

BIG 5 SPORTING GOODS CORP

Form 10-Q

November 02, 2007

**Table of Contents**

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended September 30, 2007  
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: 000-49850

**BIG 5 SPORTING GOODS CORPORATION**

(Exact name of registrant as specified in its charter)

Delaware

95-4388794

(State or Other Jurisdiction of Incorporation or Organization)

(I.R.S. Employer Identification No.)

2525 East El Segundo Boulevard  
El Segundo, California

90245

(Address of Principal Executive Offices)

(Zip Code)

Registrant's telephone number, including area code: (310) 536-0611

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 a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

There were 22,113,942 shares of common stock, with a par value of \$0.01 per share outstanding at October 26, 2007.

**BIG 5 SPORTING GOODS CORPORATION**  
**INDEX**

|  | Page |
|--|------|
| <b><u>PART I FINANCIAL INFORMATION</u></b>   |      |
| <b><u>Item 1</u></b> <u>Financial Statements</u>   |      |
| <u>Unaudited Condensed Consolidated Balance Sheets at September 30, 2007 and December 31, 2006</u>   | 3    |
| <u>Unaudited Condensed Consolidated Statements of Operations for the Thirteen and Thirty-Nine Weeks Ended September 30, 2007 and October 1, 2006</u> | 4    |
| <u>Unaudited Condensed Consolidated Statements of Cash Flows for the Thirty-Nine Weeks Ended September 30, 2007 and October 1, 2006</u>              | 5    |
| <u>Notes to Unaudited Condensed Consolidated Financial Statements</u>  | 6    |
| <b><u>Item 2</u></b> <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                                    | 14   |
| <b><u>Item 3</u></b> <u>Quantitative and Qualitative Disclosures About Market Risk</u>   | 25   |
| <b><u>Item 4</u></b> <u>Controls and Procedures</u>  | 25   |
| <b><u>PART II OTHER INFORMATION</u></b>  |      |
| <b><u>Item 1</u></b> <u>Legal Proceedings</u>  | 26   |
| <b><u>Item 1A</u></b> <u>Risk Factors</u>  | 26   |
| <b><u>Item 2</u></b> <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>  | 27   |
| <b><u>Item 3</u></b> <u>Defaults Upon Senior Securities</u>  | 28   |
| <b><u>Item 4</u></b> <u>Submission of Matters to a Vote of Security Holders</u>  | 28   |
| <b><u>Item 5</u></b> <u>Other Information</u>  | 28   |
| <b><u>Item 6</u></b> <u>Exhibits</u>   | 28   |
| <b><u>SIGNATURES</u></b>   | 29   |
| <u>EXHIBIT 31.1</u>  |      |
| <u>EXHIBIT 31.2</u>  |      |
| <u>EXHIBIT 32.1</u>  |      |
| <u>EXHIBIT 32.2</u>  |      |

---

**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**

**BIG 5 SPORTING GOODS CORPORATION**  
**UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share amounts)

|   | <b>September<br/>30,<br/>2007</b> | <b>December<br/>31,<br/>2006</b> |
|---|-----------------------------------|----------------------------------|
| <b>ASSETS</b>   |                                   |                                  |
| Current assets:   |                                   |                                  |
| Cash and cash equivalents   | \$ 5,428                          | \$ 5,145                         |
| Trade and other receivables, net of allowances of \$814 and \$314, respectively   | 8,342                             | 13,146                           |
| Merchandise inventories   | 257,930                           | 228,692                          |
| Prepaid expenses  | 9,118                             | 9,857                            |
| Deferred income taxes   | 9,803                             | 9,345                            |
| Total current assets  | 290,621                           | 266,185                          |
| Property and equipment, net of accumulated depreciation of \$103,960 and \$92,236, respectively   | 88,802                            | 88,159                           |
| Deferred income taxes   | 8,991                             | 7,795                            |
| Other assets, net of accumulated amortization of \$229 and \$590, respectively  | 1,068                             | 1,107                            |
| Goodwill  | 4,433                             | 4,433                            |
| Total assets  | \$ 393,915                        | \$ 367,679                       |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>  |                                   |                                  |
| Current liabilities:  |                                   |                                  |
| Accounts payable  | \$ 106,735                        | \$ 96,128                        |
| Accrued expenses  | 58,034                            | 66,513                           |
| Current portion of capital lease obligations  | 1,767                             | 1,995                            |
| Total current liabilities   | 166,536                           | 164,636                          |
| Deferred rent, less current portion   | 20,429                            | 19,735                           |
| Capital lease obligations, less current portion   | 2,459                             | 2,992                            |
| Long-term debt  | 95,066                            | 77,086                           |
| Other long-term liabilities   | 2,959                             | 2,770                            |
| Total liabilities   | 287,449                           | 267,219                          |
| Commitments and contingencies   |                                   |                                  |
| Stockholders' equity:   |                                   |                                  |
| Common stock, \$0.01 par value, authorized 50,000,000 shares; issued 22,894,687 and 22,848,887 shares, respectively; outstanding 22,138,942 and | 228                               | 228                              |

Edgar Filing: BIG 5 SPORTING GOODS CORP - Form 10-Q

|   |            |            |
|---|------------|------------|
| 22,670,367 shares, respectively   |            |            |
| Additional paid-in capital  | 90,269     | 87,956     |
| Retained earnings   | 29,944     | 14,126     |
| Less: Treasury stock, at cost; 755,745 and 178,520 shares, respectively | (13,975)   | (1,850)    |
| Total stockholders' equity  | 106,466    | 100,460    |
| Total liabilities and stockholders' equity                              | \$ 393,915 | \$ 367,679 |

See accompanying notes to unaudited condensed consolidated financial statements.

-3-

---

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except per share data)

|  | 13 Weeks Ended        |                    | 39 Weeks Ended        |                    |
|--|-----------------------|--------------------|-----------------------|--------------------|
|  | September<br>30, 2007 | October 1,<br>2006 | September<br>30, 2007 | October 1,<br>2006 |
| Net sales  | \$ 231,308            | \$ 223,276         | \$ 666,161            | \$ 642,263         |
| Cost of goods sold, buying and occupancy,<br>excluding depreciation and amortization<br>shown separately below | 149,289               | 145,592            | 429,036               | 414,440            |
| Gross profit   | 82,019                | 77,684             | 237,125               | 227,823            |
| Operating expenses:  |                       |                    |                       |                    |
| Selling and administrative   | 62,066                | 58,961             | 183,539               | 174,924            |
| Depreciation and amortization  | 4,554                 | 4,069              | 12,926                | 12,473             |
| Total operating expenses   | 66,620                | 63,030             | 196,465               | 187,397            |
| Operating income   | 15,399                | 14,654             | 40,660                | 40,426             |
| Interest expense   | 1,582                 | 1,709              | 4,504                 | 5,407              |
| Income before income taxes   | 13,817                | 12,945             | 36,156                | 35,019             |
| Income taxes   | 5,438                 | 5,120              | 14,247                | 13,820             |
| Net income   | \$ 8,379              | \$ 7,825           | \$ 21,909             | \$ 21,199          |
| Dividends per share declared   | \$ 0.09               | \$ 0.09            | \$ 0.27               | \$ 0.25            |
| Earnings per share:  |                       |                    |                       |                    |
| Basic  | \$ 0.37               | \$ 0.34            | \$ 0.97               | \$ 0.93            |
| Diluted  | \$ 0.37               | \$ 0.34            | \$ 0.97               | \$ 0.93            |
| Weighted-average shares of common stock<br>out standing:   |                       |                    |                       |                    |
| Basic  | 22,406                | 22,692             | 22,591                | 22,701             |
| Diluted  | 22,492                | 22,794             | 22,693                | 22,802             |

See accompanying notes to unaudited condensed consolidated financial statements.

