

STAGE STORES INC  
Form 10-Q  
December 08, 2016

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

Form 10-Q

(Mark One)

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

For the quarterly period ended October 29, 2016

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-14035

Stage Stores, Inc.

(Exact name of registrant as specified in its charter)

NEVADA

(State or other jurisdiction of incorporation or organization) 91-1826900 (I.R.S. Employer Identification No.)

2425 West Loop South, Houston, Texas

(Address of principal executive offices)

77027

(Zip Code)

(800) 579-2302

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

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Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of December 1, 2016, there were 27,165,301 shares of the registrant's common stock outstanding.

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## PART I – FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

Stage Stores, Inc.

Condensed Consolidated Balance Sheets

(in thousands, except par value)

(Unaudited)

|  | October 29,<br>2016 | January 30,<br>2016 |
|--|---------------------|---------------------|
| <b>ASSETS</b>  |                     |                     |
| Cash and cash equivalents  | \$18,902            | \$16,487            |
| Merchandise inventories, net   | 569,343             | 435,996             |
| Prepaid expenses and other current assets  | 60,283              | 48,279              |
| Total current assets   | 648,528             | 500,762             |
| Property, equipment and leasehold improvements, net of accumulated depreciation of \$660,056 and \$621,649, respectively | 315,865             | 311,717             |
| Intangible assets  | 15,235              | 15,235              |
| Other non-current assets, net  | 22,711              | 20,385              |
| Total assets   | \$1,002,339         | \$848,099           |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                     |                     |
| Accounts payable   | \$210,995           | \$84,019            |
| Accrued expenses and other current liabilities   | 64,126              | 71,863              |
| Total current liabilities  | 275,121             | 155,882             |
| Long-term debt obligations   | 236,592             | 162,876             |
| Other long-term liabilities  | 100,549             | 99,588              |
| Total liabilities  | 612,262             | 418,346             |
| Commitments and contingencies  |                     |                     |
| Common stock, par value \$0.01, 100,000 shares authorized, 32,331 and 32,030 shares issued, respectively                 | 323                 | 320                 |
| Additional paid-in capital   | 409,690             | 406,034             |
| Treasury stock, at cost, 5,175 shares, respectively  | (43,301)            | (43,068)            |
| Accumulated other comprehensive loss   | (5,936)             | (6,353)             |
| Retained earnings  | 29,301              | 72,820              |
| Total stockholders' equity   | 390,077             | 429,753             |
| Total liabilities and stockholders' equity   | \$1,002,339         | \$848,099           |

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

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Stage Stores, Inc.

Condensed Consolidated Statements of Operations and Comprehensive Loss

(in thousands, except per share data)

(Unaudited)

|   | Three Months Ended |             | Nine Months Ended |             |
|---|--------------------|-------------|-------------------|-------------|
|   | October 29,        | October 31, | October 29,       | October 31, |
|   | 2016               | 2015        | 2016              | 2015        |
| Net sales   | \$317,140          | \$351,575   | \$988,275         | \$1,101,804 |
| Cost of sales and related buying, occupancy and distribution expenses                                   | 260,550            | 275,479     | 779,128           | 846,324     |
| Gross profit  | 56,590             | 76,096      | 209,147           | 255,480     |
| Selling, general and administrative expenses  | 84,564             | 92,096      | 260,076           | 281,783     |
| Interest expense  | 1,395              | 743         | 3,616             | 1,995       |
| Loss before income tax  | (29,369 )          | (16,743 )   | (54,545 )         | (28,298 )   |
| Income tax benefit  | (13,735 )          | (6,560 )    | (23,492 )         | (11,093 )   |
| Net loss  | \$(15,634 )        | \$(10,183 ) | \$(31,053 )       | \$(17,205 ) |
| Other comprehensive income:   |                    |             |                   |             |
| Amortization of employee benefit related costs, net of tax of \$86, \$74, \$256 and \$221, respectively | \$139              | \$120       | \$417             | \$360       |
| Total other comprehensive income  | 139                | 120         | 417               | 360         |
| Comprehensive loss  | \$(15,495 )        | \$(10,063 ) | \$(30,636 )       | \$(16,845 ) |
| Basic loss per share data:  |                    |             |                   |             |
| Basic loss per share  | \$(0.58 )          | \$(0.32 )   | \$(1.15 )         | \$(0.54 )   |
| Basic weighted average shares outstanding   | 27,155             | 32,017      | 27,066            | 31,917      |
| Diluted loss per share data:  |                    |             |                   |             |
| Diluted loss per share  | \$(0.58 )          | \$(0.32 )   | \$(1.15 )         | \$(0.54 )   |
| Diluted weighted average shares outstanding   | 27,155             | 32,017      | 27,066            | 31,917      |

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

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Stage Stores, Inc.

Condensed Consolidated Statements of Cash Flows

(in thousands)

(Unaudited)

|   | Nine Months Ended   |                     |
|---|---------------------|---------------------|
|   | October 29,<br>2016 | October 31,<br>2015 |
| Cash flows from operating activities:   |                     |                     |
| Net loss  | \$(31,053)          | \$(17,205 )         |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: |                     |                     |
| Depreciation, amortization and impairment of long-lived assets                            | 54,285              | 58,326              |
| Loss on retirements of property, equipment and leasehold improvements                     | 273                 | 712                 |
| Deferred income taxes   | 1,965               | (557 )              |
| Tax (deficiency) benefit from stock-based compensation                                    | (3,295 )            | 540                 |
| Stock-based compensation expense  | 7,345               | 8,926               |
| Amortization of debt issuance costs   | 164                 | 164                 |
| Excess tax benefits from stock-based compensation   | —                   | (945 )              |
| Deferred compensation obligation  | 233                 | 163                 |
| Amortization of employee benefit related costs  | 673                 | 581                 |
| Construction allowances from landlords  | 6,994               | 2,127               |
| Other changes in operating assets and liabilities:  |                     |                     |
| Increase in merchandise inventories   | (133,347)           | (175,806 )          |
| Increase in other assets  | (18,527 )           | (3,335 )            |
| Increase in accounts payable and other liabilities  | 119,544             | 95,476              |
| Net cash provided by (used in) operating activities                                       | 5,254               | (30,833 )           |
| Cash flows from investing activities:   |                     |                     |
| Additions to property, equipment and leasehold improvements                               | (67,934 )           | (69,156 )           |
| Proceeds from disposal of assets  | 1,177               | 37                  |
| Net cash used in investing activities   | (66,757 )           | (69,119 )           |
| Cash flows from financing activities:   |                     |                     |
| Proceeds from revolving credit facility borrowings  | 389,701             | 428,783             |
| Payments of revolving credit facility borrowings  | (314,783 )          | (304,960 )          |
| Proceeds from long-term debt obligation   | 5,830               | —                   |
| Payments of long-term debt obligations  | (3,507 )            | (1,466 )            |
| Payments for stock related compensation   | (857 )              | (3,708 )            |
| Proceeds from issuance of stock awards  | —                   | 543                 |
| Excess tax benefits from stock-based compensation   | —                   | 945                 |
| Cash dividends paid   | (12,466 )           | (13,916 )           |
| Net cash provided by financing activities   | 63,918              | 106,221             |
| Net increase in cash and cash equivalents   | 2,415               | 6,269               |
| Cash and cash equivalents:  |                     |                     |
| Beginning of period   | 16,487              | 17,165              |
| End of period   | \$18,902            | \$23,434            |
| Supplemental disclosures including non-cash investing and financing activities:           |                     |                     |
| Interest paid   | \$3,425             | \$1,816             |

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|   |         |           |
|---|---------|-----------|
| Income taxes paid                           | \$2,931 | \$ 15,053 |
| Unpaid liabilities for capital expenditures | \$4,631 | \$ 10,526 |

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

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Stage Stores, Inc.

