

NEIMAN MARCUS GROUP INC  
Form 10-Q  
June 09, 2005

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

**For the Quarterly Period Ended April 30, 2005**

**OR**

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

**Commission file no. 1-9659**

**The Neiman Marcus Group, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**95-4119509**  
(I.R.S. Employer  
Identification No.)

**One Marcus Square**

**1618 Main Street**

Dallas, Texas 75201

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(Address of principal executive offices)

**(214) 741-6911**

(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

NO

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

YES

NO

As of June 3, 2005, the number of outstanding shares of each of the issuer's classes of common stock was:

Class	Outstanding Shares
Class A Common Stock, \$.01 Par Value	29,525,199
Class B Common Stock, \$.01 Par Value	19,422,379

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**THE NEIMAN MARCUS GROUP, INC.**

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**THE NEIMAN MARCUS GROUP, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(UNAUDITED)**

(in thousands)	April 30, 2005	July 31, 2004 (As Restated, See Note 9)	May 1, 2004
<b>ASSETS</b>			
Current assets:			
Cash and cash equivalents	\$ 337,589	\$ 368,367	\$ 311,985
Restricted cash	37,500		
Accounts receivable, net of allowance of \$11,956, \$10,078 and \$11,104	666,455	551,687	599,581
Merchandise inventories	788,915	720,277	715,539
Other current assets	49,715	65,835	46,372
Total current assets	1,880,174	1,706,166	1,673,477
Property and equipment, net	821,810	750,483	743,852
Other assets	137,822	160,999	119,442
Total assets	\$ 2,839,806	\$ 2,617,648	\$ 2,536,771
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
Current liabilities:			
Accounts payable	\$ 246,971	\$ 289,282	\$ 234,264
Accrued liabilities	352,526	286,833	316,305
Notes payable and current maturities of long-term liabilities	200	1,563	1,237
Current portion of borrowings under Credit Card Facility	187,500	150,000	37,500
Total current liabilities	787,197	727,678	589,306
Long-term liabilities:			
Notes and debentures	249,773	249,757	249,751
Borrowings under Credit Card Facility		75,000	187,500
Deferred real estate credits	74,429	71,898	73,208
Other long-term liabilities	133,114	112,455	97,307
Total long-term liabilities	457,316	509,110	607,766
Minority interest	13,498	10,298	12,799
Common stocks	497	492	493
Additional paid-in capital	511,338	491,849	484,151
Accumulated other comprehensive loss	(3,432)	(4,536)	(26,752)
Retained earnings	1,099,053	905,330	891,054
Treasury stock, at cost (768,731 shares, 710,227 shares and 699,777 shares)	(25,661)	(22,573)	(22,046)
Total shareholders' equity	1,581,795	1,370,562	1,326,900
Total liabilities and shareholders' equity	\$ 2,839,806	\$ 2,617,648	\$ 2,536,771

*See Notes to Condensed Consolidated Financial Statements.*



## THE NEIMAN MARCUS GROUP, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(UNAUDITED)

(in thousands, except per share data)	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004	April 30, 2005	May 1, 2004
Revenues	\$ 933,372	\$ 873,167	\$ 2,970,533	\$ 2,740,303
Cost of goods sold including buying and occupancy costs	576,204	544,663	1,892,904	1,773,999
Selling, general and administrative expenses	222,516	208,909	698,054	659,420
Loss on disposition of Chef's Catalog			15,348	
Operating earnings	134,652	119,595	364,227	306,884
Interest expense, net	2,933	4,589	10,948	11,814
Earnings before income taxes and minority interest	131,719	115,006	353,279	295,070
Income taxes	50,713	44,852	136,014	107,576
Earnings before minority interest	81,006	70,154	217,265	187,494
Minority interest in net earnings of subsidiaries	(1,231)	(1,305)	(2,787)	(3,249)
Net earnings	\$ 79,775	\$ 68,849	\$ 214,478	\$ 184,245
Weighted average number of common and common equivalent shares outstanding:				
Basic	48,390	48,208	48,309	47,929
Diluted	49,695	49,124	49,427	48,806
Earnings per share:				
Basic	\$ 1.65	\$ 1.43	\$ 4.44	\$ 3.84
Diluted	\$ 1.61	\$ 1.40	\$ 4.34	\$ 3.78

See Notes to Condensed Consolidated Financial Statements.

## THE NEIMAN MARCUS GROUP, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(in thousands)	Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004 (As Restated, See Note 9)
<b>CASH FLOWS - OPERATING ACTIVITIES</b>		
Net earnings	\$ 214,478	\$ 184,245
Adjustments to reconcile net earnings to net cash provided by (used for) operating activities:		
Depreciation	79,338	73,093
Loss on disposition of Chef's Catalog	15,348	
Minority interest	2,787	3,249
Other primarily costs related to defined benefit pension and other long-term benefit plans	27,222	24,367
	339,173	284,954
Changes in operating assets and liabilities:		
Decrease in undivided interests		242,565
Increase in accounts receivable	(114,270)	(576,986)
Increase in merchandise inventories	(78,955)	(28,477)
Decrease in other current assets	10,530	27,803
Decrease (increase) in other assets	12,276	(4,550)
Increase in accounts payable and accrued liabilities	38,763	35,347
Increase in deferred real estate credits	2,531	2,866
Funding of defined benefit pension plan	(20,000)	(30,000)
<b>Net cash provided by (used for) operating activities</b>	<b>190,048</b>	<b>(46,478)</b>
<b>CASH FLOWS - INVESTING ACTIVITIES</b>		
Capital expenditures	(150,830)	(83,152)
Increase in cash restricted for repayment of borrowings under Credit Card Facility	(37,500)	
Proceeds from sale of Chef's Catalog	14,419	
<b>Net cash used for investing activities</b>	<b>(173,911)</b>	<b>(83,152)</b>
<b>CASH FLOWS - FINANCING ACTIVITIES</b>		
Proceeds from borrowings	7,750	2,000
Repayment of debt	(9,113)	(1,500)
Borrowings under Credit Card Facility		225,000
Repayment of borrowings under Credit Card Facility	(37,500)	
Acquisitions of treasury stock	(3,088)	(7,026)
Proceeds from stock-based compensation awards	16,432	23,235
Cash dividends paid	(20,042)	(6,312)
Distributions paid	(1,354)	(732)
<b>Net cash (used for) provided by financing activities</b>	<b>(46,915)</b>	<b>234,665</b>
<b>CASH AND CASH EQUIVALENTS</b>		
(Decrease) increase during the period	(30,778)	105,035
Beginning balance	368,367	206,950
Ending balance	\$ 337,589	\$ 311,985
<b>SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION</b>		
Cash paid during the period for:		
Interest	\$ 12,992	\$ 9,050

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Income taxes	\$	98,942	\$	70,657
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*See Notes to Condensed Consolidated Financial Statements.*

**THE NEIMAN MARCUS GROUP, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(UNAUDITED)**

1. Basis of Presentation

We have prepared the Condensed Consolidated Financial Statements of The Neiman Marcus Group, Inc. and its subsidiaries (Company) in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, these financial statements do not include all of the information and footnotes required by accounting principles generally accepted for complete financial statements. Therefore, these financial statements should be read in conjunction with our amendment to the Annual Report on Form 10-K/A for the fiscal year ended July 31, 2004.

Our fiscal year ends on the Saturday closest to July 31. All references to the third quarter of 2005 relate to the thirteen weeks ended April 30, 2005 and all references to the third quarter of 2004 relate to the thirteen weeks ended May 1, 2004. All references to 2005 relate to the thirty-nine weeks ended April 30, 2005 and all references to 2004 relate to the thirty-nine weeks ended May 1, 2004.

In our opinion, the accompanying unaudited Condensed Consolidated Financial Statements contain all adjustments, consisting of normal recurring adjustments, necessary to present fairly our financial position, results of operations and cash flows for the applicable interim periods. The results of operations for these periods are not necessarily comparable to, or indicative of, results of any other interim period or for the fiscal year as a whole.

**We are required to make estimates and assumptions about future events in preparing financial statements in conformity with generally accepted accounting principles. These estimates and assumptions affect the amounts of assets, liabilities, revenues and expenses and the disclosure of gain and loss contingencies at the date of the Condensed Consolidated Financial Statements. While we believe that our past estimates and assumptions have been materially accurate, our current estimates are subject to change if different assumptions as to the outcome of future events were made. We evaluate our estimates and judgments on an ongoing basis and predicate those estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances. We make adjustments to our assumptions and judgments when facts and circumstances dictate. Since future events and their effects cannot be determined with absolute certainty, actual results may differ from the estimates used in preparing the accompanying Condensed Consolidated Financial Statements.**



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Certain prior period balances have been reclassified to conform to the current period presentation.

**We believe the following critical accounting policies, among others, encompass the more significant judgments and estimates used in the preparation of our financial statements:**



Revenue recognition;

Valuation of merchandise inventories, including determination of original retail values, recognition of markdowns and vendor allowances, estimation of inventory shrinkage, and determination of cost of goods sold;

Determination of impairment of long-lived assets;

Recognition of income and expenses related to our previous securitization program;

Recognition of advertising and catalog costs;

Measurement of liabilities related to our loyalty programs;

Recognition of income taxes; and

Measurement of accruals for litigation, general liability, workers compensation and health insurance, short-term disability, pension and postretirement health care benefits.

