years to finish the job. So that's just sort of a passage of time and continuing to spend some money on it.

The second thing is to continue to improve the merchandise content and the price points that our customers want to see in Value City. We do really think we're right ready to come down through the door with that. We've learned an awful lot in the past couple of years with market research and by trial and error. While we're not really overly proud of ourselves with the merchandise content in Value City for the spring/summer season, we are very enthusiastic. We just completed our line reviews for the back-to-school and fall season. We're enthusiastic about the content that we'll be presenting going forward, and the average unit retails.

And then, the third thing as I had mentioned earlier, we know that it's still on the docket is the restructuring of our financing.

David Mann, Johnson Rice

And just one last question on that financing timetable, I think last quarter, you talked about a second quarter timetable, though now it seems like you're talking about some time this year. Is that correct, or can you clarify?

Jim McGrady, Chief Financial Officer

This is Jim. I think it'll probably be sometime during the second quarter, David. During the second quarter, left ourselves a little bit of leeway there because we do have a couple of alternatives that we may decide to pursue that might let us leak over a little bit into the third if we go down that path. But right now, I still would anticipate that we should have something by the end of the second quarter.

David Mann, Johnson Rice

Thank you very much.

Operator

Thank you. Once again, if you do have a question, please press a "1" followed by a "4" on your touchtone phone at this time. It looks like our next question comes from Mr. Arnold {Brief} with Goldsmith & Harris. Go ahead, please.

Arnold Brief, Goldsmith & Harris

The Value City comps, do you expect that weakness to continue all year, or do you think the programs you have in place and the merchandise you expect for back-to-school will get your Value City comps up as you progress through the year?

John Rossler, President and CEO

Good morning, Arnold. It's John. I feel that we have a much better chance for the back-to-school and fall season, I think because the average unit retails will be in better condition by then and also the enthusiasm I have for the merchandise line reviews that we just completed.

Arnold Brief, Goldsmith & Harris

Okay. Filene's showed extraordinarily good comps. Earnings didn't progress as much, even when you adjust for new store opening expenses. What's transpiring there in terms of continuing the leverage of the comps, didn't get as much leverage out of the comps as you would think.

John Rossler, President and CEO

Actually, some of that's still a little bit hidden. While we talked about the pre-opening, you still have the initial operating results of those three new stores, which also would have been dilutive to the EBID margins. So in the comp stores, though, we

saw marked improvement in virtually all of the operating metrics throughout Filene's Basement.

Arnold Brief, Goldsmith & Harris

Okay. Another number I might ask for is could you, in addition to the pre-opening expenses, could you tell us what all the new stores lost in the first quarter?

John Rossler, President and CEO

Arnold, we don't talk about specifics on store-by-store basis, so I'm going to have to decline on that one. I can say that, as Ed did mention, in our comp stores, that across all the metrics that we did see improvements in every one of those categories. There was significant charge in there for the pre-opening expense, and that doesn't include the management time that goes into that, as well as some of the operating statistics that we have to kind of push aside a little bit as we go to open up a new store. And opening up three stores in the first quarter, while that was a challenge, it should start to benefit us throughout the balance of the year here, hopefully, on a very, very quick basis.

Arnold Brief, Goldsmith & Harris

Let me rephrase the question. Would you expect the stores opened in the first quarter to be profitable for the rest of the year as a total?

Male Voice

I would say that they'll probably be breakeven in the first year, Arnold.

Arnold Brief, Goldsmith & Harris

Which would mean they could be profitable for the last nine months as a total, if they lost money in the first quarter.

Male Voice

That's correct, yes.

Arnold Brief, Goldsmith & Harris

Could you discuss the inventories per store and what kind of shape – it looks to me like your inventory's in very good shape. On a per-store basis, you might actually have to build some inventory as you go through the year and use some working capital?