Condensed Consolidated Statement of Stockholders' Equity

For the Nine Months Ended October 29, 2016

(in thousands, except per share data)

(Unaudited)

|   | Common<br>Stock |        | Additional<br>Paid-in<br>Capital | Treasury Stock |            | Accumulated<br>Other<br>Comprehensive<br>Loss | Retained<br>Earnings | Total     |
|---|-----------------|--------|----------------------------------|----------------|------------|---|----------------------|-----------|
|   | Shares          | Amount |                                  | Shares         | Amount     |   |                      |           |
| Balance at January 30, 2016                                 | 32,030          | \$ 320 | \$406,034                        | (5,175)        | \$(43,068) | \$ (6,353 )                                   | \$72,820             | \$429,753 |
| Net loss  | —               | —      | —                                | —              | —          | —   | (31,053 )            | (31,053 ) |
| Other comprehensive income                                  | —               | —      | —                                | —              | —          | 417   | —                    | 417       |
| Dividends on common stock,<br>\$0.45 per share              | —               | —      | —                                | —              | —          | —   | (12,466 )            | (12,466 ) |
| Deferred compensation                                       | —               | —      | 233                              | —              | (233 )     | —   | —                    | —         |
| Issuance of equity awards, net                              | 301             | 3      | (3 )                             | —              | —          | —   | —                    | —         |
| Tax withholdings paid for net<br>settlement of stock awards | —               | —      | (624 )                           | —              | —          | —   | —                    | (624 )    |
| Stock-based compensation<br>expense                         | —               | —      | 7,345                            | —              | —          | —   | —                    | 7,345     |
| Tax deficiency from stock-based<br>compensation             | —               | —      | (3,295 )                         | —              | —          | —   | —                    | (3,295 )  |
| Balance at October 29, 2016                                 | 32,331          | \$ 323 | \$409,690                        | (5,175)        | \$(43,301) | \$ (5,936 )                                   | \$29,301             | \$390,077 |

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

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

1. Basis of Presentation

The accompanying condensed consolidated financial statements of Stage Stores, Inc. and its subsidiary (“we,” “us” or “our”) have been prepared in accordance with the requirements of the U.S. Securities and Exchange Commission (“SEC”) for interim financial information and do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (“GAAP”) for complete financial statements. Those adjustments that are, in the opinion of management, necessary for a fair presentation of the results of the interim periods have been made. Results of operations for such interim periods are not necessarily indicative of the results of operations for a full year due to seasonal and other factors. The condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto filed with our Annual Report on Form 10-K for the year ended January 30, 2016 (“Form 10-K”).

References to a particular year are to our fiscal year, which is the 52- or 53-week period ending on the Saturday closest to January 31st of the following calendar year. For example, a reference to “2016” is a reference to the fiscal year ending January 28, 2017, and “2015” is a reference to the fiscal year ended January 30, 2016. Each of 2016 and 2015 are comprised of 52 weeks.

**Customer Loyalty Program.** Prior to the third quarter of 2016, customers who spent a required amount within a specified time frame using our private label credit card received reward certificates which could be redeemed for merchandise. We estimated the net cost of the rewards and recorded a liability associated with unredeemed certificates and customer spend toward unissued certificates. The cost of the loyalty rewards program was recorded in cost of sales. In the third quarter of 2016, we expanded our loyalty program to enable all customers to earn benefits regardless of how they choose to pay. We record deferred revenue for the retail value of certificates earned, net of estimated breakage, as customers make purchases towards earning reward certificates.

**Recent Accounting Standards.** In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers, which supersedes most existing revenue recognition guidance in GAAP. The core principle of the guidance is that a company should recognize revenue when it transfers promised goods or services to customers in an amount that reflects what a company expects to be entitled to in exchange for those goods or services. ASU 2014-09 allows for either a retrospective or cumulative effect transition method of adoption. In August 2015, the FASB issued ASU 2015-14, which deferred the effective date of ASU 2014-09 by one year. The new revenue standard will be effective for us in the first quarter of fiscal year ending February 2, 2019. We do not expect the adoption of ASU 2014-09 to have a material impact on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases, which requires lessees to recognize the assets and liabilities that arise from finance and operating leases on the balance sheet. In addition, this guidance requires disclosures about the amount, timing and uncertainty of cash flows arising from leases. The new standard will be effective for us in the first quarter of fiscal year ending February 1, 2020. We are currently evaluating the impact that the adoption of this ASU will have on our consolidated financial statements and we expect that our reported assets and liabilities will significantly increase under the new standard.

In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting, which modifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities,

and classification on the statement of cash flows. Under the new standard, excess income tax benefits and tax deficiencies related to equity awards that vest or settle will be recognized as income tax expense, rather than within additional paid-in capital on the balance sheet. The recognition of excess tax benefits and losses may create significant volatility in earnings. We do not expect the adoption of the other requirements of this ASU to have a material impact on our consolidated financial statements. The new standard will be effective for us in the first quarter of fiscal year ending February 3, 2018.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which provides guidance on certain specific cash flow issues including proceeds received from the settlement of insurance claims. This guidance requires cash proceeds received from the settlement of insurance claims to be classified on the statement of cash flows on the basis of the related insurance coverage (that is, the nature of the loss). The new standard is effective for fiscal years and interim periods beginning after December 15, 2017, with early adoption permitted. We do not expect the adoption of this ASU to have a material impact on our consolidated statements of cash flows.

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## 2. Stock-Based Compensation

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

|  | Three Months Ended |                  | Nine Months Ended |                  |
|--|--------------------|------------------|-------------------|------------------|
|  | October 29, 2016   | October 31, 2015 | October 29, 2016  | October 31, 2015 |
| Stock appreciation rights ("SARs")           | \$—                | \$—              | \$—               | \$ 30            |
| Non-vested stock                             | 1,362              | 1,719            | 5,311             | 5,133            |
| Performance shares                           | (569 )             | 1,278            | 2,034             | 3,763            |
| Total compensation expense                   | 793                | 2,997            | 7,345             | 8,926            |
| Related tax benefit                          | (298 )             | (1,126 )         | (2,762 )          | (3,356 )         |
| Stock-based compensation expense, net of tax | \$495              | \$ 1,871         | \$4,583           | \$ 5,570         |

As of October 29, 2016, we have unrecognized compensation cost of \$18.6 million related to stock-based compensation awards granted. That cost is expected to be recognized over a weighted average period of 2.4 years.