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

|   | <b>39 Weeks Ended</b>         |                            |
|---|-------------------------------|----------------------------|
|   | <b>September<br/>30, 2007</b> | <b>October 1,<br/>2006</b> |
| Cash flows from operating activities:   |                               |                            |
| Net income  | \$ 21,909                     | \$ 21,199                  |
| Adjustments to reconcile net income to net cash provided by operating activities: |                               |                            |
| Depreciation and amortization   | 12,926                        | 12,473                     |
| Stock-based compensation  | 1,626                         | 1,674                      |
| Excess tax benefits of stock options exercised                                    | (155)                         | (111)                      |
| Amortization of deferred finance charges  | 37                            | 138                        |
| Deferred income taxes   | (1,654)                       | (1,903)                    |
| Gain on disposal of equipment   |                               | (200)                      |
| Changes in operating assets and liabilities:                                      |                               |                            |
| Trade and other receivables, net  | 4,804                         | 3,553                      |
| Merchandise inventories   | (29,007)                      | (17,561)                   |
| Prepaid expenses and other assets   | 741                           | (816)                      |
| Accounts payable  | 12,929                        | 10,911                     |
| Accrued expenses and other liabilities  | (10,635)                      | (9,256)                    |
| Net cash provided by operating activities   | 13,521                        | 20,101                     |
| Cash flows from investing activities:   |                               |                            |
| Purchases of property and equipment   | (11,084)                      | (13,170)                   |
| Proceeds from disposal of property and equipment                                  |                               | 223                        |
| Net cash used in investing activities   | (11,084)                      | (12,947)                   |
| Cash flows from financing activities:   |                               |                            |
| Net principal borrowings under revolving credit facilities and book overdraft     | 15,658                        | 4,486                      |
| Principal payments under term loan  |                               | (5,000)                    |
| Principal payments on capital lease obligations                                   | (1,565)                       | (1,296)                    |
| Proceeds from exercise of stock options   | 500                           | 298                        |
| Excess tax benefits of stock options exercised                                    | 155                           | 111                        |
| Purchases of treasury stock   | (10,811)                      | (1,279)                    |
| Dividends paid  | (6,091)                       | (5,677)                    |
| Net cash used in financing activities   | (2,154)                       | (8,357)                    |
| Net increase (decrease) in cash and cash equivalents                              | 283                           | (1,203)                    |
| Cash and cash equivalents at beginning of period                                  | 5,145                         | 6,054                      |
| Cash and cash equivalents at end of period  | \$ 5,428                      | \$ 4,851                   |

|  |    |        |           |
|--|----|--------|-----------|
| Supplemental disclosures of non-cash investing activities: |    |        |           |
| Property and equipment acquired under capital leases       | \$ | 825    | \$ 198    |
| Property and equipment purchases accrued                   | \$ | 3,073  | \$ 598    |
| Treasury stock purchases accrued                           | \$ | 1,314  | \$        |
| Supplemental disclosures of cash flow information:         |    |        |           |
| Interest paid  | \$ | 4,556  | \$ 6,592  |
| Income taxes paid  | \$ | 16,127 | \$ 18,769 |

See accompanying notes to unaudited condensed consolidated financial statements.

-5-

---



**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) Basis of Presentation and Description of Business**

*Business*

Big 5 Sporting Goods Corporation ( we or the Company ) is a leading sporting goods retailer in the western United States, operating 353 stores in 10 states at September 30, 2007. The Company provides a full-line product offering in a traditional sporting goods store format that averages approximately 11,000 square feet. The Company s product mix includes athletic shoes, apparel and accessories, as well as a broad selection of outdoor and athletic equipment for team sports, fitness, camping, hunting, fishing, tennis, golf, snowboarding and in-line skating. The Company is a holding company that operates its business through Big 5 Corp., its wholly-owned subsidiary, and Big 5 Services Corp., which is a wholly-owned subsidiary of Big 5 Corp. Big 5 Services Corp. provides a centralized operation for the issuance and administration of gift cards.

The accompanying interim unaudited condensed consolidated financial statements of the Company and its wholly-owned subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States ( GAAP ) for interim financial information and are presented in accordance with the requirements of Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, these interim unaudited condensed consolidated financial statements do not include all of the information and notes required by GAAP for complete financial statements. These interim unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the fiscal year ended December 31, 2006 included in the Company s Annual Report on Form 10-K. In the opinion of management, the interim unaudited condensed consolidated financial statements included herein contain all adjustments, including normal recurring adjustments, considered necessary to present fairly the Company s financial position, the results of operations and cash flows for the periods presented.

The operating results and cash flows of the interim periods presented herein are not necessarily indicative of the results to be expected for any other interim period or the full year.

*Consolidation*

The accompanying interim unaudited condensed consolidated financial statements include the accounts of Big 5 Sporting Goods Corporation, Big 5 Corp. and Big 5 Services Corp. All significant intercompany balances and transactions have been eliminated in consolidation.

*Reporting Period*

The Company follows the concept of a 52-53 week fiscal year, which ends on the Sunday nearest December 31. Fiscal year 2007 is comprised of 52 weeks and ends on December 30, 2007. Fiscal year 2006 was comprised of 52 weeks and ended on December 31, 2006. The fiscal interim periods in fiscal 2007 and fiscal 2006 are comprised of 13 weeks.

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

*Use of Estimates*

Management of the Company has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period to prepare these financial statements in conformity with GAAP. Significant items subject to such estimates and assumptions include the carrying amount of property and equipment, intangibles and goodwill; valuation allowances for receivables, sales returns, inventories and deferred income tax assets; estimates related to the valuation of stock options; and obligations related to asset retirements, litigation, workers' compensation and employee benefits. Actual results could differ significantly from these estimates under different assumptions and conditions.

*Reclassifications*

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

The Company reclassified approximately \$3.6 million, primarily representing a sales returns allowance, from trade and other receivables to accrued expenses on the December 31, 2006 balance sheet to conform to its presentation at September 30, 2007.

For the third quarter of fiscal 2007, the Company revised its previously reported consolidated statement of cash flows for the 39 weeks ended October 1, 2006 to reflect a change of approximately \$3.0 million of cash outflows from operating activities to investing activities. The revision corrects a misclassification made in presenting the cash flow statement impact of accrued liabilities related to purchases of property and equipment. The correction had no effect on the Company's previously reported consolidated balance sheets, consolidated statements of operations, consolidated statements of stockholders' equity or net cash flows, and is not considered material to any previously reported consolidated financial statements.

*Revenue Recognition*

The Company earns revenue by selling merchandise primarily through the Company's retail stores. Also included in revenue are sales of returned merchandise to vendors specializing in the resale of defective or used products, which historically have accounted for less than 1% of net sales. Revenue is recognized when merchandise is purchased by and delivered to the customer and is shown net of estimated returns during the relevant period. The allowance for sales returns is estimated based upon historical experience. Cash received from the sale of gift cards is recorded as a liability, and revenue is recognized upon the redemption of the gift card or when it is determined that the likelihood of redemption is remote and no liability to relevant jurisdictions exists.

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

*Valuation of Merchandise Inventories*

The Company's merchandise inventories are made up of finished goods and are valued at the lower of cost or market using the weighted-average cost method that approximates the first-in, first-out ( FIFO ) method. Average cost includes the direct purchase price of merchandise inventory and allocated overhead costs associated with the Company's distribution center. Management has evaluated the current level of inventories in comparison to planned sales volume and other factors and, based on this evaluation, has recorded adjustments to inventory and cost of goods sold for decreases in inventory value. These adjustments are estimates, which could vary significantly, either favorably or unfavorably, from actual results if future economic conditions, consumer demand and competitive environments differ from our expectations. The Company is not aware of any events or changes in demand or price that would indicate that the Company's inventory valuation may be materially inaccurate at this time.

