

Edgar Filing: RETAIL VENTURES INC - Form 10-Q

RETAIL VENTURES INC  
Form 10-Q  
December 10, 2004

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

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended October 30, 2004

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 1-10767

RETAIL VENTURES, INC.

-----  
(Exact name of registrant as specified in its charter)

Ohio

20-0090238

-----  
(State or other jurisdiction of  
incorporation or organization)

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

3241 Westerville Road, Columbus, Ohio

43224

-----  
(Address of principal executive offices)

-----  
(Zip Code)

(614) 471-4722

-----  
Registrant's telephone number, including area code

Not applicable

-----  
(Former name, former address and former fiscal year, if changed since last  
report)

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 and (2) has been subject to such filing requirements for  
the past 90 days. YES  NO

Indicate by check mark whether the registrant is an accelerated filer (as  
defined in Rule 12b-2 of the Exchange Act). YES  NO

The number of outstanding Common Shares, without par value, as of November 30,  
2004 was 34,076,155.

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RETAIL VENTURES, INC.  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (IN THOUSANDS, EXCEPT SHARE AMOUNTS)  
 (UNAUDITED)

	October 30, 2004	January 31, 2004
	-----	-----
ASSETS		
Cash and equivalents	\$ 17,666	\$ 14,226
Accounts receivable, net	13,135	8,969
Receivables from related parties	193	137
Inventories	584,832	420,338
Prepaid expenses and other assets	23,844	10,651
Deferred income taxes	52,120	44,933
	-----	-----
Total current assets	691,790	499,254
	-----	-----

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Property and equipment, net	269,822	251,818
Goodwill	37,619	37,619
Tradenames and other intangibles, net	44,512	43,638
Other assets	34,295	31,616
	-----	-----
Total assets	\$ 1,078,038	\$ 863,945
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Accounts payable	\$ 272,384	\$ 147,771
Accounts payable to related parties	5,178	3,335
Accrued expenses	129,285	112,550
Current maturities of long-term obligations	573	741
	-----	-----
Total current liabilities	407,420	264,397
	-----	-----
Long-term obligations, net of current maturities		
Non-related	214,286	154,724
Related parties	173,735	172,216
Other noncurrent liabilities	66,504	55,841
Commitments and contingencies		
Common shares, without par value;		
160,000,000 authorized; issued, including		
treasury shares, 34,083,706 and		
33,990,707 shares, respectively	143,395	143,077
Warrants	6,074	6,074
Retained earnings	72,994	74,321
Deferred compensation expense, net	(300)	(635)
Treasury shares, at cost, 7,551 shares	(59)	(59)
Accumulated other comprehensive loss	(6,011)	(6,011)
	-----	-----
Total shareholders' equity	216,093	216,767
	-----	-----
Total liabilities and shareholders' equity	\$ 1,078,038	\$ 863,945
	=====	=====

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

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RETAIL VENTURES, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)  
(UNAUDITED)

	Three months ended		Nine months ended	
	October 30, 2004	November 1, 2003	October 30, 2004	November 1, 2003
	-----	-----	-----	-----
Net sales, excluding sales of licensed departments	\$ 699,738	\$ 680,639	\$ 1,977,692	\$ 1,873,765
Cost of sales	(419,776)	(419,251)	(1,178,731)	(1,159,291)

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Gross profit	279,962	261,388	798,961	714,474
Selling, general and administrative expenses	(273,560)	(249,597)	(777,025)	(714,516)
License fees and other income	1,950	1,454	5,073	4,246
Operating profit	8,352	13,245	27,009	4,204
Interest expense, net				
Non-related	(3,123)	(2,959)	(8,981)	(9,268)
Related parties	(6,815)	(6,615)	(20,266)	(19,955)
(Loss) income before income taxes	(1,586)	3,671	(2,238)	(25,019)
Benefit (provision) for income taxes	646	(2,770)	911	9,099
Net (loss) income	\$ (940)	\$ 901	\$ (1,327)	\$ (15,920)
Basic and diluted (loss) income per share:				
Basic	\$ (0.03)	\$ 0.03	\$ (0.04)	\$ (0.47)
Diluted	\$ (0.03)	\$ 0.03	\$ (0.04)	\$ (0.47)
Shares used in per share calculations:				
Basic	33,978	33,783	33,914	33,738
Diluted	33,978	34,173	33,914	33,738

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

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RETAIL VENTURES, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
(IN THOUSANDS)  
(UNAUDITED)

	Number of Shares				Retained Earnings	Deferred Compensation Expense
	Common Shares	Common Shares in Treasury	Common Shares	Warrants		
BALANCE, FEBRUARY 1, 2003	33,913	8	\$143,183	\$6,074	\$ 78,767	\$ (981)
Net loss					(15,920)	
Exercise of stock options	7					
Net issuance/forfeitures of restricted shares	57					
Amortization of deferred compensation expense						214
Net unrealized gain on derivative instruments, net of taxes of \$413						

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BALANCE, NOVEMBER 1, 2003	33,977	8	\$143,183	\$6,074	\$ 62,847	\$(767)
	=====	=	=====	=====	=====	=====
BALANCE, JANUARY 31, 2004	33,991	8	\$143,077	\$6,074	\$ 74,321	\$(635)
Net loss					(1,327)	
Exercise of stock options	109		422			
Forfeiture of restricted shares	(16)		(104)			104
Amortization of deferred compensation expense						231
	-----	-	-----	-----	-----	-----
BALANCE, OCTOBER 30, 2004	34,084	8	\$143,395	\$6,074	\$ 72,994	\$(300)
	=====	=	=====	=====	=====	=====

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

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RETAIL VENTURES, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)  
(UNAUDITED)

	Nine months ended	
	October 30, 2004	November 1, 2003
	-----	-----
Cash flows from operating activities:		
Net loss	\$ (1,327)	\$ (15,920)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization of debt issuance costs and discount on debt	4,269	4,494
Amortization of deferred compensation	231	214
Depreciation and amortization	39,507	38,682
Deferred income taxes and other noncurrent liabilities	(9,008)	(5,303)
Loss on disposal of assets	737	252
Change in working capital, assets and liabilities:		
Receivables	(4,222)	2,424
Inventories	(164,494)	(157,893)
Prepaid expenses and other assets	(14,305)	11
Accounts payable	126,456	68,307
Accrued expenses	16,485	(15,585)
	-----	-----
Net cash used in operating activities	(5,671)	(80,317)
	-----	-----
Cash flows from investing activities:		
Capital expenditures	(54,927)	(43,517)
Proceeds from sale of assets	111	41
Tradename acquisition	(4,056)	--
Proceeds from lease incentives	8,605	5,873
	-----	-----
Net cash used in investing activities	(50,267)	(37,603)
	-----	-----

