

EXPRESS, INC.
Form 10-Q
December 10, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934
For the Quarterly Period Ended November 1, 2014
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 001-34742

EXPRESS, INC.
(Exact name of registrant as specified in its charter)

Delaware 26-2828128
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

1 Express Drive 43230
Columbus, Ohio (Zip Code)
(Address of principal executive offices)
Telephone: (614) 474-4001
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer

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Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes No

The number of outstanding shares of the registrant's common stock was 84,293,740 as of November 29, 2014.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q ("Quarterly Report") contains forward-looking statements that are subject to risks and uncertainties. All statements other than statements of historical fact included in this Quarterly Report are forward-looking statements. Forward-looking statements give our current expectations and projections relating to our financial condition, results of operations, plans, objectives, future performance, and business. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. These statements may include words such as "anticipate," "estimate," "expect," "project," "plan," "intend," "believe," "may," "will," "should," "likely," and other words and terms of similar meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events. For example, all statements we make relating to our estimated and projected costs, expenditures, cash flows, and financial results, our plans and objectives for future operations, growth or initiatives, strategies, plans to repurchase shares of our common stock, or the expected outcome or impact of pending or threatened litigation are forward-looking statements. All forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those that we expected, including:

- changes in consumer spending and general economic conditions;
- our ability to identify and respond to new and changing fashion trends, customer preferences, and other related factors;
 - fluctuations in our sales and results of operations on a seasonal basis and due to a variety of other factors;
- significant competition from other retailers;
- the success of the malls and shopping centers in which our stores are located and customer traffic;
- our dependence on a strong brand image;
- our ability to develop and maintain a reliable omni-channel experience for our customers;
- our reliance on information systems and any failure, inadequacy, interruption, or security failure of those systems;
- our ability to protect our customer data from fraud or theft;
- our dependence upon independent third parties to manufacture all of our merchandise;
- the availability constraints and price volatility of raw materials and labor used to manufacture our products;
- interruptions of the flow of merchandise from international manufacturers causing disruptions in our supply chain;
- shortages of inventory, delayed shipments to our online customers, and harm to our reputation due to distribution difficulties or shut-down of distribution facilities;
- our reliance upon independent third-party transportation providers for substantially all of our product shipments;
- our dependence upon key executive management;
- our growth strategy, including our new store growth, e-commerce, and international expansion plans;
- our leasing substantial amounts of space;
- our reliance on third parties to provide us with certain key services for our business;
- claims made against us resulting in litigation;
- changes in laws and regulations applicable to our business;
- our ability to protect our trademarks or other intellectual property rights;
- our substantial indebtedness and lease obligations;
- restrictions imposed by our indebtedness on our current and future operations and our ability to pay dividends and repurchase shares of common stock;
- fluctuations in energy costs;
- changes in taxation requirements or the results of tax audits;
- impairment charges on long-lived assets; and
- uncertainty associated with Sycamore Partners' expressed interest in acquiring the company.

We derive many of our forward-looking statements from our operating budgets and forecasts, which are based upon many detailed assumptions. While we believe that our assumptions are reasonable, we caution that it is very difficult to predict the impact of known factors, and it is impossible for us to anticipate all factors that could affect our actual

results. For a discussion of these risks and other risks and uncertainties that could cause actual results to differ materially from those contained in our forward-looking statements, please refer to “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended February 1, 2014 ("Annual Report"), filed with the Securities and Exchange Commission (“SEC”) on April 1, 2014, and "Part II - Item 1A. Risk Factors" of this Quarterly Report. The forward-looking statements included in this Quarterly Report are made only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events, or otherwise, except as otherwise required by law.

