CIRCUIT CITY STORES INC
Form 10-Q
October 15, 2002

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 August 31, 2002

OR

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

Commission File Number 1-5767

CIRCUIT CITY STORES, INC.
(Exact Name of Registrant as Specified in its Charter)

VIRGINIA	54-0493875
(State of Incorporation)	(I.R.S. Employer Identification No.)

9950 MAYLAND DRIVE, RICHMOND, VIRGINIA 23233
(Address of Principal Executive Offices and Zip Code)

(804) 527-4000
(Registrant's Telephone Number, Including Area Code)

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

Yes X No

Indicate the number of shares outstanding of each of the Registrant's classes of common stock, as of the latest practicable date.

Class	Outstandi
Circuit City Stores, Inc. - Circuit City Group Common Stock, par value $0.50	
Circuit City Stores, Inc. - CarMax Group Common Stock, par value $0.50	

An Index is included on Page 2 and a separate Index for Exhibits is included on Page 73.

(1) On October 1, 2002, the Registrant had 210.1 million outstanding shares of Circuit City common stock. Also on October 1, 2002, each share of CarMax Group Common Stock was redeemed in exchange for one share of CarMax, Inc. common

stock; each share of Circuit City Group Common Stock received as a dividend 0.313879 of a share of CarMax, Inc. common stock; CarMax, Inc. became an independent, separately traded public company; and Circuit City Group Common Stock was renamed Circuit City common stock. See Note 13 to the Company's consolidated financial statements.

CIRCUIT CITY STORES, INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

CIRCUIT CITY STORES, INC. AND SUBSIDIARIES
Consolidated Balance Sheets

(Amounts in thousands except share data)

	Aug. 31, 2002
	(Unaudited)
ASSETS	
Current assets:	
Cash and cash equivalents	$ 846,796
Accounts receivable, net	251,831
Retained interests in securitized receivables	598,934
Inventory	2,018,209
Prepaid expenses and other current assets	43,583
Total current assets	3,759,353
Property and equipment, net	859,868
Deferred income taxes	10,464
Other assets	29,464
TOTAL ASSETS	$ 4,659,149
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 1,274,904
Accrued expenses and other current liabilities	164,529
Accrued income taxes	-
Deferred income taxes	136,204
Short-term debt	5,206
Current installments of long-term debt	2,132
Total current liabilities	1,582,975
Long-term debt, excluding current installments	111,996
Other liabilities	158,315
Deferred income taxes	-
TOTAL LIABILITIES	1,853,286
Stockholders' equity:	
Circuit City Group Common Stock, $0.50 par value; 350,000,000 shares authorized; 210,037,018 shares issued and outstanding as of August 31, 2002	105,019
CarMax Group Common Stock, $0.50 par value; 175,000,000 shares authorized; 37,082,275 shares issued and outstanding as of August 31, 2002	18,541
Capital in excess of par value	839,567
Retained earnings	1,842,736
TOTAL STOCKHOLDERS' EQUITY	2,805,863
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 4,659,149

See accompanying notes to consolidated financial statements.

CIRCUIT CITY STORES, INC. AND SUBSIDIARIES
Consolidated Statements of Earnings (Unaudited)
(Amounts in thousands except per share data)

	Three Months Ended August 31, 2002	Three Months Ended August 31, 2001	
Net sales and operating revenues	$ 3,297,287	$ 2,962,120	$
Cost of sales, buying and warehousing	2,647,186	2,357,050	
Gross profit	650,101	605,070	
Selling, general and administrative expenses (net of finance income of $52,678 for the three months ended August 31, 2002, $47,583 for the three months ended August 31, 2001, $97,174 for the six months ended August 31, 2002, and $96,638 for the six months ended August 31, 2001)	614,215	579,465	
Interest expense	1,507	1,654	
Total expenses	615,722	581,119	
Earnings before income taxes	34,379	23,951	
Provision for income taxes	13,850	9,101	
Net earnings	$ 20,529	$ 14,850	$
Net earnings attributed to:			
Circuit City Group Common Stock	$ 9,113	$ 6,822	$
CarMax Group Common Stock	11,416	8,028	
	$ 20,529	$ 14,850	$
Weighted average common shares:			
Circuit City Group:			
Basic	207,202	205,329	
Diluted	209,094	206,924	
CarMax Group:			
Basic	37,065	29,877	
Diluted	38,618	32,025	
Net earnings per share attributed to:			
Circuit City Group:			
Basic	$ 0.04	$ 0.03	$

Diluted	$ 0.04	$ 0.03	$
CarMax Group:			
Basic	$ 0.31	$ 0.27	$
Diluted	$ 0.30	$ 0.25	$
Dividends paid per share:			
Circuit City Group Common Stock	$ 0.0175	$ 0.0175	$
CarMax Group Common Stock	$ -	$ -	$

See accompanying notes to consolidated financial statements.

CIRCUIT CITY STORES, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows (Unaudited)
(Amounts in thousands)

	Six Mon Augu 2002
Operating Activities:	
Net earnings	$ 48,511
Adjustments to reconcile net earnings to net cash (used in) provided by operating activities of continuing operations:	
Depreciation and amortization	84,970
Amortization of restricted stock awards	9,892
Loss (gain) on disposition of property and equipment	5,343
Provision for deferred income taxes	(12,854)
Changes in operating assets and liabilities:	
Increase in accounts receivable, net and retained interests in securitized receivables	(126,689)
(Increase) decrease in inventory	(384,882)
(Increase) decrease in prepaid expenses and other current assets	(2,272)
Decrease (increase) in other assets	3,027
Increase in accounts payable, accrued expenses and other current liabilities and accrued income taxes	62,113
Increase in other liabilities	9,046
Net cash (used in) provided by operating activities of continuing operations	(303,795)
Investing Activities:	
Purchases of property and equipment	(111,644)
Proceeds from sales of property and equipment, net	15,647
Net cash (used in) provided by investing activities of continuing operations	(95,997)

Financing Activities:	
(Payments on) issuance of short-term debt, net	(5,031)
Issuance of long-term debt	100,000
Payments on long-term debt	(102,009)
Issuances of Circuit City Group Common Stock, net	8,682
Issuances of CarMax Group Common Stock, net	744
Proceeds from CarMax Group stock offering, net	-
Dividends paid on Circuit City Group Common Stock	(7,330)
Net cash (used in) provided by financing activities of continuing operations	(4,944)
Cash used in discontinued operations	-
(Decrease) increase in cash and cash equivalents	(404,736)
Cash and cash equivalents at beginning of year	1,251,532
Cash and cash equivalents at end of period	$ 846,796

See accompanying notes to consolidated financial statements.

CIRCUIT CITY STORES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

At August 31, 2002, and August 31, 2001, the common stock of Circuit City Stores, Inc. consisted of two common stock series intended to reflect the performance of the Company's two businesses. The Circuit City Group Common Stock was intended to reflect the performance of the Circuit City stores and related operations and the shares of CarMax Group Common Stock reserved for the Circuit City Group or for issuance to holders of Circuit City Group Common Stock. The CarMax Group Common Stock was intended to reflect the performance of the CarMax stores and related operations. The reserved CarMax Group shares were not outstanding CarMax Group Common Stock. Therefore, net earnings attributed to the reserved CarMax Group shares were included in the net earnings and earnings per share attributed to the Circuit City Group Common Stock.

As of August 31, 2002, 65,923,200 shares of CarMax Group Common Stock were reserved for the Circuit City Group or for issuance to holders of Circuit City Group Common Stock. Excluding shares reserved for CarMax employee stock incentive plans, the reserved CarMax Group shares represented 64.0 percent of the total outstanding and reserved shares of CarMax Group Common Stock at August 31, 2002; 64.1 percent at February 28, 2002; and 64.6 percent at August 31, 2001. The terms of each series of common stock are discussed in detail in the Company's previous filings with the Securities and Exchange Commission.

The Company's consolidated financial statements included herein should be read in conjunction with the financial statements of each Group and the Company's SEC filings.

The separation of the CarMax Group from Circuit City Stores, Inc. was effective as of October 1, 2002. See Note 13 for an additional discussion of the separation.

2. Accounting Policies

The consolidated financial statements of the Company conform to accounting principles generally accepted in the United States of America. The interim period financial statements are unaudited; however, in the opinion of management, all adjustments, which consist only of normal, recurring adjustments, necessary for a fair presentation of the interim consolidated financial statements have been included. The fiscal year-end balance sheet data was derived from the audited financial statements included in the Company's fiscal 2002 Annual Report on Form 10-K/A.

3. Net Earnings per Share

Reconciliations of the numerator and denominator of the basic and diluted net earnings per share calculations are presented below.