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Cash flows from financing activities:		
Principal payments of capital lease obligations and other debt	(606)	(610)
Net increase in revolving credit facility	60,000	116,000
Debt issuance costs	(438)	--
Proceeds from exercise of stock options	422	--
	-----	-----
Net cash provided by financing activities	59,378	115,390
	-----	-----
Net increase (decrease) in cash and equivalents	3,440	(2,530)
Cash and equivalents, beginning of period	14,226	11,059
	-----	-----
Cash and equivalents, end of period	\$ 17,666	\$ 8,529
	=====	=====

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

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RETAIL VENTURES, INC.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

1. BUSINESS OPERATIONS

Retail Ventures, Inc. and its wholly owned subsidiaries are herein referred to collectively as the Company. The Company operates three segments. Value City Department Stores ("Value City") and Filene's Basement, Inc. ("Filene's Basement") segments operate full-line, off-price department stores. The DSW Shoe Warehouse, Inc. ("DSW") segment sells better-branded off-price shoes and accessories. As of October 30, 2004, there are a total of 116 Value City Department Stores located principally in the Midwestern, Eastern and Southern United States, 167 DSW stores located throughout the United States and 25 Filene's Basement stores located primarily in major metropolitan areas. DSW also supplies, under supply arrangements, to 204 locations for other non-related retailers in the United States.

On October 8, 2003, the Company reorganized its corporate structure into a holding company form whereby Retail Ventures, Inc., an Ohio corporation, became the successor issuer to Value City Department Stores, Inc. As a result of the reorganization, Value City Department Stores, Inc. became a wholly-owned subsidiary of Retail Ventures, Inc.

In connection with the reorganization, holders of common shares of Value City became holders of an identical number of common shares of Retail Ventures, Inc. The reorganization was effected by a merger which was previously approved by the Company's shareholders. Since October 8, 2003, the Company's common shares have been listed for trading under the ticker symbol "RVI" on the New York Stock Exchange.

VALUE CITY. We operate a chain of 116 off-price department stores located in the Midwestern, Eastern and Southern states, principally under the name Value City. For over 80 years, our strategy has been to provide exceptional value by offering a broad selection of brand name merchandise at prices substantially below conventional retail prices.

DSW. We operate a chain of 167 DSW stores located throughout the United

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States. The DSW stores are upscale shoe stores offering a wide selection of branded dress and casual footwear below traditional retail prices. Additionally, Shonac Corporation, the parent company of DSW, pursuant to license agreements with Value City and Filene's Basement, operates licensed shoe departments in most Value City and Filene's Basement stores. Results of operations of the licensed shoe departments are included with the Value City and Filene's Basement segments. Shonac Corporation has also entered into agreements to supply merchandise to unrelated third parties' shoe departments. The results of substantially all supply agreements are included with the DSW segment.

FILENE'S BASEMENT. We operate 25 Filene's Basement stores with 19 of the total stores located in the Boston, New York City and Washington, D.C. metropolitan areas. Filene's Basement focuses on providing the top tier brand names at everyday low prices for men's and women's apparel, jewelry, shoes, accessories and home goods.

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### RETAIL VENTURES, INC. NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

#### 2. BASIS OF PRESENTATION

The accompanying unaudited interim financial statements should be read in conjunction with the 2003 Annual Report on Form 10-K/A.

In the opinion of management, the unaudited interim financial statements reflect all adjustments consisting of only normal recurring adjustments, which are necessary to present fairly the consolidated financial position and results of operations for the periods presented. To facilitate comparisons with the current year, certain previously reported balances have been reclassified to conform to the current period presentation.

#### 3. TRADENAMES AND OTHER INTANGIBLES

During the three months ended May 1, 2004, the Company acquired the "Leslie Fay" tradename for approximately \$4.0 million. The anticipated life of the amortizing asset has been initially assigned 15 years.

#### 4. LONG-TERM OBLIGATIONS

During July, 2004 the Company extended the terms of both the \$350 million Revolving Credit Agreement and the \$100 million Term Loans by one year. The Revolving Credit Agreement and the Term Loans originally set to expire on June 11, 2005, have been extended through June 11, 2006, under substantially the same terms and conditions.

#### 5. PENSION BENEFIT PLANS

The Company has three qualified defined benefit pension plans assumed at the time of previous acquisitions. The Company's funding policy is to contribute an amount annually that satisfies the minimum funding requirements of ERISA and that is tax deductible under the Internal Revenue Code. Contributions provide not only for benefits attributed to service to date but also for those anticipated to be earned in the future. The Company uses a January 31 measurement date for its plans.

The following table shows the components of net periodic benefit cost for the three and nine months ended October 30, 2004 and November 1, 2003:

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	Three months ended		Nine months ended	
	October 30, 2004	November 1, 2003	October 30, 2004	November 1, 2003
	(in thousands)			
Service cost	\$ 11	\$ 9	\$ 32	\$ 26
Interest cost	350	323	1,051	969
Expected return on plan assets	(359)	(321)	(1,077)	(964)
Amortization of transition asset	(9)	(19)	(28)	(56)
Amortization of net loss	145	149	435	447
Net periodic benefit cost	\$ 138	\$ 141	\$ 413	\$ 422

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RETAIL VENTURES, INC.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

The Company had anticipated contributing approximately \$1.5 million in fiscal 2004 to meet minimum funding requirements. As of October 30, 2004, the Company contributed approximately \$1.7 million.

6. 401(K) AND PROFIT SHARING PLAN

The Company recently became aware of an issue involving its 401(K) and profit sharing plan. From September 2001 until July 13, 2004, the Company failed to register the Company's common shares transferred to participants in its 401(k) plan and the interests of those participants in that plan, which may also be deemed securities requiring registration. In addition, prior to November, 2004, the Company failed to deliver a prospectus that complied in all respects with SEC requirements. The Company intends to offer a 30-day right of rescission to those participants who received its common shares in violation of applicable securities laws during the one year period preceding the date of the rescission offer, the statute of limitations period the Company believes may apply to claims for rescission under applicable laws, or possibly a longer or shorter period.

Under the rescission offer, the participants will be entitled to require the Company to repurchase shares at the price per share of the Company's common shares when the shares were transferred to the participant's account, plus interest at a rate to be determined. Based upon the Company's preliminary investigation, it currently believes that up to approximately 700,000 common shares transferred to 401(k) plan participants since September 2001 may not have been properly registered in accordance with the Securities Act of 1933.

The Company has undertaken certain curative action under the applicable securities laws and is also investigating its obligations to undertake any other curative action which may be required under applicable laws. While the Company cannot predict the possible effect of federal or state regulatory action, the Company does not believe that these violations will have a material adverse effect on the Company's financial position or results of operations.



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### 7. SHAREHOLDERS' EQUITY

On September 26, 2002, the Company issued 2,954,792 warrants ("Warrants") to purchase common shares, at an initial exercise price of \$4.50 per share, to Cerberus Partners, L.P., Schottenstein Stores Corporation and Back Bay Capital Funding LLC (the "Term Loan C Lenders"). The Warrants are exercisable at any time prior to June 11, 2012. The Company has granted the Term Loan C Lenders registration rights with respect to the shares issuable upon exercise of the Warrants. The \$6.1 million value ascribed to the Warrants was estimated as of the date of issuance using the Black-Scholes pricing model with the following assumptions: risk-free interest rate of 5.6%; expected life of 10 years; expected volatility of 47%; illiquidity discount of 10%; and an expected dividend yield of 0%. The related debt discount is amortized into interest expense over the life of the debt.