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ITEM 1. FINANCIAL STATEMENTS.EXPRESS, INC.
CONSOLIDATED BALANCE SHEETS
(Amounts in Thousands, Except Per Share Amounts)
(Unaudited)

	November 1, 2014	February 1, 2014
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$217,814	\$311,884
Receivables, net	20,468	17,384
Inventories	350,269	212,510
Prepaid minimum rent	29,084	28,554
Other	22,414	13,129
Total current assets	640,049	583,461
PROPERTY AND EQUIPMENT	840,452	767,661
Less: accumulated depreciation	(424,672	) (391,539
Property and equipment, net	415,780	376,122
TRADENAME/DOMAIN NAME	197,822	197,812
DEFERRED TAX ASSETS	17,434	17,558
OTHER ASSETS	6,985	7,717
Total assets	\$1,278,070	\$1,182,670
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$226,291	\$154,736
Deferred revenue	20,248	28,436
Accrued expenses	86,354	116,035
Total current liabilities	332,893	299,207
LONG-TERM DEBT	199,435	199,170
DEFERRED LEASE CREDITS	128,161	114,509
OTHER LONG-TERM LIABILITIES	105,802	95,215
Total liabilities	766,291	708,101
COMMITMENTS AND CONTINGENCIES (Note 10)		
STOCKHOLDERS' EQUITY:		
Preferred stock – \$0.01 par value; 10,000 shares authorized; no shares issued or outstanding	—	—
Common stock – \$0.01 par value; 500,000 shares authorized; 90,392 shares and 89,859 shares issued at November 1, 2014 and February 1, 2014, respectively, and 84,292 shares and 83,966 shares outstanding at November 1, 2014 and February 1, 2014, respectively	904	899

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Additional paid-in capital	144,778	130,511	
Accumulated other comprehensive loss	(844) (728)
Retained earnings	474,995	448,460	
Treasury stock – at average cost; 6,100 shares and 5,893 shares at November 1, 2014 and February 1, 2014, respectively	(108,054	) (104,573)
Total stockholders' equity	511,779	474,569	
Total liabilities and stockholders' equity	\$1,278,070	\$1,182,670	

See notes to unaudited consolidated financial statements.

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EXPRESS, INC.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(Amounts in Thousands, Except Per Share Amounts)

(Unaudited)

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013	November 1, 2014	November 2, 2013
NET SALES	\$497,608	\$503,808	\$1,439,680	\$1,503,245
COST OF GOODS SOLD, BUYING AND OCCUPANCY COSTS	340,050	338,543	1,008,724	1,014,656
Gross profit	157,558	165,265	430,956	488,589
OPERATING EXPENSES:				
Selling, general, and administrative expenses	126,526	128,366	371,309	360,165
Other operating expense (income), net	508	169	(476)	(415)
Total operating expenses	127,034	128,535	370,833	359,750
OPERATING INCOME	30,524	36,730	60,123	128,839
INTEREST EXPENSE, NET	6,042	4,876	17,880	14,457
OTHER EXPENSE, NET	160	153	157	958
INCOME BEFORE INCOME TAXES	24,322	31,701	42,086	113,424
INCOME TAX EXPENSE	9,737	12,434	15,551	44,811
NET INCOME	\$14,585	\$19,267	\$26,535	\$68,613
OTHER COMPREHENSIVE INCOME:				
Foreign currency translation (loss) gain	(600)	) 26	(116)	) 242
COMPREHENSIVE INCOME	\$13,985	\$19,293	\$26,419	\$68,855
EARNINGS PER SHARE:				
Basic	\$0.17	\$0.23	\$0.32	\$0.81
Diluted	\$0.17	\$0.23	\$0.31	\$0.81
WEIGHTED AVERAGE SHARES OUTSTANDING:				
Basic	84,189	83,929	84,122	84,675
Diluted	84,605	84,603	84,490	85,221

See notes to unaudited consolidated financial statements.

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EXPRESS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in Thousands)
(Unaudited)

	Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$26,535	\$68,613
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	57,965	52,000
Loss on disposal of property and equipment	741	636
Impairment charge	5,087	—
Excess tax benefit from share-based compensation	(47	) (201
Share-based compensation	14,306	16,016
Deferred taxes	668	307
Landlord allowance amortization	(8,637	) (6,573
Changes in operating assets and liabilities:		
Receivables, net	(3,101	) (6,420
Inventories	(137,746	) (128,334
Accounts payable, deferred revenue, and accrued expenses	33,431	25,969
Other assets and liabilities	8,805	15,627
Net cash (used in) provided by operating activities	(1,993	) 37,640
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(86,571	) (78,772
Purchase of intangible assets	(1,010	) (69
Net cash used in investing activities	(87,581	) (78,841
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on lease financing obligations	(1,105	) (45
Excess tax benefit from share-based compensation	47	201
Proceeds from exercise of stock options	—	4,426
Repurchase of common stock	(3,481	) (37,905
Net cash used in financing activities	(4,539	) (33,323
EFFECT OF EXCHANGE RATE ON CASH	43	(220
NET DECREASE IN CASH AND CASH EQUIVALENTS	(94,070	) (74,744
CASH AND CASH EQUIVALENTS, Beginning of period	311,884	256,297
CASH AND CASH EQUIVALENTS, End of period	\$217,814	\$181,553
See notes to unaudited consolidated financial statements.		