A description of our critical accounting policies is included in our amendment to the Annual Report on Form 10-K/A for the fiscal year ended July 31, 2004.



**Stock-Based Compensation.** We account for stock-based compensation awards to employees in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Accordingly, we have recognized compensation expense on our restricted stock and purchased restricted stock awards but have not recognized compensation expense for stock options since all options granted had an exercise price equal to the market value of our common stock on the grant date.

The following table illustrates the effect on net earnings and earnings per share as if we had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation using the Black-Scholes option-pricing model for 2005 and 2004:

(in thousands, except per share data)	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004	April 30, 2005	May 1, 2004
<b>Net earnings:</b>				
As reported	\$ 79,775	\$ 68,849	\$ 214,478	\$ 184,245
Add: stock-based employee compensation recorded under intrinsic value method, net of related taxes	1,343	866	3,646	2,233
Less: stock-based employee compensation expense determined under fair value based method, net of related taxes	(3,434)	(3,076)	(9,846)	(8,644)
Pro forma	\$ 77,684	\$ 66,639	\$ 208,278	\$ 177,834
<b>Basic earnings per share:</b>				
As reported	\$ 1.65	\$ 1.43	\$ 4.44	\$ 3.84
Pro forma	\$ 1.61	\$ 1.38	\$ 4.31	\$ 3.71
<b>Diluted earnings per share:</b>				
As reported	\$ 1.61	\$ 1.40	\$ 4.34	\$ 3.78
Pro forma	\$ 1.56	\$ 1.36	\$ 4.21	\$ 3.64

The effects on pro forma net earnings and earnings per share of expensing the estimated fair value of stock options are not necessarily representative of the effects on reported net earnings for future periods due to such factors as the vesting periods of stock options and the potential issuance of additional stock options in future years. In addition, the Black-Scholes option-pricing model has inherent limitations in calculating the fair value of stock options for which no active market exists since the model does not consider the inability to sell or transfer options, vesting requirements and a reduced exercise period upon termination of employment - all of which would reduce the fair value of the options.

**Reclassification Loyalty Programs.** A substantial portion of the points earned by customers in connection with our loyalty programs are redeemed for gift cards. At the time the qualifying sales giving rise to the loyalty program points are made, we defer the portion of the revenues on the qualifying sales transactions equal to our estimate of the retail value of the gift cards to be issued upon conversion of the points to gift cards. Beginning in the first quarter of 2005, we began to record the deferral of revenues related to gift card awards under our loyalty programs as a reduction of revenues. Previously, we charged such amounts to selling, general and administrative expenses (SG&A). In addition, we now charge the cost of all other awards under our loyalty programs to cost of goods sold (COGS) rather than SG&A. These changes in classification do not impact the previously reported operating earnings, net income or earnings per share amounts.

The following table presents quarterly and annual information giving recognition to the changes in classification related to our loyalty programs:

(in thousands)	Revenues	COGS	SG&A
<b>Fiscal Year 2004:</b>			
First quarter	\$ 818,769	\$ 510,350	\$ 211,130
Second quarter	1,048,367	718,985	239,381
Third quarter	873,167	544,663	208,909
Fourth quarter	784,468	553,231	189,033
Total	\$ 3,524,771	\$ 2,327,229	\$ 848,453
<b>Fiscal Year 2003:</b>			
First quarter	\$ 727,832	\$ 455,307	\$ 197,281
Second quarter	934,844	655,459	220,981
Third quarter	718,557	465,160	181,565
Fourth quarter	699,120	502,510	179,981
Total	\$ 3,080,353	\$ 2,078,436	\$ 779,808

**Recent Accounting Pronouncements.** In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123R, Share-Based Payment. This standard is a revision of SFAS No. 123, Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS No. 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values and is effective for the first interim period or annual reporting period beginning after June 15, 2005. We expect to adopt SFAS No. 123R in the first quarter of our fiscal year 2006. We are in the process of evaluating the impact of the adoption of SFAS No. 123R. The adoption of SFAS No. 123R will reduce reported net income and earnings per share because we will be required to recognize compensation expense for our stock options.

## 2. Loss on Disposition of Chef's Catalog

In November 2004, we sold our Chef's Catalog direct marketing business to a private equity firm. Chef's Catalog is a multi-channel retailer of professional-quality kitchenware with revenues of approximately \$73 million in fiscal year 2004. At October 30, 2004, Chef's Catalog had net tangible assets, primarily inventory, of \$12.5 million and net intangible assets of \$17.2 million. We received proceeds, net of selling costs, of \$14.4 million from the sale. As the carrying value of the Chef's Catalog assets exceeded the net proceeds from the sale, we incurred a pre-tax loss of \$15.3 million in the first quarter of 2005 related to the disposition of Chef's Catalog.

## 3. Operating Segments

We have identified two reportable segments: Specialty Retail Stores and Direct Marketing. Our Specialty Retail Stores segment includes all of our Neiman Marcus and Bergdorf Goodman retail stores, including Neiman Marcus clearance stores. Our Direct Marketing segment conducts both print catalog and online operations under the Neiman Marcus, Horchow and Bergdorf Goodman brand names and, until its disposition in November 2004, the Chef's Catalog brand name. Other includes the operations of Kate Spade LLC and Gurwitch Products, LLC (the Brand Development Companies).

Both the Specialty Retail Stores and Direct Marketing segments, as well as Kate Spade LLC and Gurwitch Products, LLC, derive their revenues from the sales of high-end fashion apparel, accessories, cosmetics and fragrances from leading designers, precious and fashion jewelry and decorative home accessories.

The following table sets forth the information for our reportable segments:

(in thousands)	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004	April 30, 2005	May 1, 2004
<b>REVENUES:</b>				
Specialty Retail Stores	\$ 766,877	\$ 717,562	\$ 2,415,749	\$ 2,213,811
Direct Marketing	130,532	126,204	458,514	445,694
Other	35,963	29,401	96,270	80,798
Total	\$ 933,372	\$ 873,167	\$ 2,970,533	\$ 2,740,303
<b>OPERATING EARNINGS:</b>				
Specialty Retail Stores	\$ 125,832	\$ 114,283	\$ 343,781	\$ 276,447
Direct Marketing	16,780	9,791	55,943	45,086
Other	4,572	4,750	10,241	11,821
Subtotal	147,184	128,824	409,965	333,354
Corporate expenses	(12,532)	(9,229)	(30,390)	(26,470)
Loss on disposition of Chef's Catalog			(15,348)	
Total	\$ 134,652	\$ 119,595	\$ 364,227	\$ 306,884

## 4. Stock Repurchase Program

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In prior years, our Board of Directors authorized various stock repurchase programs and increases in the number of shares subject to repurchase. In the third quarter of 2005, we did not repurchase any shares. In the second quarter of 2005, we repurchased 4,100 shares at an average price of \$57.60. In the first quarter of 2005, we repurchased 54,404 shares at an average price of \$52.40. As of April 30, 2005, approximately 1.2 million shares remain available for repurchase under our stock repurchase programs.

5. Earnings per Share

The weighted average shares used in computing basic and diluted earnings per share (EPS) are presented in the table below. We made no adjustments to net earnings for the computations of basic and diluted EPS during the periods presented.

(in thousands of shares)	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004	April 30, 2005	May 1, 2004
Weighted average shares outstanding	48,945	48,557	48,847	48,313
Less: shares of non-vested restricted stock	(555)	(349)	(538)	(384)
Shares for computation of basic EPS	48,390	48,208	48,309	47,929
Effect of dilutive stock options and restricted stock	1,305	916	1,118	877
Shares for computation of diluted EPS	49,695	49,124	49,427	48,806
Shares represented by antidilutive stock options			190	9

We do not include antidilutive stock options in the computation of diluted EPS because the exercise price of those options is greater than the average market price of the common shares.

6. Undivided Interests in NMG Credit Card Master Trust

Pursuant to a revolving credit card securitization program (the Credit Card Facility), we transfer substantially all of our credit card receivables to a wholly-owned subsidiary, Neiman Marcus Funding Corporation, which in turn sells such receivables to the Neiman Marcus Credit Card Master Trust (Trust). At the inception of the Credit Card Facility in September 2000, the Trust issued certificates representing undivided interests in the credit card receivables to third-party investors in the face amount of \$225 million (Sold Interests). We hold certificates representing interests in the credit card portfolio equal to the excess of the balance of the credit card portfolio over \$225 million (Retained Interests). In order to maintain the committed level of securitized assets, the Trust uses cash collections on the securitized receivables to purchase new credit card balances from us in accordance with the terms of the Credit Card Facility.

From the inception of the Credit Card Facility until December 2003, our transfers and sales of credit card receivables pursuant to the terms of the Credit Card Facility were accounted for as sales (Off-Balance Sheet Accounting). As a result, we removed \$225 million of credit card receivables from our balance sheet at the inception of the Credit Card Facility and the Trust's \$225 million repayment obligation to the holders of the certificates representing the Sold Interests was not shown as a liability on our consolidated balance sheet.