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#### RETAIL VENTURES, INC. NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The number of shares issuable varies upon the occurrence of the following: (i) the issuance of additional common shares without consideration or for a consideration per share less than the Warrant exercise price; (ii) the declaration of any dividend; (iii) the combination or consolidation of the outstanding common shares into a lesser number of shares; (iv) the issuance or sale of additional shares at a price per share less than the current market price but greater than the Warrant exercise price; (v) the issuance of convertible securities which are convertible into common shares; and/or (vi) the exchange of shares in a merger or other business combination.

#### \$75 Million Senior Subordinated Convertible Loan - Related Parties

The Company amended and restated its \$75.0 million Senior Subordinated Convertible Loan Agreement on June 11, 2002 (the "Convertible Loan"). As amended, borrowings under the Convertible Loan will bear interest at 10% per annum. At the Company's option, interest may be paid-in-kind ("PIK"), from the closing date to the second anniversary thereof, and thereafter, at the option of the Company, up to 50% of the interest due may be PIK until maturity. PIK interest accrued with respect to the Convertible Loan is added to the outstanding principal balance, on a quarterly basis and is payable in cash upon the maturity of the debt. The Convertible Loan is guaranteed by all principal subsidiaries and is secured by a lien on assets junior to liens granted in favor of the lenders on the Revolving Credit Agreement and Term Loans. The Convertible Loan is not subject to prepayment until June 11, 2007. The agent has the right to designate two observers to the Board of Directors for so long as the agent is the beneficial owner of at least 50% of the advances initially made by it and has the right to designate two individuals to the Board of Directors for so long as the agent is the beneficial owner of at least 50% of the conversion shares issued or issuable upon conversion of the advances initially made by it.

The Convertible Loan is convertible at the option of the holders into common shares of the Company and has a conversion price of \$4.50. The maturity date is June 10, 2009.

### 8. EARNINGS PER SHARE

Basic earnings per share are based on the net income (loss) and a simple weighted average of common shares outstanding. Diluted earnings per share reflects the potential dilution of common shares, related to outstanding

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stock options, Stock Appreciation Rights (SARS) and warrants, calculated using the treasury stock method and convertible debt calculated using the if-converted method. The numerator for the diluted earnings per share calculation is the net income (loss) adjusted to remove the effect of interest, adjusted for tax, on the convertible debt.

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RETAIL VENTURES, INC.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

	Three months ended		Nine months ended	
	October 30, 2004	November 1, 2003	October 30, 2004	November 1, 2003
	(in thousands)			
Weighted average shares outstanding	33,978	33,783	33,914	33,738
Assumed exercise of dilutive stock options	--	390	--	--
	-----	-----	-----	-----
Number of shares for computation of dilutive earnings per share	33,978	34,173	33,914	33,738
	-----	-----	-----	-----

For the three months ended November 1, 2003, all potentially dilutive SARS, warrants and convertible debt, were anti-dilutive. For the three months ended October 30, 2004 and the nine months ended October 30, 2004 and November 1, 2003 all potentially dilutive instruments: stock options, SARS, warrants and convertible debt, were anti-dilutive.

### 9. ADOPTION OF ACCOUNTING STANDARDS

The Financial Accounting Standards Board ("FASB") periodically issues Statements of Financial Accounting Standards ("SFAS"), some of which require implementation by a date falling within or after the close of the fiscal year.

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46), which requires the consolidation of certain entities considered to be variable interest entities (VIEs). An entity is considered to be a VIE when it has equity investors who lack the characteristics of having a controlling financial interest, or its capital is insufficient to permit it to finance its activities without additional subordinated financial support. Consolidation of a VIE by an investor is required when it is determined that the investor will absorb a majority of the VIE's expected losses or residual returns if they occur. FIN 46 provides certain exceptions to these rules, relating to qualifying special purpose entities (QSPE's) subject to the requirements of SFAS No. 140. Upon its original issuance, FIN 46 required that VIEs created after January 31, 2003 would be consolidated immediately, while VIEs created prior to February 1, 2003 were to be consolidated as of July 1, 2003.

In October 2003, the FASB deferred the effective date for consolidation of VIEs created prior to February 1, 2003 to December 31, 2003 for calendar year-end companies, with earlier application encouraged.

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In December 2003, the FASB published a revision to FIN 46 (FIN 46R) to clarify some of the provisions of the original interpretation and to exempt certain entities from its requirements. FIN 46R provides special effective date provisions to enterprises that fully or partially applied to FIN 46 prior to the issuance of the revised interpretation. In particular, entities that have already adopted FIN 46 are not required to adopt FIN 46R until the quarterly reporting period ended July 31, 2004. Adoption of the required sections of FIN 46, as modified and interpreted, including the provisions of FIN 46R, did not have any effect on the Company's consolidated financial statements or disclosures.

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RETAIL VENTURES, INC.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

### 10. ACCUMULATED OTHER COMPREHENSIVE LOSS

The balance sheet caption accumulated other comprehensive loss of \$6.0 million at October 30, 2004 and January 31, 2004, relates to the minimum pension liability, net of income tax.

### 11. STOCK BASED COMPENSATION

The Company has various stock-based employee compensation plans. The Company accounts for those plans in accordance with APB No. 25, "Accounting For Stock Issued to Employees," and related Interpretations. Accordingly, no stock-based employee compensation cost has been recognized for the fixed stock option plans or the stock purchase plan. The following table illustrates the effect on net loss and loss per share if the Company had applied the fair value recognition of SFAS 123, "Accounting for Stock-Based Compensation."

	Three months ended		Nine months ended	
	October 30, 2004	November 1, 2003	October 30, 2004	November 1, 2003
	(in thousands, except per share amounts)			
Net (loss) income, as reported	\$ (940)	\$ 901	\$ (1,327)	\$ (15,920)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of tax	(468)	(1,065)	(1,895)	(3,374)
Pro forma net (loss) income	\$ (1,408)	\$ (164)	\$ (3,222)	\$ (19,294)
(Loss) income per share:				
Basic and diluted as reported	\$ (0.03)	\$ 0.03	\$ (0.04)	\$ (0.47)
Basic and diluted pro forma	\$ (0.04)	\$ 0.00	\$ (0.10)	\$ (0.57)

### 12. TAX VALUATION

The Company establishes valuation allowances for deferred tax assets when the amount of expected future taxable income is not likely to support the use of

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the deduction or credit. For the nine months ended October 30, 2004, no additional allowance has been provided. During the previous fiscal year ended January 31, 2004 an allowance of \$1.5 million was provided for as the Company determined that it was more likely than not that future taxable income may not be sufficient to fully utilize deferred tax assets.

