VALUE CITY DEPARTMENT STORES INC /OH
Form 10-Q
December 17, 2001

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

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended November 3, 2001

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

VALUE CITY DEPARTMENT STORES, INC.
(Exact name of registrant as specified in its charter)

Ohio	31-1322832
(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)

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.

The number of shares outstanding of Common Stock, without par value, as of December 2, 2001 was 34,416,960.

TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements
Consolidated Balance Sheets at November 3, 2001 and February 3, 2001.....

Consolidated Statements of Operations for the three and nine months ended November 3, 2001 and October 28, 2000.....

Consolidated Statements of Cash Flows for the nine months ended November 3, 2001 and October 28, 2000 .....

Notes to the Consolidated Financial Statements.....

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

Item 3. Quantitative and Qualitative Disclosures about Market Risk.....

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.....

Item 2. Changes in Securities and Use of Proceeds.....

Item 3. Defaults Upon Senior Securities.....

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

Item 5. Other Information.....

Item 6. Exhibits and Reports on Form 8-K.....

Signature.....

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

VALUE CITY DEPARTMENT STORES, INC.
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AMOUNTS)
(UNAUDITED)

	NOVEMBER 3, 2001	FEBRUARY 3, 2001

ASSETS		
Current assets:		
Cash and equivalents	$ 25,342	$ 10,562
Accounts receivable, net	5,805	44,927
Receivables from affiliates	2,839	9,452
Inventories	493,125	393,577
Prepaid expenses and other assets	18,705	22,290
Deferred income taxes	74,165	51,732
Total current assets	619,981	532,540
Property and equipment, at cost:		
Furniture, fixtures and equipment	227,179	223,675
Leasehold improvements	185,817	176,318
Land and building	801	801
Capital leases	37,413	38,348
	451,210	439,142
Accumulated depreciation and amortization	(211,621)	(190,103)
Property and equipment, net	239,589	249,039
Investment in joint venture	5,840	8,292
Goodwill and tradenames, net	60,044	67,056
Other assets	48,304	51,082
Total assets	$ 973,758	$ 908,009
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 205,748	$ 180,736
Accounts payable to affiliates	19,804	13,655
Accrued expenses:		
Compensation	18,363	19,662
Taxes	36,774	31,255
Other	66,453	75,227
Current maturities of long-term obligations	623	603
Total current liabilities	347,765	321,138
Long-term obligations, net of current maturities	381,382	326,449
Deferred income taxes and other noncurrent liabilities	15,127	10,115
Commitments and contingencies	-	-
Shareholders' equity:		
Common shares, without par value; 80,000,000 authorized; issued, including treasury shares, 34,416,960 and 34,330,863 shares, respectively	146,526	145,659
Retained earnings	91,107	111,155
Deferred compensation expense, net	(4,948)	(6,448)
Treasury shares, at cost, 7,651 shares	(59)	(59)
Accumulated other comprehensive loss	(3,142)	-
Total shareholders' equity	229,484	250,307
Total liabilities and shareholders' equity	$ 973,758	$ 908,009

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

VALUE CITY DEPARTMENT STORES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)
(UNAUDITED)

	THREE MONTHS ENDED		
	NOVEMBER 3, 2001	OCTOBER 28, 2000	NOVEM 20
Net sales, excluding sales of licensed departments	$ 584,403	$ 559,820	$ 1,6
Cost of sales	(360,943)	(446,973)	(1,0
Gross profit	223,460	112,847	6
Selling, general and administrative expenses	(229,167)	(235,835)	(6
License fees from affiliates	2,592	1,599	
Other operating income	1,658	614	
Operating loss	(1,457)	(120,775)	
Interest expense, net	(7,406)	(7,873)	(
(Loss) gain on disposal of assets, net	(18)	(597)	
Loss before equity in loss of joint venture and benefit for income taxes	(8,881)	(129,245)	(
Equity in loss of joint venture	(1,242)	(551)	
Loss before benefit for income taxes	(10,123)	(129,796)	(
Benefit for income taxes	3,645	50,781	
Net loss	$ (6,478)	$ (79,015)	$ (
Basic and diluted loss per share	$ (0.19)	$ (2.35)	$