(Amounts in thousands except per share data)	Three Months Ended August 31, 2002	2001
Circuit City Group:		
Weighted average common shares	207,202	205,329
Dilutive potential common shares:		
Options	746	824
Restricted stock	1,146	771
Weighted average common shares and dilutive potential common shares	209,094	206,924
Net earnings available to common shareholders	$ 9,113	$ 6,822
Basic net earnings per share	$ 0.04	$ 0.03
Diluted net earnings per share	$ 0.04	$ 0.03
CarMax Group:		
Weighted average common shares	37,065	29,877
Dilutive potential common shares:		
Options	1,548	2,121
Restricted stock	5	27
Weighted average common shares and dilutive potential common shares	38,618	32,025
Net earnings available to common shareholders	$ 11,416	$ 8,028
Basic net earnings per share	$ 0.31	$ 0.27
Diluted net earnings per share	$ 0.30	$ 0.25

In a public offering completed during the second quarter of fiscal 2002, Circuit City Stores, Inc. sold 9,516,800 CarMax Group shares that had previously been reserved for the Circuit City Group. Because both the earnings allocation and the outstanding CarMax shares were adjusted to reflect the impact of the sale, net earnings per CarMax Group share were not diluted by the sale. With the impact of the offering, 64.0 percent of the CarMax Group's fiscal 2003 second quarter and first half earnings were allocated to the Circuit City Group. Last fiscal year, 70.7 percent of the CarMax Group's second quarter earnings and 72.5 percent of the CarMax Group's first half earnings were allocated to the Circuit City Group.

Certain options were outstanding and not included in the computation of diluted net earnings per share because the options' exercise prices were greater than the average market price of the shares. For the three-month period ended August 31, 2002, options to purchase 6,846,704 shares of Circuit City Group Common Stock at prices ranging from $17.25 to $40.81 per share were outstanding and not included in the calculation. For the three-month period ended August 31, 2001, options to purchase 6,798,996 shares of Circuit City Group Common Stock at prices ranging from $17.25 to $43.03 per share were outstanding and not included in the calculation.

For the three-month period ended August 31, 2002, options to purchase 1,030,207 shares of CarMax Group Common Stock at prices ranging from $20.00 to $26.83 per share were outstanding and not included in the calculation. For the three-month period ended August 31, 2001, options to purchase 7,899 shares of CarMax Group Common Stock at $16.31 per share were outstanding and not included in the calculation.

4. Debt

On May 17, 2002, CarMax entered into a $200 million credit agreement secured by vehicle inventory. The credit agreement includes a $100 million revolving loan commitment and a $100 million term loan. Principal is due in full at maturity with interest payable monthly at a LIBOR-based rate. The agreement is scheduled to terminate in May 2004. The termination date of the agreement will be automatically extended one year on May 17, 2003, and on each May 17 thereafter unless CarMax or any lender elects, prior to the next extension date, not to extend the agreement. The value of CarMax's eligible motor vehicle inventory must be at least 150 percent of the aggregate principal amount outstanding under the credit facility on any date. As of August 31, 2002, the amount outstanding under this credit agreement was $105.2 million. Under this agreement, CarMax must meet financial covenants relating to minimum current ratio, maximum total liabilities to tangible net worth ratio and minimum fixed charge coverage ratio. CarMax was in compliance with these covenants at August 31, 2002.

5. Supplemental Financial Statement Information

For the three- and six-month periods ended August 31, 2002 and 2001, pretax finance operation income, which is recorded as a reduction to selling, general and administrative expenses, was as follows:

	Three Months Ended August 31,		Six Mont Augus
(Amounts in millions)	2002	2001	2002
Circuit City Group:			
Securitization income.......................	$ 55.5	$ 55.6	$ 106.0
Payroll and fringe benefit expenses..........	10.6	10.2	21.3
Other direct expenses.......................	18.9	20.6	38.3

Finance operation income	26.0	24.8	46.4
CarMax Group:			
Securitization income	25.8	21.4	49.1
Payroll and fringe benefit expenses	1.7	1.3	3.4
Other direct expenses	2.0	1.5	3.7
Finance operation income	22.1	18.6	42.0
Third-party financing fees	4.6	4.2	8.8
Total finance income	26.7	22.8	50.8
Circuit City Stores, Inc.:			
Consolidated finance income	$ 52.7	$ 47.6	$ 97.2

For both the Circuit City Group and the CarMax Group, the finance operation income does not include any allocation of indirect costs or income. The Company presents this information on a direct basis to avoid making arbitrary decisions regarding the periodic indirect benefit or costs that could be attributed to this operation. Examples of indirect costs not included are corporate expenses such as human resources, administrative services, marketing, information systems, accounting, legal, treasury and executive payroll, as well as retail store expenses.

6. Securitizations

(A) Credit Card Securitizations:

Circuit City enters into securitization transactions to finance consumer revolving credit card receivables originated by its finance operation. In accordance with the isolation provisions of Statement of Financial Accounting Standards No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," special purpose subsidiaries were created for the sole purpose of facilitating these securitization transactions. Credit card receivables are sold to the special purpose subsidiaries, which, in turn, transfer these receivables to securitization master trusts. For transfers of receivables that qualify as sales, Circuit City recognizes gains or losses as a component of the finance operation's profits, which are

recorded as a reduction to selling, general and administrative expenses. See Note 5. Private-label and co-branded Visa credit card receivables are securitized through one master trust, and MasterCard and Visa credit card, referred to as bankcard, receivables are securitized through a second master trust. Each master trust periodically issues securities backed by the receivables in that master trust. Each master trust has issued multiple series of term asset-backed securities having fixed initial principal amounts and, in addition, each master trust has issued a series of variable funding asset-backed securities having a variable principal amount. Investors in the variable funding asset-backed securities are generally entitled to receive monthly interest payments and have committed to acquire additional variable funding securities up to a stated amount until a stated commitment termination date. In these securitizations, Circuit City's finance operation continues to service the securitized receivables for a fee and the special purpose subsidiaries retain an undivided interest in the transferred receivables and hold various subordinated asset-backed securities that serve as credit enhancements for the asset-backed securities held by outside investors. Neither master trust agreement provides for recourse to the Company for credit losses on the securitized receivables. Circuit City employs a risk-based pricing strategy that increases the stated annual percentage rate for accounts that have a higher predicted risk of default. Under certain of the securitization programs, Circuit City must meet financial guidelines relating to minimum tangible net worth, debt to net worth and the current ratio in order to transfer additional receivables. The securitized receivables must meet performance levels relating to portfolio yield, default rates, principal payment rates and delinquency rates. Circuit City was in compliance with these guidelines and performance levels at August 31, 2002, and February 28, 2002.

The total principal amount of credit card receivables managed was $2.79 billion at August 31, 2002, and $2.85 billion at February 28, 2002. Of the total principal amounts managed, the principal amount of receivables securitized was $2.75 billion at August 31, 2002, and $2.80 billion at February 28, 2002, and the principal amount of receivables held for sale was $43.1 million at August 31, 2002, and $49.2 million at February 28, 2002. During the second quarter of fiscal 2003, the Company completed a $470.0 million bankcard receivable securitization transaction, and during the first quarter of fiscal 2003, the Company completed a $300 million private-label credit card receivable securitization transaction. No new public securitization transactions were completed in the first half of fiscal 2002. At August 31, 2002, the unused capacity of the private-label variable funding program was $248.5 million and the unused capacity of the bankcard variable funding program was $94.5 million. At February 28, 2002, the unused capacity of the private-label variable funding program was $22.9 million and the unused capacity of the bankcard variable funding program was $496.5 million.

The aggregate amount of receivables that were 31 days or more delinquent was $184.4 million at August 31, 2002, and $198.4 million at February 28, 2002. The principal amount of defaults net of recoveries totaled $63.0 million for the quarter ended August 31, 2002, and $62.3 million for the quarter ended August 31, 2001. The principal amount of defaults net of recoveries totaled $133.8 million for the six months ended August 31, 2002, and $131.9 million for the six months ended August 31, 2001.

Circuit City receives annual servicing fees approximating 2 percent of the outstanding principal balance of the credit card receivables and retains the rights to future cash flows available after the investors in the asset-backed securities have received the return for which they contracted. The servicing fees specified in the credit card securitization agreements adequately compensate the finance operation for servicing the securitized receivables. Accordingly, no servicing asset or liability has been recorded.

The table below summarizes certain cash flows received from and paid to the credit card securitization trusts.

	Three Months Ended August 31,	
(Amounts in millions)	2002	2001
Proceeds from new securitizations........................	$ 381.8	$ 204.4
Proceeds from collections reinvested in previous credit card securitizations.................	$ 361.9	$ 457.5
Servicing fees received.................................	$ 12.4	$ 12.6

Other cash flows received on retained interests*..........	$ 43.5	$ 49.7

*This amount represents cash flows received from retained interests by the transferor other than servicing fees, including cash flows from interest-only strips and cash above the minimum required level in cash collateral accounts.