Jim McGrady, Chief Financial Officer

Yeah, actually all of the increases throughout all three of the operating units, the increases in inventory, the total increase was attributable to the new stores. So really, on a store-by-store basis, we are on a flat compared to where we were in the prior year and actually, up in the Department Store segment, we have a little bit of a decline there. And that's as we want it to be. As John said, we really want to focus upon that average unit retail and reducing the number of units at the stores and the number of times that we

touch goods as they go through our processing systems to get from the vendor to the store. So, really, we are very happy about that. We're excited about the freshness of the inventory as well. We've been able to maintain a relatively good margin, as you can see, as we've operated here through the first quarter and still maintain the inventories on a seasonally fresh basis. So I agree with your statement, yes, we are in good shape with our inventories at the first quarter.

Arnold Brief, Goldsmith & Harris

Would you start some inventory builds through the rest of the year to accommodate the (inaudible) you're getting in comp stores?

Jim McGrady, Chief Financial Officer

Yeah, absolutely. The inventory will build a little bit throughout the year for the holiday seasons, obviously, and as we see more of the comp store base come to us, yes, and more of the new store openings come to us for DSW. Yeah, we'll definitely see some inventory built, but I don't think you're going to see anything that's going to build on a per-store basis that is significant, other than, as I said, for the new stores.

Arnold Brief, Goldsmith & Harris

Last question, and I give somebody else a turn. There are some fashion trends going on in the shoe business, color, platforms. When you get fashion changes like this, do they stimulate sales? Do the fashion trends last? Is there any definable period that

you can look for these trends to last, a couple of years maybe, to stimulate shoe sales, maybe a little above the historical secular trend?

John Rossler, President and CEO

Arnold, thanks, it's John. In the shoe business, we love fashion trends, fashion changes. So for instance, this spring/summer season, as I mentioned, were bright colors. We enjoyed that because women had to run out and buy lots of pairs for the fall season. It'll be about colors again or dark-end colors, and we expect momentum to be good. What we don't like in the shoe business is, from time to time, there is no change, where a fashion trend sticks too long, and we do not like when it goes back to the plain black, white, brown. But you know, the industry gives us that from time to time, and we just work through those time periods. But right now, fashion is in our favor.

Arnold Brief, Goldsmith & Harris

Could you update us on the inventory, MIS, POS, all that kind of information systems, are you on schedule? Are there any problems? What stage of implementation is Value City, etc.?

Male Voice

In the second half of its POS implementation, which is the precursor for the other systems to come online. We expect to complete that by mid-summer, and then we'll move into new store systems, and then we'll move towards merchandising and

warehousing after that. All those projects are in concert with our plan, and we are moving forward, as John said. We really feel we're about halfway through that process, and we will continue and we feel good about where we are at this time.

Arnold Brief, Goldsmith & Harris

I hate to ask this question on quarterly earnings, because I frankly don't focus that much on them, but your first quarter exceeded your expectations by quite a margin. You've upped your estimate for the year because of the first quarter. You've made no changes in the second, third and fourth quarter despite the improvement above expectations in the first quarter. I know you're up against little harder comparisons, but still in all, you've got some momentum going. It would seem, based on the first quarter and no changes in the second quarter, you might be a little conservative.

Jim McGrady, Chief Financial Officer

Arnold, it's Jim. I would say that we haven't changed our expectations for the balance of the year. As we take a look at how the seasonality happens and taking a look at the prior year's weather, you know, we still have some concerns that perhaps we did presell some shoes and things like that and some of these spring goods earlier on this year that may be we sold later on in the prior year. So we really haven't gone back and moved any of our expectations or changed anything compared to our original plans as we put them together. So, I would agree that we did exceed our expectations by a pretty good margin in the first quarter and, you know, we're quite pleased about that. But still, as we

take a look at the balance of the year, we're going to remain very, very cautious about how we're going to approach the balance of the year and our expectations.

Arnold Brief, Goldsmith & Harris

Thank you.

Operator

Thank you. And we have an additional question from Mr. David Mann with Johnson Rice. Go ahead, please.