The tax rate of 40.7% reflects the impact of the non-deductible warrant amortization included for book income but not tax.

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RETAIL VENTURES, INC.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

### 13. SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

A supplemental schedule of non-cash investing and financing activities is presented below:

	Nine months ended	
	October 30, 2004	November 1, 2003
	-----	-----
	(in thousands)	
Cash paid during the period for:		
Interest		
Non-related parties	\$ 7,346	\$11,222
Related parties	17,675	16,742
Income taxes	\$11,675	\$ 1,677

### 14. SEGMENT REPORTING

The Company is managed in three operating segments: Value City, DSW and Filene's Basement. All of the operations are located in the United States. The Company has identified such segments based on management responsibility and measures segment profit as operating profit (loss), which is defined as income before interest expense and income taxes.

The tables below present segment income statement information for the three and nine months ended October 30, 2004 and November 1, 2003 and balance sheet information as of October 30, 2004 and January 31, 2004.

	Value City	DSW	Filene's Basement	Total
	-----	-----	-----	-----
	(in thousands)			
Three months ended October 30, 2004				
Net sales	\$ 346,055	\$255,787	\$ 97,896	\$699,738
Operating (loss) profit	(7,653)	16,389	(384)	8,352
Capital expenditures	8,289	7,115	8,723	24,127
Depreciation and amortization	8,617	3,625	1,646	13,888

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	Value City -----	DSW -----	Filene's Basement -----	Total -----
	(in thousands)			
Three months ended November 1, 2003				
Net sales	\$375,393	\$215,757	\$ 89,489	\$680,639
Operating profit (loss)	6,161	9,357	(2,273)	13,245
Capital expenditures	7,816	8,582	3,615	20,013
Depreciation and amortization	5,903	5,381	1,602	12,886

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RETAIL VENTURES, INC.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

	Value City -----	DSW -----	Filene's Basement -----	Total -----
	(in thousands)			
Nine months ended October 30, 2004				
Net sales	\$ 1,002,740	\$711,488	\$ 263,464	\$1,977,692
Operating (loss) profit	(13,816)	44,604	(3,779)	27,009
Capital expenditures	17,357	20,332	17,238	54,927
Depreciation and amortization	21,665	12,832	5,010	39,507
As of October 30, 2004				
Identifiable assets	553,752	345,304	178,982	1,078,038

	Value City -----	DSW -----	Filene's Basement -----	Total -----
	(in thousands)			
Nine months ended November 1, 2003				
Net sales	\$ 1,054,809	\$591,146	\$ 227,810	\$1,873,765
Operating (loss) profit	(16,453)	23,333	(2,676)	4,204
Capital expenditures	21,294	16,798	5,425	43,517
Depreciation and amortization	22,832	11,311	4,539	38,682
As of January 31, 2004				
Identifiable assets	477,213	271,205	115,527	863,945

15. COMMITMENTS AND CONTINGENCIES

The Company is involved in various legal proceedings that are incidental to the conduct of its business. The Company estimates the range of liability related to pending litigation where the amount and range of loss can be

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estimated. The Company records its best estimate of a loss when the loss is considered probable. Where a liability is probable and there is a range of estimated loss, the Company records the minimum estimated liability related to the claim. In the opinion of management, the amount of any liability with respect to these proceedings will not be material. As additional information becomes available, the Company assesses the potential liability related to its pending litigation and revises the estimates. Revisions in the Company's estimates and potential liability could materially impact its results of operations.

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

#### RISK FACTORS AND SAFE HARBOR STATEMENT

We caution that any forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995) contained in this Report and/or other risk factors that may be described in the Safe Harbor Statement and Business Risks section of the Company's Annual Report on Form 10-K/A for the year ended January 31, 2004 (the "2003 Annual Report"), or contained in other filings with the Securities and Exchange Commission (the "SEC") or made by our management involve risks and uncertainties, and are subject to change based on various important factors. The following factors, among others, in some cases have affected the matters discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations. These same factors could cause our future financial performance in fiscal 2004 and beyond to differ materially from those expressed or implied in any such forward-looking statements. These factors include: decline in demand for our merchandise, our ability to achieve our business plans, expected cash flow from operations, vendors and their factor relations, flow of merchandise, compliance with our credit agreements, our ability to strengthen our liquidity and increase our credit availability, the availability of desirable store locations on suitable terms, changes in consumer spending patterns, marketing strategies, consumer preferences and overall economic conditions, the impact of competition and pricing, changes in weather patterns, changes in fuel and energy costs, changes in existing or potential duties, tariffs or quotas, paper and printing costs, the ability to hire and train associates and development of management information systems.

Our operations have been historically seasonal, with a disproportionate amount of sales and a majority of net income occurring in the back-to-school and Christmas selling seasons for Value City and Filene's Basement. DSW seasonal sales occur both in early Spring and Fall. As a result of seasonality, any factors negatively affecting us during these periods, including adverse weather, the timing and level of markdowns or unfavorable economic conditions, could have a material adverse effect on our financial condition and results of operations for the entire year.

#### CRITICAL ACCOUNTING POLICIES

Management's Discussion and Analysis discusses the results of operations and financial condition as reflected in our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles. As discussed in Notes to Consolidated Financial Statements that are included in our 2003 Annual Report, the preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of commitments and contingencies at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. On an ongoing basis, management evaluates its estimates and

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judgments, including, but not limited to, those related to inventory valuation, depreciation, amortization, recoverability of long-lived assets including intangible assets, the calculation of retirement benefits, estimates for self insurance reserves for

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health and welfare, workers' compensation and casualty insurance, income taxes, contingencies, litigation and revenue recognition. Management bases its estimates and judgments on its historical experience and other relevant factors, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The process of determining significant estimates is fact specific and takes into account factors such as historical experience, current and expected economic conditions, product mix, and in some cases, actuarial and appraisal techniques. We constantly re-evaluate these significant factors and make adjustments where facts and circumstances dictate.

While we believe that our historical experience and other factors considered provide a meaningful basis for the accounting policies applied in the preparation of the consolidated statements, we cannot guarantee that our estimates and assumptions will be accurate. As the determination of these estimates requires the exercise of judgment, actual results inevitably will differ from those estimates, and such differences may be material to the financial statements.

We believe the following represent the most critical estimates and assumptions, among others, used in the preparation of our consolidated financial statements. We have discussed the selection, application and disclosure of the critical accounting policies with our audit committee.

- Revenue recognition. Revenues from our retail operations are recognized at the latter of point-of-sale or the delivery of goods to the customer. Retail revenues are reduced by a provision for anticipated returns based on historical trends.
- Cost of sales and merchandise inventories. We use the retail method of accounting for substantially all of our merchandise inventories. Merchandise inventories are stated at the lower of cost, determined using the first-in, first-out basis, or market, using the retail inventory method. The retail inventory method is widely used in the retail industry due to its practicality. Under the retail inventory method, the valuation of inventories at cost and the resulting gross margins are calculated by applying a calculated cost to retail ratio to the retail value of inventories. The cost of the inventory reflected on our consolidated balance sheet is decreased by charges to cost of sales at the time the retail value of the inventory is lowered through the use of markdowns. Hence, earnings are negatively impacted as merchandise is marked down prior to sale. Reserves to value inventory at the lower of cost or market were \$39.1 million at October 30, 2004 and \$34.2 million at January 31, 2004.