When determining the fair value of retained interests, Circuit City estimates future cash flows using management's projections of key factors, such as finance charge income, default rates, payment rates, forward interest rate curves and discount rates appropriate for the type of asset and risk.

The amount by which the estimated future finance income from securitized credit card receivables exceeds the sum of the contractually specified investor returns and servicing fees, referred to as interest-only strips, is carried at fair value and amounted to $126.9 million at August 31, 2002, and $131.9 million at February 28, 2002. These amounts are included in retained interests in securitized receivables on the consolidated balance sheets. The value of the interest-only strip increased $0.1 million in the three months ended August 31, 2002 and decreased $2.4 million in the three months ended August 31, 2001. The value of the interest-only strip decreased $5.0 million in the six months ended August 31, 2002 and increased $1.4 million in the six months ended August 31, 2001.

At August 31, 2002, the fair value of retained interests was $467.8 million, with a weighted-average life ranging from 0.2 years to 4.9 years. At February 28, 2002, the fair value of retained interests was $394.5 million, with a weighted-average life ranging from 0.2 years to 1.8 years. The following table shows the key economic assumptions used in measuring the fair value of retained interests at August 31, 2002, and a sensitivity analysis showing the hypothetical effect on the fair value of those interests when there are unfavorable variations from the assumptions used. Key economic assumptions at August 31, 2002, are not materially different from assumptions used to measure the fair value of retained interests at the time of securitization. These sensitivities are hypothetical and should be used with caution. In this table, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption; in actual circumstances, changes in one factor may result in changes in another, which might magnify or counteract the sensitivities.

(Dollar amounts in millions)	Assumptions Used	Impact on Fair Value of 10% Adverse Change
Monthly payment rate..................	6.6%-10.2%	$ 9.0
Annual default rate...................	7.2%-17.7%	$ 23.0
Annual discount rate..................	8.3%-15.0%	$ 4.3

(B) Automobile Loan Securitizations:

CarMax enters into securitization transactions to finance automobile loan receivables originated by its finance operation. CarMax's finance operation sells its automobile loan receivables to a special purpose subsidiary, which, in turn, transfers those receivables to a group of third-party investors. For transfers of receivables that qualify as sales, CarMax recognizes gains or losses as a component of the finance operation's profits, which are recorded as a reduction to selling, general and administrative expenses. See Note 5. The special purpose subsidiary retains a subordinated interest in the transferred receivables. CarMax's finance operation

continues to service securitized receivables for a fee. The unused capacity of this program was $361.0 million at August 31, 2002, and $211.0 million at February 28, 2002. The automobile loan securitization agreements do not provide for recourse to the Company for credit losses on the securitized receivables. CarMax employs a risk-based pricing strategy that increases the stated annual percentage rate for accounts that have a higher predicted risk of default. Under certain of these securitization programs, CarMax must meet financial guidelines relating to maximum total liabilities to tangible net worth ratio, minimum debt to net worth, minimum tangible net worth to managed assets, minimum current ratio, minimum cash balance or borrowing capacity and minimum fixed charge coverage ratio. The securitized receivables must meet performance levels relating to portfolio yield, default rates and delinquency rates. CarMax was in compliance with these guidelines and performance levels at August 31, 2002, and February 28, 2002.

The total principal amount of automobile loan receivables managed was $1.75 billion at August 31, 2002, and $1.55 billion at February 28, 2002. Of the total principal amounts managed, the principal amount of automobile loan receivables securitized was $1.72 billion at August 31, 2002, and $1.54 billion at February 28, 2002, and the principal amount of automobile loan receivables held for sale or investment was $25.1 million at August 31, 2002, and $13.9 million at February 28, 2002. During the second quarter of fiscal 2003, CarMax completed an asset securitization transaction totaling $512.6 million of automobile loan receivables. No new public securitization transactions were completed in the first half of fiscal 2002.

The aggregate principal amount of managed automobile loans that were 31 days or more delinquent was $26.1 million at August 31, 2002, and $22.3 million at February 28, 2002, and $18.8 million at August 31, 2001. The principal amount of defaults net of recoveries on automobile loan receivables managed totaled $4.1 million for the quarter ended August 31, 2002, and $2.6 million for the quarter ended August 31, 2001. The principal amount of defaults net of recoveries on automobile loan receivables managed totaled $7.3 million for the six months ended August 31, 2002, and $4.5 million for the six months ended August 31, 2001.

CarMax receives annual servicing fees approximating 1 percent of the outstanding principal balance of the securitized automobile loan receivables and retains the rights to future cash flows available after the investors in the asset-backed securities have received the return for which they contracted. The servicing fees specified in the automobile loan securitization agreements adequately compensate the finance operation for servicing the securitized receivables. Accordingly, no servicing asset or liability has been recorded.

The table below summarizes certain cash flows received from and paid to the automobile loan securitization trusts.

(Amounts in millions)	Three Months Ended August 31, 2002	Three Months Ended August 31, 2001
Proceeds from new securitizations........................	$ 266.6	$ 181.0
Proceeds from collections reinvested in previous automobile loan securitizations.............	$ 124.1	$ 126.9

Servicing fees received..................................	$ 3.9	$ 3.5
Other cash flows received on retained interests*...........	$ 24.1	$ 16.5

*This amount represents cash flows received from retained interests by the transferor other than servicing fees, including cash flows from interest-only strips and cash above the minimum required level in cash collateral accounts.

When determining the fair value of retained interests, CarMax estimates future cash flows using management's projections of key factors, such as finance charge income, default rates, payment rates and discount rates appropriate for the type of asset and risk.

The amount by which the estimated future finance income from securitized automobile loan receivables exceeds the sum of the contractually specified investor returns and servicing fees, referred to as interest-only strips, is carried at fair value and amounted to $84.2 million at August 31, 2002, and $74.3 million at February 28, 2002. These amounts are included in retained interests in securitized receivables on the consolidated

balance sheets. Gains of $18.1 million on sales of automobile loan receivables were recorded for the three months ended August 31, 2002; gains of $14.7 million on sales of automobile loan receivables were recorded for the three months ended August 31, 2001. Gains of $33.7 million on sales of automobile loan receivables were recorded for the six months ended August 31, 2002; gains of $27.8 million on sales of automobile loan receivables were recorded for the six months ended August 31, 2001.

At August 31, 2002, the fair value of retained interests was $131.1 million, with a weighted-average life of 1.6 years. At February 28, 2002, the fair value of retained interests was $120.7 million, with a weighted-average life of 1.6 years. The following table shows the key economic assumptions used in measuring the fair value of retained interests at August 31, 2002, and a sensitivity analysis showing the hypothetical effect on the fair value of those interests when there are unfavorable variations from the assumptions used. Key economic assumptions at August 31, 2002, are not materially different from assumptions used to measure the fair value of retained interests at the time of securitization. These sensitivities are hypothetical and should be used with caution. In this table, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption; in actual circumstances, changes in one factor may result in changes in another, which might magnify or counteract the sensitivities.

(Dollar amounts in millions)	Assumptions Used	Impact on Fair Value of 10% Adverse Change	Impact on Fair Value of 20% Adverse Change
Prepayment rate.................	1.5%-1.6%	$ 4.4	$8.8
Annual default rate.............	1.0%-1.2%	$ 2.3	$4.5
Annual discount rate............	12.0%	$ 1.6	$3.1

7. Financial Derivatives

On behalf of Circuit City, the Company enters into interest rate cap agreements to meet the requirements of the credit card receivable securitization transactions. During the first quarter of fiscal 2003 and in conjunction with the private-label public securitization, the Company purchased and sold three offsetting interest rate caps with an aggregate initial notional amount of $280.5 million. The total notional amount of interest rate caps outstanding was $935.4 million at August 31, 2002, and $654.9 million at February 28, 2002. Purchased interest rate caps were included in net accounts receivable and had a fair value of $7.0 million as of August 31, 2002, and $2.4 million as of February 28, 2002. Written interest rate caps were included in accounts payable and had a fair value of $7.0 million as of August 31, 2002, and $2.4 million as of February 28, 2002.

On behalf of CarMax, the Company enters into amortizing swaps relating to automobile loan receivable securitizations to convert variable-rate financing costs to fixed-rate obligations to better match funding costs to the receivables being securitized. During the second quarter of fiscal 2003, the Company entered into three 40-month amortizing interest rate swaps with an initial notional amount totaling approximately $226.0 million. The current amortized notional amount of all outstanding swaps related to the automobile loan receivable securitizations was approximately $388.4 million at August 31, 2002, and $413.3 million at February 28, 2002. At August 31, 2002, the fair value of swaps totaled a net liability of $4.6 million and were included in accounts payable. At February 28, 2002, the fair value of swaps totaled a net liability of $841,000 and were included in accounts payable.