David Mann, Johnson Rice

Can you talk a little bit about the latest information you've gotten from your market research in terms of what you're doing at Value City?

John Rossler, President and CEO

David, it's John. I think probably the most impactful thing that we have determined is that, coming back to the idea that our customer does not need us to be chintzy cheap, we've learned our customer is just looking for good value. We have found by a thorough study of our merchandise content and sales that we've been selling some of the same product that we can find in our principal competitors for such a huge discount off of their lowest, final, bottom barrel, clearance season price for the same units that we think that research gives us the confidence that we can take the higher average

unit retail, push our top line up, and help our margin but, yet, still be able to be in line with the extreme value requirement of our customers. I think that's the one biggest thing, that we found our pricing so low, out of line in relation to the same goods in other retailers.

David Mann, Johnson Rice

Can you give a sense on what the trend was in traffic and average unit retail in the quarter?

Jim McGrady, Chief Financial Officer

David, it's Jim. We actually saw in the first quarter, on average, an improved customer count coming through the doors at the Department Stores. Our average unit retail was about flat compared to the first quarter of last year. And as far as units were concerned, we did see a slight decline, very, very minimal. So overall, it was the slight decline in the unit count going through the register that really seemed to affect our sales volume for the period. But again, as we take a look at that with the IMU that we were able to maintain throughout the quarter, I can't say that we want to maintain negative sales momentum that we have going here, but we do seem to be able to sell units at a higher price. So that's really one thing that we see improving for us as we go out throughout the balance of the year as we are, again, able to get this buying cycle cleared through us that we had in the last year, when this AUR issue first arose.

David Mann, Johnson Rice

So should we not expect you to be profitable in Value City in the second quarter?

Jim McGrady, Chief Financial Officer

I wouldn't say I wouldn't expect that. I would say that it's probably going to be close to a break-even scenario.

Ed Kozlowski, Chief Operating Operator

David, this is Ed. One of the things that's going to occur in the second quarter, with inventories in Value City being more tightly controlled, there's less units to clear. So as a result, those less units to clear mean less units out the door. The real key is going to be selling fresh product, new introduced product at fuller margin. So I think that slightly less units is not necessarily a negative as you look at the second quarter, because if you sell more first-priced units at a higher retail and a higher margin versus trying to clear what we ran into clearly a year ago when we had too many units as we were heading out of the season. So I think it's the quality of that sale that's really going to be improved in the second quarter.

David Mann, Johnson Rice

And then, one last question for me would be the Leslie Fay brand that you purchased, can you just give us a sense of what your plans are for that and how that may or may not show up in the numbers in the guidance you've given?

John Rossler, President and CEO

It's John, David. First of all, the decision about doing the Leslie Fay was an investment decision. We just felt the pricing of the brand was such that we had to do it as an investment opportunity. We see two possibilities, whether we would just split the brand out in a very short time frame, which seems to be possible and it would have been a good investment. But on the other hand, what our more probable outcome will be is we have a tremendous amount of licensee interest to license the brand for apparel. And then, after we have that in place, we would license it out for the other categories, handbags and shoes and accessories. I don't believe that the Leslie Fay brand will be a factor in our earning statements for probably at least 12 months, unless of course we would choose to flip it.

David Mann, Johnson Rice

Should we expect to see Leslie Fay merchandise within each of your stores, or just in Value City, or how should we expect that?

John Rossler, President and CEO

It's a Retail Ventures investment, and if we develop it through licensing arrangements, we'll see it in some level of retail stores. And what we'll see in Value City or Filene's Basement would be just be, to a great extent, standard closeout business like we see work with other national brands. And same thing, once we get in the shoe

licensing, it would end up maybe in DSW the same as other national brands ends up, but not a larger representation.

David Mann, Johnson Rice

Thank you.

Operator

Thank you. Our next question comes from Miss Julie Lerner with Metropolitan Capital. Go ahead, please.