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

VALUE CITY DEPARTMENT STORES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	NINE MONTHS ENDED	
	NOVEMBER 3, 2001	OCTOBER 2 2000
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (20,048)	$ (78,892
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	38,972	32,854
Deferred income taxes and other noncurrent liabilities	(17,421)	(32,183
Equity in loss of joint venture	2,453	712
Loss (gain) on disposal of assets	13	(244
Change in working capital, assets and liabilities excluding effects of acquisition:		
Receivables	49,270	(48,154
Inventories	(99,548)	(64,224
Prepaid expenses and other assets	3,585	3,165
Accounts payable	31,172	59,983
Accrued expenses	(8,384)	10,809
Net cash used in operating activities	(19,936)	(116,174
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(22,588)	(55,052
Proceeds from sale of assets	131	359
Acquisition	-	(3,506
Other assets and lease acquisition costs	1,096	(14,392
Net cash used in investing activities	(21,361)	(72,591
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common shares	784	1,374
Net proceeds from issuance of debt	55,293	186,478
Net cash provided by financing activities	56,077	187,852
Net increase (decrease) in cash and equivalents	14,780	(913
Cash and equivalents, beginning of period	10,562	6,027
Cash and equivalents, end of period	$ 25,342	$ 5,114

Non-cash transactions:		
Issuance of common shares related to acquisition	-	$ 5,500
Contribution made in treasury shares	-	$ 1,080

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

VALUE CITY DEPARTMENT STORES, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE AND NINE MONTHS ENDED NOVEMBER 3, 2001 AND OCTOBER 28, 2000
(unaudited)

---

1. BASIS OF PRESENTATION

The accompanying consolidated financial statements include the accounts of Value City Department Stores, Inc. (VCDS) and its wholly owned subsidiaries. These entities are herein referred to collectively as the Company. The Company operates a chain of full-line, off-price department stores, principally under the name "Value City", a chain of off-price specialty retail stores under the name "Filene's Basement", as well as better-branded off-price shoe stores, under the name "DSW Shoe Warehouse." As of November 3, 2001 a total of 238 stores were open, including 118 Value City stores located principally in Ohio (23 stores) and Pennsylvania (19 stores) with the remaining stores dispersed throughout the Midwest, East and South, 100 DSW Shoe Warehouse stores (DSW) located throughout the United States, and 20 Filene's Basement stores ("Filene's") located principally in the New England states.

The accompanying consolidated financial statements reflect all adjustments consisting of only normal recurring adjustments, which are, in the opinion of management, necessary to present fairly the consolidated financial position and results of operations for the periods presented.

Certain previously reported balances have been reclassified to conform with the current period presentation.

2. SHAREHOLDERS' EQUITY

The Company entered into a $75.0 million Senior Subordinated Convertible Loan Agreement ("Senior Facility"), dated as of March 15, 2000. The Senior Facility bears interest at various rates, currently equal to 325 basis points over LIBOR. The interest rate increases an additional 50 basis points every 90 days after the first anniversary date. The Senior Facility is due in September 2003. In December 2000, pursuant to terms of the Senior Facility, Schottenstein Stores Corporation ("SSC"), direct owner of approximately 53.0% of the Company's common shares, purchased the outstanding balance under the same continuing terms. The terms, as amended, provide that if prior to November 5, 2001, the balance outstanding thereunder is not repaid from the proceeds of an equity offering or other subordinated debt acceptable to lenders under the Credit Agreement, then after that date SSC, as the lender, has the right to convert the debt into our common stock at a price equal to 95% of the 20-day average of high and low sales prices reported on the New York Stock Exchange at the time of conversion. The Company paid SSC a one time fee of 200 basis points, or

$1.5 million, in December 2000 as consideration for entering into a Put Agreement associated with the Senior Facility.

3. VALUATION ACCOUNTS

For the three and nine months ended November 3, 2001, charges to the inventory realignment reserve were $-0- and $43.7 million and charges to the accrued severance liability were $1.8 million and $3.4 million, respectively.