## SARs

Prior to 2012, we granted stock options and SARs to our employees, which generally vested over four years from the date of grant. There were no stock options outstanding as of January 30, 2016. Outstanding SARs will expire, if not exercised or forfeited, within seven years from the date of grant. Exercised SARs are settled by the issuance of common stock in an amount equal to the increase in our stock price between the grant date and the exercise date.

The following table summarizes SARs activity for the nine months ended October 29, 2016:

| SARs  | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (years) | Aggregate Intrinsic Value (in thousands) |
|---|------------------|---------------------------------|---|--|
| Outstanding, vested and exercisable at January 30, 2016 | 224,400          | \$ 17.16                        |   |  |
| Forfeited   | (39,750 )        | 14.66                           |   |  |
| Outstanding, vested and exercisable at October 29, 2016 | 184,650          | \$ 17.70                        | 1.1   | \$ —                                     |

No SARs were exercised during the nine months ended October 29, 2016. The aggregate intrinsic value of stock options and SARs exercised during the nine months ended October 31, 2015 was \$0.9 million.

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## Non-vested Stock

We grant shares of non-vested stock to our employees and non-employee directors. The non-vested stock converts one-for-one to common stock at the end of the vesting period at no cost to the recipient to whom it is awarded. The vesting period of the non-vested stock ranges from one to four years from the date of grant.

The following table summarizes non-vested stock activity for the nine months ended October 29, 2016:

| Non-vested Stock                | Number of Shares | Weighted Average Grant Date Fair Value |
|---------------------------------|------------------|--|
| Outstanding at January 30, 2016 | 894,526          | \$ 20.20                               |
| Granted                         | 1,396,947        | 6.78                                   |
| Vested                          | (371,656 )       | 19.45                                  |
| Forfeited                       | (238,290 )       | 12.25                                  |
| Outstanding at October 29, 2016 | 1,681,527        | 10.34                                  |

The weighted-average grant date fair value for non-vested stock granted during the nine months ended October 29, 2016 and October 31, 2015 was \$6.78 and \$20.65, respectively. The aggregate intrinsic value of non-vested stock that vested during the nine months ended October 29, 2016 and October 31, 2015, was \$2.7 million and \$5.4 million, respectively. The payment of the employees' tax liability for a portion of the vested shares was satisfied by withholding shares with a fair value equal to the tax liability. As a result, the actual number of shares issued during nine months ended October 29, 2016 was 289,757.

## Performance Shares

We grant performance shares as a means of rewarding management for our long-term performance based on shareholder return performance measures. The actual number of shares that may be issued ranges from zero to a maximum of twice the number of granted shares outstanding, as reflected in the table below, and is based on our shareholder return performance relative to a specific group of companies over a 3-year performance cycle. If earned, the performance shares vest following the 3-year cycle. Compensation expense is recorded ratably over the vesting period and is based on the fair value at grant date as determined using a Monte Carlo probability model. Grant recipients do not have any shareholder rights until the granted shares have been issued.

The following table summarizes information about the performance shares that were outstanding at October 29, 2016:

| Period Granted | Target Shares Outstanding at January 30, 2016 | Target Shares Granted | Target Shares Vested | Target Shares Forfeited | Target Shares Outstanding at October 29, 2016 | Weighted Average Grant Date Fair Value Per Share |
|----------------|---|-----------------------|----------------------|-------------------------|---|--|
| 2014           | 160,423                                       | —                     | (3,438 )             | (36,667 )               | 120,318                                       | \$ 33.84   |
| 2015           | 223,876                                       | —                     | (6,983 )             | (45,707 )               | 171,186                                       | 28.33  |
| 2016           | —   | 451,680               | (5,168 )             | (90,439 )               | 356,073                                       | 8.69   |
| Total          | 384,299                                       | 451,680               | (15,589 )            | (172,813 )              | 647,577                                       |  |

The weighted-average grant date fair value for performance shares granted during the nine months ended October 29, 2016 and October 31, 2015 was \$8.69 and \$28.33, respectively. For the 2013 performance grant, none of the 112,750 target shares that were outstanding at January 30, 2016 were earned. The aggregate intrinsic value of performance shares that vested during the nine months ended October 29, 2016 and October 31, 2015 was \$0.1 million and \$4.9 million, respectively. The payment of the employees' tax liability for the vested shares was satisfied by withholding shares with a fair value equal to the tax liability. As a result, the actual number of shares issued during nine months ended October 29, 2016 was 11,323.

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## 3. Debt Obligations

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

|   | October 29,<br>2016 | January 30,<br>2016 |
|---|---------------------|---------------------|
| Revolving Credit Facility                 | \$ 231,758          | \$ 156,840          |
| Finance obligations                       | 2,981               | 3,764               |
| Other financing                           | 8,225               | 5,119               |
| Total debt obligations                    | 242,964             | 165,723             |
| Less: Current portion of debt obligations | 6,372               | 2,847               |
| Long-term debt obligations                | \$ 236,592          | \$ 162,876          |

On October 6, 2014, we entered into a Second Amended and Restated Credit Agreement for a \$300.0 million senior secured revolving credit facility (“Revolving Credit Facility”) with a seasonal increase to \$350.0 million and a \$50.0 million letter of credit subfacility. The Revolving Credit Facility matures on October 6, 2019.

We use the Revolving Credit Facility to provide financing for working capital and general corporate purposes, as well as to finance capital expenditures and to support our letter of credit requirements. Borrowings are limited to the availability under a borrowing base that is determined principally on eligible inventory as defined by the Revolving Credit Facility agreement. Inventory, cash and cash equivalents are pledged as collateral. The daily interest rates are determined by a prime rate or LIBOR, plus an applicable margin, as set forth in the Revolving Credit Facility agreement. For the nine months ended October 29, 2016, the weighted average interest rate on outstanding borrowings and the average daily borrowings were 1.83% and \$188.0 million, respectively.

Letters of credit issued under the Revolving Credit Facility support certain merchandise purchases and collateralize retained risks and deductibles under various insurance programs. At October 29, 2016, outstanding letters of credit totaled approximately \$5.7 million. These letters of credit expire within twelve months of issuance. Excess borrowing availability under the Revolving Credit Facility at October 29, 2016 was \$112.2 million.