Inherent in the calculation of inventories are certain significant management judgments and estimates, including setting the original merchandise retail value or markon, markups of initial prices established, reduction of pricing due to customer's value perception or perceived value known as markdowns, and estimates of losses between physical inventory counts or shrinkage, which, combined with the averaging process within the retail method, can significantly impact the ending inventory valuation at cost and the resulting gross margins.

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- Long-lived assets. In evaluating the fair value and future benefits of long-lived assets, we perform an analysis of the anticipated undiscounted future cash flows of the related long-lived asset and reduce the carrying value by the excess where the recorded value exceeds the fair value. Goodwill is tested on an annual basis using a fair value based approach.

For the nine months ended October 30, 2004 we recorded an impairment of \$0.7 million related to the Value City segment for store assets. For the period ended November 1, 2003, we recorded no impairments related to long-lived assets.

We believe at this time that the remaining long-lived assets' carrying values and useful lives continue to be appropriate. To the extent these future projections or our strategies change, the conclusion regarding impairment may differ from our current estimates.

- Self-insurance reserves. We record estimates for certain health and welfare, workers compensation and casualty insurance costs that are self-insured programs. These estimates are based on actuarial assumptions and are subject to change based on actual results. Should a greater amount of claims occur compared to what was estimated for costs of certain health and welfare, workers compensation and casualty insurance increase beyond what was anticipated, reserves recorded may not be sufficient and to the extent actual results vary from assumptions, earnings would be impacted.
- Pension. The obligations and related assets of defined benefit retirement plans are included in the Notes to Consolidated Financial Statements in the Company's 2003 Annual Report. Plan assets, which consist primarily of marketable equity and debt instruments, are valued using market quotations. Plan obligations and the annual pension expense are determined by independent actuaries and through the use of a number of assumptions. Key assumptions in measuring the plan obligations include the discount rate, the rate of salary increases and the estimated future return on plan assets. In determining the discount rate, we utilize the yield on fixed-income investments currently available with maturities corresponding to the anticipated timing of the benefit payments. Salary increase assumptions are based upon historical experience and anticipated future management actions. Asset returns are based upon the anticipated average rate of earnings expected on the invested funds of the plans. At October 30, 2004, the actuarial assumptions of our plans have remained unchanged from our 2003 Annual Report. To the extent actual results vary from assumptions, earnings would be impacted.
- Customer loyalty program. We maintain a customer loyalty program for our DSW operations in which customers receive a future discount on qualifying purchases. The DSW "Reward Your Style" program is designed to promote customer awareness and loyalty plus provide the Company with the ability to

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communicate with our customers and enhance our understanding of their spending trends. Upon reaching the target level, customers may redeem these discounts on a future purchase. Generally, these future discounts must be redeemed within six months. DSW's accrued liability as of



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October 30, 2004 and January 31, 2004 was \$4.0 million and \$3.0 million, respectively.

During the third quarter of 2004, Filene's Basement implemented a limited-time customer rewards program. The rewards program will provide qualifying customers with a Filene's Basement certificate in various denominations based on their cumulative spending during the program period (October 1, 2004 through December 31, 2004). Filene's Basement had an accrued liability related to the rewards program of \$0.4 million at October 30, 2004.

For the DSW and Filene's Basement rewards programs, we accrue the estimated costs of the anticipated redemptions of the discount earned at the time of the initial purchase and charge such costs to selling, general and administrative expense based on historical experience. The estimates of the costs associated with the loyalty programs require us to make assumptions related to customer purchase levels and redemption rates. To the extent assumptions of purchases and redemption rates vary from actual results, earnings would be impacted.

- Income taxes. We do business in numerous jurisdictions that impose taxes. Management is required to determine the aggregate amount of income tax expense to accrue and the amount which will be currently payable based upon tax statutes of each jurisdiction. The estimation process involves adjusting income determined by the application of generally accepted accounting principles for items that are treated differently by the applicable taxing authorities. Deferred tax assets and liabilities are reflected on our balance sheet for temporary differences that will reverse in subsequent years. If different management judgments had been made, our tax expense, assets and liabilities could be different. During fiscal 2003, we established a reserve for deferred income tax assets of \$1.5 million for carry forwards related to state and local net operating losses and for excess contribution carry forwards. For the nine months ended October 30, 2004, no additional allowance has been provided.

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### RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated, the percentage relationships to net sales of the listed items included in the Company's Consolidated Statements of Operations.

	Three months ended(1)		Nine months ended(1)	
	October 30, 2004	November 1, 2003	October 30, 2004	November 2003
Net sales, excluding sales of licensed departments	100.0%	100.0%	100.0%	100.0%
Cost of sales	(60.0)	(61.6)	(59.6)	(61.9)
Gross profit	40.0	38.4	40.4	38.1
Selling, general and administrative expenses	(39.1)	(36.7)	(39.3)	(38.1)
License fees and other income	0.3	0.2	0.3	0.2

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Operating profit (loss)	1.2	1.9	1.4	0.2
Interest expense, net	(1.4)	(1.4)	(1.5)	(1.5)
	-----	-----	-----	-----
(Loss) Income before income taxes	(0.2)	0.5	(0.1)	(1.3)
Benefit (Provision) for income taxes	0.1	(0.4)	-	0.5
	=====	=====	=====	=====
Net (loss) income	(0.1)%	0.1%	(0.1)%	(0.8)%
	-----	-----	-----	-----

(1) Because of the seasonal nature of our retail business cycle, the results of operations for the 13 weeks and 39 weeks ended October 30, 2004 and November 1, 2003 (which do not include the Christmas holiday season) are not necessarily indicative of the Company's results of operations for the fiscal year.

THREE MONTHS ENDED OCTOBER 30, 2004 COMPARED TO THREE MONTHS ENDED NOVEMBER 1, 2003

Net sales increased \$19.1 million, or 2.8%, from \$680.6 million to \$699.7 million. Comparable store sales decreased 4.1% and, by segment, were:

	Three months ended	
	-----	-----
	October 30, 2004	November 1, 2003
	-----	-----
Value City	(7.8)%	2.3%
DSW	0.7%	11.7%
Filene's Basement	1.2%	8.5%
	----	----
Total	(4.1)%	5.4%
	=====	=====

Value City comparable stores sales for the quarter decreased 7.8% due to a decline in customer traffic against the comparable period partially offset by higher average unit retail. DSW and Filene's Basement sales increased for the same period due to increases in customer traffic and average unit retail.