Julie Lerner, Metropolitan Capital

Hi, how are you guys doing today?

Male Voice

Good morning, Julie.

Julie Lerner, Metropolitan Capital

Great, congratulations. A quick question for you, I'm just thinking about the Value City comps, which have been I guess negative to a large extent, wondering if the gas prices are perhaps behind that and I guess your concerns given that it is a lower-end customer and how that might affect, I guess, the third and fourth quarter as you get into that.

John Rossler, President and CEO

Julie, it's John. Hi. There's no question that DSW and Filene's Basement have some luxury elements or luxury characteristics to their brands and maybe the stock market or the Dow is more impactful to those retail brands. And in the case of Value City, issues such as unemployment, which of course trailed the recovery in the financial markets, has kind of being an anchor around us in the Value City business. But as you mentioned, home heating costs and gasoline prices certainly affect the Value City customer much more than the Filene's Basement, DSW customer. And it will continue; I think it will continue. It has affected us; it will continue in second, third, fourth quarters. But amongst ourselves, we feel that there's things that we can do to impact the business positively, more than what the gasoline prices are going to affect us negatively. But yes, it is an additional challenge to that customer.

Julie Lerner, Metropolitan Capital

Did you guys see a drop-off drastically in traffic starting April when gas prices started to spike, and does your forecast incorporate a similar traffic pattern or not?

Jim McGrady, Chief Financial Officer

We did not see what I would call a significant drop-off in the traffic patterns across any of the operating units, Julie, in April when, as you said, the escalation started. But have we factored that into the balance of the year? I would say that we have not taken that into consideration beyond where we did at the beginning of the year when we

put together some of our estimates and things like that. We certainly are very aware of it and are cognizant of it and watch these statistics very, very closely. So as we proceed throughout the year, if we do see a market decline in the customer counts and believe that that's attributable to external factors that we can't control, we'll obviously make adjustments as we go throughout the balance of the year at that time. But until that statistic starts to really be extremely impactful and beyond things that we can do, as John said, within our control to affect us, that we think that we have some momentum going here, we're not at this point in time changing our expectations.

Julie Lerner, Metropolitan Capital

Great, well, congratulations.

Operator

Thank you, and it looks like our next question comes from Mr. Arnold Brief with Goldsmith & Harris. Go ahead, please.

Arnold Brief, Goldsmith & Harris

Would you discuss your sourcing, in trends in sourcing over the last three, four months? I'm thinking in terms of where there any unusual buys, number one, and number two, have you opened up any new brand names that you previously didn't have, any new relationships?

John Rossler, President and CEO

Arnold, it's John. I think on the negative side on our buying, in the case of Department Stores, we really were late pulling the trigger on purchasing makeup goods, branded and unbranded makeup programs to start the season off with the great colors that were impactful for the spring/summer season. We waited around too long for the closeout market, and the closeout market never delivered color to us. And I think that's where, from a sourcing standpoint, we got ourselves on the negative side. And on a positive side, I don't really feel there were any major brands added and, this past quarter, no substantive big special buys made that were impactful. But what it is is it's been a methodical process of improving the grade of merchandise that we're buying from our existing vendors. I think that's been continuing to improve for us. And I think, as I mentioned earlier, our brands where we did jump all over the color of the spring/summer season, the bright colors, that sourcing was very helpful to our business.

Arnold Brief, Goldsmith & Harris

Thank you.

John Rossler, President and CEO

And, Arnold, for fall as I said, it's still colors; it's a version of colors, the darker version of colors, but I think that all three brands will be well positioned for fall with the colors, upcoming color season.

Operator

Thank you. At this time, we'll pause a few more moments to allow for any additional questions or comments. (Pause) And it appears we have no further questions at this time.

John Rossler, President and CEO

All right, thank you everyone. Thank you, Connie, and look forward to seeing everybody and have a good second quarter.

Operator

This concludes today's conference call. Thank you for your participation.

(End of Conference Call)