The Revolving Credit Facility agreement contains covenants which, among other things, restrict, based on required levels of excess availability, (i) the amount of additional debt or capital lease obligations, (ii) the payment of dividends to \$30 million in a fiscal year, and (iii) the repurchase of common stock under certain circumstances. The agreement also contains a fixed charge coverage ratio covenant in the event excess availability is below a defined threshold or an event of default has occurred. At October 29, 2016, we were in compliance with all of the debt covenants of the Revolving Credit Facility agreement and we expect to remain in compliance.

During the nine months ended October 29, 2016, we borrowed approximately \$5.8 million under an equipment financing note bearing an effective interest rate of 3.2%. The equipment financing note is payable in monthly installments over a three-year term and is secured by certain equipment.

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## 4. Earnings per Share

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

|  | Three Months Ended |                  | Nine Months Ended |                  |
|--|--------------------|------------------|-------------------|------------------|
|  | October 29, 2016   | October 31, 2015 | October 29, 2016  | October 31, 2015 |
| Basic EPS:   |                    |                  |                   |                  |
| Net loss   | \$(15,634)         | \$(10,183)       | \$(31,053)        | \$(17,205)       |
| Less: Allocation of earnings to participating securities | —                  | —                | —                 | —                |
| Net loss allocated to common shares                      | (15,634)           | (10,183)         | (31,053)          | (17,205)         |
| Basic weighted average shares outstanding                | 27,155             | 32,017           | 27,066            | 31,917           |
| Basic EPS  | \$(0.58)           | \$(0.32)         | \$(1.15)          | \$(0.54)         |

|  | Three Months Ended |                  | Nine Months Ended |                  |
|--|--------------------|------------------|-------------------|------------------|
|  | October 29, 2016   | October 31, 2015 | October 29, 2016  | October 31, 2015 |
| Diluted EPS:   |                    |                  |                   |                  |
| Net loss   | \$(15,634)         | \$(10,183)       | \$(31,053)        | \$(17,205)       |
| Less: Allocation of earnings to participating securities | —                  | —                | —                 | —                |
| Net loss allocated to common shares                      | (15,634)           | (10,183)         | (31,053)          | (17,205)         |
| Basic weighted average shares outstanding                | 27,155             | 32,017           | 27,066            | 31,917           |
| Add: Dilutive effect of stock awards                     | —                  | —                | —                 | —                |
| Diluted weighted average shares outstanding              | 27,155             | 32,017           | 27,066            | 31,917           |
| Diluted EPS  | \$(0.58)           | \$(0.32)         | \$(1.15)          | \$(0.54)         |

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

|  | Three Months Ended |                  | Nine Months Ended |                  |
|--|--------------------|------------------|-------------------|------------------|
|  | October 29, 2016   | October 31, 2015 | October 29, 2016  | October 31, 2015 |
| Number of anti-dilutive shares due to net loss for the period  | 20                 | 9                | 42                | 52               |
| Number of anti-dilutive SARs due to exercise price greater than average market price of our common stock | 187                | 224              | 198               | 158              |

## 5. Stockholders' Equity

On November 17, 2016, our Board of Directors ("Board") declared a quarterly cash dividend of \$0.15 per share of common stock, payable on December 14, 2016 to shareholders of record at the close of business on November 29, 2016.





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## 6. Pension Plan

We sponsor a frozen defined benefit pension plan. The components of net periodic pension cost were as follows (in thousands):

|                                | Three Months Ended |                  | Nine Months Ended |                  |
|--------------------------------|--------------------|------------------|-------------------|------------------|
|                                | October 29, 2016   | October 31, 2015 | October 29, 2016  | October 31, 2015 |
| Employer service cost          | \$85               | \$ 88            | \$255             | \$ 262           |
| Interest cost                  | 400                | 391              | 1,198             | 1,174            |
| Expected return on plan assets | (437 )             | (549 )           | (1,312 )          | (1,646 )         |
| Net loss amortization          | 225                | 194              | 673               | 581              |
| Net periodic pension cost      | \$273              | \$ 124           | \$814             | \$ 371           |

Our funding policy is to make contributions to maintain the minimum funding requirements for our pension obligations in accordance with the Employee Retirement Income Security Act. We may elect to contribute additional amounts to maintain a level of funding to minimize the Pension Benefit Guaranty Corporation premium costs or to cover the short-term liquidity needs of the plan in order to maintain current invested positions. We made no contributions during the nine months ended October 29, 2016.

## 7. Fair Value Measurements

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

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

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

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

|  | October 29, 2016 |             |              |      |
|--|------------------|-------------|--------------|------|
|  | Quoted           | Significant | Significant  |      |
|  | Prices in        | Other       | Unobservable |      |
|  | Active           | Observable  | Inputs       |      |
| Balance  | Markets for      | Inputs      | (Level 3)    |      |
|  | Identical        | (Level 2)   |              |      |
|  | Instruments      |             |              |      |
|  | (Level 1)        |             |              |      |
| Other assets:  |                  |             |              |      |
| Securities held in grantor trust for deferred compensation plans <sup>(a)(b)</sup> | \$18,623         | \$ 18,623   | \$ —         | \$ — |

|  | January 30, 2016 |             |              |      |
|--|------------------|-------------|--------------|------|
|  | Quoted           | Significant | Significant  |      |
|  | Prices in        | Other       | Unobservable |      |
|  | Active           | Observable  | Inputs       |      |
| Balance  | Markets for      | Inputs      | (Level 3)    |      |
|  | Identical        | (Level 2)   |              |      |
|  | Instruments      |             |              |      |
|  | (Level 1)        |             |              |      |
| Other assets:  |                  |             |              |      |
| Securities held in grantor trust for deferred compensation plans <sup>(a)(b)</sup> | \$17,286         | \$ 17,286   | \$ —         | \$ — |

<sup>(a)</sup> The liability for the amount due to participants corresponding in value to the securities held in the grantor trust is recorded in other long-term liabilities.

<sup>(b)</sup> Using the market approach, the fair values of these items represent quoted market prices multiplied by the quantities held. Net gains and losses related to the changes in fair value in the assets and liabilities under the various deferred compensation plans are recorded in selling, general and administrative expenses and were nil for the nine months ended October 29, 2016 and for the fiscal year ended January 30, 2016.

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

|   | October 29, 2016  |   |  |           |
|---|---|---|--|-----------|
|   | Quoted<br>Prices in<br>Active<br>Markets for<br>Identical<br>Instruments<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
| Assets:   |   |   |  |           |
| Store property, equipment and leasehold improvements <sup>(a)</sup> | \$473   | \$  | —\$  | —\$ 473   |
|   | January 30, 2016  |   |  |           |
|   | Quoted<br>Prices in<br>Active<br>Markets for<br>Identical<br>Instruments<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
| Assets:   |   |   |  |           |
| Store property, equipment and leasehold improvements <sup>(a)</sup> | \$3,895   | \$  | —\$  | —\$ 3,895 |

<sup>(a)</sup> In accordance with ASC No. 360-10, Accounting for the Impairment or Disposal of Long-Lived Assets, we review the carrying value of long-lived assets periodically and when events or circumstances indicate a potential impairment has occurred. Using an undiscounted cash flow model, we evaluate the cash flow trends of our stores to identify property, equipment and leasehold improvements that may not be fully recoverable. When a store's projected undiscounted cash flows indicate impairment, we use a discounted cash flow model to estimate the fair value of the underlying long-lived assets. An impairment write-down is recorded if the carrying value of a long-lived asset exceeds its fair value. Key assumptions in estimating future cash flows include, among other things, expected future operating performance, including expected closure date and lease term, and changes in economic conditions. For the nine months ended October 29, 2016 and fiscal year 2015, we recognized impairment charges of \$0.5 million and \$10.6 million, respectively. Impairment charges are recorded in cost of sales and related buying, occupancy and distribution expenses. We believe estimated future cash flows are sufficient to support the carrying value of our long-lived assets. If estimated cash flows significantly differ in the future, there could be additional asset impairments.