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Notes to Unaudited Consolidated Financial Statements (unaudited)

1. Description of Business and Basis of Presentation

Business Description

Express, Inc., together with its subsidiaries ("Express" or the "Company"), is a specialty apparel and accessories retailer of women's and men's merchandise, targeting the 20 to 30 year old customer. Express merchandise is sold through retail and factory outlet stores and the Company's website, www.express.com. As of November 1, 2014, Express operated 609 primarily mall-based retail stores in the United States, Canada, and Puerto Rico as well as 29 factory outlet stores. Additionally, the Company earned revenue from 30 franchise stores in the Middle East, Latin America, and South Africa. These franchise stores are operated by franchisees pursuant to franchise agreements. Under the franchise agreements, the franchisees operate stores that sell Express-branded apparel and accessories purchased directly from the Company.

Fiscal Year

The Company's fiscal year ends on the Saturday closest to January 31. Fiscal years are referred to by the calendar year in which the fiscal year commences. References herein to "2014" and "2013" represent the 52-week periods ended January 31, 2015 and February 1, 2014, respectively. All references herein to "the third quarter of 2014" and "the third quarter of 2013" represent the thirteen weeks ended November 1, 2014 and November 2, 2013, respectively.

Basis of Presentation

The accompanying unaudited Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP") for interim financial information. Accordingly, they do not include all of the information or footnotes required by GAAP for complete financial statements. In the opinion of management, the accompanying unaudited Consolidated Financial Statements reflect all adjustments (which are of a normal recurring nature) necessary to state fairly the financial position, results of operations, and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for 2014. Therefore, these statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto for the year ended February 1, 2014, included in the Company's Annual Report on Form 10-K, filed with the SEC on April 1, 2014.

Principles of Consolidation

The unaudited Consolidated Financial Statements include the accounts of Express, Inc. and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting period, as well as the related disclosure of contingent assets and liabilities as of the date of the Consolidated Financial Statements. Actual results may differ from those estimates. The Company revises its estimates and assumptions as new information becomes available.

Reclassifications and Revisions

Certain prior period amounts have been reclassified or revised to conform to the current period presentation. This includes a revision to reclassify sell-off revenue from "Cost of Goods Sold, Buying and Occupancy Costs" to "Net Sales" in the amount of \$0.8 million and \$5.6 million for the thirteen and thirty-nine weeks ended November 2, 2013, respectively. This revision did not impact the Company's reported gross profit, net earnings, earnings per share, or cash flows for the prior periods. The Company has assessed the related error and concluded that it was not material to the Company's previously issued interim consolidated financial statements.

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Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09. ASU 2014-09 supersedes the revenue recognition requirements in “Revenue Recognition (Topic 605),” and requires entities to recognize revenue in a way that accounts for the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period, and is to be applied retrospectively, with early application not permitted. The Company is evaluating the new standard, but does not, at this time, anticipate a material impact to the financial statements once implemented.

2. Segment Reporting

The Company defines an operating segment on the same basis that it uses to evaluate performance internally. The Company has determined that, together, its Chief Executive Officer, President, and Chief Operating Officer are the Chief Operating Decision Maker and that there is one operating segment. Therefore, the Company reports results as a single segment, which includes the operation of its Express brick-and-mortar retail and outlet stores, e-commerce operations, and franchise operations.