The market and credit risks associated with interest rate caps and interest rate swaps are similar to those relating to other types of financial instruments. Market risk is the exposure created by potential fluctuations in interest rates and is directly related to the product type, agreement terms and transaction volume. The Company has entered into offsetting interest rate cap positions and, therefore, does not anticipate significant market risk arising from interest rate caps. The Company does not anticipate significant market risk from swaps as they are used on a monthly basis to match funding costs to the use of the funding. Credit risk is the exposure to nonperformance of another party to an agreement. The Company mitigates credit risk by dealing with highly rated bank counterparties.

8. Appliance Exit Costs

In the second quarter of fiscal 2001, the Company began to exit the major appliance category and expand its selection of key consumer electronics and home office products in all Circuit City Superstores. This process was completed in November 2000. To exit the appliance business, the Company closed eight distribution centers and eight service centers. The Company leases the majority of these closed properties. While the Company has entered into contracts to sublease some of these properties, it continues the process of marketing the remaining properties to be subleased.

In fiscal 2001, the Company recorded appliance exit costs of $30.0 million. In the fourth quarter of fiscal 2002, the Company recorded additional lease termination costs of $10.0 million to reflect the rental market for these leased properties. These expenses are reported separately on the consolidated statements of earnings. The appliance exit cost liability is included in accrued expenses and other current liabilities on the consolidated balance sheets.

The appliance exit cost accrual activity and the remaining liability at August 31, 2002, are presented in the following table.

(Amounts in millions)	Total Exit Cost Accrual	Liability at February 28, 2002	Fiscal 2003 Payments or Write-Downs
Lease termination costs.............	$ 27.8	$ 19.7	$ 3.4
Fixed asset write-downs, net........	5.0	-	-
Employee termination benefits.......	4.4	-	-
Other...............................	2.8	-	-
Appliance exit costs................	$ 40.0	$ 19.7	$ 3.4

9. Operating Segment Information

The Company has conducted business in two operating segments: Circuit City and CarMax. These segments have been identified and managed by the Company based on the different products and services offered by each. See Note 13. Circuit City refers to the retail operations bearing the Circuit City name and to all related operations, such as Circuit City's finance operation. This segment is engaged in the business of selling brand-name consumer electronics, personal computers and entertainment software. CarMax refers to the used- and new-car retail locations bearing the CarMax name and to all related operations, such as CarMax's finance operation.

Financial information for these segments for the three- and six-month periods ended August 31, 2002 and 2001, is presented in the following tables.

Three Months Ended August 31, 2002

(Amounts in thousands)	Circuit City	CarMax	Total Operati Segments
Revenues from external customers..........	$ 2,221,204	$ 1,076,083	$ 3,297,287
Interest expense..........................	550	957	1,507
Depreciation and amortization............	40,800	4,286	45,086
(Loss) earnings before income taxes.......	(18,041)	52,420	34,379
Income tax (benefit) provision............	(6,856)	20,706	13,850
Net (loss) earnings.......................	(11,185)	31,714	20,529
Total assets..............................	$ 3,837,533	$ 825,922	$ 4,659,149

Three Months Ended August 31, 2001

(Amounts in thousands)	Circuit City	CarMax	Total Operati Segments
Revenues from external customers..........	$ 2,023,209	$ 938,911	$ 2,962,120
Interest (income) expense.................	(432)	2,086	1,654
Depreciation and amortization.............	33,888	4,612	38,500
(Loss) earnings before income taxes.......	(20,227)	44,178	23,951
Income tax (benefit) provision............	(7,686)	16,787	9,101
Net (loss) earnings.......................	(12,541)	27,391	14,850
Total assets..............................	$ 3,264,090	$ 694,453	$ 3,958,543

Six Months Ended August 31, 2002

(Amounts in thousands)	Circuit City	CarMax	Total Operati Segments
Revenues from external customers..........	$ 4,339,447	$ 2,077,647	$ 6,417,094

Interest expense.........................	550	1,983	2,533
Depreciation and amortization............	76,546	8,424	84,970
(Loss) earnings before income taxes.......	(20,066)	100,747	80,681
Income tax (benefit) provision...........	(7,625)	39,795	32,170
Net (loss) earnings......................	(12,441)	60,952	48,511
Total assets.............................	$ 3,837,533	$ 825,922	$ 4,659,149

Six Months Ended August 31, 2001

(Amounts in thousands)	Circuit City	CarMax	Total Operati Segments
Revenues from external customers..........	$ 3,893,830	$ 1,817,911	$ 5,711,741
Interest expense.........................	9	4,637	4,646
Depreciation and amortization............	68,377	9,305	77,682
(Loss) earnings before income taxes.......	(35,719)	87,037	51,318
Income tax (benefit) provision...........	(13,573)	33,074	19,501
Net (loss) earnings......................	(22,146)	53,963	31,817
Total assets.............................	$ 3,264,090	$ 694,453	$ 3,958,543

In the preceding tables, the net loss for Circuit City excludes the net earnings attributed to the reserved CarMax Group shares. Total assets for Circuit City exclude the reserved CarMax Group shares. As of August 31, 2001, total assets for Circuit City also exclude the discontinued Divx operations, which are discussed in Note 10.

10. Discontinued Operations

On June 16, 1999, Digital Video Express announced that it would cease marketing the Divx home video system and discontinue operations. At August 31, 2002, current liabilities of $8.0 million related to the former Divx operations were reflected in the consolidated balance sheet. At February 28, 2002, current liabilities of $18.5 million related to the former Divx operations were reflected in the consolidated balance sheet. For the three- and six-month periods ended August 31, 2002 and 2001, the discontinued Divx operations had no impact on the net earnings of Circuit City Stores, Inc. Discontinued operations have been segregated on the consolidated statements of cash flows.

11. Recent Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board issued SFAS No. 142, "Goodwill and Other Intangible Assets," effective for fiscal years beginning after December 15, 2001. Under the provisions of SFAS No. 142, goodwill and intangible assets deemed to have indefinite lives are no longer amortized but instead are subject to annual impairment tests in accordance with the pronouncement. Other intangible

assets that are identified to have finite useful lives continue to be amortized in a manner that reflects the estimated decline in the economic value of the intangible asset and are subject to review when events or circumstances which indicate impairment arise. The Company has performed the first of the required impairment tests of goodwill and indefinite-lived intangible assets, as outlined in the pronouncement. Based on the results of tests performed, as well as ongoing periodic assessments of goodwill, the Company did not recognize any impairment losses. Application of the nonamortization provisions of SFAS No. 142 in the first half of fiscal 2003 did not have a material impact on the financial position, results of operations or cash flows of the Company.

In August 2001, the FASB issued SFAS No. 143, "Accounting For Asset Retirement Obligations." This statement addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. It applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or the normal operation of a long-lived asset, except for certain obligations of lessees. This standard requires entities to record the fair value of a liability for an asset retirement obligation in the period incurred. SFAS No. 143 is effective for fiscal years beginning after June 15, 2002. The Company has not yet determined the impact, if any, of adopting this standard.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This statement addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." It applies to costs associated with an exit activity that does not involve an entity newly acquired in a business combination and costs associated with a disposal activity covered by SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This standard requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value when the liability is incurred, rather than at the date of commitment to an exit or disposal plan. SFAS No. 146 is effective for exit or disposal activities initiated after December 31, 2002. The Company has not yet determined the impact, if any, of adopting this standard.

12. Reclassifications

Certain prior year amounts have been reclassified to conform to the current presentation. Effective in the first quarter of fiscal 2003, Circuit City Stores adopted EITF No. 00-14, "Accounting for Certain Sales Incentives," which provides that sales incentives, such as mail-in rebates, offered to customers should be classified as a reduction of revenue. Previously, the Company recorded these rebates in cost of sales, buying and warehousing. The reclassification of rebates from cost of sales, buying and warehousing to sales decreased sales and cost of sales, buying and warehousing by $13.4 million for the quarter ended August 31, 2001, and $24.4 million for the six months ended August 31, 2001. This reclassification had no impact on the Company's net earnings.

For the three- and six-month periods ended August 31, 2001, CarMax wholesale sales have been reclassified and reported in net sales and operating revenues. In previous periods, wholesale sales were recorded as reductions to cost of sales. The reclassification of wholesale sales to sales increased sales and cost of sales by $90.0 million for the quarter ended August 31, 2001, and $174.6 million for the six months ended August 31, 2001. An additional reclassification between sales and cost of sales made to conform to the current presentation decreased sales and cost of sales by $2.5 million for the quarter ended August 31, 2001, and $4.8 million for the six months ended August 31, 2001. These reclassifications had no impact on the Company's net earnings.