Inventory shrinkage is accrued as a percentage of merchandise sales based on historical inventory shrinkage trends. The Company performs physical inventories of its stores and distribution center throughout the year. The reserve for inventory shrinkage represents an estimate for inventory shrinkage for each location since the last physical inventory date through the reporting date.

*Leases*

The Company leases all but one of its store locations. The Company accounts for its leases under the provisions of Statement of Financial Accounting Standards ( SFAS ) No. 13, *Accounting for Leases*, and subsequent amendments, which require that its leases be evaluated and classified as operating or capital leases for financial reporting purposes.

Certain leases have scheduled rent increases and certain leases include an initial period of free or reduced rent as an inducement to enter into the lease agreement ( rent holidays ). The Company recognizes rental expense for rent increases and rent holidays on a straight-line basis over the terms of the underlying leases, without regard to when rent payments are made. The calculation of straight-line rent is based on the reasonably assured lease term as defined in SFAS No. 98, *Accounting for Leases: Sales-Leaseback Transactions Involving Real Estate, Sales-Type Leases of Real Estate, Definition of the Lease Term, and Initial Direct Costs of Direct Financing Leases* an amendment of FASB Statements No. 13, 66 and 91 and a rescission of FASB Statement No. 26 and Technical Bulletin No. 79-11. This amended definition of the lease term may exceed the initial non-cancelable lease term.

Certain leases also may provide for payments based on future sales volumes at the leased location, which are not measurable at the inception of the lease. In accordance with SFAS No. 29, *Determining Contingent Rentals*, an amendment of FASB Statement No. 13, these contingent rents are expensed as they accrue.

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

*Recently Issued Accounting Pronouncements*

In September 2006, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 157, *Fair Value Measurements*. This standard provides guidance for using fair value to measure assets and liabilities. The standard also responds to investors' requests for expanded information about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value, but does not expand the use of fair value in any new circumstances. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. There are numerous previously issued statements dealing with fair values that are amended by SFAS No. 157. The Company is in the process of evaluating the impact, if any, that the adoption of SFAS No. 157 will have on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*. SFAS No. 159 provides companies with an option to report many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective of SFAS No. 159 is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. The FASB believes that SFAS No. 159 helps to mitigate accounting-induced volatility by enabling companies to report related assets and liabilities at fair value, which would likely reduce the need for companies to comply with detailed rules for hedge accounting. SFAS No. 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities, and would require entities to display the fair value of those assets and liabilities for which the company has chosen to use fair value on the face of the balance sheet. The new statement does not eliminate disclosure requirements included in other accounting standards, including requirements for disclosures about fair value measurements included in SFAS No. 157, *Fair Value Measurements*. This statement is effective as of the beginning of an entity's first fiscal year beginning after November 15, 2007. The Company is in the process of evaluating the impact, if any, that the adoption of SFAS No. 159 will have on the Company's consolidated financial statements.

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

**(2) Accrued Expenses**

Accrued expenses consist of the following:

|                              | <b>September<br/>30,<br/>2007</b> | <b>December<br/>31,<br/>2006</b> |
|------------------------------|-----------------------------------|----------------------------------|
|                              | <b>(In thousands)</b>             |                                  |
| Payroll and related expenses | \$ 16,394                         | \$ 18,150                        |
| Self-insurance               | 8,176                             | 8,047                            |
| Occupancy costs              | 6,738                             | 5,912                            |
| Sales tax                    | 6,323                             | 10,836                           |
| Gift cards and certificates  | 4,300                             | 6,510                            |
| Advertising                  | 3,937                             | 5,504                            |
| Other                        | 12,166                            | 11,554                           |
| Accrued expenses             | \$ 58,034                         | \$ 66,513                        |

**(3) Income Taxes**

The Company accounts for income taxes under the asset and liability method whereby deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. The realizability of deferred tax assets is assessed throughout the year and a valuation allowance is recorded if necessary to reduce net deferred tax assets to the amount more likely than not to be realized. The Company's practice is to recognize interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. At September 30, 2007, the Company had no accrued interest or penalties.

The Company files a consolidated federal income tax return and files tax returns in various state and local jurisdictions. The Company believes that the statutes of limitations for its consolidated federal income tax returns are open for years after 2002 and state and local income tax returns are open for years after 2001. The Company is not currently under examination by the Internal Revenue Service or any other taxing authority.

The Company adopted the provisions of FASB Interpretation No. 48 ( FIN 48 ), *Accounting for Uncertainty in Income Taxes*, on January 1, 2007. The adoption of FIN 48 had no impact on the Company's condensed consolidated financial statements. At September 30, 2007, the Company had no unrecognized tax benefits that, if recognized, would affect the Company's effective income tax rate over the next 12 months.

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

**(4) Stock-Based Compensation**

The Company accounts for its stock-based compensation in accordance with SFAS No. 123(R), *Share-Based Payment*. The fair value of each option on the date of grant is estimated using the Black-Scholes method based on the following weighted-average assumptions:

|                         | 13 Weeks Ended           |                        | 39 Weeks Ended           |                       |
|-------------------------|--------------------------|------------------------|--------------------------|-----------------------|
|                         | September<br>30,<br>2007 | October<br>1,<br>2006* | September<br>30,<br>2007 | October<br>1,<br>2006 |
| Risk-free interest rate | 4.6%                     | 4.6%                   | 4.6%                     | 4.7%                  |
|                         | 6.25                     | 6.25                   | 6.25                     | 6.25                  |
| Expected term           | years                    | years                  | years                    | 6.25 years            |
| Expected volatility     | 43%                      | 43%                    | 43%                      | 52%                   |
| Expected dividend yield | 1.67%                    | 1.67%                  | 1.42%                    | 1.97%                 |

\* No share options were granted during the 13 weeks ended October 1, 2006.

The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected term of the option; the expected term represents the weighted-average period of time that options granted are expected to be outstanding giving consideration to vesting schedules and using the simplified method pursuant to Securities and Exchange Commission ( SEC ) Staff Accounting Bulletin ( SAB ) No. 107, *Share-Based Payment*; the expected volatility is based upon historical volatilities of the Company's common stock, and for 2006 an index of a peer group; and the expected dividend yield is based upon the Company's current dividend rate and future expectations. The Company recognized approximately \$0.6 million and \$1.6 million in stock-based compensation expense for the 13 weeks and 39 weeks ended September 30, 2007, respectively, compared to \$0.6 million and \$1.7 million for the 13 weeks and 39 weeks ended October 1, 2006, respectively.

Through the 39 weeks ended September 30, 2007, the Company granted 70,200 stock options to certain employees and directors under the Company's 2002 Stock Incentive Plan and 2007 Equity and Performance Incentive Plan (collectively, the Plans ). Under the Plans, options granted generally vest and become exercisable at the rate of 25% per year with a maximum life of ten years. The exercise price of these options is equal to the market price of the Company's common stock on the date of grant. The weighted-average grant-date fair value of stock options granted for the 39 weeks ended September 30, 2007 and October 1, 2006 was \$10.87 and \$8.96, respectively.

As of September 30, 2007, there was \$4.1 million of total unrecognized compensation cost related to nonvested stock options granted. That cost is expected to be recognized over a weighted-average period of 2.3 years.

