

RETAIL VENTURES, INC.
THIRD QUARTER EARNINGS
December 7, 2005 – 5:00 P. M. ET

OPERATOR: Good afternoon. Welcome to the RVI Third Quarter Earnings release conference call. As a reminder, all lines will be on listen only mode and we will conduct a Q & A session at the end of the call. If you need any technical assistance, please press star zero to speak to an operator.

Today's presenters are Heywood Wilansky and Jim McGrady. At this time I'd like to turn the call over to Jim McGrady so that we may begin. Jim?

JIM MCGRADY: Okay. Thank you Dawn. Good afternoon and welcome to RVI's discussion of the third quarter fiscal 2005 operating results. Before proceeding, as always, I'd like to restate for you the company's policy with respect to forward looking information pursuant to the Private Securities Litigation 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, projections of the future, are forward looking statements. Actual results could materially differ from those forward looking statements. Factors that could cause or contribute to such differences include but are not limited to the factors and risks discussed in a company's annual report on Form 10K for the year ended January 29th, 2005, the S1 that was filed for DSW, Inc., and the other reports we file from time to time with the SEC. Any forward looking statements made during this call are based upon information presently available to the company and the company assumes no obligations to update any such forward looking statements.

Again, today, as you are aware, we announced third quarter net income of \$54.2 million or 88 cents per share on a diluted basis. This is compared to a net loss last year of \$1.3 million or 4 cents per share on a diluted basis, again. For the nine months in the year to date period we are reporting a net loss of \$72.8 million compared to a prior year net loss of \$2.5 million. The net loss per share for each respective period is a \$1.97.

The third quarter in the year to date periods include non-cash accounting adjustments of \$64.8 million in income and \$31.1 million in expense, respectively, related to the modification and issuance of the warrants pursuant to FAS 133. If you remember, we discussed this at the end of the second quarter conference call.

Total sales for the third quarter increased \$46.4 million or about 6.6 percent to \$746.1 million from \$699.7 million. Comparable store sales for the quarter increased 1 percent. By segment, as we reported earlier, the Value City stores decreased by 1 percent for the quarter. DSW increased 3.5 percent for the quarter. Filene's Basement was positive 2.1 and again overall we were positive 1 percent.

Value City's comp store sales decreased primarily due to declines in customer traffic. Apparel and hard lines area had declines in the quarter and men's, excuse me-- Our apparel categories in men's and children's also had decreases of 0.6 and 8.5 percent. Ladies had an increase of 6.6 percent and jewelry and shoes had increases over last year of 7.8 percent and 6 percent respectively. DSW sales were \$302 million which is a 15.2 percent increase in the quarter which includes a net increase of 30 stores, 7 affiliated, excuse me, non-affiliated leased shoe departments, and two Filene's Basement leased shoe departments. This also includes a re-categorization of two DSW Filene's Basement combination stores and this is consistent with the reporting practice we adopted earlier in the year.

Filene's Basement sales increased about 13.4 percent to \$102.2 million and this includes a net increase of two stores and the quarterly comp store sales increase I talked about a little bit earlier. The merchandise categories of men's, ladies, and children's had comp sales increases of 3.5, 1.2, and 25.5 percent, respectively. The jewelry category had an increase of 15.7 percent which was driven by watches and costume jewelry. Also, the home goods area increased 2.8 percent.

Total gross profit increased \$3.7 million to \$283.7 million. In the third quarter, gross profit, as a percentage of sales, decreased approximately 200 basis points from the previous year's quarter which was 40 percent. The decline in gross profit is comprised of a decrease in the Value City and DSW segments. By segment, our margin was at Value City Department Stores, 35.4 percent. DSW was 41.8 percent. Filene's Basement was 35.6 percent. And again, the total was 38 percent.

Value City's gross profit decreased about \$14.3 million from the comparable period of 2004, and this is attributable to lower initial markups, a result of the planned shift in inventory strategy towards more brand name merchandise, better assortments, and at compelling prices. Value City also had some additional markdowns within the quarter related to increased point of sales discounts on clearance merchandise and initial price reductions for permanent markdowns.

At DSW, the gross profit increased \$12.4 million to \$126.4 million in the third quarter of fiscal '05. The decrease in rate as a percentage of sales at DSW is primarily attributable to increased markdowns which was caused by a higher average retail unit on items in clearance and additional markdowns in the accessory category. These negative factors were partially offset by an increase in initial markups.