4. 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 our fiscal year.

SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, is effective for all fiscal years beginning after June 15, 2000. SFAS 133, as amended, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. Under SFAS 133, certain contracts that were not formerly considered derivatives may now meet the definition of a derivative. The Company's adoption of SFAS 133 effective February 4, 2001 did not have a significant impact on the financial position, results of operations, or cash flows of the Company.

The Company utilizes interest rate swap agreements to manage its interest rate risks on borrowings under its $300 million variable rate credit agreement. The Company does not hold or issue derivative financial instru-

ments for trading purposes. The Company does not have derivative financial instruments that are held or issued and accounted for as hedges of anticipated transactions.

In June 2001, the FASB issued SFAS 141, "Business Combinations", and SFAS No. 142, "Goodwill and Other Intangible Assets". The guidance in SFAS No. 141 supercedes APB 16 and is applicable to business combinations initiated after June 30, 2001. Upon adoption of SFAS No. 142, goodwill will cease to be amortized and will instead be subject to at least an annual assessment for impairment as set forth in the new standard. The Company is currently evaluating the Statement's impairment provisions and has not yet determined what effect, if any, they might have on the consolidated financial position and results of operations of the Company.

The Company has approximately $49.4 million in goodwill recorded in its consolidated balance sheet as of November 3, 2001. Amortization of the goodwill is generally not subject to taxes. Under the provisions of SFAS No. 142, goodwill will cease to be amortized for fiscal years beginning after December 15, 2001 (fiscal 2002) for the Company. The Company recorded

approximately $2.8 million in amortization expense related to goodwill for the nine months ended November 3, 2001. The Company intends to adopt SFAS No. 142 for the 2002 fiscal year.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. Under this Statement obligations that meet the definition of a liability will be recognized consistently with the retirement of the associated tangible long-lived assets. This Statement is effective for financial statements issued for fiscal years beginning after June 15, 2002.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This Statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Because SFAS No. 121 did not address the accounting for a segment of a business accounted for as a discontinued operation under Opinion 30, two accounting models existed for long-lived assets to be disposed of. The Board decided to establish a single accounting model, based on the framework established in Statement 121, for long-lived assets to be disposed of by sale. This Statement is effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years.

The Company is currently assessing the impact of SFAS No. 143 and 144. At this time, the Company has yet to determine the effect of these pronouncements on its results of operations and its financial position.

5. ACCUMULATED OTHER COMPREHENSIVE LOSS

Accumulated other comprehensive loss is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from nonowner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. The difference between net earnings and comprehensive earnings for the quarter ending November 3, 2001 relates to the change in the fair market value of interest rate swap agreements. Other comprehensive loss is $0.8 million and $3.1 million greater than net loss for the three and nine month periods ended November 3, 2001, respectively.

6. INVESTMENT IN JOINT VENTURE

Pursuant to the terms of the joint venture Operating Agreement, the Company in July 2001 informed Mazel Stores, Inc. of its intention to terminate the joint venture. The Company is in discussion with Mazel regarding the notice of termination.

7. SEGMENT REPORTING

The Company is managed in three operating segments: Value City Department Stores, DSW Shoe Warehouse stores and Filene's Basement stores, acquired effective March 17, 2000. 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 (loss) profit that is defined as income (loss) before interest expense and income taxes. Corporate assets include goodwill and loan costs related to the Shonac/DSW business acquisition.

THREE-MONTH PERIOD ENDED NOVEMBER 3, 2001 (IN THOUSANDS):

	VALUE CITY	DSW	FILENE'S	CORPOR
Net sales	$370,543	$136,219	$77,641	-
Operating (loss) profit	(4,649)	2,094	1,098	-
Capital expenditures	2,175	5,432	216	-
Depreciation and amortization	8,640	1,984	1,825	$1,2

THREE-MONTH PERIOD ENDED OCTOBER 28, 2000 (IN THOUSANDS):

	VALUE CITY	DSW	FILENE'S	CORPOR
Net sales	$375,525	$111,472	$72,823	-
Operating (loss) profit	(125,027)	5,906	(1,654)	-
Capital expenditures	14,298	3,891	2,383	-
Depreciation and amortization	8,884	785	3,272	$92