**(5) Quarterly Dividend**

A quarterly dividend of \$0.07 per share was paid in the first quarter of fiscal 2006. In the second quarter of fiscal 2006, the Company's Board of Directors authorized an increase of the dividend to an annual rate of \$0.36 per share of outstanding common stock. Quarterly dividend payments of \$0.09 per share were paid during the remainder of fiscal 2006 and the first three

Table of Contents

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

quarters of fiscal 2007. In the fourth quarter of fiscal 2007, the Company's Board of Directors declared a quarterly cash dividend of \$0.09 per share of outstanding common stock, which will be paid on December 14, 2007 to stockholders of record as of November 30, 2007.

**(6) Earnings Per Share**

The Company calculates earnings per share in accordance with SFAS No. 128, *Earnings Per Share*, which requires a dual presentation of basic and diluted earnings per share. Basic earnings per share is calculated by dividing net income by the weighted-average shares of common stock outstanding during the period. Diluted earnings per share is calculated by using the weighted-average shares of common stock outstanding adjusted to include the potentially dilutive effect of outstanding stock options.

The following table sets forth the computation of basic and diluted net income per common share:

|   | <b>13 Weeks Ended</b>                           |                                | <b>39 Weeks Ended</b>             |                                |
|---|---|--------------------------------|-----------------------------------|--------------------------------|
|   | <b>September<br/>30,<br/>2007</b>               | <b>October<br/>1,<br/>2006</b> | <b>September<br/>30,<br/>2007</b> | <b>October<br/>1,<br/>2006</b> |
|   | <b>(In thousands, except per share amounts)</b> |                                |                                   |                                |
| Net income  | \$ 8,379  | \$ 7,825                       | \$ 21,909                         | \$ 21,199                      |
| Weighted-average shares of common stock<br>outstanding:                   |   |                                |                                   |                                |
| Basic   | 22,406  | 22,692                         | 22,591                            | 22,701                         |
| Dilutive effect of common stock equivalents<br>arising from stock options | 86  | 102                            | 102                               | 101                            |
| Diluted   | 22,492  | 22,794                         | 22,693                            | 22,802                         |
| Basic earnings per share  | \$ 0.37   | \$ 0.34                        | \$ 0.97                           | \$ 0.93                        |
| Diluted earnings per share  | \$ 0.37   | \$ 0.34                        | \$ 0.97                           | \$ 0.93                        |

The computation of diluted earnings per share for the 13 weeks ended September 30, 2007, the 39 weeks ended September 30, 2007, the 13 weeks ended October 1, 2006 and the 39 weeks ended October 1, 2006 does not include options of 928,527, 451,357, 891,129 and 761,665, respectively, that were outstanding and antidilutive.

**Table of Contents**

**BIG 5 SPORTING GOODS CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(continued)**

The Company repurchased 561,425 and 577,225 shares of our common stock for \$11.7 million and \$12.1 million during the 13 weeks and 39 weeks ended September 30, 2007, respectively, under the Company's existing share repurchase program. Subsequent to the third quarter ended September 30, 2007 and through October 31, 2007, the Company repurchased 25,000 shares of its common stock for \$0.5 million. Total common stock repurchased by the Company under the share repurchase program during 2007 through October 31, 2007 was 602,225 shares for \$12.6 million. Since the inception of this share repurchase program through October 31, 2007, the Company has repurchased a total of 666,535 shares for a total expenditure of \$13.9 million, leaving a remaining authorized balance of \$1.1 million under this program.

Subsequent to the third quarter ended September 30, 2007, the Company's Board of Directors authorized an additional share repurchase program for the purchase of up to \$20.0 million of the Company's common stock. Under the authorization, the Company may purchase shares from time to time in the open market or in privately negotiated transactions in compliance with the applicable rules and regulations of the SEC. However, the timing and amount of such purchases, if any, would be at the discretion of management, and would depend upon market conditions and other considerations.

As of October 31, 2007, a total of \$21.1 million remained available for share repurchases under both share repurchase programs.

**(7) Contingencies**

On December 1, 2006, the Company was served with a complaint filed in the California Superior Court in the County of Orange, entitled Jack Lima v. Big 5 Sporting Goods Corporation, et al., Case No. 06CC00243, alleging violations of the California Labor Code and the California Business and Professions Code. This complaint was brought as a purported class action on behalf of the Company's California store managers. The plaintiff alleges, among other things, that the Company improperly classified store managers as exempt employees not entitled to overtime pay for work in excess of forty hours per week and failed to provide store managers with paid meal and rest periods. Subsequent to the third quarter ended September 30, 2007, the Company and the plaintiff reached a confidential agreement providing for the full and complete settlement and release of all of the plaintiff's individual claims and a dismissal of all claims purportedly brought on behalf of the class members in exchange for the Company's payment of non-material amounts to the plaintiff and the plaintiff's counsel. The Company admitted no liability or wrongdoing with respect to the claims set forth in the lawsuit.

In addition, the Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position, results of operations or liquidity.



**Table of Contents**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our interim unaudited condensed consolidated financial statements and the notes thereto included herein. Our interim unaudited condensed consolidated financial statements filed in this Form 10-Q and the discussions contained herein should be read in conjunction with our consolidated financial statements and related notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended December 31, 2006, all contained in our Annual Report on Form 10-K.

**CRITICAL ACCOUNTING POLICIES**

We believe that the following discussion addresses our critical accounting policies, which are those that are most important to the portrayal of our interim financial condition.

*Use of Estimates*

We have made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period to prepare these financial statements in conformity with accounting principles generally accepted in the United States ( GAAP ). Significant items subject to such estimates and assumptions include the carrying amount of property and equipment, intangibles and goodwill; valuation allowances for receivables, sales returns, inventories and deferred income tax assets; estimates related to the valuation of stock options; and obligations related to asset retirements, litigation, workers' compensation and employee benefits. Actual results could differ significantly from these estimates under different assumptions and conditions.

*Revenue Recognition*

We earn revenue by selling merchandise primarily through our retail stores. Also included in revenue are sales of returned merchandise to vendors specializing in the resale of defective or used products, which historically has accounted for less than 1% of net sales. Revenue is recognized when merchandise is purchased by and delivered to the customer and is shown net of estimated returns during the relevant period. The allowance for sales returns is estimated based upon historical experience. Cash received from the sale of gift cards is recorded as a liability, and revenue is recognized upon the redemption of the gift card or when it is determined that the likelihood of redemption is remote and no liability to relevant jurisdictions exists.

*Valuation of Merchandise Inventories*

Our merchandise inventories are made up of finished goods and are valued at the lower of cost or market using the weighted-average cost method that approximates the first-

**Table of Contents**

in, first-out ( FIFO ) method. Average cost includes the direct purchase price of merchandise inventory and allocated overhead costs associated with our distribution center. Management has evaluated the current level of inventories in comparison to planned sales volume and other factors and, based on this evaluation, has recorded adjustments to inventory and cost of goods sold for decreases in inventory value. These adjustments are estimates, which could vary significantly, either favorably or unfavorably, from actual results if future economic conditions, consumer demand and competitive environments differ from our expectations. We are not aware of any events or changes in demand or price that would indicate to us that our inventory valuation may be materially inaccurate at this time.

Inventory shrinkage is accrued as a percentage of merchandise sales based on historical inventory shrinkage trends. We perform physical inventories of our stores and distribution center throughout the year. The reserve for inventory shrinkage represents an estimate for inventory shrinkage for each location since the last physical inventory date through the reporting date.

*Leases*

We lease all but one of our store locations. We account for our leases under the provisions of Statement of Financial Accounting Standards ( SFAS ) No. 13, *Accounting for Leases*, and subsequent amendments, which require that our leases be evaluated and classified as operating or capital leases for financial reporting purposes.