Beginning in December 2003, transfers to the Trust ceased to qualify for Off-Balance Sheet Accounting. Rather, credit card receivables transferred to the Trust after November 2003 remain on our balance sheet and our borrowings collateralized by those accounts receivable are recorded as liabilities on our balance sheet (Financing Accounting). The transition period from Off-Balance Sheet Accounting to Financing Accounting (Transition Period) lasted approximately four months (December 2003 to March 2004). During the Transition Period, we allocated cash collections on our credit card receivables to the previous Sold Interests and Retained Interests until such time as those balances were reduced to zero and we recorded a liability for our repayment obligation to the holders of the \$225 million of certificates representing the Sold

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Interests. At the end of the Transition Period, our entire credit card portfolio was included in accounts receivable in our consolidated balance sheet and the \$225 million repayment obligation was shown as a liability.

As of the start of the Transition Period in December 2003, the carrying value of the Sold and Retained Interests exceeded face value by approximately \$7.6 million as a result of the application of the provisions of current accounting rules related to the calculation of the gains on sale of the previous Sold Interests and the valuation of both Sold and Retained Interests. During the Transition Period, the \$7.6 million premium was amortized as a reduction of our net earnings from our credit card portfolio (recorded as a reduction of selling, general and administrative expenses in the consolidated statements of earnings). Of the \$7.6 million premium, \$2.3 million was amortized in the third quarter of 2004.

Beginning in March 2005, cash collections were used by the Trust to begin repayment of the \$225 million principal balance of the Class A Certificates in six monthly installments of \$37.5 million. As of April 30, 2005, the Trust had made the first installment repayment of \$37.5 million to reduce the principal balance of the Class A Certificates to \$187.5 million. In addition, we held cash of \$37.5 million at April 30, 2005, generated from collections received in April 2005 on our credit card receivables, restricted to the payment of the second installment repayment required to be made by the Trust in May 2005.

## 7. Employee Benefit Plans

*Description of Benefit Plans.* We sponsor a defined benefit pension plan (Pension Plan) covering substantially all full-time employees. We also sponsor an unfunded supplemental executive retirement plan (SERP Plan) that provides additional pension benefits to certain employees. Benefits under both plans are based on the employees' years of service and compensation over defined periods of employment. Pension Plan assets consist primarily of equity and fixed income securities.

Retirees and active employees hired prior to March 1, 1989 are eligible to participate in a plan providing certain limited postretirement health care benefits (Postretirement Plan) if they have met certain service and minimum age requirements.

*Costs of Benefits.* The components of the expenses incurred under our Pension Plan, SERP Plan and Postretirement Plan are as follows:

(in thousands)	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004	April 30, 2005	May 1, 2004
<b>Pension Plan:</b>				
Service cost	\$ 3,196	\$ 2,366	\$ 9,588	\$ 8,469
Interest cost	4,636	3,603	13,907	12,894
Expected return on plan assets	(4,712)	(3,612)	(14,137)	(12,928)
Net amortization of losses and prior service costs	1,208	698	3,626	2,498
Pension Plan expense	\$ 4,328	\$ 3,055	\$ 12,984	\$ 10,933
<b>SERP Plan:</b>				
Service cost	\$ 361	\$ 342	\$ 1,084	\$ 1,024
Interest cost	1,014	978	3,042	2,930
Net amortization of losses and prior service costs	384	366	1,151	1,099
SERP Plan expense	\$ 1,759	\$ 1,686	\$ 5,277	\$ 5,053

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Postretirement Plan:

Service cost	\$	15	\$	20	\$	44	\$	60
Interest cost		318		386		954		1,156
Net amortization of losses		26		110		79		331
Postretirement Plan expense	\$	359	\$	516	\$	1,077	\$	1,547



**Funding Policy and Plan Assets.** Our policy is to fund the Pension Plan at or above the minimum required by law. In the third quarter of 2005, we made a voluntary contribution of \$20.0 million for the plan year ended July 31, 2004. In 2004, we made voluntary contributions of \$30.0 million in the second quarter for the plan year ended July 31, 2003 and \$15.0 million in the fourth quarter for the plan year ended July 31, 2004. Based upon currently available information, we will not be required to make contributions to the Pension Plan for either the 2004 or 2005 plan years.

**Effect of Medicare Subsidy on Postretirement Plan.** In December 2003, the U.S Congress enacted the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (Act) that will provide a prescription drug subsidy, beginning in 2006, to companies that sponsor postretirement health care plans that provide drug benefits. Based upon the provisions of the legislation enacted in January 2005, we reviewed the provisions of our Postretirement Plan with our actuaries to determine whether the benefits offered by our plan meet the statutory definition of actuarially equivalent prescription drug benefits that qualify for the federal subsidy. Based upon this review, we believe that our benefits qualify for the subsidy. We expect to avail ourselves of the benefit of the subsidy although we are still evaluating the manner in which we and/or the participants in the Postretirement Plan will receive the subsidy.

As of July 31, 2004, the projected benefit obligation for our Postretirement Plan, using a discount rate of 6.25 percent, was approximately \$21.0 million. In accordance with the provisions of the FASB Staff Position 106-2, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003, we revalued our projected benefit obligation as of January 31, 2005 to 1) incorporate the benefit associated with the federal subsidy we expect to receive and 2) reduce the discount rate to 5.75 percent. The revised obligation as January 31, 2005 is approximately \$19.1 million, reflecting a reduction of approximately \$2.6 million for the impact of the federal subsidy, offset by an increase of approximately \$0.8 million for the change in discount rate.

## 8. Commitments and Contingencies

**We are involved in various suits and claims in the ordinary course of business. We do not believe that the disposition of any such suits or claims will have a material adverse effect upon our consolidated results of operations, cash flows or financial position.**

## 9. Restatements

**Construction Allowances.** We receive allowances from developers related to the construction of our stores. These allowances are recorded as deferred real estate credits and are recognized as a reduction of rent expense on a straight-line basis over the lease term. Prior to 2005, we recorded these allowances as a reduction of capital expenditures and, as a result, the carrying values of our property and equipment. We have corrected the errors in the classification of construction allowances and, as a result, we have restated our balance sheets at May 1, 2004 and July 31, 2004 and our statement of cash flows for the thirty-nine weeks ended May 1, 2004.



*Retained Interests.* Pursuant to the terms of the Credit Card Facility, as more fully described in Note 6, our Retained Interests fluctuate monthly based on the underlying balance of our credit card receivables. We previously reflected the changes in our Retained Interests in the determination of cash flows from investing activities. We have determined that such presentation is not in accordance with generally accepted accounting principles and have corrected such error by restating our statements of cash flows to include the changes in the Retained Interests in the determination of cash flows from operating activities.

**The following table summarizes the impact of these restatements in our previously issued financial statements:**



	As Originally Reported	Construction Allowances	Restatements Changes in Retained Interests	As Restated
<b>Fiscal Year 2004</b>				
<b>Consolidated Balance Sheet:</b>				
Property and equipment, net	\$ 693,772	\$ 56,711	\$	\$ 750,483
Other assets	145,812	15,187		160,999
Total assets	2,545,750	71,898		2,617,648
Deferred real estate credits		71,898		71,898
Total long-term liabilities	437,212	71,898		509,110
<b>Third Quarter 2004</b>				
<b>Consolidated Balance Sheet:</b>				
Property and equipment, net	\$ 685,928	\$ 57,924	\$	\$ 743,852
Other assets	104,158	15,284		119,442
Total assets	2,463,563	73,208		2,536,771
Deferred real estate credits		73,208		73,208
Total long-term liabilities	534,558	73,208		607,766
<b>Consolidated Statement of Cash Flows:</b>				
Net cash used for operating activities	\$ (291,289)	\$ 2,246	\$ 242,565	\$ (46,478)
Net cash provided by (used for) investing activities	161,659	(2,246)	(242,565)	(83,152)

## 10. Recent Developments

*Sale of Company.* On March 16, 2005, we announced that we were exploring various strategic alternatives to enhance shareholder value, including a possible sale of the Company, and that we had retained Goldman Sachs & Co. as the financial advisor to assist us in the review.

On May 1, 2005, our Board of Directors approved a definitive agreement to sell the Company to an investment group consisting of Texas Pacific Group and Warburg Pincus LLC. Under the terms of the agreement, Texas Pacific Group and Warburg Pincus will acquire all of the outstanding Class A and Class B shares of the Company for \$100.00 per share in cash, representing a transaction value of approximately \$5.1 billion. Each of the investors will own equal stakes in the Company upon completion of the transaction. Completion of this transaction is contingent upon regulatory review and approval by the Company's shareholders and is expected to occur by November 1, 2005.

10. Recent Developments (continued)

*Sale of Credit Card Portfolio.* As contemplated in the negotiations that led to the sale of the Company for approximately \$5.1 billion, we entered into a strategic alliance with HSBC-North America's Retail Services (HSBC) on June 8, 2005 to support and enhance our credit card operations. In connection with this transaction, HSBC will purchase the private label credit card accounts and related assets of both Neiman Marcus and Bergdorf Goodman, as well as the outstanding balances associated with such accounts, for an amount equal to the face value of the outstanding receivables and accumulated accounts receivable collections. We expect to close this transaction by July 31, 2005, subject to customary review and closing conditions, for a purchase price of approximately \$640 million, of which we will receive net cash proceeds of approximately \$527 million and HSBC will assume \$113 million of outstanding liabilities under our Credit Card Facility. In addition, we will receive on-going payments based on credit sales generated under the agreement. We will continue to handle key customer service functions including new account processing, transaction authorization, billing adjustments, collection services and customer inquiries.