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

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

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

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

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

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

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

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

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

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For purposes of the following discussion, all references to the “third quarter 2016” and the “third quarter 2015” are for the 13-week fiscal periods ended October 29, 2016 and October 31, 2015, respectively, and all references to “year-to-date 2016” and “year-to-date 2015” are for the 39-week fiscal periods ended October 29, 2016 and October 31, 2015, respectively.

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

### Our Business

We are a retailer operating specialty department stores primarily in small and mid-sized towns and communities. Our merchandise assortment is a well-edited selection of moderately priced brand name and private label apparel, accessories, cosmetics, footwear and home goods. As of October 29, 2016, we operated 820 specialty department stores located in 38 states under the BEALLS, GOODY’S, PALAIS ROYAL, PEEBLES and STAGE nameplates and a direct-to-consumer business.

### Results of Operations

Select financial results for the third quarter 2016 were as follows (comparisons are to the third quarter 2015):

Net sales decreased \$34.4 million, or 9.8%.

Comparable sales decreased 8.2%.

Gross profit decreased \$19.5 million, or 25.6%.

Selling, general and administrative (“SG&A”) expenses decreased \$7.5 million, or 8.2%.

Diluted loss per common share was (\$0.58), compared with (\$0.32).

Adjusted diluted loss per common share (non-GAAP) was (\$0.57), compared with (\$0.29) (see reconciliation of non-GAAP financial measures on page 17).

We declared and paid cash dividends of \$4.2 million, or \$0.15 per common share.

Inventories were down approximately 8%.

### 2016 Strategy and Outlook

Sales for the year-to-date 2016 were lower compared to the year-to-date 2015, primarily attributable to a decline in traffic in our stores. Sales for the year-to-date 2016 have been particularly challenged in Texas, Louisiana, Oklahoma and New Mexico, which have been impacted by depressed oil prices and the weak Mexican peso. Compared with the first and second quarter 2016, comparable sales for the third quarter 2016 improved slightly. We have responded to the challenging sales environment by controlling our inventories, reducing expenses and lowering capital expenditures.

During the third quarter 2016, we took additional markdowns to move clearance merchandise and we had a clean, fresh inventory position going into the fourth quarter. We have increased our emphasis on gifts for the holiday season, building upon last year’s well received selection of men’s gifts and adding an extensive collection of items for women, including new bath and cosmetic offerings and hair styling products. We also have a strong assortment of seasonal apparel, including lightweight sweaters, fleece and outerwear. In our women’s categories, we have focused on popular trends, such as little black dresses, bomber jackets and fashion boots.

We scaled back our advertising and store expenses during the year-to-date 2016 to be better positioned to invest in these areas for the holiday season. We plan to increase the presence of sales associates in our stores to provide a higher level of customer service during the holiday season and we have several new promotions that align with the heavier shopping periods. We will also be reaching out to more customers through our marketing campaigns to highlight our merchandise offerings and our stores will feature improved signage to showcase our value and compelling price points.

We are offering greater value to our customers with our tender-neutral loyalty program, Style Circle Rewards®, which we launched in the third quarter 2016. This new loyalty club complements our existing private label credit card program and will allow us to better understand our customers' shopping habits, offer even more personalized promotional offers, and provide attractive rewards. We believe that these loyalty programs provide enhanced benefits to our customers and are powerful tools to drive higher transaction value and frequency of visits.

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During the year-to-date 2016, we have made strategic investments in our stores and our e-commerce technology to create a more enjoyable shopping experience for our customers. We remodeled and refreshed an additional 85 stores, and have updated over 200 stores representing approximately 45% of our sales base since the initiative began in 2015. The investments in our stores include improved lighting, upgraded fixtures, comfortable fitting rooms and enhanced layouts. We have also improved the navigation of our website to make it simpler and faster to shop and we continue to enhance the functionality of our mobile app.

As part of our strategic initiative to exit stores that do not meet our sales productivity and profitability benchmarks, we closed 15 stores during the year-to-date 2016, and we expect to close approximately 35 stores in total for 2016.

## Non-GAAP Financial Measures

The following supplemental information presents the results from operations for the three and nine months ended October 29, 2016 and October 31, 2015 on a GAAP basis and on a non-GAAP basis to show earnings excluding charges related to: (i) our corporate headquarters consolidation, which includes duplicate rent expense and moving related costs; (ii) severance associated with our workforce reduction initiative; and (iii) our strategic store closures, which includes fixture moving costs and lease termination charges. We believe this supplemental financial information enhances an investor's understanding of our financial performance as it excludes those items which impact comparability of operating trends. The non-GAAP financial information should not be considered in isolation or viewed as a substitute for net loss, diluted loss per common share, cash flow from operations or other measures of performance as defined by GAAP. Moreover, the inclusion of non-GAAP financial information as used herein is not necessarily comparable to other similarly titled measures of other companies due to the potential inconsistencies in the method of presentation and items considered. The following tables set forth the supplemental financial information and the reconciliation of GAAP disclosures to non-GAAP financial measures (in thousands, except diluted loss per common share):

|  | Three Months Ended |             | Nine Months Ended |             |
|--|--------------------|-------------|-------------------|-------------|
|  | October 29,        | October 31, | October 29,       | October 31, |
|  | 2016               | 2015        | 2016              | 2015        |
| Net loss (GAAP)  | \$(15,634)         | \$(10,183 ) | \$(31,053)        | \$(17,205 ) |
| Consolidation of corporate headquarters (pretax)               | —                  | 1,313       | 110               | 1,941       |
| Severance charges associated with workforce reduction (pretax) | —                  | —           | 794               | —           |
| Strategic store closures and other initiatives (pretax)        | 443                | 183         | 1,394             | 8,834       |
| Income tax impact  | (271 )             | (692 )      | (989 )            | (4,224 )    |
| Adjusted net loss (non-GAAP)                                   | \$(15,462)         | \$(9,379 )  | \$(29,744)        | \$(10,654 ) |
| Diluted loss per share (GAAP)                                  | \$(0.58 )          | \$(0.32 )   | \$(1.15 )         | \$(0.54 )   |
| Consolidation of corporate headquarters (pretax)               | —                  | 0.04        | —                 | 0.06        |
| Severance charges associated with workforce reduction (pretax) | —                  | —           | 0.03              | —           |
| Strategic store closures and other initiatives (pretax)        | 0.02               | 0.01        | 0.05              | 0.28        |
| Income tax impact  | (0.01 )            | (0.02 )     | (0.03 )           | (0.13 )     |
| Adjusted diluted loss per share (non-GAAP)                     | \$(0.57 )          | \$(0.29 )   | \$(1.10 )         | \$(0.33 )   |