Certain leases have scheduled rent increases and certain leases include an initial period of free or reduced rent as an inducement to enter into the lease agreement ( rent holidays ). We recognize rental expense for rent increases and rent holidays on a straight-line basis over the terms of the underlying leases, without regard to when rent payments are made. The calculation of straight-line rent is based on the reasonably assured lease term as defined in SFAS No. 98, *Accounting for Leases: Sales-Leaseback Transactions Involving Real Estate, Sales-Type Leases of Real Estate, Definition of the Lease Term, and Initial Direct Costs of Direct Financing Leases* an amendment of FASB Statements No. 13, 66 and 91 and a rescission of FASB Statement No. 26 and Technical Bulletin No. 79-11. This amended definition of the lease term may exceed the initial non-cancelable lease term.

Certain leases also may provide for payments based on future sales volumes at the leased location, which are not measurable at the inception of the lease. In accordance with SFAS No. 29, *Determining Contingent Rentals*, an amendment of FASB Statement No. 13, these contingent rents are expensed as they accrue.

**Table of Contents****RESULTS OF OPERATIONS**

The results of the interim periods are not necessarily indicative of results for the entire fiscal year.

**13 Weeks Ended September 30, 2007 Compared to 13 Weeks Ended October 1, 2006**

The following table and related discussion set forth selected items from our operating results as a percentage of our net sales for the periods indicated:

|                               | <b>13 Weeks Ended</b>                     |                        |            |        |
|-------------------------------|---|------------------------|------------|--------|
|                               | <b>September 30, 2007</b>                 | <b>October 1, 2006</b> |            |        |
|                               | <b>(In thousands, except percentages)</b> |                        |            |        |
| Net sales                     | \$ 231,308                                | 100.0%                 | \$ 223,276 | 100.0% |
| Costs of sales <sup>(1)</sup> | 149,289                                   | 64.5                   | 145,592    | 65.2   |
| Gross profit                  | 82,019                                    | 35.5                   | 77,684     | 34.8   |
| Operating expenses:           |   |                        |            |        |
| Selling and administrative    | 62,066                                    | 26.8                   | 58,961     | 26.4   |
| Depreciation and amortization | 4,554                                     | 2.0                    | 4,069      | 1.8    |
| Total operating expenses      | 66,620                                    | 28.8                   | 63,030     | 28.2   |
| Operating income              | 15,399                                    | 6.7                    | 14,654     | 6.6    |
| Interest expense              | 1,582                                     | 0.7                    | 1,709      | 0.8    |
| Income before income taxes    | 13,817                                    | 6.0                    | 12,945     | 5.8    |
| Income taxes                  | 5,438                                     | 2.4                    | 5,120      | 2.3    |
| Net income                    | \$ 8,379                                  | 3.6%                   | \$ 7,825   | 3.5%   |

<sup>(1)</sup> Costs of sales include cost of goods sold, buying and occupancy charges, excluding depreciation and amortization shown separately in this table.

**Net Sales.** Net sales increased by \$8.0 million, or 3.6%, to \$231.3 million in the 13 weeks ended September 30, 2007 from \$223.3 million in the same period last year. The growth in net sales was mainly attributable to an increase of \$9.5 million in new store sales, which reflected the opening of 24 new stores, net of relocations, since July 2, 2006 and an increase of \$0.2 million, or 0.1%, in same store sales. The increase in new and same store sales was partially offset by a decrease in closed store sales of \$2.2 million in the 13 weeks ended September 30, 2007 versus the 13 weeks ended October 1, 2006. Additionally, our net sales for the 13 weeks ended September 30, 2007 reflected the benefit of an extinguishment of \$0.4 million in store layaway liabilities. Store count at September 30, 2007 was 353

versus 334 at October 1, 2006. We opened 5 new stores, net of closures and relocations, in the 13 weeks ended September 30, 2007, and opened 5 new stores in the 13 weeks ended October 1, 2006. We expect to open approximately 20 new stores during fiscal 2007, net of closures and relocations.

Gross Profit. Gross profit increased by \$4.3 million, or 5.6%, to \$82.0 million in the 13 weeks ended September 30, 2007 from \$77.7 million in the 13 weeks ended October 1, 2006. Our gross profit margin was 35.5% in the 13 weeks ended September 30, 2007

**Table of Contents**

compared to 34.8% in the same period last year. Product selling margins, which exclude buying, occupancy and distribution costs, increased by approximately 30 basis points versus the same period in the prior year. Distribution center costs during the third quarter decreased \$1.0 million, or 57 basis points, from the prior year as a result of operational efficiencies realized in our new distribution center. Distribution center costs capitalized into inventory decreased by \$0.5 million, or 21 basis points, compared to the same period last year due primarily to higher costs in the prior year associated with the transition to our new larger distribution center. Store occupancy costs increased by \$0.7 million, or 10 basis points, over the comparable prior year quarter due mainly to new store openings. Inventory reserve provisions increased by \$0.4 million, or 12 basis points, from the prior year due primarily to higher inventory shrink.

**Selling and Administrative.** Selling and administrative expenses increased by \$3.1 million to \$62.1 million, or 26.8% of net sales, in the 13 weeks ended September 30, 2007 from \$59.0 million, or 26.4% of net sales, in the same period last year. The increase in selling and administrative expense as a percentage of sales for the fiscal 2007 third quarter compared to the prior year in part reflects softness in our sales. Store-related expenses, excluding occupancy, increased by \$1.7 million due primarily to an increase in store count. Advertising expense increased by \$0.6 million from the prior year, mainly to support overall sales and additional circulars to support new stores, and reflected an increased benefit from higher co-op advertising cost reimbursements from vendors of \$0.3 million over the prior year. Administrative expenses increased by \$0.7 million reflecting increased labor-related costs and other expenses to support our continuing growth and financial reporting initiatives.

**Depreciation and Amortization.** Depreciation and amortization expense increased \$0.5 million, or 11.9%, to \$4.6 million for the 13 weeks ended September 30, 2007 from \$4.1 million for the same period last year. The higher expense was primarily due to the increase in store count to 353 stores at the end of the third quarter of fiscal 2007 from 334 stores at the end of the third quarter of fiscal 2006 and higher expense from our distribution center.

**Interest Expense.** Interest expense decreased by \$0.1 million, or 7.4%, to \$1.6 million in the 13 weeks ended September 30, 2007 from \$1.7 million in the same period last year. The decrease in interest expense primarily reflects lower average debt levels, partially offset by slightly higher interest rates in 2007.

**Income Taxes.** The provision for income taxes was \$5.4 million for the 13 weeks ended September 30, 2007 and \$5.1 million for the 13 weeks ended October 1, 2006. Our effective tax rate was 39.4% for the third quarter of fiscal 2007 and 39.6% for the third quarter of fiscal 2006.