Filene's Basement gross profit increased by \$5.6 million. This is attributable to new stores offset by increased markdowns in the ready wear categories and slow moving spring, domestic, and certain imported stock categories. During the quarter, the initial markup remained comparable to that of the prior year.

Our total ST&A expense for the comparative quarters increased by \$16.4 million to \$290.4 million and as a percentage of sales, decreased from 39.2 percent to 38.9 percent. The 30 new DSW stores, 7 new of non-affiliated leased shoe departments added approximately \$7.8 million and \$300,000 respectively to our ST&A expenses while the two new Filene's Basement stores added approximately 1.4 million. Additionally, as you may recall, earlier this year we reported a \$6.5 million charge related to the theft of credit cards and other purchase information from a portion of our DSW customers.

ST&A expense for the third quarter by division was as follows. Value City Department Stores was at 42.7, DSW was at 36, Filene's Basement at 37, and our total was 38.9. Again, as you'll see on the Statement of Operations, RVI recognized non-cash income of about \$64.8 million in the third quarter representing the change in market value of the conversion and term loan warrants.

Our interest expense for the quarter decreased \$6.7 million to \$3.2 million. This is primarily due to the decrease of \$253 million, and average borrowings during the three months, and it's also, we saw a decrease in our average borrowing rate of approximately 0.6 percent. Also, as you remember, we used the proceeds from the DSW IPO to repay the term loans, part of the convertible debt, and a good piece of our revolving credit facility.

The effective tax rate for the three months was a negative 3.2 percent compared to 32.5 percent for the three months last year. This reflects the negative impact in the change in the fair value on the mark to market accounting for the term loan warrants and conversion warrants that are included for book income but not for tax.

As we take a look at our balance sheet, inventory totaled \$617.9 million at October 29th, '05 versus \$584 million last year. This is an increase of approximately 5.7 percent. The total increase includes approximately \$21.2 million for the 30 new DSW stores and approximately \$1.4 million for the new leased apartments.

Our net working capital, October 29th, was \$323.5 million compared to \$279.3 million last year. Current ratios were 1.6 and 1.7, respectively. Adjusting for the warrant liability included in current liabilities, working capital would have been \$372 million with a current ratio of 1.8. Net cash used for capital expenditures was approximately \$33.4 million for the year to date period while depreciation and amortization for the year totaled \$43 million, compared with \$40 million in the prior year.

During fiscal '05, capital expenditures including non-cash additions included \$9.5 million for new stores, \$16 million for improvements in existing stores, and \$11.4 million for information technology equipment upgrades and new systems.

EBITDA in the third quarter was \$70 million versus \$22.1 million for last year's quarter. Consolidated availability, excuse me, under our secured revolving credit facility at October 29th was \$250.4 million. Outstanding letters of credit totaled approximately \$17.5 million at that time.

That really concludes the review of our third quarter of operations. Looking to 2006, what we

would see here for next fiscal year, we believe that, again, our comps at Value City and Filene's Basement will be in the low single digit range and we do expect to see a margin improvement in both of those divisions of approximately 50 basis points. We also expect to see leverage from our sales improvements and also expense reductions that we are implementing throughout the organization. And we would expect to see Value City's ST&A decline somewhere in the 75 to 100 basis point range and be a flat to small improvement at Filene's Basement.

The operating profit for Value City and Filene's Basement on a combined basis is expected to be somewhere in the area of a negative 1 percent to a positive 1 percent. I won't go any further than that at this point in time because it's very difficult to make an estimation of the change in the value of the warrants and also our tax rate that is very, very heavily influenced by the change in the value of our warrants.

Some other information that I want to notify you about is that we will be filing an amendment to our second quarter 2005 Form 10Q which will reflect a better methodology for reporting the estimated book tax difference of DSW. This is a non-cash adjustment which does not change the previous reported Statement of Operations. The adjustment will increase other non-current liabilities by approximately \$22.8 million with a corresponding reduction in equity. Again, this amendment is non-cash. It does not change RVI's previously reported Statement of Operations, and it has no impact whatsoever on DSW.

Additionally, beginning in the first quarter of 2006, we will begin to report comparable store sales on a quarterly basis. This is similar to the change that DSW just announced and we believe that it will provide consistency in reporting for the two organizations.

At this time, I'd like to turn the call over to Heywood.