The following is information regarding the Company's major product categories and sales channels:

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013	November 1, 2014	November 2, 2013
	(in thousands)		(in thousands)	
Apparel	\$438,552	\$442,196	\$1,259,465	\$1,313,175
Accessories and other	50,936	52,699	152,227	162,059
Other revenue	8,120	8,913	27,988	28,011
Total net sales	\$497,608	\$503,808	\$1,439,680	\$1,503,245
	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013	November 1, 2014	November 2, 2013
	(in thousands)		(in thousands)	
Stores	\$410,355	\$423,720	\$1,201,748	\$1,273,452
E-commerce	79,133	71,175	209,944	201,782
Other revenue	8,120	8,913	27,988	28,011
Total net sales	\$497,608	\$503,808	\$1,439,680	\$1,503,245

Other revenue consists primarily of sell-off revenue, shipping and handling revenue related to e-commerce activity, gift card breakage, and revenue from franchise agreements.

Revenue and long-lived assets relating to the Company's international operations for the thirteen and thirty-nine weeks ended November 1, 2014 and November 2, 2013, respectively, were not material for any period presented and, therefore, are not reported separately from domestic revenue or long-lived assets.

3. Earnings Per Share

The following table provides a reconciliation between basic and diluted weighted-average shares used to calculate basic and diluted earnings per share:

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013	November 1, 2014	November 2, 2013

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	(in thousands)			
Weighted-average shares - basic	84,189	83,929	84,122	84,675
Dilutive effect of stock options, restricted stock units, and restricted stock	416	674	368	546
Weighted-average shares - diluted	84,605	84,603	84,490	85,221

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Equity awards representing 4.3 million and 4.1 million shares of common stock were excluded from the computation of diluted earnings per share for the thirteen and thirty-nine weeks ended November 1, 2014, respectively, as the inclusion of these awards would have been anti-dilutive. Equity awards representing 2.0 million shares of common stock were excluded from the computation of diluted earnings per share for the thirteen and thirty-nine weeks ended November 2, 2013, as the inclusion of these awards would have been anti-dilutive.

Additionally, for the thirteen and thirty-nine weeks ended November 1, 2014, there were 0.5 million shares excluded from the computation of diluted weighted average shares because the number of shares that will ultimately be issued is contingent on the Company's performance compared to pre-established performance goals which have not been achieved as of November 1, 2014.

4. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Assets and liabilities measured at fair value are classified using the following hierarchy, which is based upon the transparency of inputs to the valuation as of the measurement date.

Level 1-Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2-Valuation is based upon quoted prices for similar assets and liabilities in active markets or other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3-Valuation is based upon other unobservable inputs that are significant to the fair value measurement.

Financial Assets

The following table presents the Company's financial assets measured at fair value on a recurring basis as of November 1, 2014 and February 1, 2014, aggregated by the level in the fair value hierarchy within which those measurements fall.

	November 1, 2014		
	Level 1	Level 2	Level 3
	(in thousands)		
U.S. treasury securities money market funds	\$178,886	\$—	\$—
	February 1, 2014		
	Level 1	Level 2	Level 3
	(in thousands)		
U.S. treasury securities money market funds	\$290,361	\$—	\$—

The carrying amounts reflected on the unaudited Consolidated Balance Sheets for cash, cash equivalents, receivables, prepaid expenses, and payables as of November 1, 2014 and February 1, 2014 approximated their fair values.

Non-Financial Assets

The Company's non-financial assets, which include fixtures, equipment, improvements, and intangible assets, are not required to be measured at fair value on a recurring basis. However, if certain triggering events occur indicating the carrying value of these assets may not be recoverable, or annually in the case of indefinite lived intangibles, an impairment test is required. The impairment test requires the Company to estimate the fair value of the assets and compare this to the carrying value of the assets. If the fair value of the asset is less than the carrying value, then an impairment charge is recognized and the non-financial assets are recorded at fair value. The Company estimates the fair value using a discounted cash flow model. Factors used in the evaluation include, but are not limited to, management's plans for future operations, recent operating results, and projected cash flows. During the thirteen and thirty-nine weeks ended November 1, 2014, the Company recognized impairment charges of approximately \$2.3 million and \$5.1 million, respectively. These charges were related to three stores for the thirteen weeks ended November 1, 2014, and nine stores for the thirty-nine weeks ended November 1, 2014. There were no impairment charges recognized during the thirteen or thirty-nine weeks ended November 2, 2013.