**Table of Contents****39 Weeks Ended September 30, 2007 Compared to 39 Weeks Ended October 1, 2006**

The following table and related discussion set forth selected items from our operating results as a percentage of our net sales for the periods indicated:

|                               | <b>39 Weeks Ended</b>                     |        |            |                        |
|-------------------------------|---|--------|------------|------------------------|
|                               | <b>September 30, 2007</b>                 |        |            | <b>October 1, 2006</b> |
|                               | <b>(In thousands, except percentages)</b> |        |            |                        |
| Net sales                     | \$ 666,161                                | 100.0% | \$ 642,263 | 100.0%                 |
| Costs of sales <sup>(1)</sup> | 429,036                                   | 64.4   | 414,440    | 64.5                   |
| Gross profit                  | 237,125                                   | 35.6   | 227,823    | 35.5                   |
| Operating expenses:           |   |        |            |                        |
| Selling and administrative    | 183,539                                   | 27.6   | 174,924    | 27.3                   |
| Depreciation and amortization | 12,926                                    | 1.9    | 12,473     | 1.9                    |
| Total operating expenses      | 196,465                                   | 29.5   | 187,397    | 29.2                   |
| Operating income              | 40,660                                    | 6.1    | 40,426     | 6.3                    |
| Interest expense              | 4,504                                     | 0.7    | 5,407      | 0.8                    |
| Income before income taxes    | 36,156                                    | 5.4    | 35,019     | 5.5                    |
| Income taxes                  | 14,247                                    | 2.1    | 13,820     | 2.2                    |
| Net income                    | \$ 21,909                                 | 3.3%   | \$ 21,199  | 3.3%                   |

(1) Costs of sales include cost of goods sold, buying and occupancy charges, excluding depreciation and amortization shown separately in this table.

**Net Sales.** Net sales increased by \$23.9 million, or 3.7%, to \$666.2 million in the 39 weeks ended September 30, 2007 from \$642.3 million in the same period last year. The growth in net sales was mainly attributable to an increase of \$1.5 million in same store sales and an increase of \$26.2 million in new store sales, partially offset by a decrease of \$4.6 million in closed store sales, which reflected the opening of 29 new stores, net of closures and relocations, since January 2, 2006. Same store sales increased 0.2% in the 39 weeks ended September 30, 2007 versus the 39 weeks ended October 1, 2006. Additionally, our net sales for the 39 weeks ended September 30, 2007 reflected the benefit of an extinguishment of \$0.4 million in store layaway liabilities. Store count at September 30, 2007 was 353 versus 334 at October 1, 2006. We opened 10 new stores, net of closures and relocations, in the 39 weeks ended September 30, 2007, and opened 10 new stores in the 39 weeks ended October 1, 2006. We expect to open approximately 20 new

stores during fiscal 2007, net of closures and relocations.

**Gross Profit.** Gross profit increased by \$9.3 million, or 4.1%, to \$237.1 million in the 39 weeks ended September 30, 2007 from \$227.8 million in the 39 weeks ended October 1, 2006. Our gross profit margin was 35.6% in the 39 weeks ended September 30, 2007 compared to 35.5% in the same period last year. Product selling margins, which exclude buying, occupancy and distribution costs, increased by approximately 35 basis points versus the same period in the prior year, primarily due to sales of winter merchandise earlier in the year at higher margins along with improved margins for various product categories. Distribution center costs during the period decreased \$3.6 million, or 72 basis points, due

-18-

---

**Table of Contents**

primarily to additional costs in the first quarter of the prior year associated with completing the transition to our new distribution center and operational efficiencies realized in our new distribution center. Distribution center costs capitalized into inventory decreased by \$3.8 million, or 59 basis points, compared to the same period last year due primarily to higher costs in the prior year associated with the transition to our new larger distribution center. Store occupancy costs increased by \$2.7 million, or 18 basis points, year-over-year due mainly to new store openings. Inventory reserve provisions increased by \$1.6 million, or 21 basis points, from the prior year due primarily to higher provisions for the realizability of the value of returned goods inventories and inventory shrink.

**Selling and Administrative.** Selling and administrative expenses increased by \$8.6 million to \$183.5 million, or 27.6% of net sales, in the 39 weeks ended September 30, 2007 from \$174.9 million, or 27.3% of net sales, in the same period last year. The increase in selling and administrative expense as a percentage of sales for the 39 weeks ended September 30, 2007 compared to the same period last year in part reflects softness in our sales. Store-related expenses, excluding occupancy, increased by \$5.0 million, or 14 basis points, due primarily to an increase in store count. Advertising expense increased by \$2.2 million from the prior year mainly to support overall sales and additional circulars to support new stores, and reflected an increased benefit from higher co-op advertising cost reimbursements from vendors of \$1.2 million over the prior year. Administrative expenses increased \$1.4 million reflecting increased labor-related costs and other expenses to support our continuing growth and financial reporting initiatives, along with a reduction in professional fees of \$1.2 million versus the prior year. Store-related expenses for the first 39 weeks of last year were favorably impacted by the receipt of \$0.7 million of proceeds as a participant in the settlement of a class-action lawsuit relating to credit card fees, which was offset by an increased provision of \$0.6 million for public liability claims.

**Depreciation and Amortization.** Depreciation and amortization expense increased \$0.4 million, or 3.6%, to \$12.9 million in the 39 weeks ended September 30, 2007 from \$12.5 million for the same period last year. The increase in expense is mainly due to the increase in store count to 353 stores at the end of the current period compared with 334 stores at the end of the prior period and higher expense from our distribution center.

**Interest Expense.** Interest expense decreased by \$0.9 million, or 16.7%, to \$4.5 million in the 39 weeks ended September 30, 2007 from \$5.4 million in the same period last year. The decrease in interest expense primarily reflects lower average debt levels, partially offset by slightly higher interest rates in 2007.

**Income Taxes.** The provision for income taxes was \$14.2 million for the 39 weeks ended September 30, 2007 and \$13.8 million for the 39 weeks ended October 1, 2006. Our effective tax rate was 39.4% for the 39 weeks ended September 30, 2007 and 39.5% for the 39 weeks ended October 1, 2006.

**LIQUIDITY AND CAPITAL RESOURCES**

Our principal liquidity requirements are for working capital, capital expenditures, debt repayments and cash dividends. We fund our liquidity requirements with cash on hand, cash flows from operations and borrowings from our revolving credit facility.



**Table of Contents**

**Operating Activities.** Net cash provided by operating activities was \$13.5 million and \$20.1 million for the first 39 weeks of fiscal 2007 and fiscal 2006, respectively. A substantial portion of our net sales are in cash, and therefore provide a significant source of liquidity. Cash is used in operating activities primarily to fund growth in inventory and other assets, net of accounts payable. Comparing the first 39 weeks of fiscal 2007 to the corresponding period in the prior year, the increased funding for working capital primarily reflects an increase in inventory purchases in anticipation of the upcoming holiday season, partially offset by higher accounts payable.

**Investing Activities.** Net cash used in investing activities for the first 39 weeks of fiscal 2007 and fiscal 2006 was \$11.1 million and \$12.9 million, respectively. Capital expenditures, excluding non-cash acquisitions, for the first 39 weeks of fiscal 2007 were \$11.1 million compared to \$13.2 million for the same period last year. We use cash flows from operations to fund our investing activities primarily for expenditures associated with opening new stores, improvements to existing stores and our distribution center, expenditures for equipment and computer software in support of our system initiatives and for our corporate headquarters. The decrease in cash used for capital expenditures in the current year compared with the prior year was due primarily to additional capital expenditures in the first quarter of the prior year associated with completing the transition to our new distribution center.

**Financing Activities.** Net cash used in financing activities for the first 39 weeks of fiscal 2007 and fiscal 2006 was \$2.2 million and \$8.4 million, respectively. For both periods, cash provided primarily by borrowings under our revolving credit facility was used to pay down debt and fund dividend payments. For fiscal 2007, revolving credit borrowings were also used to fund stock repurchases.

As of September 30, 2007, we had revolving credit borrowings of \$95.1 million and letter of credit commitments of \$4.5 million outstanding under our financing agreement. These balances compare to revolving credit borrowings of \$88.4 million, a term loan balance of \$8.3 million and letter of credit commitments of \$3.7 million outstanding under our financing agreement as of October 1, 2006.