*Litigation.* On May 4, 2005, a purported class action complaint, *NECA-IBEW Pension Fund (The Decatur Plan) v. The Neiman Marcus Group, Inc. et al.* (CA No. 3-05 CV-0898B), was filed by a putative stockholder of the Company in federal court in the Northern District of Texas against the Company and its directors challenging the proposed merger.

The complaint alleges a cause of action for breach of fiduciary duty against our directors, claiming, among other things, that the merger consideration to be paid to the Company's stockholders in the merger is grossly inadequate and unfair and that the defendants failed to maximize shareholder value through a proper sale of the Company and its assets. In addition, the complaint alleges that the Company's directors breached their fiduciary duties in connection with the approval of the merger by, among other things, tailoring the transaction to serve the interests of the defendants and the family of Richard A. Smith, Chairman of our board of directors and the Company's largest stockholder, rather than structuring the merger to obtain the highest price for our stockholders, depriving public stockholders of the value of certain assets of the Company (primarily the Company's credit card division), failing to realize the financial benefits from a separate sale of the Company's credit card division, not engaging in a fair process of negotiating at arm's length and structuring a preferential deal for Company insiders. The complaint seeks, among other things, injunctive relief to enjoin the consummation of the merger, rescind any actions taken to effect the merger, direct the defendants to sell or auction the Company for the highest possible price, and impose a constructive trust in favor of plaintiffs upon any benefits improperly received by defendants.

The lawsuit is in its preliminary stage. We believe that the lawsuit is without merit and intend to defend vigorously against it.

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

**EXECUTIVE OVERVIEW**

**Company Profile**

The Neiman Marcus Group, Inc., together with its operating divisions and subsidiaries, is a high-end specialty retailer. Our operations include the Specialty Retail Stores segment and the Direct Marketing segment. Our Specialty Retail Stores segment consists primarily of Neiman Marcus and Bergdorf Goodman stores. Our Direct Marketing segment conducts both print catalog and online operations under the brand names of Neiman Marcus, Horchow and Bergdorf Goodman and until its disposition in November 2004, the Chef's Catalog brand name. In November 2004, we sold our Chef's Catalog operations, as more fully described in Note 2 to the Condensed Consolidated Financial Statements.

We own a 51 percent interest in Gurwitch Products, LLC, which distributes and markets the Laura Mercier cosmetic line, and a 56 percent interest in Kate Spade LLC, a manufacturer and retailer of high-end designer handbags and accessories. Gurwitch Products, LLC and Kate Spade LLC are hereafter referred to collectively as the Brand Development Companies.

Our fiscal year ends on the Saturday closest to July 31. All references to the third quarter of 2005 relate to the thirteen weeks ended April 30, 2005 and all references to the third quarter of 2004 relate to the thirteen weeks ended May 1, 2004. All references to 2005 relate to the thirty-nine weeks ended April 30, 2005 and all references to 2004 relate to the thirty-nine weeks ended May 1, 2004.

The information contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) should be read in conjunction with our Annual Report on Form 10-K/A for the fiscal year ended July 31, 2004. Unless otherwise specified, the meanings of all defined terms in MD&A are consistent with the meanings of such terms as defined in the Notes to the Condensed Consolidated Financial Statements.

**Overview of the Business**

We believe that our unique product assortment of luxury, designer and fashion merchandise, coupled with our sales promotion activities and our commitment to superior customer service, have been critical to our success in the past. In addition, we believe these factors are critical to our future growth and success.

We conduct our selling activities in two primary selling seasons - Fall and Spring. The Fall Season is comprised of our first and second fiscal quarters and the Spring Season is comprised of our third and fourth fiscal quarters. The first quarter is generally characterized by a higher level of full-price selling with a focus on the initial introduction of Fall Season fashions. Aggressive in-store marketing activities designed to stimulate customer buying, a lower level of markdowns and higher margins are characteristic of this quarter. The second quarter is more



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focused on promotional activities related to the December holiday season, the early introduction of resort season collections from certain designers and the sale of Fall Season goods on a marked down basis. As a result, margins are typically lower in the second quarter. However, due to the seasonal increase in sales that occurs during the holiday season, the second quarter is typically the quarter in which our sales are the highest and in which expenses are the lowest as a percentage of revenues. Our working capital requirements are also the greatest in the first and second quarters as a result of higher seasonal levels of accounts receivable and inventory.

Similarly, the third quarter is generally characterized by a higher level of full-price selling with a focus on the initial introduction of Spring Season fashions. Aggressive in-store marketing activities designed to stimulate customer buying, a lower level of markdowns and higher margins are again characteristic of this quarter. Sales are generally the lowest in the fourth quarter and are focused on promotional activities offering Spring Season goods to the customer on a marked down basis, resulting in lower margins during the quarter. As a result of the seasonality of our selling activities, inventory management is critical to our success.

Inherent in the successful execution of our business plans, particularly our inventory management strategy, is our ability both to predict the fashion trends that will be of interest to our customers and to anticipate the future spending patterns of our customer base. Accordingly, we monitor the sales performance of our inventories throughout each season. We seek to order additional goods to supplement our original purchasing decisions when the level of customer demand is higher than originally anticipated. However, in certain merchandise categories, particularly fashion apparel, our ability to purchase additional goods can be limited. This can result in lost sales in the event of higher than anticipated demand for the fashion

goods offered or a higher than anticipated level of consumer spending. Conversely, in the event we buy fashion goods that are not accepted by our customer or the level of consumer spending is less than we anticipated, we typically incur a higher than anticipated level of markdowns, net of vendor allowances, to sell the goods that remain at the end of the season, resulting in lower operating profits. We believe that the experience of our merchandising and selling organizations helps to minimize the inherent risk in predicting fashion trends and related demand.

### **Third Quarter Fiscal Year 2005 Highlights**

Diluted earnings per share for the third quarter of 2005 increased 15.0 percent to \$1.61 from \$1.40 in the prior year period. Other significant highlights for the third quarter of 2005 include:

**Revenues** Our revenues for the third quarter of 2005 were \$933.4 million compared to \$873.2 million in the prior year period. Revenues increased 6.9 percent in the third quarter of 2005 while comparable revenues increased 8.0 percent. Year to date, revenues have increased 8.4 percent while comparable revenues have increased 9.9 percent. For Specialty Retail Stores, our sales per square foot for the last twelve trailing months increased to \$564 as of April 2005 compared to \$517 as of April 2004.

**Gross margins** Margins increased to 38.3 percent of revenues in the third quarter of 2005 from 37.6 percent in the third quarter of 2004. Year to date, margins have increased to 36.3 percent of revenues from 35.3 percent in the prior year period. These increases are reflective of the high level of acceptance and demand for the fashion goods we offer as well as our efforts to align purchases and customer demand.

**Selling, general and administrative expenses** Selling, general and administrative (SG&A) expenses decreased to 23.8 percent of revenues in the third quarter of 2005 from 23.9 percent in the third quarter of 2004 and to 23.5 percent of revenues year to date from 24.1 percent in the prior year period.

**Operating earnings** Operating earnings increased 12.6 percent in the third quarter of 2005, representing 14.4 percent of our revenues compared to 13.7 percent in the third quarter of 2004. Year to date, operating earnings increased 18.7 percent, representing 12.3 percent of our revenues for 2005 compared to 11.2 percent in 2004. Operating earnings were 16.4 percent of revenues in the third quarter and 14.2 percent year to date for our Specialty Retail Stores and 12.9 percent of revenues in the third quarter and 12.2 percent year to date for Direct Marketing.

### **Recent Developments**

*Sale of Company.* On March 16, 2005, we announced that we were exploring various strategic alternatives to enhance shareholder value, including a possible sale of the Company, and that we had retained Goldman Sachs & Co. as the

financial advisor to assist us in the review.

**On May 1, 2005, our Board of Directors approved a definitive agreement to sell the Company to an investment group consisting of Texas Pacific Group and Warburg Pincus LLC.** Under the terms of the agreement, Texas Pacific Group and Warburg Pincus will acquire all of the outstanding Class A and Class B shares of The Neiman Marcus Group for \$100.00 per share in cash, representing a transaction value of approximately \$5.1 billion. Each of the investors will own equal stakes in the company upon completion of the transaction. Completion of this transaction is contingent upon regulatory review and approval by the Company's shareholders and is expected to occur by November 1, 2005.

*Sale of Credit Card Portfolio.* As contemplated in the negotiations that led to the sale of the Company for approximately \$5.1 billion, we entered into a strategic alliance with HSBC-North America's Retail Services (HSBC) on June 8, 2005 to support and enhance our credit card operations. In connection with this transaction, HSBC will purchase the private label credit card accounts and related assets of both Neiman Marcus and Bergdorf Goodman, as well as the outstanding balances associated with such accounts, for an amount equal to the face value of the outstanding receivables and accumulated accounts receivable collections. We expect to close this transaction by July 31, 2005, subject to customary review and closing conditions, for a purchase price of approximately \$640 million, of which we will receive net cash proceeds of approximately \$527 million and HSBC will assume \$113 million of outstanding liabilities under our Credit Card Facility. In addition, we will receive on-going payments based on credit sales generated under the agreement. We will continue to handle key customer service functions including new account processing, transaction authorization, billing adjustments, collection services and customer inquiries.