13. Subsequent Event

On September 10, 2002, the Company's shareholders approved the separation of the CarMax Group from Circuit City Stores, Inc. and the Company's board of directors authorized the redemption of the Company's CarMax Group Common Stock and the distribution of CarMax, Inc. common stock to effect the separation. The separation was effective October 1, 2002. Each outstanding share of CarMax Group Common Stock was redeemed in exchange for one share of new CarMax, Inc. common stock. In addition, each holder of Circuit City Group Common Stock received as a tax-free distribution 0.313879 of a share of CarMax, Inc. common stock for each share of Circuit City Group Common Stock owned as of September 16, 2002, the record date for the distribution. Following the separation, the Circuit City Group Common Stock was renamed Circuit City common stock, representing an ownership interest only in the Circuit City business, and CarMax, Inc. became an independent, separately traded public company. Effective with the separation, Circuit City will report CarMax as a discontinued operation.

ITEM 2.

CIRCUIT CITY STORES, INC. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In this discussion, "we," "our" and "Circuit City Stores" refer to Circuit City Stores, Inc. and our wholly owned subsidiaries, unless the context requires otherwise. "Circuit City business" and "Circuit City" refer to the retail operations bearing the Circuit City name and to all related operations such as product service and Circuit City's finance operation. "Circuit City Group" refers to the Circuit City business and the reserved CarMax Group shares. "CarMax business," "CarMax" and "CarMax Group" refer to retail locations bearing the CarMax name and to all related operations such as CarMax's finance operation. All references to "quarter" and "year" refer to our fiscal year periods rather than calendar year periods unless stated otherwise.

On September 10, 2002, the Company's shareholders approved the separation of the CarMax Group from Circuit City Stores, Inc. and the Company's board of directors authorized the redemption of the Company's CarMax Group Common Stock and the distribution of CarMax, Inc. common stock to effect the separation. The separation was effective October 1, 2002. Each outstanding share of CarMax Group Common Stock was redeemed in exchange for one share of new CarMax, Inc. common stock. In addition, each holder of Circuit City Group Common Stock received as a tax-free distribution 0.313879 of a share of CarMax, Inc. common stock for each share of Circuit City Group Common Stock owned as of September 16, 2002, the record date for the distribution. Following the separation, the Circuit City Group Common Stock was renamed Circuit City common stock, representing an ownership interest only in the Circuit City business, and CarMax, Inc. became an independent, separately traded public company. Effective with the separation, Circuit City will report CarMax as a discontinued operation.

CRITICAL ACCOUNTING POLICIES

See the discussion of critical accounting policies included in the Circuit City Stores, Inc. 2002 Annual Report to Shareholders. These policies relate to the calculation of the value of retained interests in securitization transactions and the calculation of the liability for lease termination costs.

RESULTS OF OPERATIONS

Effective in the first quarter of fiscal 2003, Circuit City Stores adopted Emerging Issues Task Force No. 00-14, "Accounting for Certain Sales Incentives," which provides that sales incentives, such as mail-in rebates, offered to customers should be classified as a reduction of revenue. Previously, the Company recorded these rebates in cost of sales, buying and warehousing. The reclassification of rebates from cost of sales, buying and warehousing to sales decreased sales and cost of sales, buying and warehousing by $13.4 million for the quarter ended August 31, 2001, and $24.4 million for the six months ended August 31, 2001. This reclassification had no impact on the Company's net earnings.

Effective in the first quarter of fiscal 2003, CarMax classifies revenue from the sale of wholesale vehicles in net sales and operating revenues. Previously, CarMax wholesale vehicle sales were recorded as reductions to cost of sales. The reclassification of wholesale sales to sales increased sales and cost of sales by $90.0 million for the quarter ended August 31, 2001, and $174.6 million for the six months ended August 31, 2001. An additional reclassification between sales and cost of sales made to conform to the current presentation decreased sales and cost of sales by $2.5 million for the quarter ended August 31, 2001, and $4.8 million for the six months ended August 31, 2001. These reclassifications had no impact on the Company's net earnings.

Our operations, in common with other retailers in general, are subject to seasonal influences. Historically, the Circuit City business has realized more of its net sales and net earnings in the fourth quarter, which includes the December holiday selling season, than in any other fiscal quarter. The CarMax business, however, has experienced more of its net sales in the first half of the fiscal year. The net earnings of any quarter are seasonally disproportionate to net sales since administrative and certain operating expenses remain relatively constant during the year. Therefore, quarterly results should not be relied upon as necessarily indicative of results for the entire fiscal year.

Net Sales and Operating Revenues

Circuit City Stores, Inc. Total sales for Circuit City Stores for the second quarter of fiscal 2003 were $3.30 billion, an increase of 11 percent from $2.96 billion for the same period last year. For the six months ended August 31, 2002, total sales increased 12 percent to $6.42 billion from $5.71 billion for the same period last year.

Circuit City Group. Total sales for the Circuit City Group for the second quarter of fiscal 2003 increased 10 percent to $2.22 billion from $2.02 billion in last year's second quarter. Comparable store sales increased 10 percent for the second quarter of fiscal 2003. For the six months ended August 31, 2002, total sales increased 11 percent to $4.34 billion from $3.89 billion in last year's first half. Comparable store sales increased 11 percent for the first half of fiscal 2003. A Circuit City store is included in comparable store sales after the store has been open for a full year. Relocated stores are included in the comparable store base.

Second quarter Circuit City sales for fiscal 2003 reflected continued progress in both the high-service and packaged goods arenas. We posted strong sales growth in categories such as video, including big-screen televisions, particularly digital televisions. Due in part to back-to-school traffic, increased sales of notebook computers, printers, monitors, personal digital assistants and personal computer accessories drove sales growth in the information technology category. We also experienced significant sales gains in more promotional traffic-driving categories such as entertainment software and entry-level electronics.

The percent of merchandise sales represented by each major product category during the second quarter of fiscal years 2003 and 2002 was as follows:

Product Mix	Three Months Ended August 31, 2002	2001	Six Mon Augu 2002
Video	39%	38%	39%
Audio	14	16	15
Information Technology	36	36	35
Entertainment	11	10	11
TOTAL	100%	100%	100%

Circuit City sells extended warranty programs on behalf of unrelated third parties that are the primary obligors. Under these third-party warranty programs, we have no contractual liability to the customer. The total extended warranty revenue that is reported in total sales was $84.0 million, or 3.8 percent of sales, in the second quarter of fiscal 2003, compared with $86.7 million, or 4.3 percent of sales, in last year's second quarter. The total extended warranty revenue that is reported in total sales was $171.9 million, or 4.0 percent of sales, in the first half of fiscal 2003, compared with $166.8 million, or 4.3 percent of sales, in last year's first half.

The following table provides details on the Circuit City retail units:

Store Mix	Aug. 31, 2002	Aug. 31, 2001	Estimate Feb. 28, 2003	Feb.
Superstores	606	598	611	
Mall-based Express stores	17	29	17	
Total	623	627	628	

Circuit City expects to open approximately eight Superstores and relocate an estimated 10 Superstores in the current fiscal year. In the second quarter of fiscal 2003, we opened three Superstores, relocated two Superstores and closed two mall-based Express stores. For the first half of fiscal 2003, we opened three Superstores, relocated four Superstores, closed one Superstore and closed three mall-based Express stores.

CarMax Group. Total sales for the CarMax Group for the second quarter of fiscal 2003 increased 15 percent to $1.08 billion from $938.9 million in last year's second quarter. For the six months ended August 31, 2002, total sales increased 14 percent to $2.08 billion from $1.82 billion in last year's first half.

Retail Vehicle Sales. Retail vehicle sales increased 15 percent to $936.7 million in the second quarter of fiscal 2003 from $813.1 million in the second quarter of fiscal 2002. In the second quarter of fiscal 2003, used vehicle sales increased 18 percent to $784.8 million from $662.4 million for the same period last year, and new vehicle sales increased 1 percent to $151.9 million from $150.7 million for the same period last year. For the six months ended August 31, 2002, retail vehicle sales increased 15 percent to $1.81 billion from $1.57 billion in the prior year. For the six months ended August 31, 2002, used vehicle sales increased 19 percent to $1.52 billion from $1.28 billion last year, and new vehicle sales decreased 4 percent to $284.2 million from $296.4 million in the same period last year.