**Future Capital Requirements.** We had cash and cash equivalents on hand of \$5.4 million at September 30, 2007. We expect capital expenditures for the fourth quarter of fiscal 2007, excluding non-cash acquisitions, to range from \$6.0 million to \$7.0 million, primarily to fund the opening of approximately 10 new stores, store-related remodeling, distribution center and corporate office improvements and computer hardware and software purchases. We expect to pay dividends of approximately \$2.0 million on December 14, 2007 in connection with the recent dividend declaration.

During the second quarter of fiscal 2006, our Board of Directors authorized a share repurchase program for the purchase of up to \$15.0 million of our common stock. We repurchased 561,425 and 577,225 shares of our common stock for \$11.7 million and \$12.1 million during the 13 weeks and 39 weeks ended September 30, 2007, respectively, under our existing share repurchase program. Subsequent to the third quarter ended September 30, 2007 and through October 31, 2007, we repurchased 25,000 shares of our common stock for \$0.5 million. Total common stock repurchased under the share repurchase program during 2007 through October 31, 2007 was 602,225 shares for \$12.6 million. Since the inception of this share repurchase program through October 31, 2007, we have repurchased a total of 666,535 shares for a total expenditure of \$13.9 million, leaving a remaining authorized balance of \$1.1 million under this program.

**Table of Contents**

The timing, price and quantity of any share repurchases are made at the discretion of management, depending upon market conditions and other considerations.

Subsequent to the third quarter ended September 30, 2007, the Company's Board of Directors authorized an additional share repurchase program for the purchase of up to \$20.0 million of the Company's common stock. Under the authorization, the Company may purchase shares from time to time in the open market or in privately negotiated transactions in compliance with the applicable rules and regulations of the Securities and Exchange Commission. However, the timing and amount of such purchases, if any, would be at the discretion of management, and would depend upon market conditions and other considerations.

As of October 31, 2007, a total of \$21.1 million remained available for share repurchases under both share repurchase programs.

We believe we will be able to fund our future cash requirements for operations from cash on hand, operating cash flows and borrowings from the revolving credit facility. We believe these sources of funds will be sufficient to continue our operations and planned capital expenditures, satisfy payments under debt and capital lease obligations, repurchase common stock and pay quarterly dividends for at least the next twelve months. However, our ability to satisfy such obligations depends upon our future performance, which in turn is subject to general economic conditions and regional risks, and to financial, business and other factors affecting our operations, including factors beyond our control. See Part II, Item 1A, "Risk Factors" included in this report and Part I, Item 1A, "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

If we are unable to generate sufficient cash flow from operations to meet our obligations and commitments, we will be required to refinance or restructure our indebtedness or raise additional debt or equity capital. Additionally, we may be required to sell material assets or operations, suspend dividend payments, delay or forego expansion opportunities or suspend the repurchase of common stock. We might not be able to effect these alternative strategies on satisfactory terms, if at all.

**Contractual Obligations and Other Commitments.** Our material off-balance sheet contractual commitments are operating lease obligations and letters of credit. We excluded these items from the balance sheet in accordance with GAAP.

Operating lease commitments consist principally of leases for our retail store facilities, distribution center and corporate office. These leases frequently include options which permit us to extend the terms beyond the initial fixed lease term. With respect to most of those leases, we intend to renegotiate those leases as they expire.

Issued and outstanding letters of credit were \$4.5 million at September 30, 2007, compared with \$3.7 million at October 1, 2006, and were related primarily to importing of merchandise and funding insurance program liabilities.

In the ordinary course of business, we enter into arrangements with vendors to purchase merchandise in advance of expected delivery. Because most of these purchase

**Table of Contents**

orders do not contain any termination payments or other penalties if cancelled, they are not included as outstanding contractual obligations.

**Financing Agreement.** On December 15, 2004, we entered into a \$160.0 million financing agreement with The CIT Group/Business Credit, Inc. and a syndicate of other lenders. On May 24, 2006, we amended the financing agreement to, among other things, increase the line of credit to \$175.0 million, consisting of a non-amortizing \$161.7 million revolving credit facility and an amortizing term loan balance of \$13.3 million. The amortizing term loan balance was prepaid in full during 2006.

The initial termination date of the revolving credit facility is March 20, 2011 (subject to annual extensions thereafter). The revolving credit facility may be terminated by the lenders by giving at least 90 days prior written notice before any anniversary date, commencing with its anniversary date on March 20, 2011. We may terminate the revolving credit facility by giving at least 30 days prior written notice, provided that if we terminate prior to March 20, 2011, we must pay an early termination fee. Unless it is terminated, the revolving credit facility will continue on an annual basis from anniversary date to anniversary date beginning on March 21, 2011.

The revolving credit facility bears interest at various rates based on our overall borrowings, with a floor of LIBOR plus 1.00% or the JP Morgan Chase Bank prime lending rate and a ceiling of LIBOR plus 1.50% or the JP Morgan Chase Bank prime lending rate.

Our financing agreement is secured by a first priority security interest in substantially all of our assets. Our financing agreement contains various financial and other covenants, including covenants that require us to maintain a fixed-charge coverage ratio, restrict our ability to incur indebtedness or to create various liens and restrict the amount of capital expenditures that we may incur. Our financing agreement also restricts our ability to engage in mergers or acquisitions, sell assets or pay dividends. We may declare a dividend only if no default or event of default exists on the dividend declaration date and a default is not expected to result from the payment of the dividend and certain other criteria are met, which may include the maintenance of certain financial ratios. We are currently in compliance with all covenants under our financing agreement. If we fail to make any required payment under our financing agreement or if we otherwise default under this instrument, our debt may be accelerated under this agreement. This acceleration could also result in the acceleration of other indebtedness that we may have outstanding at that time.

**SEASONALITY**

We experience seasonal fluctuations in our net sales and operating results. In fiscal 2006, we generated 26.8% of our net sales and 30.8% of our operating income in the fourth fiscal quarter, which includes the holiday selling season as well as the peak winter sports selling season. As a result, we incur significant additional expenses in the fourth fiscal quarter due to higher purchase volumes and increased staffing. If we miscalculate the demand for our products generally or for our product mix during the fourth fiscal quarter, our net sales could decline, resulting in excess inventory, which could harm our financial performance. Because a substantial portion of our operating income is derived from our

**Table of Contents**

fourth fiscal quarter net sales, a shortfall in fourth fiscal quarter net sales could cause our annual operating results to suffer significantly.

**RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

In September 2006, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 157, *Fair Value Measurements*. This standard provides guidance for using fair value to measure assets and liabilities. The standard also responds to investors' requests for expanded information about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value, but does not expand the use of fair value in any new circumstances. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. There are numerous previously issued statements dealing with fair values that are amended by SFAS No. 157. The Company is in the process of evaluating the impact, if any, that the adoption of SFAS No. 157 will have on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*. SFAS No. 159 provides companies with an option to report many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective of SFAS No. 159 is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. The FASB believes that SFAS No. 159 helps to mitigate accounting-induced volatility by enabling companies to report related assets and liabilities at fair value, which would likely reduce the need for companies to comply with detailed rules for hedge accounting. SFAS No. 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities, and would require entities to display the fair value of those assets and liabilities for which the company has chosen to use fair value on the face of the balance sheet. The new statement does not eliminate disclosure requirements included in other accounting standards, including requirements for disclosures about fair value measurements included in SFAS No. 157, *Fair Value Measurements*. This statement is effective as of the beginning of an entity's first fiscal year beginning after November 15, 2007. The Company is in the process of evaluating the impact, if any, that the adoption of SFAS No. 159 will have on the Company's consolidated financial statements.