Value City's segment sales decreased \$29.3 million to \$346.1 million, a 7.8% comparable store sales decrease in the quarter. The decrease in comparable sales is comprised of decreases in

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non-apparel hardlines of 3.0%, apparel of 8.6% and Jewelry of 14.2%. The merchandise categories of mens, ladies and childrens had decreases of 8.3%, 9.4% and 7.7%, respectively. Shoe sales in the Value City segment were a negative 10.7% in the quarter.

DSW segment sales were \$255.8 million, an 18.6% increase in the quarter which includes a net increase of 30 stores over the comparable period along with the comparable store sales increase of 0.7%. The DSW operations in the segment merchandise category of athletics had an increase of 12.9% while the mens and womens areas had decreases of 2.1% and 1.2%, respectively. During the quarter we had a net increase of 49 leased shoe departments covered under various supply agreements over the comparable prior year period.

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Filene's Basement sales increased 9.4% in the quarter to \$97.9 million which includes a net increase of 4 stores over the prior year's period and a comparable store sales increase of 1.2%. Merchandise categories of mens, ladies and childrens had comparable sale increases of 0.5%, 6.7% and 15.9%, respectively. The shoe and jewelry categories had increases of 2.6% and 1.5%, respectively. Home sales in the segment decreased 6.1%.

Total gross profit increased \$18.6 million to \$280.0 million. Gross profit, as a percentage of sales, increased to 40.0% compared to 38.4% for the prior year. The increase in our overall margin rate is attributable to higher initial markups for all retail business operations. The Value City segment improved average unit retail, initial retail markup and reduced markdowns to obtain the gross margin increase. The continued improvement in comparable sales in DSW and Filene's Basement segments reduced the need for promotional markdowns during the period. Gross profit, as a percent of sales by segment in the third quarter, was:

	Three months ended	
	October 30, 2004	November 1, 2003
Value City	38.9%	38.0%
DSW	43.5%	40.8%
Filene's Basement	34.9%	34.2%
	----	----
Total	40.0%	38.4%
	====	====

Selling, general and administrative expenses ("SG&A") increased \$24.0 million from \$249.6 million to \$273.6 million. Approximately \$4.0 million is associated with the increase in pre-opening expenses incurred during the three months ended October 30, 2004 compared with the three months ended November 1, 2003. Total SG&A expense associated with stores opened subsequent to November 1, 2003 and through October 30, 2004 was \$18.0 million and represents approximately 75% of the increase in SG&A expense. As a percentage of sales SG&A was 39.1% compared to 36.7% in the comparable quarter last year. SG&A, as a percent of sales by segment in the third quarter, was:

	Three months ended	
	October 30, 2004	November 1, 2003
Value City	41.5%	35.8%
DSW	37.1%	40.1%
Filene's Basement	35.7%	32.2%
	----	----
Total	39.1%	36.7%
	====	====

License fees and other income were \$2.0 million and \$1.5 million for the

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comparative periods. License fees and other income are comprised of fees from licensees, layaway fees and vending income. These sources of income can vary based on customer traffic and contractual arrangements.

Operating profit decreased to \$8.4 million from \$13.2 million and decreased as a percentage of sales from 1.9% to 1.2%.

Net interest expense for the quarter increased \$0.4 million to \$9.9 million. The increase is due primarily to an increase in our weighted average borrowing rate and an increase of \$25.3 million in average borrowings from last year to this year.

The effective tax rate for the three months ended October 30, 2004 was 40.7% as compared to 75.5% for the three months ended November 1, 2003. The tax rate reflects the impact of the non-deductible warrant amortization included for book income but not tax.

NINE MONTHS ENDED OCTOBER 30, 2004 COMPARED TO NINE MONTHS ENDED NOVEMBER 1, 2003

Net sales increased \$103.9 million, or 5.5% from \$1,873.8 million to \$1,977.7 million. Comparable store sales decreased 0.7% and, by segment, were:

	Nine months ended	
	October 30, 2004	November 1, 2003
	-----	-----
Value City	(4.9)%	(0.4)%
DSW	4.5%	4.2%
Filene's Basement	6.6%	0.6%
	----	----
Total	(0.7)%	0.9%
	====	====

Value City's segment sales were \$1,002.7 million, a 4.9% decrease in the nine-month period. Value City's non-apparel comparable sales decreased 1.2% while apparel sales decreased 6.2%. Non-apparel sales were positively impacted by increases in domestics of 5.2%. The three apparel divisions, mens, ladies and childrens had negative comparable sales for the nine-month period of 5.6%, 7.9% and 3.0%, respectively. The customer traffic decrease from the comparable nine months a year ago is partially offset by average unit retail increase.

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DSW segment sales were \$711.5 million, a 20.4% increase in the nine-month period, which includes a net increase of 30 DSW stores and the net increase of 49 leased locations over the comparable prior year period. During the nine month period comparable store sales increased 4.5%. DSW increases in the nine-month period for womens, mens and athletic were 3.6%, 0.1% and 9.7%, respectively.

Filene's Basement segment sales were \$263.5 million, a 15.7% increase in the nine-month period, which includes a net increase of 4 stores over the comparable prior year period. Merchandise categories of mens, ladies and childrens had comparable increases of 7.3%, 6.9% and 26.2%, respectively, while other categories of shoes and home had increases of 9.6% and 5.4%, respectively. During the nine-month period comparable store sales increased 6.6%.

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Gross profit increased by \$84.5 million to \$799.0 million, from \$714.5 million, and increased as a percentage of sales from 38.1% to 40.4%. The Value City segment improved average unit retail, initial retail markup and reduced markdowns to obtain the gross margin improvement. The positive sales, higher initial markups and markdown management in DSW and Filene's Basement segments positively impacted the gross margin for these segments in the nine-month period comparison. Total gross profit increased 11.8%. Gross profit, as a percent of sales by segment in the nine-month period, was:

	Nine months ended	
	October 30, 2004	November 1, 2003
Value City	39.6%	37.9%
DSW	43.4%	40.2%
Filene's Basement	35.4%	33.7%
	----	----
Total	40.4%	38.1%
	=====	=====

SG&A increased \$62.5 million, from \$714.5 million to \$777.0 million, and increased as a percentage of sales from 38.1% to 39.3%. Approximately \$7.3 million is associated with the increase in pre-opening expenses incurred during the nine months ended October 30, 2004 compared with the nine months ended November 1, 2003. This increase includes \$28.8 million attributable to new stores and leased shoe departments in operation at DSW and \$8.6 million attributable to new stores in the Filene's Basement division. The increase in SG&A as a percentage of sales is due in part to additional marketing efforts to promote sales and create brand awareness. SG&A as a percent of sales by segment in the nine-month period was:

	Nine months ended	
	October 30, 2004	November 1, 2003
Value City	41.3%	39.2%
DSW	37.2%	37.6%
Filene's Basement	37.3%	34.6%
	----	----
Total	39.3%	38.1%
	=====	=====

License fees and other operating income increased approximately \$0.9 million, from \$4.2 million to \$5.1 million, and increased as a percentage of sales from 0.2% to 0.3%. License fees and

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other income are comprised of fees from licensees, layaway fees and vending income. These sources of income can vary based on customer traffic and contractual arrangements.