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## Third Quarter 2016 Compared to Third Quarter 2015

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

|   | Three Months Ended |                |                  |                |            |          |
|---|--------------------|----------------|------------------|----------------|------------|----------|
|   | October 29, 2016   |                | October 31, 2015 |                | Change     |          |
|   | Amount             | % to Sales (a) | Amount           | % to Sales (a) | Amount     | %        |
| Net sales   | \$317,140          | 100.0 %        | \$351,575        | 100.0 %        | \$(34,435) | (9.8) %  |
| Cost of sales and related buying, occupancy and distribution expenses | 260,550            | 82.2 %         | 275,479          | 78.4 %         | (14,929)   | (5.4) %  |
| Gross profit  | 56,590             | 17.8 %         | 76,096           | 21.6 %         | (19,506)   | (25.6) % |
| Selling, general and administrative expenses                          | 84,564             | 26.7 %         | 92,096           | 26.2 %         | (7,532)    | (8.2) %  |
| Interest expense  | 1,395              | 0.4 %          | 743              | 0.2 %          | 652        | 87.8 %   |
| Loss before income tax  | (29,369)           | (9.3) %        | (16,743)         | (4.8) %        | (12,626)   | 75.4 %   |
| Income tax benefit  | (13,735)           | (4.3) %        | (6,560)          | (1.9) %        | (7,175)    | 109.4 %  |
| Net loss  | \$(15,634)         | (4.9) %        | \$(10,183)       | (2.9) %        | \$(5,451)  | 53.5 %   |

(a) Percentages may not foot due to rounding.

## Net Sales

Sales for the third quarter 2016 of \$317.1 million decreased \$34.4 million, or 9.8%, from \$351.6 million for the third quarter 2015. Comparable sales, which are sales in stores that are open for at least 14 full months prior to the reporting period, including direct-to-consumer sales, decreased 8.2% in the third quarter 2016 compared to a 3.5% decrease in the third quarter 2015. Direct-to-consumer sales contributed 0.3% to the comparable sales rate in the third quarter 2016 and 0.4% in the third quarter 2015. The 8.2% decrease in comparable sales reflects a decrease of 12.1% in the number of transactions, partially offset by an increase of 4.4% in average transaction value. The decrease in transactions is primarily attributable to a decline in traffic in our stores. The growth in average transaction value was comprised of a 3.4% decline in average unit retail and an increase of 8.1% in units per transaction. Sales were negatively impacted by unseasonably warm weather and lower consumer demand, especially in our stores in Texas, Louisiana, Oklahoma and New Mexico, which continued to be impacted by depressed oil prices, and in our markets near the Mexican border due to the weak Mexican peso. Comparable sales in these four states were down 9.4%, while comparable sales in the balance of our chain was down 6.8%.

Our best performing merchandise categories were home and cosmetics. Dresses and women's denim were the best performing apparel categories. Sales of our fall seasonal merchandise, which includes sweaters, outerwear, fleece and boots were lower than expected as a result of warmer temperatures in our markets.

## Gross Profit

Gross profit for the third quarter 2016 was \$56.6 million, a decrease of \$19.5 million or 25.6%, from \$76.1 million for the third quarter 2015. Gross profit, as a percent of sales, decreased to 17.8% for the third quarter 2016 from 21.6% for the third quarter 2015. The 3.8% decrease in the gross profit rate reflects a 1.8% increase in merchandise cost of sales rate and a 2% increase in the buying, occupancy and distribution expenses rate. The increase in merchandise cost of sales rate is the result of additional markdowns to drive sales and clear inventories in the third quarter 2016 compared to the third quarter 2015. The increase in the buying, occupancy and distribution expense rate is the result of deleverage from lower sales in the third quarter 2016 compared to the third quarter 2015.

Selling, General and Administrative Expenses

SG&A expenses for the third quarter 2016 decreased \$7.5 million to \$84.6 million from \$92.1 million for the third quarter 2015. The decrease in SG&A expenses for third quarter 2016 compared to the third quarter 2015 is primarily due to lower payroll, advertising and incentive compensation expense. As a percent of sales, SG&A expenses increased to 26.7% for the third quarter 2016 from 26.2% for the third quarter 2015 due to deleverage from lower sales.

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## Interest Expense

Net interest expense was \$1.4 million for the third quarter 2016, compared to \$0.7 million for the third quarter 2015. Interest expense is primarily comprised of interest on borrowings under the Revolving Credit Facility, related letters of credit and commitment fees, amortization of debt issuance costs and interest on finance obligations. The increase in interest expense is primarily due to an increase in the average daily borrowings under the Revolving Credit Facility for the third quarter 2016 compared to the third quarter 2015.

## Income Taxes

Our effective income tax rate for the third quarter 2016 was 46.8%, resulting in an estimated tax benefit of \$13.7 million. This compares to income tax benefit of \$6.6 million and effective tax rate of 39.2% for the third quarter 2015. We are currently estimating an annual net loss for fiscal year 2016 which causes permanent tax benefits that would normally reduce the effective tax rate to be reflected as an increased percentage of the net loss.

## Year-to-Date 2016 Compared to Year-to-Date 2015

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

|   | Nine Months Ended |                |                  |                |             |          |
|---|-------------------|----------------|------------------|----------------|-------------|----------|
|   | October 29, 2016  |                | October 31, 2015 |                | Change      |          |
|   | Amount            | % to Sales (a) | Amount           | % to Sales (a) | Amount      | %        |
| Net sales   | \$988,275         | 100.0 %        | \$1,101,804      | 100.0 %        | \$(113,529) | (10.3) % |
| Cost of sales and related buying, occupancy and distribution expenses | 779,128           | 78.8 %         | 846,324          | 76.8 %         | (67,196)    | (7.9) %  |
| Gross profit  | 209,147           | 21.2 %         | 255,480          | 23.2 %         | (46,333)    | (18.1) % |
| Selling, general and administrative expenses                          | 260,076           | 26.3 %         | 281,783          | 25.6 %         | (21,707)    | (7.7) %  |
| Interest expense  | 3,616             | 0.4 %          | 1,995            | 0.2 %          | 1,621       | 81.3 %   |
| Loss before income tax  | (54,545)          | (5.5) %        | (28,298)         | (2.6) %        | (26,247)    | 92.8 %   |
| Income tax benefit  | (23,492)          | (2.4) %        | (11,093)         | (1.0) %        | (12,399)    | 111.8 %  |
| Net loss  | \$(31,053)        | (3.1) %        | \$(17,205)       | (1.6) %        | \$(13,848)  | 80.5 %   |

(a) Percentages may not foot due to rounding.