**See Note 10 to the Condensed Consolidated Financial Statements for further discussion.**



## OPERATING RESULTS

## Performance Summary

The following table sets forth certain items expressed as percentages of net sales for the periods indicated.

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004	April 30, 2005	May 1, 2004
Revenues	100.0%	100.0%	100.0%	100.0%
Cost of goods sold including buying and occupancy costs	61.7	62.4	63.7	64.7
Selling, general and administrative expenses	23.8	23.9	23.5	24.1
Loss on disposition of Chef's Catalog			0.5	
Operating earnings	14.4	13.7	12.3	11.2
Interest expense, net	0.3	0.5	0.4	0.4
Earnings before income taxes and minority interest	14.1	13.2	11.9	10.8
Income taxes	5.4	5.1	4.6	3.9
Earnings before minority interest	8.7	8.0	7.3	6.8
Minority interest in net earnings of subsidiaries	(0.1)	(0.1)	(0.1)	(0.1)
Net earnings	8.6%	7.9%	7.2%	6.7%

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Set forth in the following table is certain summary information with respect to our operations for the periods indicated.

(dollars in millions)	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	April 30, 2005	May 1, 2004	April 30, 2005	May 1, 2004
<b>REVENUES</b>				
Specialty Retail Stores	\$ 766.9	\$ 717.6	\$ 2,415.7	\$ 2,213.8
Direct Marketing	130.5	126.2	458.5	445.7
Other (1)	36.0	29.4	96.3	80.8
Total	\$ 933.4	\$ 873.2	\$ 2,970.5	\$ 2,740.3
<b>OPERATING EARNINGS</b>				
Specialty Retail Stores	\$ 125.8	\$ 114.3	\$ 343.8	\$ 276.5
Direct Marketing	16.8	9.8	55.9	45.1
Other (1)	4.6	4.7	10.2	11.8
Subtotal	147.2	128.8	409.9	333.4
Corporate expenses	(12.5)	(9.2)	(30.4)	(26.5)
Loss on disposition of Chef's Catalog			(15.3)	
Total	\$ 134.7	\$ 119.6	\$ 364.2	\$ 306.9
<b>OPERATING PROFIT MARGIN</b>				
Specialty Retail Stores	16.4%	15.9%	14.2%	12.5%
Direct Marketing	12.9%	7.8%	12.2%	10.1%
Total	14.4%	13.7%	12.3%	11.2%
<b>COMPARABLE REVENUES (2)</b>				
Specialty Retail Stores (3)	6.5%	22.2%	9.1%	13.7%
Direct Marketing (4)	16.8%	14.4%	15.3%	18.5%
Total (3), (4)	8.0%	22.0%	9.9%	14.9%
<b>SALES PER SQUARE FOOT</b>				
Specialty Retail Stores	\$ 141	\$ 133	\$ 445	\$ 411
<b>STORE COUNT</b>				
Neiman Marcus and Bergdorf Goodman stores:				
Open at beginning of period	37	37	37	37
Opened during the period				
Open at end of period	37	37	37	37
Clearance centers:				
Open at beginning of period	15	14	14	14
Opened during the period			1	
Open at end of period	15	14	15	14

(1) Other includes the operations of the Brand Development Companies.

(2) Comparable revenues include 1) revenues derived from our retail stores open for more than 52 weeks, including stores that have been relocated or expanded, 2) revenues from our Direct Marketing operations and 3) wholesale revenues from our Brand Development Companies.

(3) The calculation of the changes in comparable revenues has been adjusted to give recognition to the change in classification of revenues deferred in connection with our loyalty programs, as more fully described in Note 1 to the Condensed Consolidated Financial Statements.

(4) The calculation of the changes in comparable revenues has been adjusted to exclude the revenues of Chef's Catalog for all periods prior to our sale of these operations in November 2004, as more fully described in Note 2 to the Condensed Consolidated Financial Statements.

**Thirteen Weeks Ended April 30, 2005 Compared to Thirteen Weeks Ended May 1, 2004**

**Revenues.** Our revenues for the third quarter of 2005 of \$933.4 million increased \$60.2 million, or 6.9 percent, from \$873.2 million in the third quarter of 2004.

Comparable revenues of \$927.7 million in the third quarter of 2005 increased 8.0 percent compared to the prior year period. Comparable revenues increased 6.5 percent for Specialty Retail Stores and 16.8 percent for Direct Marketing. Comparable revenues in the third quarter of 2004 increased by 22.0 percent.

Revenues increased in the third quarter of 2005 compared to the prior year at all our operating companies, consistent with a higher level of consumer spending, in general, with a higher increase coming from the affluent luxury customer served by the Company. In addition, we believe the increases in comparable revenues were driven by sales events conducted by our Specialty Retail Stores and by the growth of internet sales for Direct Marketing. In the third quarter of 2005, internet sales by Direct Marketing were \$73.8 million, an increase of 47.4 percent from the third quarter of 2004.

**Gross margin.** Our gross margin was 38.3 percent of revenues for the third quarter of 2005 compared to 37.6 percent in the prior year period. The increase in gross margin from the prior year period was due primarily to:

the increase in product margins by approximately 0.8 percent of revenues; offset by

an increase in buying and occupancy costs by approximately 0.2 percent of revenues.

We generated higher product margins during the third quarter of 2005. We believe this increase in product margins was due primarily to:

the higher level of full-price sales generated during the quarter by our Specialty Retail Stores;

higher margins realized by Direct Marketing after the disposition of Chef's Catalog, which generated lower margins than our other Direct Marketing brands; and

our continued emphasis on inventory management.



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Consistent with industry business practice, we receive allowances from certain of our vendors in support of the merchandise we purchase for resale. We receive certain allowances to reimburse us for markdowns taken and/or to support the gross margins earned in connection with the sales of the vendor's merchandise. We recognize these allowances as an increase to gross margin when the allowances are earned and approved by the vendor. Other allowances we receive represent reductions to the amounts paid to acquire the merchandise. We recognize these allowances as a reduction in the cost of the acquired merchandise resulting in an increase to gross margin at the time the goods are sold. As a percentage of revenues, the level of vendor allowances we received in the third quarter of 2005 was consistent with the prior year and did not have a significant impact on the year-over-year change in the gross margin we realized in the third quarter of 2005.

A significant portion of our buying and occupancy costs are fixed in nature. Buying and occupancy costs increased as a percentage of revenues during the third quarter of 2005 compared to the prior year period primarily due to higher depreciation and rent expenses as a percentage of revenues due to:

a higher level of capital spending in recent years; and

adjustments to rent and depreciation aggregating approximately \$2.6 million, or 0.3 percent of revenues, made in connection with our review of the amortization periods assigned to our leased property and equipment and deferred real estate credits.

*Selling, general and administrative expenses.* SG&A expenses were 23.8 percent of revenues in the third quarter of 2005 compared to 23.9 percent of revenues in the prior year period.

The net decrease in SG&A expenses as a percentage of revenues in the third quarter of 2005 was primarily due to:

a decrease in marketing and advertising costs by approximately 0.5 percent of revenues primarily due to the elimination of expenditures for Chef's Catalog, which were higher as a percentage of revenues than our other Direct Marketing brands; and

an increase in the net income generated by our credit card portfolio by approximately 0.1 percent of revenues consistent with the increase in our sales.

In addition, SG&A expense declined as a percentage of revenues in the third quarter of 2005 compared to the prior year period by approximately 0.3 percent due to a \$2.3 million reduction in the income generated by our credit card portfolio in the third quarter of 2004 related to the required amortization of the premium associated with the carrying values of the Retained and Sold Interests, as more fully described in Note 6 of the Notes to Condensed Consolidated Financial Statements.

These decreases in SG&A expenses, as a percentage of revenues, were partially offset by:

higher employee benefit expenses, including medical and pension expenses, by approximately 0.3 percent of revenues;

an increase in costs, primarily payroll, by approximately 0.2 percent of revenues, incurred by our Direct Marketing and the Brand Development Companies in support of new business initiatives and the expansion of Kate Spade operations; and

the increase in professional fees and other costs incurred in connection with the proposed sale of the Company by approximately 0.1 percent of revenues.

**Segment operating earnings.** Operating earnings for our Specialty Retail Stores segment were \$125.8 million for the third quarter of 2005 compared to \$114.3 million for the prior year period. This 10.1 percent increase was primarily the result of increased revenues and gross margins and net decreases in SG&A expenses as a percentage of revenues, offset by increases in buying and occupancy expenses as a percentage of revenues.

Operating earnings for Direct Marketing increased to \$16.8 million in the third quarter of 2005 from \$9.8 million for the prior year period, primarily as a result of increased revenues and gross margins and net decreases in both buying and occupancy costs and SG&A expenses as

percentages of revenues.

**Interest expense, net.** Net interest expense was \$2.9 million in the third quarter of 2005 and \$4.6 million for the prior year period. The decrease in net interest expense is primarily due to increases in 1) investment income generated by higher cash balances and 2) capitalized interest charges associated with store construction and remodeling activities.

**Income taxes.** Our effective income tax rate was 38.5 percent for the third quarter of 2005 and 39.0 percent for the prior year period.

**Thirty-Nine Weeks Ended April 30, 2005 Compared to Thirty-Nine Weeks Ended May 1, 2004**

**Revenues.** Our revenues for 2005 of \$2,970.5 million increased \$230.2 million, or 8.4 percent, from \$2,740.3 million in 2004.