Operating profit increased to \$27.0 million from \$4.2 million and improved as a percentage of sales from 0.2% to 1.4%. The operating profit increase is

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attributable to the increased margin partially offset by increased expenses.

Net interest expense for the nine-month period was comparable at \$29.2 million.

The effective tax rate for the nine months ended October 30, 2004 is 40.7% versus 36.4% for the nine months ended November 1, 2003.

### LIQUIDITY AND CAPITAL RESOURCES

Our primary ongoing cash requirements are for seasonal and new store inventory purchases, capital expenditures in connection with expansion, remodeling and information technology development. The primary sources of funds for these liquidity needs are cash flow from operations and credit facilities. Our working capital and inventory levels typically build throughout the year and reach the highest level in the fall, peaking during the holiday selling season.

Net working capital was \$284.4 million and \$234.9 million at October 30, 2004 and January 31, 2004, respectively. Current ratios at those dates were 1.7 and 1.9, respectively. The increase in net working capital is primarily due to the increased inventory levels at October 30, 2004, due to the seasonality of the Company's business. The decrease in the current ratio is primarily due to the increase in accounts payable partially offset by the increased inventory levels.

Net cash used in operations was \$5.7 million in year-to-date fiscal 2004 as compared to \$80.3 million in year-to-date fiscal 2003.

Net cash used for capital expenditures was \$54.9 million and \$43.5 million for the nine months ended October 30, 2004 and November 1, 2003, respectively. During the nine months ended October 30, 2004, capital expenditures included \$31.7 million for new stores, \$14.6 million for improvements in existing stores and \$8.6 million for information technology equipment upgrades and new systems. The primary increase in capital expenditures is due to an increase in new store openings during the nine month period ending October 30, 2004 compared with the nine month period ending November 1, 2003. In addition to the capital expenditures during the nine-month period, we acquired a tradename for \$4.0 million. A source of cash from investing activities is the proceeds from lease incentives which are amortized as a reduction of rent expense over the life of the lease.

On June 11, 2002, Value City Department Stores, Inc., together with certain other principal subsidiaries of Retail Ventures, Inc., entered into a \$525.0 million refinancing that consists of three separate credit facilities (collectively, the "Credit Facilities"): (i) a three-year \$350.0 million revolving credit facility (the "Revolving Credit Facility"), (ii) two \$50.0 million term loan facilities provided equally by Cerberus Partners, L.P. and Schottenstein Stores Corporation (the "Term Loans"), and (iii) an amended and restated \$75.0 million senior subordinated convertible loan, initially entered into by us on March 15, 2000, which is held equally by Cerberus Partners, L.P.

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and Schottenstein Stores Corporation (the "Convertible Loan"). These Credit Facilities are guaranteed by Retail Ventures, Inc. and substantially all of its subsidiaries.

We are not subject to any financial covenants under these Credit Facilities; however, there are numerous restrictive covenants relating to our management and operation. These non-financial covenants include, among other restrictions, limitations on indebtedness, guarantees, mergers, acquisitions, fundamental corporate changes, financial reporting requirements, budget approval, disposition of assets, investments, loans and advances, liens, dividends, stock

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purchases, transactions with affiliates, issuance of securities and the payment of and modification to debt instruments. These Credit Facilities are also subject to an Intercreditor Agreement, which provides for an established order of payment of obligations from the proceeds of collateral upon default (the "Intercreditor Agreement").

### \$350 Million Revolving Credit Facility

Under the Revolving Credit Facility, the borrowing base formula is structured in a manner that allows us and our subsidiaries availability based on the value of inventories and receivables. Primary security for the Revolving Credit Facility is provided by a first priority lien on all of our inventory and accounts receivable, as well as certain intercompany notes and payment intangibles. Subject to the Intercreditor Agreement, the Revolving Credit Facility also has a second priority perfected interest in all of the collateral securing the Term Loans. Interest on borrowings is calculated at the bank's base rate or Eurodollar rate plus 2.00% to 2.75%, depending upon the level of average excess availability we maintain. The maturity date was amended in the current quarter to expire on June 11, 2006. At October 30, 2004 and January 31, 2004, \$108.8 million and \$137.7 million were available under the Revolving Credit Facility, respectively. Direct borrowings aggregated \$185.0 million and \$125.0 million at October 30, 2004 and at January 31, 2004, respectively, while \$21.2 million and \$23.4 million letters of credit were issued and outstanding, respectively.

### \$100 Million Term Loans - Related Parties

The Term Loans are comprised of a \$50.0 million Term Loan B and a \$50.0 million Term Loan C. All obligations under the Term Loans are senior debt and, subject to the Intercreditor Agreement, have the same rights and privileges as the Revolving Credit Facility and the Convertible Loan. We and our principal subsidiaries are obligated on the facility. The maturity date as amended is June 11, 2006.

The Term Loans' stated rate of interest per annum during the initial two years is 14% if paid in cash and 15% if we elect a PIK option. During the first two years of the Term Loans, we may pay all interest in PIK. During the final year of the Term Loans, the stated rate of interest is 15.0% if paid in cash or 15.5% if PIK and the PIK option is limited to 50% of the interest due. At the nine months ended October 30, 2004 and for the year ended January 31, 2004, we elected to pay interest in cash.

We issued 2,954,792 Warrants to purchase shares of common stock, at an initial exercise price of \$4.50 per share, to the Term Loan C Lenders. The Warrants are exercisable at any time prior to June 11, 2012. We have granted the Term Loan C Lenders registration rights with respect to

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the shares issuable upon exercise of the Warrants. The \$6.1 million value ascribed to the Warrants was estimated as of the date of issuance using the Black-Scholes Pricing Model with the following assumptions: risk-free interest rate of 5.6%; expected life of 10 years; expected volatility of 47%; illiquidity discount of 10%; and an expected dividend yield of 0%. The related debt discount is amortized into interest expense over the life of the debt.

The number of shares issuable varies upon the occurrence of the following: (i) the issuance of additional shares of common stock without consideration or for a consideration per share less than the Warrant exercise price; (ii) the declaration of any dividend; (iii) the combination or consolidation of the outstanding shares of common stock into a lesser number of shares; (iv) the issuance or sale of additional shares at a price per share less than the current

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market price but greater than the Warrant exercise price; (v) the issuance of convertible securities which are convertible into shares of common stock; and/or (vi) the exchange of shares in a merger or other business combination.