NINE-MONTH PERIOD ENDED NOVEMBER 3, 2001 (IN THOUSANDS):

	VALUE CITY	DSW	FILENE'S	CORPOR
Net sales	$1,052,042	$388,885	$210,067	-
Operating (loss) profit	(18,136)	5,810	5,401	-
Identifiable assets	661,101	168,060	118,101	$26,4
Capital expenditures	10,022	11,999	567	-
Depreciation and amortization	26,456	4,702	5,030	2,7

NINE-MONTH PERIOD ENDED OCTOBER 28, 2000 (IN THOUSANDS):

	VALUE CITY	DSW	FILENE'S	CORPOR
Net sales	$1,086,432	$300,998	$162,689	-
Operating (loss) profit	(127,050)	15,048	4,075	-
Identifiable assets	720,346	98,373	139,526	$28,8
Capital expenditures	42,473	9,720	2,859	-

Depreciation and amortization	23,570	2,191	4,272	2,8

8. NON-BINDING LETTER OF INTENT FOR THE SALE OF CERTAIN OPERATIONS

In August 2001, the Company entered into a non-binding letter of intent with SSC whereby SSC may acquire all of the outstanding stock or assets of Shonac Corporation, DSW Shoe Warehouse, Inc. and Filene's Basement, Inc. (the "Businesses") for an aggregate purchase price of $275 million, comprised of $200 million in cash and the assumption of the $75 million Senior Subordinated Convertible Loan held by SSC.

The non-binding letter of intent, as amended, allowed the Company to solicit third party preliminary non-binding indications of interest for one or more of the Businesses through September 2001 and to terminate the letter of intent or any definitive purchase agreement with SSC pursuant to a superior proposal for one or more of the Businesses through the later of October 25, 2001, or the execution of a definitive agreement with SSC, subject to the payment of a termination fee of $8.45 million.

As part of the consideration, in September 2001, SSC agreed to increase immediately the line of credit under the Value City Subordinated Credit Agreement from $50 million to $100 million under the same terms as set forth in the Subordinated Credit Agreement.

The Company is currently considering and evaluating various alternatives to the non-binding letter of intent.

9. SUBSEQUENT EVENT

In conjunction with the release of the third quarter results of operations on November 27, 2001, the Company announced the implementation of a corporate restructuring and workforce reduction program that will be concluded in the fourth quarter. This reduction, which is primarily at the Company's corporate offices, includes the immediate elimination of numerous positions, which will result in approximate annual savings of $8.5 million. In the fourth quarter, the Company will recognize a pretax charge related to severance and outplacement costs of approximately $3.5 million.

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

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		N
	November 3, 2001	October 28, 2000	November 3,
Net sales	100.0%	100.0%	100.0%
Gross profit	38.2	20.1	38.2
Selling, general and administrative expenses	(39.2)	(42.1)	(39.3)
License fees from affiliates and other operating income	0.7	0.4	0.7
Operating loss	(0.3)	(21.6)	(0.4)
Interest expense, net, and (loss) gain on disposals	(1.2)	(1.5)	(1.4)
Equity in loss of joint venture	(0.2)	(0.1)	(0.2)
Loss before income taxes	(1.7)	(23.2)	(2.0)
Benefit for income taxes	0.6	9.1	0.8
Net loss	(1.1)%	(14.1)%	(1.2)%

THREE MONTHS ENDED NOVEMBER 3, 2001 COMPARED TO THREE MONTHS ENDED OCTOBER 28, 2000

The Company's net sales increased $24.6 million, or 4.4%, from $559.8 million to $584.4 million. Fiscal 2001 includes sales of $77.6 million for Filene's Basement which was acquired in March 2000. The prior year third quarter sales for Filene's Basement were $72.8 million. Comparable stores sales for the quarter decreased 0.7%. By segment, comparable store sales were:

	2001	2000
Value City Department Stores	(0.1)%	(8.1)%
DSW	(2.4)%	18.3%
Filene's Basement	(1.2)%	N/A

TOTAL	(0.7)%	(4.3)%

Value City's non-apparel comparable sales increased 9.0% while apparel sales decreased 2.1%. Children's had a comparable store sales increase of 6.6% while men's and ladies decreased 2.7% and 5.8%, respectively.