Comparable revenues of \$2,942.8 million in 2005 increased 9.9 percent compared to the prior year period. Comparable revenues increased 9.1 percent for Specialty Retail Stores and 15.3 percent for Direct Marketing. Comparable revenues in 2004 increased by 14.9 percent.

Excluding the revenues from our Chef's Catalog operations in 2004, revenues increased in 2005 compared to the prior year at all our operating companies, consistent with a higher level of consumer spending, in general, with a higher increase coming from the affluent luxury customer served by the Company. In addition, we believe the increases in comparable revenues were driven by sales events conducted by our Specialty Retail Stores and by the growth of internet sales for Direct Marketing. In 2005, internet sales by Direct Marketing, excluding Chef's Catalog, were \$233.1 million, an increase of 46.8 percent from 2004.

**Gross margin.** Gross margin was 36.3 percent of revenues in 2005 compared to 35.3 percent in the prior year period. The increase in gross margin was due primarily to:

the increase in product margins by approximately 0.9 percent of revenues; and

a decrease in buying and occupancy costs by approximately 0.2 percent of revenues.

We generated higher product margins at both our Specialty Retail Stores and our Direct Marketing operations during 2005. We believe the increase in product margins at our Specialty Retail Stores was due primarily to the higher level of full-price sales generated for the period, a lower level of net markdowns and our continued emphasis on inventory management. We also generated higher product margins in our Direct Marketing operations in 2005 subsequent to our disposition of Chef's Catalog in November 2004. Chef's Catalog generated lower margins than our other Direct Marketing brands. However, we have incurred a higher level of net markdowns in 2005 for Direct Marketing due primarily to lower than anticipated sales in our catalog operations during the December holiday season.

Consistent with industry business practice, we receive allowances from certain of our vendors in support of the merchandise we purchase for resale. We receive certain allowances to reimburse us for markdowns taken and/or to support the gross margins earned in connection with the sales of the vendor's merchandise. We recognize these allowances as an increase to gross margin when the allowances are earned and approved by the vendor. Other allowances we receive represent reductions to the amounts paid to acquire the merchandise. We recognize these allowances as a reduction in the cost of the acquired merchandise resulting in an increase to gross margin at the time the goods are sold. While the dollar value of the vendor reimbursements we received decreased slightly as a percentage of revenues in 2005 compared to the prior year period, primarily due to a higher level of full-price selling, this decrease did not have a significant impact on the year-over-year change in the gross margin we realized in 2005.

A significant portion of our buying and occupancy costs are fixed in nature. Buying and occupancy costs decreased as a percentage of revenues during 2005 compared to the prior year period primarily due to the leveraging of fixed expenses, including payroll expenses and depreciation, over the higher level of revenues we generated during 2005. Included in buying and occupancy costs in 2005 are adjustments to rent and depreciation aggregating approximately \$4.8 million, or 0.2 percent of revenues, made in the second and third quarters of 2005 in connection with our review of the amortization periods assigned to our leased property and equipment and deferred real estate credits.

**Selling, general and administrative expenses.** SG&A expenses were 23.5 percent of revenues in 2005 compared to 24.1 percent of revenues in the prior year period.

The net decrease in SG&A expenses as a percentage of revenues in 2005 was primarily due to:

a decrease in marketing and advertising costs by approximately 0.3 percent of revenues, primarily due to the elimination of expenditures for Chef's Catalog which were higher as a percentage of revenues than for our other Direct Marketing brands;

a decrease in incentive compensation by approximately 0.2 percent of revenues; and

an increase in the net income generated by our credit card portfolios by approximately 0.1 percent of revenues consistent with the increase in our sales revenues.

In addition, SG&A expense declined as a percentage of revenues in 2005 by approximately 0.3 percent due to a \$7.6 million reduction in the income generated by our credit card portfolio in 2004 related to the required amortization of the premium associated with the carrying value of the Retained and Sold Interests, as more fully described in Note 6 of the Notes to Condensed Consolidated Financial Statements.

These decreases in SG&A expenses as a percentage of revenues, were partially offset by:

an increase in costs, primarily payroll, by approximately 0.2 percent of revenues incurred by Direct Marketing and the Brand Development Companies in support of new business initiatives and the expansion of Kate Spade operations;

an increase in employee benefit expenses, including medical and pension expenses, by approximately 0.1 percent of revenues; and

a \$3.7 million reduction in SG&A expenses recorded in the second quarter of 2004 for the favorable impact of conclusions of certain sales tax and unclaimed property examinations for which the agreed-on settlements were less than the amounts we previously estimated.

**Loss on disposition of Chef's Catalog.** In November 2004, we sold our Chef's Catalog direct marketing business to a private equity firm. Chef's Catalog is a multi-channel retailer of professional-quality kitchenware with revenues of approximately \$73 million in fiscal year 2004. At October 30, 2004, Chef's Catalog had net tangible assets, primarily inventory, of \$12.5 million and net intangible assets of \$17.2 million. We received proceeds, net of selling costs, of \$14.4 million from the sale. As the carrying value of the Chef's Catalog assets exceeded the net proceeds from the sale, we incurred a pre-tax loss of \$15.3 million in the first quarter of 2005 related to the disposition of Chef's Catalog.

**Segment operating earnings.** Operating earnings for our Specialty Retail Stores segment were \$343.8 million for 2005 compared to \$276.5 million for the prior year period. This 24.4 percent increase was primarily the result of increased sales and margins and net decreases in both buying and occupancy expenses and SG&A expenses as a percentage of revenues.

Operating earnings for Direct Marketing increased to \$55.9 million in 2005 from \$45.1 million for the prior year period, primarily as a result of increased revenues and margins and a decrease in SG&A expenses as a percentage of revenues.

**Interest expense, net.** Net interest expense was \$10.9 million in 2005 and \$11.8 million for the prior year period.

The net decrease in net interest expense was due to increases in:

interest income generated by higher cash balances;

capitalized interest charges associated with store construction and remodeling activities, offset by;

an increase in the interest expense attributable to the monthly distributions to the holders of the Sold Interests that began to be charged to interest expense in December 2003 as a result of the discontinuance of Off-Balance Sheet Accounting.

*Income taxes.* Our effective income tax rate was 38.5 percent for 2005 and 36.5 percent for the prior year period. In the second quarter of 2004, the Company recognized a net income tax benefit of \$7.5 million related to favorable settlements associated with previous state tax filings. Excluding this benefit, the effective tax rate was 39.0 percent for 2004.

## **Outlook**

Based on current estimates, we anticipate increases in comparable store revenues of 5 to 7 percent for our fourth quarter ending July 30, 2005. Comparable revenues increased by 12.6 percent in our quarter ended July 31, 2004. The accuracy of our assumptions and forecasts is subject to uncertainties and circumstances beyond our control. Consequently, actual results could differ materially from the forecasted results. See *Factors That May Affect Future Results* for a discussion of items and events that could cause our actual results to vary from our expectations.

## **Inflation and Deflation**

We believe changes in revenues and net earnings that have resulted from inflation or deflation have not been material during the periods presented. In recent years, we have experienced certain inflationary conditions related to 1) increases in product costs due primarily to changes in foreign currency exchange rates that have reduced the purchasing power of the U.S. dollar and 2) increases in SG&A. We attempt to offset the effects of inflation through control of expenses and price increases, although our ability to increase prices may be limited by competitive factors. We attempt to offset the effects of merchandise deflation, which has occurred on a limited basis in recent years, through control of expenses. There is no assurance, however, that inflation or deflation will not materially affect our operations in the future.

**LIQUIDITY AND CAPITAL RESOURCES**





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Our cash requirements consist principally of:

the funding of our accounts receivable and merchandise purchases;

capital expenditures for new store growth, store renovations and upgrades of our management information systems;

debt service requirements; and

obligations related to our Pension Plan.

Our working capital requirements fluctuate during the year, increasing substantially during the first and second quarters of each fiscal year as a result of higher seasonal levels of accounts receivable and inventory. We typically finance the increases in working capital needs during the first and second fiscal quarters with cash flows from operations, cash provided from the Credit Card Facility and borrowings under our \$350 million unsecured Credit Agreement.

Our primary sources of short-term liquidity are comprised of cash on hand and availability under our Credit Agreement. As of April 30, 2005, we had cash and cash equivalents of \$337.6 million and no outstanding borrowings under our Credit Agreement. Our cash and cash equivalents consisted principally of invested cash and store operating cash. At May 1, 2004, we had cash and cash equivalents of \$312.0 million and no outstanding borrowings under a previous \$300 million unsecured revolving credit facility. The amount of cash on hand and borrowings under the credit facility are influenced by a number of factors, including revenues, accounts receivable and inventory levels, vendor terms, the level of capital expenditures, cash requirements related to financing instruments, Pension Plan funding obligations and tax payment obligations, among others.

We believe that operating cash flows, currently available vendor financing and amounts available pursuant to our Credit Agreement should be sufficient to fund our operations and debt service requirements, including repayment of the \$225 million Credit Card Facility, Pension Plan funding requirements, contractual obligations and commitments and currently anticipated capital expenditure requirements through the end of 2005.