### \$75 Million Senior Subordinated Convertible Loan - Related Parties

We have amended and restated our \$75.0 million Convertible Loan dated March 15, 2000. As amended, borrowings under the Convertible Loan bears interest at 10% per annum. At our option, interest may be PIK during the first two years, and thereafter, at our option, up to 50% of the interest due may be PIK until maturity. PIK interest accrued with respect to the convertible loan is added to the outstanding principal balance, on a quarterly basis, and is payable in cash upon the maturity of the debt. The Convertible Loan is guaranteed by all principal subsidiaries and is secured by a lien on assets junior to liens granted in favor of the lenders on the Revolving Credit Facility and Term Loans. The Convertible Loan is not prepayable until June 11, 2007, and has a maturity date of June 10, 2009. The agent has the right to designate two observers to our Board of Directors for so long as the agent is the beneficial owner of at least 50% of the advances initially made by it and has the right to designate two individuals to our Board of Directors for so long as the agent is the beneficial owner of at least 50% of the conversion shares issued or issuable upon conversion of the advances initially made by it.

The Convertible Loan is convertible at the option of the holders into shares of our common stock at an initial conversion price of \$4.50. The conversion price is subject to adjustment upon the occurrence of specified events.

Achievement of expected cash flows from operations and compliance with the restrictive covenants of our credit agreements (as discussed in the Notes to Consolidated Financial Statements that are included in our 2003 Annual Report) are dependent upon a number of factors, including the attainment of sales, gross profit, expense levels, vendor relations, and flow of merchandise that are consistent with our financial projections. Future limitations of credit availability by factor organizations and/or vendors will restrict our ability to obtain merchandise and services and may impair operating results. We believe that cash generated by operations, along with the available proceeds from our credit agreements and other sources of financing will be sufficient to meet our obligations for working capital, capital expenditures, and debt service. However, there is no assurance that we will be able to meet our projections. Further, there is no assurance that extended financing will be available in the future if we fail to meet our projections or on terms acceptable to us.

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### Contractual Obligations and Off-Balance Sheet Arrangements

During the current year, we have continued to enter into various construction commitments, including capital items to be purchased for projects that were under construction, or for which a lease has been signed. Our obligations under these commitments aggregated approximately \$0.5 million at October 30, 2004. In addition, we signed lease agreements for new store locations with annual rent of approximately \$12.7 million and average terms of ten years. Associated with the new lease agreements, we will receive approximately \$9.1 million of tenant improvement allowances which will offset future capital expenditures.

There are no "off-balance sheet" arrangements as of October 30, 2004 as that term is described by the SEC.

### ADOPTION OF ACCOUNTING STANDARDS

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of



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Variable Interest Entities" (FIN 46), which requires the consolidation of certain entities considered to be VIEs. An entity is considered to be a VIE when it has equity investors who lack the characteristics of having a controlling financial interest, or its capital is insufficient to permit it to finance its activities without additional subordinated financial support. Consolidation of a VIE by an investor is required when it is determined that the investor will absorb a majority of the VIE's expected losses or residual returns if they occur. FIN 46 provides certain exceptions to these rules, relating to QSPE's subject to the requirements of SFAS No. 140. Upon its original issuance, FIN 46 required that VIEs created after January 31, 2003 would be consolidated immediately, while VIEs created prior to February 1, 2003 were to be consolidated as of July 1, 2003.

In October 2003, the FASB deferred the effective date for consolidation of VIEs created prior to February 1, 2003 to December 31, 2003 for calendar year-end companies, with earlier application encouraged.

In December 2003, the FASB published a revision to FIN 46 (FIN 46R) to clarify some of the provisions of the original interpretation and to exempt certain entities from its requirements. FIN 46R provides special effective date provisions to enterprises that fully or partially applied to FIN 46 prior to the issuance of the revised interpretation. In particular, entities that have already adopted FIN 46 are not required to adopt FIN 46R until the quarterly reporting period ended July 31, 2004. Adoption of the required sections of FIN 46, as modified and interpreted, including the provisions of FIN 46R, did not have any effect on the Company's consolidated financial statements or disclosures.

### SARBANES-OXLEY ACT

We are in the process of documenting and testing our internal control procedures in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act, which requires annual management assessments of the effectiveness of our internal controls over financial reporting and a report by our Independent Auditors addressing these assessments. During the course of our testing we may identify deficiencies which we may not be able to remediate in time to meet the

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deadline imposed by the Sarbanes-Oxley Act for compliance with the requirements of Section 404. In addition, if we fail to maintain the adequacy of our internal controls, as such standards are modified, supplemented or amended from time to time, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal controls over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act. Failure to achieve and maintain an effective internal control environment could have a material adverse effect on our stock price.

### INFLATION

The results of operations and financial condition are presented based upon historical cost. While it is difficult to accurately measure the impact of inflation because of the nature of the estimates required, management believes that the effect of inflation, if any, on the Company's results of operations and financial condition has been minor; however, there can be no assurance that the Company's business will not be affected by inflation in the future.

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

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We are exposed to market risk from changes in interest rates, which may adversely affect our financial position, results of operations and cash flows. In seeking to minimize the risks from interest rate fluctuations, we manage exposures through our regular operating and financing activities and, when deemed appropriate, through the use of derivative financial instruments. We do not use financial instruments for trading or other speculative purposes and are not party to any leveraged financial instruments.

We are exposed to interest rate risk primarily through our borrowings under our Revolving Credit Facility. At October 30, 2004, direct borrowings aggregated \$185.0 million and an additional \$21.2 million of letters of credit were outstanding against the Revolving Credit Facility. The Revolving Credit Facility permits debt commitments up to \$350.0 million, matures on June 11, 2006 and generally bears interest at the bank's base rate of Eurodollar rate plus 2.0% to 2.75% based on the average excess availability during the previous quarter.

A hypothetical 100 basis point increase in interest rates on our variable rate debt outstanding for the nine months ended October 30, 2004, net of income taxes, would have an approximate \$0.7 million impact to our financial position, liquidity and results of operation.

### ITEM 4. CONTROLS AND PROCEDURES

The Company, under the supervision, and with the participation, of its management, including its Chief Executive Officer and Chief Financial Officer, performed an evaluation of the Company's disclosure controls and procedures, as contemplated by Securities Exchange Act Rule 13a-15. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded, as of the end of the period covered by this report, that such disclosures and procedures were effective.

No change was made in the Company's internal control over financial reporting during the Company's most recent fiscal quarter that has materially affected, or is reasonable likely to affect, the Company's internal control over financial reporting.

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## PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS. Not applicable

ITEM 2. CHANGES IN SECURITIES, USE OF PROCEEDS AND ISSUER PURCHASES OF EQUITY SECURITIES. Not applicable

ITEM 3. DEFAULTS UPON SENIOR SECURITIES. Not applicable

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS. None

ITEM 5. OTHER INFORMATION. Not applicable

ITEM 6. EXHIBITS

See Index to Exhibits on page 31.

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SIGNATURE

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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.

RETAIL VENTURES, INC.  
(Registrant)

Date: December 10, 2004

By: /s/ James A. McGrady

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James A. McGrady  
Executive Vice President, Chief  
Financial Officer, Treasurer and  
Secretary of Retail Ventures, Inc.

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### INDEX TO EXHIBITS

EXHIBIT NUMBER -----	DESCRIPTION -----
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a)/15d-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

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