DSW sales were $136.2 million, a 22.2% increase in the quarter, which includes a net increase of 25 stores.

Gross profit increased $110.7 million, from $112.8 million to $223.5 million, and increased as a percentage of sales from 20.1% to 38.2%. Last year's gross margin for the quarter included a $87.4 million charge for the realignment of excess inventory quantities. Gross profit, as a percent of sales by segment in the third quarter, were:

	2001	2000
Value City Department Stores	38.6%	12.4%
DSW	39.4%	37.5%
Filene's Basement	34.6%	33.5%
TOTAL	38.2%	20.2%

Selling, general and administrative expenses ("SG&A") decreased $6.6 million, from $235.8 million to $229.2 million, and decreased as a percentage of sales from 42.1% to 39.2%. This decrease is after an additional $6.9 million was incurred for new stores in operation at DSW and Filene's Basement. Fiscal 2001 third quarter SG&A includes an additional charge of $8.0 million across all segments for costs associated with employee health and welfare and employment taxes. In addition, there is a charge of $1.3 million for two store closings in Value City. SG&A as a percent of sales by segment in the third quarter were:

	2001	2000
Value City Department Stores	40.9%	44.8%
DSW	37.8%	37.0%
Filene's Basement	33.6%	36.3%
TOTAL	39.2%	42.1%

License fees from affiliates and other operating income increased $2.0 million, from $2.2 million to $4.2 million, and increased as a percentage of sales from 0.4% to 0.7%.

Operating loss decreased $119.3 million, from $120.8 million to $1.5 million, and decreased as a percentage of sales from 21.6% to 0.3%. It has been the Company's experience that new stores generally achieve profitability and contribute to net income after the first full year of operations. 15 department stores opened less than twelve months had an operating loss of $6.0 million for the current three-month period.

Interest expense, net of interest income, decreased $0.5 million, from $7.9 million to $7.4 million, and decreased as a percentage of sales from 1.5% to 1.2%. This decrease is attributable to higher weighted average borrowings offset by lower effective interest rates.

Equity in the loss of the joint venture represents the Company's fifty percent interest in a joint venture with Mazel Stores, Inc. and increased from a loss of $0.6 million to a loss of $1.2 million. Pursuant to terms of the Operating Agreement, the Company, on July 19, 2001, informed Mazel Stores, Inc. of its intention to terminate the joint venture. The Company is in discussion with Mazel regarding the notice of termination.

The effective tax rate for the three months ended November 3, 2001 is 36.0% versus 39.1% for the three months ended October 28, 2000. The Company expects its tax rate to trend lower during the remainder of the year, but it will ultimately depend on operating results for the fourth quarter and the relative impact of permanent differences between tax and book income.

NINE MONTHS ENDED NOVEMBER 3, 2001 COMPARED TO NINE MONTHS ENDED OCTOBER 28, 2000

The Company's net sales increased $100.9 million, or 6.5%, from $1,550.1 million to $1,651.0 million. Fiscal 2001 includes sales of $210.1 million for Filene's Basement which was acquired in March 2000. The prior year third quarter sales for Filene's Basement were $162.7 million. Comparable stores sales for the nine-month period decreased 3.0%. By segment comparable store sales were:

	2001	2000
Value City Department Stores	(4.6)%	(2.1)%
DSW	0.4%	21.7%
Filene's Basement	2.3%	N/A
TOTAL	(3.0)%	1.5%

Value City's non-apparel comparable sales increased 3.7% while apparel sales

decreased 7.0%. Children's had a comparable stores sales increase of 2.4% while the men's division was down 4.8% and the ladies division was down 12.3%.

DSW sales were $388.9 million, a 29.2% increase in the nine-month period, which includes a net increase of 25 stores.