We generated cash from operations, prior to changes in operating assets and liabilities, of \$339.2 million in 2005 compared to \$285.0 million in prior year period. This \$54.2 million increase in cash generated from operations was due to higher sales and earnings levels realized in 2005. Net cash provided by operating activities was \$190.0 million in 2005. In the presentation of net cash flows used for operating activities in 2004 of \$46.5 million in the accompanying statement of cash flows, the cash generated from operations was reduced by the increase in the undivided interests in the NMG Credit Card Master Trust and accounts receivable from \$265.7 million at August 2, 2003 to \$599.6 million at May 1, 2004. This increase in accounts receivable is attributable both to a higher investment in accounts receivable due to higher revenues during 2005 and the discontinuance of Off-Balance Sheet Accounting beginning in December 2003, as more fully described in Note 6 of the Notes to Condensed Consolidated Financial Statements.

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Net cash used for investing activities was \$173.9 million in 2005 compared to \$83.2 million in the prior year period. The increase in cash used for investing activities in 2005 was primarily due to a higher level of capital expenditures in 2005 and the \$37.5 million of cash restricted as of April 30, 2005 for the repayment of the outstanding indebtedness on our Credit Card Facility, offset by \$14.4 million of proceeds from the sale of Chef's Catalog in 2005.

Capital expenditures were \$150.8 million in 2005 and \$83.2 million in the prior year period. We incurred capital expenditures in the third quarter of 2005 related to the ongoing construction of new stores in San Antonio, Texas and Boca Raton, Florida and the remodels of our San Francisco, Houston, Los Angeles and Newport Beach stores. We currently project capital expenditures for 2005 to be approximately \$200 million to \$210 million primarily for new store construction, store renovations and upgrades to information systems, including warehousing systems to support our Direct Marketing operation and a new human capital management system. In support of our store construction and renovation activities, we expect to receive construction allowances of \$20 million to \$25 million in 2005. We completed the renovation of our store in Newport Beach in the third quarter of 2005 and we are currently remodeling our stores in Los Angeles, San Francisco and Houston. We expect to complete the expansion and renovation of the Los Angeles store in the fourth quarter of 2005 and the San Francisco and Houston stores in the spring of fiscal year 2006. We expect to open our San Antonio and Boca Raton stores in the first quarter of fiscal year 2006.

## Financing Structure

Our major sources of funds are comprised of vendor financing, the \$350 million unsecured Credit Agreement, the \$225 million Credit Card Facility, \$125 million senior unsecured notes, \$125 million senior unsecured debentures, operating leases and capital leases.

At April 30, 2005, we had \$187.5 million borrowings under our Credit Card Facility. Repayment of this obligation began in April 2005 in six monthly installments of \$37.5 million. Borrowings pursuant to the Credit Card Facility bear interest at the contractually-defined rate of one month LIBOR plus 0.27 percent (3.22 percent at April 30, 2005) and are payable monthly to the holders of the Class A Certificates.

In the second quarter of 2005, our Board of Directors increased our quarterly cash dividend to \$0.15 per share from \$0.13 per share in the prior year quarter. We declared dividends on April 29, 2005 aggregating \$7.4 million. These dividends were paid in May 2005.

In prior years, our Board of Directors authorized various stock repurchase programs and increases in the number of shares subject to repurchase. We did not repurchase any shares in the third quarter of 2005. As of April 30, 2005, approximately 1.2 million shares remain available for repurchase under the stock repurchase programs.

## Off-Balance Sheet Arrangements

Pursuant to a revolving Credit Card Facility, we transfer substantially all of our credit card receivables to a wholly-owned subsidiary, Neiman Marcus Funding Corporation, which in turn sells such receivables to the Neiman Marcus Credit Card Master Trust (Trust). At the inception of the Credit Card Facility in September 2000, the Trust issued certificates representing undivided interests in the credit card receivables to third-party investors in the face amount of \$225 million (Sold Interests). We hold certificates representing interests in the credit card portfolio equal to the excess of the balance of the credit card portfolio over \$225 million (Retained Interests). In order to maintain the committed level of securitized assets, the Trust uses cash collections on the securitized receivables to purchase new credit card balances from us in accordance with the terms of the Credit Card Facility.

From the inception of the Credit Card Facility until December 2003, our transfers and sales of credit card receivables pursuant to the terms of the Credit Card Facility were accounted for as sales (Off-Balance Sheet Accounting). As a result, we removed the \$225 million of credit card receivables sold from our balance sheet at the inception of the Credit Card Facility and our \$225 million repayment obligation to the holders of the certificates representing the Sold Interests was not required to be shown as a liability on our consolidated balance sheet.

As more fully described in Note 6 of the Notes to Condensed Consolidated Financial Statements, beginning in December 2003, subsequent transfers to the Trust ceased to qualify for Off-Balance Sheet Accounting. Rather, credit card receivables transferred to the Trust after November 2003 remain on our balance sheet and are recorded as secured borrowings. Our entire credit card portfolio is now included in accounts receivable and the outstanding borrowings under the Credit Card Facility are shown as a liability in our condensed consolidated balance sheet.

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Beginning in March 2005, cash collections were used by the Trust to begin repayment of the \$225 million principal balance of the Class A Certificates in six monthly installments of \$37.5 million. As of April 30, 2005, the Trust had made the first installment repayment of \$37.5 million to reduce the principal balance of the Class A Certificates to \$187.5 million. In addition, we held cash of \$37.5 million at April 30, 2005, generated from collections received in April 2005 on our credit card receivables, restricted to the payment of the second installment repayment required to be made by the Trust in May 2005.

## OTHER MATTERS

### Factors That May Affect Future Results

Matters discussed in MD&A include forward-looking statements. Forward-looking statements generally can be identified by the use of forward-looking terminology such as may, will, plan, project, predict, expect, estimate, intend, would, could, should, and anticipate. We make these forward-looking statements based on our expectations and beliefs concerning future events, as well as currently available data. These forward-looking statements involve a number of risks and uncertainties and, therefore, are not guarantees of future performance. A variety of factors could cause our actual results to differ materially from the anticipated or expected results expressed in our forward-looking statements. Factors that could affect future performance include, but are not limited, to:

#### Political and General Economic Conditions

current political and general economic conditions or changes in such conditions;

terrorist activities in the United States;

political, social, economic, or other events resulting in the short or long-term disruption in business at our stores, distribution centers or offices;

#### Customer Demographic Issues

changes in the demographic or retail environment;

changes in consumer confidence resulting in a reduction of discretionary spending on goods that are, or are perceived to be, luxuries ;

changes in consumer preferences or fashion trends;

changes in our relationships with key customers;

changes in our proprietary credit card arrangement that adversely impact our ability to provide consumer credit;

**Merchandise Procurement and Supply Chain Considerations**

changes in our relationships with designers, vendors and other sources of merchandise, including adverse changes in their financial viability;

delays in receipt of merchandise ordered due to work stoppages and/or other causes of delay in connection with either the manufacture or shipment of such merchandise;

changes in foreign currency exchange rates;

significant increases in paper, printing and postage costs;

**Industry and Competitive Factors**

competitive responses to our marketing, merchandising and promotional efforts and/or inventory liquidations by vendors or other retailers;

seasonality of the retail business;

adverse weather conditions or natural disasters, particularly during peak selling seasons;

delays in anticipated store openings and renovations;

**Employee Considerations**

changes in key management personnel;

changes in our relationships with certain of our key sales associates;

**Legal and Regulatory Issues**

changes in government or regulatory requirements increasing our costs of operations;



litigation that may have an adverse effect on our financial results or reputation;

**Other Factors**

impact of funding requirements related to our noncontributory defined benefit pension plan; and

the design and implementation of new information systems as well as enhancements of existing systems.

**We undertake no obligation to update or revise (publicly or otherwise) any forward-looking statements to reflect subsequent events, new information or future circumstances.**

**Critical Accounting Policies**

The preparation of condensed financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions about future events. These estimates and assumptions affect amounts of assets, liabilities, revenues and expenses and the disclosure of gain and loss contingencies at the date of the Condensed Consolidated Financial Statements. While we believe that our past estimates and assumptions have been materially accurate, our current estimates are subject to change if different assumptions as to the outcome of future events were made. We evaluate our estimates and judgments on an ongoing basis and predicate those estimates and judgments on historical experience and on various other factors that we believe are reasonable under the circumstances. We make adjustments to our assumptions and judgments when facts and circumstances dictate. Since future events and their effects cannot be determined with absolute certainty, actual results may differ from the estimates we used in preparing the accompanying Condensed Consolidated Financial Statements.

**See Note 1 of the Notes to Condensed Consolidated Financial Statements in Item 1 for a summary of our critical accounting policies. A complete description of our critical accounting policies is included in our amendment to the Annual Report to Shareholders on Form 10-K/A for the fiscal year ended July 31, 2004.**



**Reclassification Loyalty Programs.** As more fully described in Note 1, a substantial portion of the points earned by customers in connection with our loyalty programs are redeemed for gift cards. At the time the qualifying sales giving rise to the loyalty program points are made, we defer the portion of the revenues on the qualifying sales transactions equal to our estimate of the retail value of the gift cards to be issued upon conversion of the points to gift cards. Beginning in the first quarter of 2005, we began to record the deferral of revenues related to gift card awards under our loyalty programs as a reduction of revenues. Previously, we charged such amounts to selling, general and administrative expenses. In addition, we now charge the cost of all other awards under our loyalty programs to cost of goods sold rather than SG&A. These changes in classification do not impact the previously reported operating earnings, net income or earnings per share amounts.