HEYWOOD WILANSKY: Thank you, Jim. I want to spend just a few minutes talking about the progress we've made versus the outline strategy that we have talked about in the past. First of all, we'll talk about Filene's Basement for a moment. The Basement is well on its way to executing the continued strategy of trying to be the high-end off-price player. Their comp businesses are quite good. November was quite good. Early December is also quite good although it's quite early in the month. And the manufacturing community continues to support them in their endeavors and we see nothing to change from a strategic point of view and we expect to have consistent comps, certainly in the 2 to 3 percent range, on a go forward basis, and that's what we have been accomplishing year to date at this point through the end of November of this year.

So the real question then is what do we do with Value City. The Basement has a strategic initiative that we're comfortable with. Results seem to indicate that it's working the way we intended and that over time, as the base of business gets bigger there, they will move to operating profitability as we open more stores and get a bigger comp line base to run our SG&A against.

Value City was a different story and we announced, I guess, early in this year, a strategic initiative to move Value City from what we call the lowest tier off-price player to more of a mid-tier off-price player, competing with the likes of a TJ Maxx or a Marshalls, and to some degree a Kohl's and a Penneys for the mid-tier customer offering a great branded product at outstanding prices in a more comfortable shopping environment than they had done in the past. We spent a small amount of capital to upgrade some of the soft lines fixturing over the course of 2005 to give us a better understanding of what we could accomplish with a better presentation of merchandise in addition to the change in merchandise mix.

The beginning of a significant private label business that will give us both exclusivity and also additional marketing opportunities, additional business opportunities. And we said that we would have improved ladies business by the third quarter of 2005. We thought we might have improved men's business by late in the third quarter of 2005. We thought we'd have improved business in ladies accessories, [unintelligible] apparel, also by the third quarter of 2005. And that the children's business wouldn't really get resurrected until the Spring of 2006. In addition, we gave up, or exited businesses totaling close to \$60 million in the home world and we felt that we would not have increased sales in the home business until we anniversaried that strategic decision, probably around August 1st of next year, perhaps a touch sooner. And we exited businesses that we felt were not in line with trying to execute a mid-tier strategy which included, you know, toilet paper, and cleaning supplies, and drug store buyouts, and things of that nature. And while we did a significant amount of business on it, it really pointed itself toward the lowest consumer that we had attracted and we wanted to move off of that so we'd be more of a mid-tier player.

So what's happened? And when we look at – I'm really going to be talking about season to date businesses from August 1st through the end of November. And, what's happened? First of all, the total business for this season to date is comping at a negative five tenths of one percent through the end of November. And now, within that number, we have a soft lines business that now is comping at positive 3 percent for the Fall season. And that would include certain numbers. The men's business is comping, season to date, at plus, almost plus 2, and they had a big increase in November of over 7 percent comp. So that's really taking hold.

In ladies accessories and in hosiery they're ahead over 19 percent for the season with an increase of over 30 percent in the month of November. And ladies apparel for the season, we

have an increase of over 8 percent on a comp basis and yet in the month of November we had increase that was approaching 12 percent for the month of November. In intimate apparel, we have a comp increase of one tenth of one percent but in the month of November it was comping at over 10 percent positively.

In children's, we have a negative 4.7 percent comp increase going for the season although November was positive 7.7 percent. I'm still holding with my opinion that children's really doesn't get fixed, to speak, until sometime in the first quarter of 2006, and some of the increase in the children's business resulted in maybe markdowns to try to clear the inventory to get ready for 2006.

So those are all positive. The total soft lines business really has shown a lot of life, particularly as we get into the October / November time period as we've gotten more and more of our inventories in line with what we're trying to accomplish. However, in the home business where we said we would have significant decreases until we anniversaried ourselves, we've accomplished that as well with a season to date decrease of about 12 percent and November at about 17 percent decrease. Those decreases may not be as severe as 17 on a go forward basis but they'll be severe until we anniversary the exiting of the businesses that we've talked about exiting.

So by and large, the consumer has voted that the change in merchandise mix in soft lines, the entry into the private label business which we've been very successful with so far using brands such as Leslie Fay that we own the trademark on, has been well received by the consumer. The fixture changeout that we spent maybe 2 to \$2.5 million in fixture upgrades across a hundred and some odd stores to get a light increase in fixture presentation in the soft lines businesses has really worked well and the feedback we're getting from our consumers is very

positive.

And how do we know what else is happening? In terms of charge accounts, the penetration of new charge accounts – last year we had applications for new charge accounts around 100,000 and so far this season they were taking over 300,000 charge account applications indicating strong consumer interest in trying to become part of our family. So, all signs point to go. We're very comfortable with the entry into 2006 and we've just got to keep working on changing out the home business and following the strategy of increased branded and private label soft lines merchandise.