## Net Sales

Sales for the year-to-date 2016 of \$988.3 million decreased \$113.5 million, or 10.3%, from \$1,101.8 million for the year-to-date 2015. Comparable sales, which are sales in stores that are open for at least 14 full months prior to the reporting period, including direct-to-consumer sales, decreased 8.9% for the year-to-date 2016 compared to a 1.3% decrease for year-to-date 2015. Direct-to-consumer sales contributed 0.2% to the comparable sales rate in the year-to-date 2016 and 0.4% in the year-to-date 2015. The 8.9% decrease in comparable sales reflects a decrease of 13.5% in the number of transactions, partially offset by an increase of 5.3% in average transaction value. The decrease in transactions is primarily attributable to a decline in traffic in our stores. The growth in average transaction value was comprised of a 0.1% improvement in average unit retail and an increase of 5.2% in units per transaction. Sales were negatively impacted by lower consumer demand, especially in our stores in Texas, Louisiana, Oklahoma and New Mexico, which continued to be impacted by depressed oil prices, and in our markets near the Mexican border due to the weak Mexican peso. Comparable sales in these four states were down 11.3%, while comparable sales in the balance of our chain was down 6%.

Our best performing merchandise categories were home, cosmetics and men's. Activewear and women's denim were the best performing apparel categories.

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Gross Profit

Gross profit for the year-to-date 2016 was \$209.1 million, a decrease of \$46.3 million, or 18.1%, compared to \$255.5 million for the year-to-date 2015. Gross profit, as a percent of sales, decreased to 21.2% for the year-to-date 2016 from 23.2% for the year-to-date 2015. The 2.0% decrease in the gross profit rate reflects a 0.6% increase in merchandise cost of sales rate and a 1.4% increase in the buying, occupancy and distribution expenses rate. The increase in merchandise cost of sales rate is the result of additional markdowns to drive sales and clear inventories in the year-to-date 2016 compared to the year-to-date 2015. The increase in the buying, occupancy and distribution expense rate is the result of deleverage from lower sales and higher depreciation related to strategic investments, partially offset by \$8.2 million higher impairment charges recognized in the year-to-date 2015 compared with the year-to-date 2016.

Selling, General and Administrative Expenses

SG&A expenses for the year-to-date 2016 decreased \$21.7 million to \$260.1 million, from \$281.8 million for the year-to-date 2015. The decrease in SG&A expenses is primarily due lower payroll, advertising, benefits and incentive compensation expense. As a percent of sales, SG&A expenses increased to 26.3% for the year-to-date 2016 from 25.6% for the year-to-date 2015 due to deleverage from lower sales.

Interest Expense

Net interest expense was \$3.6 million for the year-to-date 2016 and \$2.0 million for the year-to-date 2015. Interest expense is primarily comprised of interest on borrowings under the Revolving Credit Facility (see "Liquidity and Capital Resources"), related letters of credit and commitment fees, amortization of debt issuance costs and interest on finance obligations. The increase in interest expense is primarily due to an increase in the average daily borrowings under the Revolving Credit Facility for the year-to-date 2016 as compared with the year-to-date 2015.

Income Taxes

Our effective income tax rate for the year-to-date 2016 was 43.1%, resulting in an estimated tax benefit of \$23.5 million. This compares to an income tax benefit of \$11.1 million for the year-to-date 2015 at an effective rate 39.2%. We are currently estimating an annual net loss for fiscal year 2016 which causes permanent tax benefits that would normally reduce the effective tax rate to be reflected as an increased percentage of the net loss.

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## Seasonality and Inflation

Our business is seasonal and historically sales are lower during the first three quarters of the fiscal year (February through October) and higher during the last quarter of the fiscal year (November through January). The fourth quarter usually accounts for approximately 30% of our annual sales, with each of the other quarters accounting for approximately 22% to 24%. Working capital requirements fluctuate during the year and generally reach their highest levels during the third and fourth quarters. We do not believe that inflation has had a material effect on our results of operations. However, there can be no assurance that our business will not be affected by inflation in the future.

## Liquidity and Capital Resources

Our liquidity is currently provided by (i) existing cash balances, (ii) operating cash flows, (iii) normal trade credit terms from our vendors and their factors and (iv) our Revolving Credit Facility. Our primary cash requirements are for seasonal inventory purchases, capital investments in our stores, direct-to-consumer business and information technology and the payment of our quarterly cash dividends.

While there can be no assurances, we believe that our sources of liquidity will be sufficient to cover working capital needs, planned capital expenditures and debt service requirements for the remainder of 2016 and the foreseeable future.

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

|                                 | Nine Months Ended |                  |
|---------------------------------|-------------------|------------------|
|                                 | October 2016      | October 31, 2015 |
| Net cash provided by (used in): |                   |                  |
| Operating activities            | \$5,254           | \$(30,833)       |
| Investing activities            | (66,757)          | (69,119)         |
| Financing activities            | 63,918            | 106,221          |

## Operating Activities

During the year-to-date 2016, we generated \$5.3 million in cash from operating activities. Net loss, adjusted for non-cash expenses, provided cash of approximately \$30.6 million. Changes in operating assets and liabilities used net cash of approximately \$32.3 million, which included increases of \$133.3 million in merchandise inventories, primarily due to seasonal receipts, and \$18.5 million in other assets, partially offset by an increase of \$119.5 million in accounts payable and other liabilities primarily related to inventory purchases. Additionally, cash flows from operating activities included construction allowances from landlords of \$7.0 million, which funded a portion of the capital expenditures related to leasehold improvements in our new corporate office building and store leasehold improvements in relocated, expanded and remodeled stores.

During the year-to-date 2015, we used \$30.8 million in cash from operating activities. Net loss, adjusted for non-cash expenses, provided cash of approximately \$50.7 million. Changes in operating assets and liabilities used net cash of approximately \$83.7 million, which included increases of \$175.8 million in merchandise inventories, primarily due to seasonal receipts and strategic investments in cosmetics, and \$3.3 million in other assets, partially offset by an increase of \$95.5 million in accounts payable and other liabilities primarily related to inventory purchases. Additionally, cash flows from operating activities included construction allowances from landlords of \$2.1 million, which funded a portion of the capital expenditures related to store leasehold improvements in new, relocated, expanded and remodeled stores.



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### Investing Activities

Capital expenditures were \$67.9 million for the year-to-date 2016 compared to \$69.2 million for the year-to-date 2015. The decrease in capital expenditures in the year-to-date 2016 compared to the year-to-date 2015 is due to a decrease in store expansions and remodels. We received construction allowances from landlords of \$7.0 million in the year-to-date 2016 and \$2.1 million in the year-to-date 2015 to fund a portion of the capital expenditures related to store leasehold improvements and our new corporate office building. These funds are recorded as a deferred rent credit on the balance sheet and are recognized as an offset to rent expense over the lease term commencing with the date the allowances are earned.