**Changes in Comparable Revenues.** As more fully described in Note 2, we have sold our Chef's Catalog operations. The changes in comparable revenues have been adjusted 1) to exclude the revenues of Chef's Catalog operations for all periods prior to the sale and 2) to give recognition to the change in classification of revenues deferred in connection with our loyalty programs and are summarized below:

	Total	Specialty Retail Stores	Direct Marketing
<b>Fiscal Year 2004:</b>			
First quarter	10.9%	9.6%	13.2%
Second quarter	12.7%	10.2%	25.7%
Third quarter	22.0%	22.2%	14.4%
Fourth quarter	12.6%	11.3%	21.7%
Fiscal year 2004	14.4%	13.1%	19.2%
<b>Fiscal Year 2003:</b>			
First quarter	6.3%	5.0%	15.7%
Second quarter	0.9%	(2.1)%	18.7%
Third quarter	1.6%	(0.6)%	14.8%
Fourth quarter	9.0%	6.3%	22.3%
Fiscal year 2003	4.1%	1.8%	17.8%

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

The market risk inherent in our financial instruments represents the potential loss arising from adverse changes in interest rates and foreign currency exchange rates. We do not enter into derivative financial instruments for trading purposes. We seek to manage exposure to adverse interest rate changes through our normal operating and financing activities. We are exposed to interest rate risk through our securitization and borrowing activities, which are described in Notes 2 and 5 to our Consolidated Financial Statements in our amendment to the Annual Report on Form 10-K/A for the fiscal year ended July 31, 2004.

As of April 30, 2005, we had no borrowings outstanding under our Credit Agreement. Future borrowings under our Credit Agreement, to the extent of outstanding borrowings, would be affected by interest rate changes.

Our outstanding long-term debt as of April 30, 2005 is at fixed interest rates and would not be affected by interest rate changes. Based upon quoted prices, the fair value of our senior notes and debentures (face value of \$250 million) was \$273.9 million as of April 30, 2005.

Pursuant to our proprietary credit card securitization program that begins to expire in September 2005, we have sold substantially all of our credit card receivables through a subsidiary in exchange for certificates representing undivided interests in such receivables. We sold the Class A Certificates, which have an aggregate principal value of \$225 million, to investors. The holders of the Class A Certificates are entitled to monthly interest distributions from the Trust at the contractually-defined rate of one month LIBOR plus 0.27 percent annually. The distributions to the Class A Certificate holders are payable from the finance charge income generated by the credit card receivables held by the Trust. At April 30, 2005, we estimate a 100 basis point increase in LIBOR would result in an approximate annual increase of \$2.25 million in the interest distributions to the Class A Certificate holders.

We use derivative financial instruments to manage foreign currency risk related to the procurement of merchandise inventories from foreign sources. We enter into foreign currency contracts denominated in the euro and British pound. We had foreign currency contracts in the form of forward exchange contracts in the amount of approximately \$35.7 million as of April 30, 2005. The market risk inherent in these instruments was not material to our consolidated financial position, results of operations or cash flows in the third quarter of 2005.

**The effects of changes in the U.S. equity and bond markets serve to increase or decrease the value of Pension Plan assets, resulting in an increase or decrease in our cash funding obligation. We seek to manage exposure to adverse equity and bond returns by maintaining diversified investment portfolios and utilizing professional investment managers.**

Based on a review of our financial instruments outstanding at April 30, 2005 that are sensitive to market risks, we have determined that there was no material market risk exposure to our consolidated financial position, results of operations, or cash flows as of such date.

### ITEM 4. CONTROLS AND PROCEDURES

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In accordance with Exchange Act Rules 13a-15 and 15d-15, we carried out an evaluation, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, as well as other key members of our management, of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective, as of the end of the period covered by this report, to provide reasonable assurance that information we are required to disclose in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

In the ordinary course of business, we routinely enhance our information systems by either upgrading our current systems or implementing new systems. No change in our internal controls occurred during the quarter ended April 30, 2005 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

**PART II**

**ITEM 1. LEGAL PROCEEDINGS**

We are involved in various suits and claims in the ordinary course of business. We do not believe that the disposition of any such suits or claims will have a material adverse effect upon our consolidated results of operations, cash flows or financial position. This belief is subject to the risks and uncertainties discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations Factors That May Affect Future Results.

On May 4, 2005, a purported class action complaint, *NECA-IBEW Pension Fund (The Decatur Plan) v. The Neiman Marcus Group, Inc. et al.* (CA No. 3-05 CV-0898B), was filed by a putative stockholder of the Company in federal court in the Northern District of Texas against the Company and its directors challenging the proposed merger.

The complaint alleges a cause of action for breach of fiduciary duty against our directors, claiming, among other things, that the merger consideration to be paid to the Company's stockholders in the merger is grossly inadequate and unfair and that the defendants failed to maximize shareholder value through a proper sale of the Company and its assets. In addition, the complaint alleges that the Company's directors breached their fiduciary duties in connection with the approval of the merger by, among other things, tailoring the transaction to serve the interests of the defendants and the family of Richard A. Smith, Chairman of our board of directors and the Company's largest stockholder, rather than structuring the merger to obtain the highest price for our stockholders, depriving public stockholders of the value of certain assets of the Company (primarily the Company's credit card division), failing to realize the financial benefits from a separate sale of the Company's credit card division, not engaging in a fair process of negotiating at arm's length and structuring a preferential deal for Company insiders. The complaint seeks, among other things, injunctive relief to enjoin the consummation of the merger, rescind any actions taken to effect the merger, direct the defendants to sell or auction the Company for the highest possible price, and impose a constructive trust in favor of plaintiffs upon any benefits improperly received by defendants.

The lawsuit is in its preliminary stage. We believe that the lawsuit is without merit and intend to defend vigorously against it.

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



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The following table indicates our repurchases of equity securities in the third quarter of 2005:

Third Quarter 2005	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number of Shares that May Yet Be Purchased under the Plans or Programs
February 2005 (1/30/05 to 2/26/05)				1,155,869
March 2005 (2/27/05 to 4/2/05)				1,155,869
April 2005 (4/3/05 to 4/30/05)				1,155,869

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(1) In April 2000, the Board of Directors authorized up to 4.0 million shares to be repurchased, with no expiration date.



**ITEM 6. EXHIBITS**

- 2.1 Agreement and Plan of Merger, dated May 1, 2005, among The Neiman Marcus Group, Inc., Newton Acquisition, Inc., and Newton Merger Sub, Inc., incorporated herein by reference to the Company's Current Report on Form 8-K dated May 4, 2005.
- 3.1 Restated Certificate of Incorporation of the Company, incorporated herein by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended January 26, 2002.
- 3.2 Bylaws of the Company, incorporated herein by reference to the Company's Current Report on Form 8-K dated April 8, 2005.
- 4.1 Certificates of Designation with respect to Series A Junior Participating Preferred Stock, Series B Junior Participating Preferred Stock and Series C Junior Participating Preferred Stock, incorporated herein by reference to the Company's Annual Report on Form 10-K for the fiscal year ended July 31, 2004.
- 4.2 Indenture, dated as of May 27, 1998, between the Company and The Bank of New York, as trustee (the Indenture), incorporated herein by reference to the Company's Annual Report on Form 10-K for the fiscal year ended July 31, 2004.
- 4.3 Form of 6.65 percent Senior Note Due 2008, dated May 27, 1998, issued by the Company pursuant to the Indenture, incorporated herein by reference to the Company's Annual Report on Form 10-K for the fiscal year ended July 31, 2004.
- 4.4 Form of 7.125 percent Senior Note Due 2008, dated May 27, 1998, issued by the Company pursuant to the Indenture, incorporated herein by reference to the Company's Annual Report on Form 10-K for the fiscal year ended July 31, 2004.
- 4.5 Amended and Restated Rights Agreement, dated as of August 8, 2002, between the Company and Mellon Investor Services LLC, as Rights Agent, incorporated herein by reference to the Company's Annual Report on Form 10-K for the fiscal year ended August 3, 2002.
- 4.6 First Amendment to the Amended and Restated Rights Agreement, dated as of May 1, 2005, between The Neiman Marcus Group, Inc. and other parties signatory thereto, incorporated herein by reference to the Company's Current Report on Form 8-K dated May 4, 2005.
- 10.43\* Change of Control Termination Protection Agreement between the Company and Burton M. Tansky dated April 1, 2005. (1)
- 10.44\* Form of Change of Control Termination Protection Agreement between the Company and certain eligible executives, including the named executive officers, dated April 1, 2005, (1)
- 10.45\* The Neiman Marcus Group, Inc. Executive Change of Control Severance Plan dated April 1, 2005, (1)
- 10.46\* The Neiman Marcus Group, Inc. General Change of Control Severance Plan dated April 1, 2005. (1)
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (1)
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (1)
- 32 Certifications of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1)

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(1) Filed herewith.

\* Management contract or compensatory plan or arrangement.

SIGNATURES

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

THE NEIMAN MARCUS GROUP, INC.  
(Registrant)

<b>Signature</b>	<b>Title</b>	<b>Date</b>
/s/ T. Dale Stapleton T. Dale Stapleton	Vice President and Controller and Duly Authorized Officer (principal accounting officer)	June 9, 2005