So, with that, I guess, Jim, we could take any questions that people might have. Dawn?

OPERATOR: Thank you. At this time I'd like to open up the call for Q & A. Please press zero one on your keypad if you would like to ask a question. [pause] Again, please press zero one on your keypad if you would like to ask a question. Okay, and this first question is from David Mann with Johnson Rice. Please proceed with your question.

DAVID MANN: Hi. Yes, good afternoon. Jim or Heywood, can you talk a little bit about how you expect the mix changes you've done to affect the gross margin in the fourth quarter and in '06.

HEYWOOD WILANSKY: Well, in 2006 we expect to see, as Jim said, you know, at least a 50 base improvement in gross margin at Value City. And we're quite comfortable with his estimate.

DAVID MANN: Okay. And in terms of the success that you're having on the soft line side, is that occurring across the store base or are there still some stores that are sort of pulling up the

rear that need to be addressed in some other way?

HEYWOOD WILANSKY: Well, there's always a few stores that are pulling up the rear, David, but by and large, the soft lines improvement is pretty consistent across the overwhelming majority of the stores. And we'll still be looking at selected stores at the end of the year to examine their performance and to understand what stores we'd like to exit and how we exit them. But to this point we have not finalized that analysis and, you know, we still got another five weeks or so to understand what the impact is on the change of mix on all the stores.

DAVID MANN: And you alluded to the fact, I guess, that you're going through some review of expenses. Can you give an idea of what kind of cuts you're already doing, what areas that – and are any of them at the store level?

JIM MCGRADY: There are some at the store level. A lot of these have already been put in place, we just haven't seen the impact of them yet on the year. They started late in the third quarter. Also we'll see a lot of efficiencies once our JDA [phonetic] system's in place. We hope to see a better planning and allocation process take hold for us, probably at the end of the second quarter. The actual system will be in sometime around the end of the fiscal year. But again, it's going to take a little bit of time to get the history caught up with it and everything like that so the information is comparable. But we expect to see that, we expect to see some efficiencies come out of some cost docking projects that we put into place at the warehouse, and again, we continue to review, line by line, our expenses throughout the entire organization.

HEYWOOD WILANSKY: And hey, David, one last thing. You know, when we charted, oh, maybe eight, ten months ago, what we thought we would want to accomplish and what we might expect if things were going pretty well, and almost exactly what we had hoped would

happen is happening, so we're pretty pleased, particularly as we see the October / November results come in and the reaction as we've gotten the inventories fully in place in a lot of these areas.

DAVID MANN: Absolutely. Turning the ship is taking some time but you're definitely accomplishing a lot of that. Jim, on the expense reduction, is the bulk of next year's leverage just going to come from the expense reduction so the cuts are about 10 million?

JIM MCGRADY: Well, I think it'll, the expense reductions will come from two places and, I mean, the leverage will come from increased sales base so as a percent to sale will improve on our fixed costs right there, but again, I do expect to see some cost reductions of about the area that you just mentioned there.

DAVID MANN: Okay. And then one last question. Can either of you talk about any specific metric on the advertising that, you know, you've upped that, it seems to be more effective. Any other data on how that is helping to drive traffic?

HEYWOOD WILANSKY: Well, here's what's going on. You know, we've increased our spend, some might say overspend, on electronic media during this Fall season to get the message out. We've made the decision that we need to continue to do that for 2006. We'll probably be able to pull back from that level in 2007 and beyond but we want to keep pounding on the message that we're different than we have been, with different products and different opportunities for consumers to buy. So we'll probably spend a similar amount of marketing media dollars in 2006 as we ended up spending in 2005. It's a little high but we definitely see increases when we run the electronic media on the Thursdays, Fridays, and Saturdays of the business. Newspaper readership is certainly down across America. We use newspaper inserts on Sundays. And so

the Sundays, Mondays, and Tuesdays are usually a little tougher for us and the weekends a little better for us. Over time we'll try to shift some dollars from one to the other as we get a chance to do that but we're still getting the branding message out there and that takes some time. It needs some consistency.

DAVID MANN: Thank you very much.

OPERATOR: And if you would like to ask a question, please press zero one on your keypad.

[pause]

JIM MCGRADY: All right Dawn. If there's no more questions at this point in time, I'd like to thank everybody for dialing and being with us. I wish everybody a happy holidays and we'll be around. Thank you again.

OPERATOR: Thank you. This call has been concluded.

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