Gross profit increased $140.1 million, from $490.9 million to $631.0 million, and increased as a percentage of sales from 31.7% to 38.2%. Last year's gross profit included a $87.4 million charge for the realignment of excess inventory quantities. Gross profit as a percent of sales by segment in the nine-month period quarter were:

	2001	2000
Value City Department Stores	38.5%	29.2%
DSW	39.1%	38.4%
Filene's Basement	35.3%	35.8%
TOTAL	38.2%	31.7%

Selling, general and administrative expenses ("SG&A") increased $41.9 million, from $607.1 million to $649.0 million, and increased as a percentage of sales from 39.2% to 39.3%. The percentage increase was due in part to the weak sales performance in the Value City department stores. $26.1 million of the increase in SG&A is associated with new DSW stores and Filene's Basement stores. New store pre-opening expenses for the nine-month period were $4.9 million less than last year. Fiscal 2001 SG&A includes an additional charge of $7.9 million across all segments for costs associated with employee health and welfare and employment taxes. In addition, there is a charge of $1.3 million for two store closings in Value City. SG&A as a percent of sales by segment in the nine-month period were:

	2001	2000
Value City Department Stores	41.1%	40.7%
DSW	37.7%	36.2%
Filene's Basement	33.5%	34.6%
TOTAL	39.3%	39.2%

License fees from affiliates and other operating income increased $2.8 million, from $8.3 million to $11.1 million, and increased from 0.5% to 0.7% as a percentage of sales.

Operating loss decreased $101.0 million, from $107.9 million to $6.9 million, and decreased as a percentage of sales from 7.0% to 0.4%. 15 department stores opened less than twelve months had an operating loss of $14.4 million for the current nine-month period, and 28 DSW stores opened less than twelve months had an operating profit of $2.4 million, including $4.4 million of pre-opening expenses. 3 Filene's Basement stores opened less than twelve months had an operating profit of $0.4 million, including $0.4 million of pre-opening expenses.

Interest expense, net of interest income, increased $2.7 million, from $21.2 million to $23.9 million, and remained at 1.4% of sales.

Equity in the loss of the joint venture represents the Company's fifty percent interest in a joint venture with Mazel Stores, Inc. The loss increased from $0.7 million to $2.5 million. Pursuant to terms of the Operating Agreement, the Company, on July 19, 2001 informed Mazel Stores, Inc. of its intention to terminate the joint venture. The Company is in discussion with Mazel regarding the notice of termination.

The effective tax rate for the nine months ended November 3, 2001 is 39.8% versus 39.1% for the nine months ended October 28, 2000. The Company expects its tax rate to trend lower during the remainder of the year, but it will ultimately depend on our operating results for the fourth quarter and the relative impact of our permanent differences between tax and book income.

LIQUIDITY AND CAPITAL RESOURCES

Net working capital was $272.2 million at November 3, 2001, compared to $251.9 million at October 28, 2000. Current ratios at those dates were each 1.78 and 1.72, respectively.

Net cash used in operating activities totaled $19.9 million and $116.2 million for the nine months ended November 3, 2001 and October 28, 2000, respectively. Earnings before interest, taxes, depreciation and amortization (EBITDA) for the nine months ended November 3, 2001 was $29.6 million.

Net cash used for capital expenditures was $22.6 million and $55.1 million for the nine months ended November 3, 2001 and October 28, 2000, respectively. During the nine months ended November 3, 2001, capital expenditures included $2.2 million for new stores, $7.1 million on existing stores and $13.3 million for relocation of office, warehousing and operations of our shoe business.

At November 3, 2001, the Company had a $300 million Amended and Restated Credit Agreement ("Credit Agreement"), dated as of March 15, 2000. The Credit Agreement, which expires on March 15, 2003, provides for revolving and overnight loans and issuance of letters of credit. Outstanding advances are secured by a lien on assets and are subject to a monthly borrowing base of eligible inventories and receivables, as defined. Terms of the Credit Agreement require compliance with certain restrictive covenants, including limitations on dividends, the incurrence of additional debt and financial ratio tests. Additionally, the Company has provided an unconditional guarantee of 50% of amounts outstanding on VCM, Ltd's ("VCM") $25.0 million revolving line of credit. At November 3, 2001, $18.0 million was available under the Credit Agreement. The Credit Agreement provides for various borrowing rates, currently equal to 275 basis points over LIBOR. The LIBOR rate on $75.0 million has been locked in at a fixed annual rate of 6.99% through March 2003 under a swap agreement.