**Table of Contents**

**FORWARD-LOOKING STATEMENTS**

This document includes certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements relate to, among other things, our financial condition, our results of operations, our growth strategy and the business of our Company generally. In some cases, you can identify such statements by terminology such as may, will, could, project, estimate, potential, continue, should, plans, anticipates, believes, intends or other such terminology. These forward-looking statements involve known unknown risks, uncertainties and other factors that may cause our actual results in future periods to differ materially from forecasted results. These risks and uncertainties include, among other things, the competitive environment in the sporting goods industry in general and in our specific market areas, inflation, product availability and growth opportunities, seasonal fluctuations, weather conditions, changes in costs of goods, operating expense fluctuations, disruption in product flow or increased costs related to distribution center operations, changes in interest rates and economic conditions in general. Those and other risks and uncertainties are more fully described in Part II, Item 1A, Risk Factors in this report and in Part I, Item 1A, Risk Factors in our Annual Report on Form 10-K and other risks and uncertainties more fully described in our other filings with the SEC. We caution that the risk factors set forth in this report are not exclusive. In addition, we conduct our business in a highly competitive and rapidly changing environment. Accordingly, new risk factors may arise. It is not possible for management to predict all such risk factors, nor to assess the impact of all such risk factors on our business or the extent to which any individual risk factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement. We disclaim any obligation to revise or update any forward-looking statement that may be made from time to time by us or on our behalf.

**Table of Contents**

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are subject to risks resulting from interest rate fluctuations since interest on our borrowings under our revolving credit facility are based on variable rates. If the LIBOR rate were to increase 1.0% as compared to the rate at September 30, 2007, our interest expense would increase approximately \$1.0 million on an annual basis based on the outstanding balance of our borrowings under our revolving credit facility at September 30, 2007. We do not hold any derivative instruments and do not engage in foreign currency transactions or hedging activities.

**Item 4. Controls and Procedures**

**Evaluation of Disclosure Controls and Procedures**

We conducted an evaluation, under the supervision and with the participation of our Chief Executive Officer ( CEO ) and Chief Financial Officer ( CFO ), of the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act )) as of the end of the period covered by this report. Based on such evaluation, our CEO and CFO have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

**Changes in Internal Control Over Financial Reporting**

During the fiscal quarter ended September 30, 2007, no changes occurred with respect to our internal control over financial reporting that materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

**Table of Contents**

**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

On December 1, 2006, the Company was served with a complaint filed in the California Superior Court in the County of Orange, entitled Jack Lima v. Big 5 Sporting Goods Corporation, et al., Case No. 06CC00243, alleging violations of the California Labor Code and the California Business and Professions Code. This complaint was brought as a purported class action on behalf of the Company's California store managers. The plaintiff alleges, among other things, that the Company improperly classified store managers as exempt employees not entitled to overtime pay for work in excess of forty hours per week and failed to provide store managers with paid meal and rest periods. Subsequent to the third quarter ended September 30, 2007, the Company and the plaintiff reached a confidential agreement providing for the full and complete settlement and release of all of the plaintiff's individual claims and a dismissal of all claims purportedly brought on behalf of the class members in exchange for the Company's payment of non-material amounts to the plaintiff and the plaintiff's counsel. The Company admitted no liability or wrongdoing with respect to the claims set forth in the lawsuit.

In addition, the Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position, results of operations or liquidity.

**Item 1A. Risk Factors**

There have been no material changes to the risk factors identified in Part I, Item 1A, Risk Factors, of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

-26-

---

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following tabular summary reflects the Company's share repurchase activity during the fiscal quarter ended September 30, 2007:

**ISSUER PURCHASES OF EQUITY SECURITIES<sup>1</sup>**

| <i>Period</i>            | <i>Total<br/>Number of<br/>Shares<br/>Purchased</i> | <i>Average<br/>Price Paid<br/>per Share</i> | <i>Total Number<br/>of Shares<br/>Purchased as<br/>Part of<br/>Publicly<br/>Announced<br/>Plans or<br/>Programs</i> | <i>Maximum<br/>Number (or<br/>Approximate<br/>Dollar Value) of<br/>Shares that May<br/>Yet Be<br/>Purchased<br/>Under the Plans<br/>or Programs</i> |
|--------------------------|---|---|---|---|
| July 2 - July 29         | 190,600   | \$ 23.11                                    | 190,600   | \$ 8,937,000  |
| July 30 - August 26      | 195,825   | \$ 19.91                                    | 195,825   | \$ 5,038,000  |
| August 27 - September 30 | 175,000   | \$ 19.67                                    | 175,000   | \$ 1,596,000  |
| Total                    | 561,425   | \$ 20.92                                    | 561,425   | \$ 1,596,000 <sub>2</sub>   |

<sup>1</sup> On May 11, 2006, the Company announced that its Board of Directors authorized a share repurchase program for the purchase of up to \$15.0 million of the Company's common stock. Under the authorization, the Company may purchase shares from time to time in the open market or in privately negotiated transactions in compliance with the applicable rules and regulations of



the SEC.

However, the timing and amount of such purchases, if any, would be at the discretion of management, and would depend upon market conditions and other considerations.

- <sup>2</sup> Subsequent to the third quarter ended September 30, 2007 and through October 31, 2007, the Company repurchased 25,000 shares of its common stock for \$0.5 million under the share repurchase program, representing an average price per share of \$18.75.

Subsequent to the third quarter ended September 30, 2007, the Company's Board of Directors authorized an additional share repurchase program for the purchase of up to \$20.0 million of the Company's common stock. Under the authorization, the Company may purchase shares from time to time in the open market or in privately negotiated transactions in compliance with the applicable rules and regulations of the SEC. However, the timing and amount of such purchases, if any, would be at the discretion of management, and would depend upon market conditions and other considerations.

As of October 31, 2007, a total of \$21.1 million remained available for share repurchases under both share repurchase programs.

**Table of Contents****Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Submission of Matters to a Vote of Security Holders**

None.

**Item 5. Other Information**

During the second quarter of fiscal 2007, the Company commenced negotiations on a new contract with The Steel, Paper House, Chemical Drivers & Helpers, Local Union 578 ( Local 578 ), affiliated with the International Brotherhood of Teamsters, covering certain hourly employees in the Company's distribution center. The Company had previously negotiated an extension of this contract through August 31, 2007. During the third quarter ended September 30, 2007, the Company commenced negotiations on a separate contract with Local 578 relating to certain store employees, which also was scheduled to expire on August 31, 2007. The Company and Local 578 continued negotiations on both contracts during and subsequent to the third quarter ended September 30, 2007, and the negotiations are ongoing. Pending the negotiations, on August 28, 2007, the Company agreed with Local 578 to extend the existing contracts covering the distribution center employees and store employees on a day-to-day basis, subject to termination by either party on ten (10) days' written notice.

**Item 6. Exhibits**

(a) Exhibits

| <b>Exhibit Number</b> | <b>Description of Document</b>                           |
|-----------------------|--|
| 31.1                  | Rule 13a-14(a) Certification of Chief Executive Officer. |
| 31.2                  | Rule 13a-14(a) Certification of Chief Financial Officer. |
| 32.1                  | Section 1350 Certification of Chief Executive Officer.   |
| 32.2                  | Section 1350 Certification of Chief Financial Officer.   |

-28-

**Table of Contents**

**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.

**BIG 5 SPORTING GOODS  
CORPORATION,**  
a Delaware corporation

Date: November 2, 2007

By: /s/ Steven G. Miller

Steven G. Miller  
*Chairman of the Board of Directors,  
President, Chief Executive Officer  
and Director of the Company*

Date: November 2, 2007

By: /s/ Barry D. Emerson

Barry D. Emerson  
*Senior Vice President,  
Chief Financial Officer and Treasurer  
(Principal Financial and  
Accounting Officer)*