A CarMax store is included in comparable store retail sales after the store has been open for a full year. Comparable store retail vehicle dollar and unit sales for the second quarter and the first six months of fiscal years 2003 and 2002 were as follows:

Comparable Store Retail Vehicle	Three Months Ended August 31,		Six Months Ended August 31,	
Sales Change	2002	2001	2002	2001
Vehicle units:				
Used vehicles	12%	22%	12%	21%
New vehicles	5%	12%	1%	15%
Total	11%	21%	10%	20%
Vehicle dollars:				
Used vehicles	12%	30%	13%	29%
New vehicles	8%	14%	2%	18%
Total	11%	27%	11%	27%

For the second quarter of fiscal 2003, the overall increase in retail sales is attributed to the 12 percent growth in comparable store used-unit sales, the three CarMax stores opened since the first quarter of fiscal 2002 and the slight increase in the average retail selling price for used vehicles. For the three-month period ended August 31, 2002, the comparable store new-unit sales were in line with the new-car industry's performance as the industry benefited from the re-introduction of zero-percent financing incentives in July. This second-quarter performance more than offset the weakness in new-car sales experienced in the first quarter, which also was in line with the industry, delivering comparable store new-unit growth of 1 percent for the six-month period ended August 31, 2002.

Average Retail Selling Prices	Three Months Ended August 31,		Six Months Ended August 31,	
	2002	2001	2002	200
Used vehicles	$15,400	$15,300	$15,400	$15,2
New vehicles	$23,400	$22,800	$23,200	$23,0
Blended average	$16,300	$16,300	$16,300	$16,2

Retail Vehicle Sales Mix	Three Months Ended August 31,		Six Months Ended August 31,	
	2002	2001	2002	2001
Vehicle units:				
Used vehicles	89%	87%	89%	87%
New vehicles	11	13	11	13
Total	100%	100%	100%	100%
Vehicle dollars:				
Used vehicles	84%	81%	84%	81%
New vehicles	16	19	16	19
Total	100%	100%	100%	100%

Wholesale Vehicle Sales. CarMax's operating strategy is to build customer confidence and satisfaction by offering only high-quality vehicles; therefore, fewer than half of the vehicles acquired through the appraisal process meet the CarMax retail standard. Those vehicles that do not meet CarMax's standards are sold at its own on-site wholesale auctions. Wholesale vehicle sales totaled $97.7 million in the second quarter of fiscal 2003, compared with $90.0 million in the same period last year. For the six months ended August 31, 2002, wholesale vehicle sales totaled $190.1 million, compared with $174.6 million in the same period last year. These increases were consistent with increased traffic at CarMax stores, the impact of which was partially offset by lower average wholesale sale prices.

Other Sales and Revenues. Other sales and revenues include extended warranty revenues, service department sales and processing fees collected from consumers for the purchase of their vehicles at a CarMax retail location and totaled $41.7 million in the second quarter of fiscal 2003, compared with $35.8 million in the same period last year. For the six months ended August 31, 2002, other sales and revenues totaled $80.7 million, compared with $69.3 million in the same period last year.

CarMax sells extended warranties on behalf of unrelated third parties who are the primary obligors. Under these third-party warranty programs, CarMax has no contractual liability to the customer. Extended warranty revenue was $18.1 million in the second quarter of fiscal 2003 and $14.4 million in the second quarter of fiscal 2002. For the six months ended August 31, 2002, extended warranty revenue was $34.8 million, compared with $27.9 in the same period last year. These increases in warranty revenue reflect improved penetration, a result in part of continuing enhancement of CarMax's extended warranty offer, and strong sales growth for used cars, which achieve a higher extended warranty penetration rate than new cars.

Service sales were $15.9 million in the second quarter of fiscal 2003, compared with $14.7 million in the same period last year. For the six months ended August 31, 2002, service sales were $31.4 million compared with $28.6 million in the same period last year. These increases in service sales reflect the overall increase in CarMax's customer base.

Processing fees were $7.7 million in the second quarter of fiscal 2003, compared with $6.7 million in the same period last year. For the six months ended August 31, 2002, processing fees were $14.5 million, compared with $12.8 million in the same period last year. Consumers are assessed a processing fee when selling a vehicle to a CarMax retail location after the appraisal process. These increases in processing fee revenue resulted from increased traffic and increased consumer response to CarMax's vehicle purchase program.

Retail Stores. In September 2002, CarMax opened a satellite superstore in Charlotte, N.C. During the second half of the year, CarMax also plans to enter the Knoxville, Tenn., market and add satellite superstores in the Chicago, Ill., and Atlanta, Ga., markets. CarMax also has announced that it plans to enter the Las Vegas, Nev., market in early March 2003, shortly after the end of fiscal 2003.

The following table provides detail on the CarMax retail stores:

Store Mix	Aug. 31, 2002	Aug. 31, 2001	Estima Feb. 28,
Mega superstores	13	13	13
Standard superstores	18	16	19
Prototype satellite stores	5	4	8
Co-located new-car stores	2	2	2
Stand-alone new-car stores	2	5	2
Total	40	40	44

Cost of Sales, Buying and Warehousing

Circuit City Stores, Inc. The gross profit margin for Circuit City Stores was 19.7 percent of sales in the second quarter of fiscal 2003, compared with 20.4 percent in the same period last year. For the six months ended August 31, 2002, the gross profit margin was 20.0 percent compared with 20.5 percent in the same period last year.

Circuit City Group. The gross profit margin for the Circuit City Group was 23.7 percent of sales in the second quarter of fiscal 2003, compared with 24.5 percent in the same period last year. For the six months ended August 31, 2002, the gross profit margin was 24.0 percent compared with 24.6 percent in the same period last year. The gross profit margin declines reflect the margin pressure generated by stronger sales of entry-level electronics and personal computers compared with last year's second quarter and our more aggressive promotional stance in traffic-driving categories, partly offset by the growing sales of fully featured products such as big-screen televisions.

CarMax Group. The total gross profit margin for the CarMax Group was 11.5 percent of sales in the second quarter of fiscal 2003 and 11.6 percent for the second quarter of fiscal 2002. For the six months ended August 31, 2002 and 2001, the total gross profit margin was 11.7 percent of sales.

Retail Vehicle Gross Profit Margin. The retail vehicle gross profit margin was 9.8 percent of sales in the second quarter of fiscal 2003 versus 9.9 percent for the same period last year. For the six months ended August 31, 2002, the retail gross profit margin was 9.8 percent compared with 10.0 percent for the same period last year. In the second quarter, CarMax experienced a slight shortfall in its used average gross-margin-dollars-per-unit target partly as a result of taking selective markdowns in response to the July resumption of broad-based, zero-percent financing incentives on new cars. The slight shortfall was partially offset by the higher mix of used- to new-unit sales. Used vehicles carry a higher margin than new vehicles. The result was a retail vehicle gross profit margin that slightly declined in relation to the first six months of last fiscal year.

Wholesale Vehicle Gross Profit Margin. The wholesale vehicle gross profit margin was 4.4 percent of sales in the second quarter of fiscal 2003, compared with 4.6 percent for the same period last year. The slight decline in the wholesale gross profit margin during the second quarter of fiscal 2003, compared with the second quarter of fiscal 2002 is due to pricing adjustments in the wholesale marketplace. For the six months ended August 31, 2002, the wholesale vehicle gross profit margin was 5.5 percent, compared with 5.1 percent for the same period last year. Both the average wholesale cost and average wholesale sales price declined compared with the first six months of fiscal 2002; however, the decrease in the average wholesale sales price was less than the decrease in the average wholesale cost.

Other Gross Profit Margin. The gross profit margin for other sales and revenues was 68.0 percent of sales in the second quarter of fiscal 2003, compared with 66.6 percent for the same period last year. For the six months ended August 31, 2002 and 2001, the gross profit margin for other sales and revenues was 67.3 percent.

Selling, General and Administrative Expenses

Circuit City Stores, Inc. The selling, general and administrative expense ratio for Circuit City Stores was 18.6 percent of sales in the second quarter of fiscal 2003, compared with 19.6 percent for the same period last year. For the six-month period ended August 31, 2002, the Company's selling, general and administrative expense ratio was 18.7 percent compared with 19.5 percent for the same period last year. Interest income is recorded as a reduction to selling, general and administrative expenses.

Circuit City Group. The selling, general and administrative expense ratio for the Circuit City Group was 24.5 percent of sales in the second quarter of fiscal 2003, compared with 25.6 percent for the same period last year. For the six months ended August 31, 2002, the ratio was 24.4 percent of sales, compared with 25.5 percent in the same period last year. The improved expense ratios principally resulted from the leverage

achieved through increased sales, which more than offset the impact of increased remodeling and relocation expenses.