To supplement operating cash requirements the Company has a $50.0 million

Subordinated Credit Agreement with Schottenstein Stores Corp. ("SSC Facility"). In September 2001, the SSC Facility was increased to $100 million. Outstanding advances under the SSC Facility are subordinated to the Credit Agreement and are subject to a junior lien on assets securing the Credit Agreement. At November 3, 2001, $35.0 million was outstanding. The interest rate and terms of the SSC Facility are generally the same as the Credit Agreement.

The Company has a $75.0 million Senior Subordinated Convertible Loan Agreement ("Senior Facility"), dated as of March 15, 2000. The Senior Facility bears interest at various rates, currently equal to 325 basis points over LIBOR. The interest rate increases an additional 50 basis points every 90 days after the first anniversary date. The Senior Facility is due in September 2003, and is due to Schottenstein Stores Corp. ("SSC") The terms, as amended, provide that if prior to November 5, 2001, the balance outstanding thereunder is not repaid from the proceeds of an equity offering or other subordinated debt acceptable to lenders under the Credit Agreement, then after that date SSC, as the lender, has the right to convert the debt into common stock at a price equal to 95% of the 20-day average of high and low sales prices reported on the New York Stock Exchange at the time of conversion. SSC was paid a one-time fee of 200 basis points, or $1.5 million, in December 2000 as consideration for entering into a Put Agreement associated with the Senior Facility.

In the first quarter of fiscal 2001 a major factor reduced our availability of credit and indicated that the Company needed to strengthen its liquidity and increase its credit availability from other sources. Future limitations of credit availability by factors and/or vendors will restrict the ability of the Company to obtain merchandise and services and may impair operating results. Although operating results in the first nine fiscal months of 2001 were below plan, management believes that cash generated by operations, along with the available proceeds from our Credit Agreement, SSC Facility and other sources of financing will be sufficient to meet our obligations for working capital,

capital expenditures, and debt service requirements. However, there is no assurance that the Company will be able to meet its projections. Further, there is no assurance that extended financing will be available to the Company in the future if it fails to meet its projections.

In August 2001, the Company entered into a non-binding letter of intent with SSC whereby SSC may acquire all of the outstanding stock or assets of Shonac Corporation, DSW Shoe Warehouse, Inc. and Filene's Basement, Inc. (the "Businesses") for an aggregate purchase price of $275 million, comprised of $200 million in cash and the assumption of the $75 million Senior Subordinated Convertible Loan held by SSC.

The non-binding letter of intent, as amended, allowed the Company to solicit third party preliminary non-binding indications of interest for one or more of the Businesses through September 2001 and to terminate the letter of intent or any definitive purchase agreement with SSC pursuant to a superior proposal for one or more of the Businesses through the later of October 25, 2001, or the execution of a definitive agreement with SSC, subject to the payment of a termination fee of $8.45 million.

As part of the consideration, in September 2001 SSC agreed to increase immediately the line of credit under the Value City Subordinated Credit Agreement from $50 million to $100 million under the same terms as set forth in the Subordinated Credit Agreement.

The Company is currently considering and evaluating various alternatives to the non-binding letter of intent.

SUBSEQUENT EVENT

In conjunction with the release of the third quarter results of operations on November 27, 2001, the Company announced the implementation of a corporate restructuring and workforce reduction program that will be completed in the fourth quarter. This reduction, which is primarily at the Company's corporate offices, includes the immediate elimination of numerous positions, which will result in approximate annual savings of $8.5 million. In the fourth quarter, the Company will recognize a pretax charge related to severance and outplacement costs of approximately $3.5 million.

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 our fiscal year.