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5. Intangible Assets

The following table provides the significant components of intangible assets:

	November 1, 2014		
	Cost	Accumulated Amortization	Ending Net Balance
	(in thousands)		
Tradenname	\$ 196,144	\$—	\$ 196,144
Internet domain names/trademarks	1,678	—	1,678
Net favorable lease obligations/other	21,146	19,664	1,482
	\$218,968	\$ 19,664	\$ 199,304
	February 1, 2014		
	Cost	Accumulated Amortization	Ending Net Balance
	(in thousands)		
Tradenname	\$ 196,144	\$—	\$ 196,144
Internet domain names/trademarks	1,668	—	1,668
Net favorable lease obligations/other	20,175	19,106	1,069
	\$217,987	\$ 19,106	\$ 198,881

The Company's tradenname, internet domain names, and trademarks have indefinite lives. Net favorable lease obligations and other intangibles are amortized over a period between five and ten years and are included in other assets on the unaudited Consolidated Balance Sheets. Amortization expense totaled approximately \$0.2 million and \$0.6 million during the thirteen and thirty-nine weeks ended November 1, 2014, respectively, and \$0.3 million and \$1.0 million during the thirteen and thirty-nine weeks ended November 2, 2013.

6. Income Taxes

The provision for income taxes is based on a current estimate of the annual effective tax rate adjusted to reflect the impact of discrete items. The Company's effective income tax rate may fluctuate from quarter to quarter as a result of a variety of factors, including changes in the Company's assessment of certain tax contingencies, valuation allowances, changes in tax law, outcomes of administrative audits, the impact of discrete items, and the mix of earnings.

During the second quarter of 2014, the Internal Revenue Service (IRS) completed its examination of the Company's 2012, 2011, and 2010 income tax returns. The Company released net uncertain tax positions of \$1.7 million and the related accrued interest of \$0.1 million as a result of the conclusion of this examination.

The Company's effective tax rate was 40.0% and 39.2% for the thirteen weeks ended November 1, 2014 and November 2, 2013, respectively. The Company's effective tax rate was 37.0% and 39.5% for the thirty-nine weeks ended November 1, 2014 and November 2, 2013, respectively. The reduction of the rate for the thirty-nine weeks ended November 1, 2014 primarily related to the net \$1.7 million tax benefit from the release of uncertain tax positions following the conclusion of the IRS examination discussed above.

7. Lease Financing Obligations

In certain lease arrangements, the Company is involved in the construction of the building. To the extent the Company is involved in the construction of structural improvements or takes construction risk prior to commencement of a lease, it is deemed the owner of the project for accounting purposes. Accordingly, the Company records an asset in property and equipment on the unaudited Consolidated Balance Sheets, including any capitalized interest costs. The Company also records related liabilities in accrued interest and lease financing obligations included in other long-term liabilities on the unaudited Consolidated Balance Sheets, for the replacement cost of the Company's portion of the pre-existing building plus the amount of construction costs incurred by the landlord as of the balance sheet date. Once construction is complete, the Company considers the requirements for sale-leaseback treatment, including the transfer of all risks of ownership back to the landlord, and whether the Company has any continuing involvement in the leased property. If the arrangement does not qualify for sale-leaseback

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treatment, the building assets subject to these obligations remain on the Company's unaudited Consolidated Balance Sheets at their historical cost, and such assets are depreciated over their remaining useful lives. The replacement cost of the pre-existing building, as well as the costs of construction paid by the landlord, are recorded as lease financing obligations, and a portion of the lease payments are applied as payments of principal and interest. The interest rate selected for lease financing obligations is evaluated at lease inception based on the Company's incremental borrowing rate. At the end of the initial lease term, should the Company decide not to renew the lease, the Company would reverse equal amounts of the remaining net book value of the assets and the corresponding lease financing obligations. The initial lease terms related to these lease arrangements are expected to expire in 2023 and 2030. As of November 1, 2014 and February 1, 2014 there was \$71.9 million and \$63.2 million, respectively, of net landlord funded construction, replacement cost of pre-existing property, and capitalized interest in property and equipment on the unaudited Consolidated Balance Sheets. There were also \$73.8 million and \$63.0 million of lease financing obligations as of November 1, 2014 and February 1, 2014, respectively, in other long-term liabilities on the unaudited Consolidated Balance Sheets. The transactions involving the initial recording of these assets and liabilities are classified as non-cash items for purposes of the unaudited Consolidated Statements of Cash Flows.