The fiscal 2003 second quarter expense ratio includes $25.8 million associated with remodeling and relocation activities, while the fiscal 2002 second quarter ratio includes $12.8 million of remodeling and relocation costs. The fiscal 2003 first half expense ratio includes $33.8 million associated with remodeling and relocation activities, while the fiscal 2002 first half ratio includes $15.8 million of remodeling and relocation costs. As of August 31, 2002, the Company had relocated two Superstores, completed more than 225 of the approximately 300 video department remodels planned for fiscal 2003 and substantially all of the approximately 300 full-store lighting upgrades scheduled for completion this fiscal year. As of August 31, 2001, the Company had relocated two Superstores and completed full-store remodels of 23 Superstores primarily located in Chicago, Ill.; Baltimore, Md.; and Washington, D.C.

Finance Operations. For the three- and six-month periods ended August 31, 2002 and 2001, pretax finance operation income, which is recorded as a reduction to selling, general and administrative expenses, was as follows:

	Three Months Ended August 31,		Six Months E August 31	
(Amounts in millions)	2002	2001	2002	
Securitization income....................	$ 55.5	$ 55.6	$ 106.0	$
Payroll and fringe benefit expenses......	10.6	10.2	21.3	
Other direct expenses....................	18.9	20.6	38.3	
Finance operation income.................	$ 26.0	$ 24.8	$ 46.4	$

Receivables generated by the Circuit City finance operation are sold through securitization transactions. Circuit City continues to service the securitized receivables for a fee. For the quarter ended August 31, 2002, serviced receivables averaged $2.75 billion compared with $2.55 billion for the quarter ended August 31, 2001. For the six months ended August 31, 2002, serviced receivables averaged $2.77 billion, compared with $2.60 billion for the same period last year.

For the Circuit City Group, securitization income includes the gain on the sale of these receivables and other income related to servicing these receivables. The amount by which the estimated future finance income from securitized credit card receivables exceeds the sum of the contractually specified investor returns and servicing fees, referred to as interest-only strips, is carried at fair value and amounted to $126.9 million at August 31, 2002, and $131.9 million at February 28, 2002. The key assumptions and estimates in determining the fair value of interest-only strips include management's projections of key factors, such as finance charge income, default rates, payment rates, forward interest rate curves and discount rates appropriate for the type of asset and risk. Based on these assumptions and estimates and the operation's securitization volume, the value of the interest-only strip increased $0.1 million in the three months ended August 31, 2002, and decreased $2.4 million in the three months ended August 31, 2001. The value of the interest-only strip decreased $5.0 million in the six months ended August 31, 2002, and increased $1.4 million in the six months ended August 31, 2001. Management reviews the assumptions and estimates used in determining the fair value of the interest-only strip on a quarterly basis. If these assumptions change or the actual results differ from the projected results, securitization income will be affected.

For the Circuit City Group, the finance operation income does not include any allocation of indirect costs or income. Examples of indirect costs not included are corporate expenses such as human resources, administrative services, marketing, information systems, accounting, legal, treasury and executive payroll, as well as retail store expenses. Payroll and fringe benefit expenses generally vary with the size of the serviced portfolio and increased only slightly during the quarter ended August 31, 2002, compared with the same period last year. Other direct expenses include third-party data processing, rent, credit promotion expenses, Visa and MasterCard fees, and other operating expenses. For the second quarter ended August 31, 2002, the finance operation benefited from favorable interest rates and reduced other operating expenses, which more than offset expenses associated with the new public securitization issued in July 2002.

CarMax Group. The selling, general and administrative expense ratio for the CarMax Group was 6.6 percent of sales in the second quarter of both fiscal 2003 and 2002. For the six months ended August 31, 2002, the ratio was 6.7 percent of sales, compared with 6.6 percent in the same period last year. The expense ratio in this year's first six months includes a higher level of expenses associated with geographic expansion, compared with last year's first six months, and $3.1 million of one-time separation costs, offset by continued above-expectation income from the finance operation.

Finance Income. For the second quarter and first six months of fiscal 2003 and 2002, pretax finance income, which is recorded as a reduction to selling, general and administrative expenses, was as follows:

	Three Months Ended August 31,		Six Months E August 31
(Amounts in millions)	2002	2001	2002
Securitization income....................	$25.8	$21.4	$49.1
Payroll and fringe benefit expenses......	1.7	1.3	3.4
Other direct expenses....................	2.0	1.5	3.7
Finance operation income.................	22.1	18.6	42.0
Third-party financing fees...............	4.6	4.2	8.8
Total finance income.....................	$26.7	$22.8	$50.8

Receivables generated by the CarMax finance operation are sold through securitization transactions. CarMax continues to service these receivables in exchange for a contractually specified servicing fee. For the quarter ended August 31, 2002, serviced receivables averaged $1.65 billion compared with $1.37 billion for the quarter ended August 31, 2001. For the six months ended August 31, 2002, serviced receivables averaged $1.60 billion, compared with $1.32 billion for the same period last year. The principal amount of defaults net of recoveries on managed receivables totaled $4.1 million for the quarter ended August 31, 2002, and $2.6 million for the quarter ended August 31, 2001. The principal amount of defaults net of recoveries totaled $7.3 million for the six months ended August 31, 2002, and $4.5 million for the six months ended August 31, 2001. Despite the weak economic environment, the managed receivables continue to perform in-line with our initial gain assumptions.

For the CarMax Group, securitization income includes the gain on sale of receivables and other income related to servicing these receivables. CarMax recorded gains on the sales of receivables totaling $18.1 million for the quarter ended August 31, 2002, compared with gains of $14.7 million for the period ended August 31, 2001. For the six months ended August 31, 2002, gains on the sales of receivables totaled $33.7 million, compared with $27.8 million for the same period last year. The increased gains on sale of receivables resulted from an increase in loan origination volume driven by increased sales. In addition, the cost of funds for the CarMax finance operation declined in the second quarter of this fiscal year compared with the first quarter of this year and the same period last year. This decline was partially offset by the decline in the interest rates for auto loans to consumers. In recording these gains, management estimates key assumptions such as finance charge income, default rates, payment rates and discount rates appropriate for the type of asset and risk. If these assumptions were to change, or the actual results were to differ from the projected results, securitization income would be affected.

For the CarMax Group, finance operation income does not include any allocation of indirect costs or income. Examples of indirect costs not included are retail store expenses and corporate expenses such as human resources, administrative services, marketing, information systems, accounting, legal, treasury and executive payroll. Payroll, fringe benefit expenses and other direct expenses increased proportionately to the average

managed receivable balance. Other direct expenses include collection expenses, rent and facility expenses and loan processing costs.

Fees received from arranging customer automobile financing through third parties were $0.4 million higher in the second quarter of fiscal 2003 than the same period last year. For the six months ended August 31, 2002, fees were $0.8 million higher than the same period last year. The increase in customer fees was a result of the total increase in retail vehicle sales.

Income Taxes

The effective income tax rate increased to 40.3 percent for the second quarter of fiscal 2003 from 38.0 percent for the second quarter of fiscal 2002. For the six months ended August 31, 2002, the effective income tax rate was 39.9 percent, compared with 38.0 percent for the same period last year. The increase in the fiscal 2003 effective tax rate reflects CarMax's non-tax deductible separation costs of $1.3 million in the second quarter and $3.1 million in the first half of the year.

Net Earnings (Loss)

Circuit City Stores, Inc. Net earnings for Circuit City Stores increased to $20.5 million in the second quarter of fiscal 2003 from $14.9 million in last year's second quarter. For the six-month period ended August 31, 2002, net earnings increased to $48.5 million from $31.8 million for the same period last year.

Circuit City Group. Excluding the earnings attributed to the reserved CarMax Group shares, the Circuit City business produced a loss of $11.2 million, or 5 cents per Circuit City Group share, in the second quarter ended August 31, 2002, compared with a loss of $12.5 million, or 6 cents per Circuit City Group share, for the same period last year. For the six months ended August 31, 2002, the Circuit City business produced a loss of $12.4 million, or 6 cents per Circuit City Group share, compared with a loss of $22.1 million, or 11 cents per Circuit City Group share, for the same period last year.

The net earnings attributed to the reserved CarMax Group shares were $20.3 million in the second quarter of this fiscal year, compared with $19.4 million in last fiscal year's second quarter. For the six-month period ended August 31, 2002, net earnings attributed to the reserved CarMax Group shares were $39.0 million compared with $39.1 million for the same period last year.

Net earnings of the Circuit City Group were $9.1 million, or 4 cents per Circuit City Group share, in the second quarter of fiscal 2003, compared with $6.8

million, or 3 cents per Circuit City Group share, in the second quarter of fiscal 2002. For the six-month period ended August 31, 2002, net earnings of the Circuit City Group were $26.6 million, or 13 cents per Circuit City Group share, compared with net earnings of $17.0 million, or 8 cents per Circuit City Group share, for the same period last year.