Statement of Financial Accounting Standards (SFAS) No. 133, Accounting for Derivative Instruments and Hedging Activities, is effective for all fiscal years beginning after June 15, 2000. SFAS 133, as amended, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. Under SFAS 133, certain contracts that were not formerly considered derivatives may now meet the definition of a derivative. The Company's adoption of SFAS 133 effective February 4, 2001 did not have a significant impact on the financial position, results of operations, or cash flows of the Company.

The Company utilizes interest rate swap agreements to manage its interest rate risks on borrowings under its $300 million variable rate credit agreement. The Company does not hold or issue derivative financial instruments for trading purposes. The Company does not have derivative financial instruments that are held or issued and accounted for as hedges of anticipated transactions.

In July 2001, the FASB issued SFAS 141, "Business Combinations", and SFAS No. 142, "Goodwill and Other Intangible Assets". The guidance in SFAS No. 141 supercedes APB 16 and is applicable to business combinations initiated after June 30, 2001. Upon adoption of SFAS No. 142, goodwill will cease to be amortized and will instead be subject to periodic impairment reviews as set forth in the new standard. The Company is currently evaluating the Statement's impairment provisions and has not yet determined what effect, if any, they might have on the consolidated financial position and results of operations of the Company.

The Company has approximately $49.4 million in goodwill recorded in its consolidated balance sheet as of November 3, 2001. Amortization of the goodwill is generally not subject to taxes. Under the provisions of SFAS No. 142,

goodwill will cease to be amortized for fiscal years beginning after December 15, 2001 (fiscal 2002) for the Company). The Company recorded approximately $2.8 million in amortization expense related to goodwill for the nine months ended November 3, 2001. The Company intends to adopt SFAS No. 142 for the 2002 fiscal year.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 addressed financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. Under this Statement obligations that meet the definition of a liability will be recognized consistently with the retirement of the associated tangible long-lived assets. This Statement is effective for financial statements issued for fiscal years beginning after June 15, 2002.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This Statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Because SFAS No. 121 did not address the accounting for a segment of a business accounted for as a discontinued operation under Opinion 30, two accounting models existed for long-lived assets to be disposed of. The Board decided to establish a single accounting model, based on the framework established in Statement 121, for long-lived assets to be disposed of by sale. This Statement is effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years.

The Company is currently assessing the impact of SFAS No. 143 and 144. At this time, the Company has yet to determine the effect of these pronouncements on its results of operations and its financial position.

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 the effect of inflation, if any, on the results of operations and financial condition has been minor.

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, other filings with the Securities and Exchange Commission 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 and in the future could affect our financial performance and actual results and could cause actual results for 2001 and beyond to differ materially from those expressed or implied in any such forward-looking statements: decline in demand for our merchandise, our ability to attain our fiscal 2001 business plan, expected cash from operations, vendor and their factor relations, flow of merchandise, compliance with the credit agreement, 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, consumer preferences and overall economic conditions, the impact of competition and pricing, changes in weather patterns, changes in existing or potential duties, tariffs or quotas, paper and printing costs, and the ability to hire and train associates.

Historically, our operations have been seasonal, with a disproportionate amount of sales and a majority of net income occurring in the back-to-school and Christmas selling seasons. As a result of this seasonality, any factors negatively affecting us during this period, 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.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's primary market risk results from fluctuations in interest rates. The Company is exposed to interest rate risk through borrowings under its revolving credit agreement, which permits borrowings up to $300 million. To minimize the effect of interest rate fluctuations, the Company has entered into a $75 million interest rate swap arrangement. Under this agreement, the Company pays a fixed rate of interest on a portion of the outstanding balance.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS. Not applicable

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS. Not applicable

ITEM 3. DEFAULTS UPON SENIOR SECURITIES. Not applicable

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS. Not applicable

ITEM 5. OTHER INFORMATION. Not applicable

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

Part A Exhibits. Not applicable

Part B Reports on Form 8-K

Forms 8-K/A were filed on October 24, 2001 and on September 19, 2001 relating to Item 5 - "Other Items".

SIGNATURE

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.

VALUE CITY DEPARTMENT STORES, INC.

(Registrant)

Date: December 17, 2001 By: /s/ James A. McGrady

James A. McGrady,
Chief Financial Officer and Treasurer