Rent expense relating to the land is recognized on a straight-line basis once construction begins. The Company does not report rent expense for the portion of the rent payment determined to be related to the lease obligations which are owned for accounting purposes. Rather, this portion of the rent payment under the lease is recognized as a reduction of the lease financing obligations and as interest expense.

8. Debt

Borrowings outstanding consisted of the following:

	November 1, 2014 (in thousands)	February 1, 2014
8 3/4% Senior Notes	\$200,850	\$200,850
Debt discount on Senior Notes	(1,415	) (1,680
Total long-term debt	\$199,435	\$199,170

Revolving Credit Facility

On July 29, 2011, Express Holding, LLC, a wholly-owned subsidiary ("Express Holding"), and its subsidiaries entered into an Amended and Restated \$200.0 million secured Asset-Based Credit Facility ("Revolving Credit Facility"). As of November 1, 2014, there were no borrowings outstanding and approximately \$197.6 million available under the Revolving Credit Facility.

The Revolving Credit Facility requires Express Holding and its subsidiaries to maintain a fixed charge coverage ratio of at least 1.0:1.0 if excess availability plus eligible cash collateral is less than 10% of the borrowing base for 15 consecutive days. In addition, the Revolving Credit Facility contains customary covenants and restrictions on Express Holding and its subsidiaries' activities, including, but not limited to, limitations on the incurrence of additional indebtedness; liens, negative pledges, guarantees, investments, loans, asset sales, mergers, acquisitions, and prepayment of other debt; distributions, dividends, and the repurchase of capital stock; transactions with affiliates; and the ability to change the nature of its business or its fiscal year. All obligations under the Revolving Credit Facility are guaranteed by Express Holding and its domestic subsidiaries (that are not borrowers) and secured by a lien on substantially all of the assets of Express Holding and its domestic subsidiaries.

Senior Notes

On March 5, 2010, Express, LLC and Express Finance Corp. ("Express Finance"), wholly-owned subsidiaries of the Company, co-issued, in a private placement, \$250.0 million of 8^{3/4}% Senior Notes due in 2018 (the "Senior Notes") at an offering price of 98.6% of the face value.

The Senior Notes may be redeemed in part or in full at the following percentages of the outstanding principal amount prepaid: 104.38% prior to March 1, 2015; 102.19% on or after March 1, 2015, but prior to March 1, 2016; and at the principal amount on or after March 1, 2016.

The indenture governing the Senior Notes contains customary covenants and restrictions on the activities of Express, LLC, Express Finance, and Express, LLC's restricted subsidiaries, including, but not limited to, the incurrence of additional indebtedness; payment of dividends or distributions in respect of capital stock or certain other restricted payments or investments; entering into agreements that restrict distributions from restricted subsidiaries; the sale or disposal of assets,

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including capital stock of restricted subsidiaries; transactions with affiliates; the incurrence of liens; and mergers, consolidations, or the sale of substantially all of Express, LLC's assets. Certain of these covenants will be suspended if the Senior Notes are assigned an investment grade rating by both Standard & Poor's and Moody's Investors Service and no default has occurred or is continuing. If either rating on the Senior Notes should subsequently decline to below investment grade, the suspended covenants would be reinstated.

Fair Value of Debt

The fair value of the Senior Notes was estimated using a number of factors, such as recent trade activity, size, timing, and yields of comparable bonds and is, therefore, within Level 2 of the fair value hierarchy. As of November 1, 2014, the estimated fair value of the Senior Notes was \$207.9 million.