CarMax Group. The CarMax Group's second quarter fiscal 2003 net earnings increased 16 percent to $31.7 million from $27.4 million in the second quarter of fiscal 2002. Second quarter fiscal 2003 earnings include $1.3 million of one-time, non-tax-deductible costs associated with the separation of CarMax from Circuit City Stores. Excluding the one-time separation costs, net earnings were 20 percent higher in the second quarter of fiscal 2003 than the same period last year. For the six months ended August 31, 2002, net earnings increased 13 percent to $61.0 million from $54.0 million. Earnings for the six months ended August 31, 2002, include $3.1 million of one-time, non-tax-deductible costs associated with the separation. Excluding the one-time separation costs, net earnings increased 19 percent to $64.1 million in the first six months of fiscal 2003 compared with the same period last year.

In the second quarter of fiscal 2003, net earnings attributed to the CarMax Group Common Stock were $11.4 million, or 30 cents per CarMax Group share, compared with $8.0 million, or 25 cents per CarMax Group share, in the second quarter of last fiscal year. For the six months ended August 31, 2002, net earnings attributed to the CarMax Group Common Stock were $21.9 million, or 57 cents per CarMax Group share, compared with $14.9 million, or 50 cents per CarMax Group share, in the same period last year. The

remainder of the CarMax Group's net earnings was attributed to the shares of CarMax Group Common Stock reserved for the Circuit City Group or for issuance to the holders of Circuit City Group Common Stock.

Operations Outlook

Circuit City Group. In fiscal 2001, we introduced a store design that includes a more customer-friendly layout with better product adjacencies; a brighter more contemporary appearance; additional product on the sales floor; shopping carts and easily accessible cash registers. All new stores continue to follow this design. In fiscal 2001 and fiscal 2002, we also undertook several remodels and product category tests to evaluate how best to add these features into existing stores. We decided to begin in fiscal 2003 a three-year multi-phased remodeling program that will cover approximately 300 stores. As part of this remodeling program, we are in fiscal 2003 introducing a remodeled video department and upgrading the lighting in these stores, spending an average of $325,000 to $350,000 per store. We believe that rolling out this remodeled department will enable us to increase Circuit City's market share in the growing and highly profitable big-screen television category and further solidify our position in the overall video category. The Consumer Electronics Association projects that big-screen television sales will grow at a double-digit rate in calendar 2002. By beginning with the video department, we believe that we can affect a large number of Circuit City Superstores in a manner that has significant potential for incremental benefit while minimizing the disruptive impact of the remodeling process.

In addition to remodeling, we expect to relocate approximately 10 Superstores in the current fiscal year. We expect that fiscal 2003 expenditures for Circuit City remodeling and relocations will total approximately $130 million, of which we expect to capitalize approximately $70 million and expense approximately $60 million, or no more than 18 cents per Circuit City share.

In fiscal 2003, we also will continue testing design ideas for other departments in the Circuit City Superstores. In fiscal 2004 and fiscal 2005, we expect to introduce these design ideas into many of the approximately 300 stores being remodeled under the three-year remodeling plan. We continue to review the suitability of our remaining Superstore base for either remodeling or relocation and anticipate relocating additional stores in fiscal 2004 and fiscal 2005. We currently anticipate that in fiscal 2004 and fiscal 2005 the impact of remodeling and relocations on earnings per share will be similar to the anticipated fiscal 2003 impact.

Given our presence in virtually all of the nation's top metropolitan markets, new Superstores are being added only in small markets or to increase our penetration in existing major markets. We plan to open approximately eight Circuit City Superstores in fiscal 2003. Because of limited planned geographic expansion, we expect total Circuit City sales growth to only slightly exceed comparable store sales growth. We expect that categories where we expanded selection following our exit from the appliance business and categories, such as big-screen televisions, that are benefiting from digital product innovation, will contribute to Circuit City's total and comparable store sales growth. However, we also anticipate that Circuit City's sales growth will reflect our focus on sales counselor training and customer service, store remodeling, effective marketing programs and a competitive merchandise assortment with attractive prices. We expect that the gross profit margin will reflect the mix of merchandise sold and our efforts to remain competitive and achieve profitable market share growth and that the expense ratio will reflect increases in Circuit City expenses associated with remodeling and relocation as discussed above, advertising and systems enhancements and the total sales volume achieved. For the full year, we expect the fiscal 2003 profit contribution from Circuit City's finance operation to be similar to the contribution in fiscal 2002.

With existing Circuit City initiatives, additional efforts to enhance the business and a relatively stable economy, we believe the Circuit City business will contribute 57 cents per share to 67 cents per share to the fiscal 2003 earnings of Circuit City, including remodeling and relocation expenses. Excluding these expenses, we expect the Circuit City business will contribute 75 cents per share to 85 cents per share to the fiscal 2003 earnings of Circuit City. Effective with the separation, Circuit City will report CarMax as a discontinued operation.

Circuit City and other consumer electronics retailers receive a large number of consumer electronics products and parts through West Coast ports served by union-represented dockworkers. In recent months, the union and port operators have been involved in an ongoing labor dispute which has included a management lockout

lasting approximately ten days. In response to the possibility of work stoppage, Circuit City has accelerated inventory purchases when possible. However, the closure of or work slowdowns at the ports could have a materially negative impact on Circuit City's sales and earnings for the second half of the fiscal year. The ultimate impact will depend on the amount of time until shipping returns to normal at these ports and the duration of any further closures or work slowdowns.

CarMax Group. For more than two years, CarMax has demonstrated that its consumer offer and business model can produce strong sales and earnings growth. At the beginning of fiscal 2002, CarMax announced that it would resume geographic growth, opening two superstores in fiscal 2002, four to six superstores in fiscal 2003 and six to eight stores in each of fiscal years 2004, 2005 and 2006. This expansion is proceeding as planned with three more used-car superstores scheduled to open during the second half of the fiscal year, bringing the total number of stores opened in fiscal 2003 to five.

Comparable store used-unit sales growth is a primary driver of CarMax's profitability. Given CarMax's performance in the first half of the fiscal year, it now expects second half used-unit comparable store growth in the mid- to high-single digit range.

Fiscal 2003 is a year of transition for CarMax as it ramps up the growth pace and assumes additional expenses related to the separation from Circuit City. The expense leverage that CarMax would expect from the used-unit comparable store growth during this fiscal year will be partially offset by increased expenses in the second half of fiscal 2003 resulting from diseconomies of scale and incremental expenses due to the separation from Circuit City and growth related costs. Increases in benefit plans, insurance and management are examples of cost increases resulting from the separation. Growth related costs include the development of a management bench for store expansion for the next two fiscal years store openings and pre-opening expenses for stores opening over the second half of the fiscal year and the first quarter of next year. In addition, other growth related costs such as training, recruiting and employee relocation for new stores also moderate the expense leverage that CarMax would expect from used unit comparable store growth this year.

For fiscal 2003, CarMax initially had anticipated that interest rates would rise above the low levels experienced in fiscal 2002 resulting in reduced yield spreads from the CarMax finance operation throughout fiscal 2003. If the current favorable interest rate environment continues, CarMax may not experience the reduction in yield spreads originally anticipated.

RECENT ACCOUNTING PRONOUNCEMENTS

On March 1, 2002, Circuit City Stores adopted EITF No. 00-14, "Accounting for Certain Sales Incentives," which provides that sales incentives, such as mail-in rebates, offered to customers should be classified as a reduction to revenue. The Company reclassified these rebate expenses from cost of sales, buying and warehousing to net sales and operating revenues. The adoption did not have a material impact on the Company's financial position, results of operations or cash flows.

In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," effective for fiscal years beginning after December 15, 2001. Under the provisions of SFAS No. 142, goodwill and intangible assets deemed to have indefinite lives are no longer amortized but instead are subject to annual impairment tests in accordance with the pronouncement. Other intangible assets that are identified to have finite useful lives continue to be amortized in a manner that reflects the estimated decline in the economic value of the intangible asset and are subject to review when events or circumstances which indicate impairment arise. The Company has performed the first of the required impairment tests of goodwill and indefinite-lived intangible assets, as outlined in the pronouncement. Based on the results of tests performed, as well as ongoing periodic assessments of goodwill, the Company did not recognize any impairment losses. Application of the nonamortization provisions of SFAS No. 142 in the first half of fiscal 2003 did not have a material impact on the financial position, results of operations or cash flows of the Company.

In August 2001, the FASB issued SFAS No. 143, "Accounting For Asset Retirement Obligations." This statement addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. It applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or the normal operation of a long-lived asset, except for certain obligations of lessees. This standard requires entities to record the fair value of a liability for an asset retirement obligation in the period incurred. SFAS No. 143 is effective for fiscal years beginning after June 15, 2002. The Company has not yet determined the impact, if any, of adopting this standard.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This statement addresses financi