We estimate that capital expenditures in 2016, net of construction allowances from landlords, will be approximately \$65 million as compared to \$87 million for 2015. The expenditures are principally for store remodels, expansions and relocations, and investments in our technology and direct-to-consumer business.

### Financing Activities

We use the Revolving Credit Facility to provide financing for working capital and general corporate purposes, as well as to finance capital expenditures and to support our letter of credit requirements. Borrowings are limited to the availability under a borrowing base that is determined principally on eligible inventory as defined by the Revolving Credit Facility agreement. Inventory, cash and cash equivalents are pledged as collateral. The daily interest rates are determined by a prime rate or LIBOR, plus an applicable margin, as set forth in the Revolving Credit Facility agreement. For the year-to-date 2016, the weighted average interest rate on outstanding borrowings and the average daily borrowings were 1.83% and \$188.0 million, respectively, compared to 1.50% and \$80.2 million year-to-date 2015. The increase in average daily borrowings for the year-to-date 2016 compared to the year-to-date 2015 is primarily due to stock repurchases made in the fourth quarter 2015 and capital expenditures.

Letters of credit issued under the Revolving Credit Facility support certain merchandise purchases and collateralize retained risks and deductibles under various insurance programs. At October 29, 2016, outstanding letters of credit totaled approximately \$5.7 million. These letters of credit expire within twelve months of issuance. Excess borrowing availability under the Revolving Credit Facility at October 29, 2016 was \$112.2 million.

The Revolving Credit Facility agreement contains covenants which, among other things, restrict, based on required levels of excess availability, (i) the amount of additional debt or capital lease obligations, (ii) the payment of dividends to \$30.0 million in a fiscal year, and (iii) the repurchase of common stock under certain circumstances. The agreement also contains a fixed charge coverage ratio covenant in the event excess availability is below a defined threshold or an event of default has occurred. At October 29, 2016, we were in compliance with all of the debt covenants of the agreement and we expect to remain in compliance.

During the year-to-date 2016, we borrowed approximately \$5.8 million under an equipment financing note bearing an effective interest rate of 3.2%. The equipment financing note is payable in monthly installments over a three-year term and is secured by certain equipment.

We paid \$12.5 million in cash dividends during the year-to-date 2016. On November 17, 2016, our Board declared a quarterly cash dividend of \$0.15 per share of common stock, payable on December 14, 2016 to shareholders of record at the close of business on November 29, 2016.



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Recent Accounting Standards

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

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

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

Internal Control Over Financial Reporting

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

- (1) Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer;
- (2) Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer; and
- (3) Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the issuer’s assets that could have a material adverse effect on the financial statements.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. There were no changes in our internal control over financial reporting during the three months ended October 29, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

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

ITEM 1A. RISK FACTORS

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

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

On March 7, 2011, our Board approved a stock repurchase program (“2011 Stock Repurchase Program”) which authorized us to repurchase up to \$200.0 million of our outstanding common stock. The 2011 Stock Repurchase Program will expire when we have repurchased \$200.0 million of our outstanding common stock, unless terminated earlier by our Board. Through January 30, 2016, we repurchased approximately \$141.6 million of our outstanding common shares under the 2011 Stock Repurchase Program. Also in March 2011, our Board authorized us to repurchase shares of our outstanding common stock equal to the amount of the proceeds and related tax benefits from the exercise of stock options, stock appreciation rights (“SARs”) and other equity grants. Purchases of shares of our common stock may be made from time to time, either on the open market or through privately negotiated transactions and are financed by our existing cash, cash flow and other liquidity sources, as appropriate.

The table below sets forth information regarding our repurchases of common stock during the three months ended October 29, 2016:

## ISSUER PURCHASES OF EQUITY SECURITIES

| Period                              | Total<br>Number of<br>Shares<br>Purchased<br>(a) | Average<br>Price<br>Paid Per<br>Share (a) | Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Approximate<br>Dollar Value<br>of Shares<br>that May<br>Yet Be<br>Purchased<br>Under the<br>Plans or<br>Programs (b) |
|-------------------------------------|--|---|--|--|
| July 31, 2016 to August 27, 2016    | 3,818  | \$ 6.00                                   | —  | \$58,351,202   |
| August 28, 2016 to October 1, 2016  | 8,039  | 5.37                                      | —  | \$58,351,202   |
| October 2, 2016 to October 29, 2016 | 1,195  | 5.14                                      | —  | \$58,351,202   |
| Total                               | 13,052   | \$ 5.53                                   | —  |  |

(a) Although we did not repurchase any of our common stock during the three months ended October 29, 2016 under the 2011 Stock Repurchase Program:

We reacquired 2,462 shares of common stock from certain employees to cover tax withholding obligations from the vesting of restricted and performance stock at a weighted average acquisition price of \$5.80 per common share; and The trustee of the grantor trust established by us for the purpose of holding assets under our deferred compensation plan purchased an aggregate of 10,590 shares of our common stock in the open market at a weighted average price of \$5.47 in connection with the option to invest in our stock under the deferred compensation plan and reinvestment of dividends paid on our common stock held in trust in the deferred compensation plan.

(b) Reflects the \$200.0 million authorized under the 2011 Stock Purchase Program, less the \$141.6 million repurchased using our existing cash, cash flow and other liquidity sources since March 2011.

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ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

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

| Exhibit<br>Number | Description  |
|-------------------|--|
| 3*                | Amended and Restated Bylaws of Stage Stores, Inc. dated September 15, 2016.  |
| 10.1*             | Employment Agreement between Thorsten I. Weber and Stage Stores, Inc. dated September 29, 2016.  |
| 10.2*             | Form of Indemnity Agreement.   |
| 31.1*             | Certification of Chief Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2*             | Certification of Chief Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32*               | Certification Pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 101.INS           | XBRL Instance Document   |
| 101.SCH           | XBRL Taxonomy Extension Schema Document  |
| 101.CAL           | XBRL Taxonomy Extension Calculation Linkbase Document  |
| 101.DEF           | XBRL Taxonomy Extension Definition Linkbase Document   |
| 101.LAB           | XBRL Taxonomy Extension Label Linkbase Document  |
| 101.PRE           | XBRL Taxonomy Extension Presentation Linkbase Document   |

\*Filed electronically herewith.

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SIGNATURES

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

STAGE STORES, INC.

Dated: December 8, 2016 /s/ Michael L. Glazer  
Michael L. Glazer  
President and Chief Executive Officer  
(Principal Executive Officer)

Dated: December 8, 2016 /s/ Oded Shein  
Oded Shein  
Executive Vice President, Chief Financial Officer and Treasurer  
(Principal Financial Officer)