Letters of Credit

The Company may enter into various trade letters of credit ("trade LCs") in favor of certain vendors to secure merchandise. These trade LCs are issued for a defined period of time, for specific shipments, and generally expire three weeks after the merchandise shipment date. As of November 1, 2014 and February 1, 2014, there were no outstanding trade LCs. Additionally, the Company enters into stand-by letters of credit ("stand-by LCs") on an as-needed basis to secure merchandise and fund other general and administrative costs. As of November 1, 2014 and February 1, 2014, outstanding stand-by LCs totaled \$2.4 million and \$2.0 million, respectively.

9. Share-Based Compensation

The Company records the fair value of share-based payments to employees in the unaudited Consolidated Statements of Income and Comprehensive Income as compensation expense, net of forfeitures, over the requisite service period.

Share-Based Compensation Plans

The following summarizes our share-based compensation expense:

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013	November 1, 2014	November 2, 2013
	(in thousands)			
Restricted stock units and restricted stock	\$2,670	\$3,044	\$8,017	\$9,353
Stock options	1,369	2,135	6,289	6,662
Restricted shares (equity issued pre-IPO)	—	—	—	1
Total share-based compensation	\$4,039	\$5,179	\$14,306	\$16,016

The stock compensation related income tax benefit recognized by the Company during the thirteen and thirty-nine weeks ended November 1, 2014 was \$0.2 million and \$3.6 million, respectively. The stock compensation related income tax benefit recognized by the Company during the thirteen and thirty-nine weeks ended November 2, 2013 was \$1.2 million and \$3.4 million, respectively.

Stock Options

During the thirty-nine weeks ended November 1, 2014, the Company granted stock options under the Amended and Restated Express, Inc. 2010 Incentive Compensation Plan (the "2010 Plan"). The fair value of the stock options is determined using the Black-Scholes-Merton option-pricing model as described later in this note. Stock options granted in 2014 under the 2010 Plan vest 25% per year over four years or upon reaching retirement eligibility, defined as

providing 10 years of service and being at least 55 years old. These options have a 10 year contractual life. Options granted to the Chief Executive Officer in prior years vest ratably over three years. The expense for stock options is recognized using the straight-line attribution method.

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The Company's activity with respect to stock options during the thirty-nine weeks ended November 1, 2014 was as follows:

	Number of Shares	Grant Date Weighted Average Exercise Price Per Share	Weighted-Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
	(in thousands, except per share amounts and years)			
Outstanding, February 1, 2014	3,234	\$18.85		
Granted	378	\$15.86		
Exercised	—	\$—		
Forfeited or expired	(78)	\$19.64		
Outstanding, November 1, 2014	3,534	\$18.51	7.0	\$203
Expected to vest at November 1, 2014	1,180	\$18.45	8.3	\$95
Exercisable at November 1, 2014	2,306	\$18.56	6.3	\$103

The following provides additional information regarding the Company's stock options:

	Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013
	(in thousands, except per share amounts)	
Weighted average grant date fair value of options granted (per share)	\$8.51	\$9.49
Total intrinsic value of options exercised	\$—	\$904

As of November 1, 2014, there was approximately \$6.6 million of total unrecognized compensation expense related to stock options, which is expected to be recognized over a weighted average period of approximately 1.5 years.

The Company uses the Black-Scholes-Merton option-pricing model to value stock options granted to employees and directors. The Company's determination of the fair value of stock options is affected by the Company's stock price as well as a number of subjective and complex assumptions. These assumptions include the risk-free interest rate, the Company's expected stock price volatility over the term of the award, expected term of the award, and dividend yield.

The following assumptions were used in estimating the fair value of the stock options on the date of the grant:

	Thirty-Nine Weeks Ended		
	November 1, 2014	November 2, 2013	
Risk-free interest rate ⁽¹⁾	1.90	% 1.13	%
Price Volatility ⁽²⁾	54.7	% 55.9	%
Expected term (years) ⁽³⁾	6.25	6.20	
Dividend yield ⁽⁴⁾	—	—	

(1) Represents the yield on U.S. Treasury securities with a term consistent with the expected term of the stock options.

Beginning in May 2012, the Company began using its own volatility in addition to the historical volatility of selected comparable companies to estimate expected volatility. Comparable companies were selected primarily based on industry, stage of life cycle, and size. The historical lookback period is consistent with the expected term of the stock options.

(2) Calculated utilizing the "simplified" methodology prescribed by Staff Accounting Bulletin No. 107 due to the lack of historical exercise data necessary to provide a reasonable basis upon which to estimate the term.

(4) The Company does not currently plan on paying regular dividends.

Restricted Stock Units and Restricted Stock

During the thirty-nine weeks ended November 1, 2014, the Company granted restricted stock units (“RSUs”) under the 2010 Plan, including 0.5 million RSUs with performance conditions. The fair value of RSUs is determined based on the Company's stock price on the grant date. The expense for RSUs without performance conditions is recognized using the straight-line attribution method. The expense for RSUs with performance conditions is recognized using the graded vesting method based on the expected achievement of the performance conditions. The RSUs with performance conditions are also subject to time-

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based vesting. One-half of these RSUs that are earned based on the achievement of performance criteria will vest on the second anniversary of the date of the grant and the remainder will vest on the third anniversary of the date of the grant. RSUs without performance conditions vest ratably over four years.

The Company's activity with respect to RSUs and restricted stock for the thirty-nine weeks ended November 1, 2014 was as follows:

	Number of Shares	Grant Date Weighted Average Fair Value Per Share
	(in thousands, except per share amounts)	
Unvested, February 1, 2014	1,487	\$ 19.29
Granted*	756	\$ 15.72
Vested	(568)	) \$ 19.20
Forfeited	(58)	) \$ 18.11
Unvested, November 1, 2014	1,617	\$ 17.70

*There were approximately 0.5 million RSUs with two-year performance conditions granted in the first quarter of 2014. None of these RSUs are currently included as granted in the table above. The number of performance based RSUs that are ultimately earned may vary from 0% to 125% of target depending on the achievement of predefined financial performance targets.

The total fair value/intrinsic value of RSUs and restricted stock that vested during the thirty-nine weeks ended November 1, 2014 was \$10.9 million. As of November 1, 2014, there was approximately \$17.3 million of total unrecognized compensation expense related to unvested RSUs and restricted stock that is expected to be recognized over a weighted-average period of approximately 1.7 years.

10. Commitments and Contingencies

During 2013 and 2014, the Company received letters from two individuals claiming that the Company unlawfully collected their zip codes in connection with a retail purchase made at a Massachusetts Express store and thereafter used that information to send them unwanted marketing materials. These letters indicate that the individuals may file suit on behalf of a class of customers whose zip codes were collected and recorded at Company stores in Massachusetts in connection with credit card purchases, and claims that the Company used the collected zip code data to obtain customers' addresses for purposes of mailing them unwanted advertising material. These letters further seek monetary damages pursuant to a claim under Chapter 93A of the General Laws of Massachusetts. In the first quarter of 2014, after providing the claimants with information about the Company's collection practices, the Company received notice that one of the claimants will not pursue the claims previously alleged against the Company. The other claimant has not yet responded. The Company believes the allegations in the letters are without merit and intends to vigorously defend against any claims that are filed in court. Due to the uncertainties of litigation, it is reasonably possible that the Company may incur a loss related to these potential suits. However, the amount of such loss, if any, cannot be estimated as of the date these financial statements are issued.

From time to time the Company is subject to various other claims and contingencies arising in the normal course of business. Management believes that the ultimate liability arising from such other claims and contingencies, if any, is not likely to have a material adverse effect on the Company's results of operations, financial condition, or cash flows.

11. Guarantor Subsidiaries

On March 5, 2010, Express, LLC and Express Finance (the “Subsidiary Issuers”), both 100% owned indirect subsidiaries of Express, Inc., issued the Senior Notes. Express, Inc. (“Guarantor”) and certain of its indirect 100% owned subsidiaries (“Guarantor Subsidiaries”) have guaranteed, on a joint and several basis, the obligations under the Senior Notes. The guarantees are not full and unconditional because Guarantor Subsidiaries can be released and relieved of their obligations under certain customary circumstances contained in the indenture governing the Senior Notes. These circumstances include the following, so long as other applicable provisions of the indenture are adhered to: any sale or other disposition of all or substantially all of the assets of any Guarantor Subsidiary, any sale or other disposition of capital stock of any Guarantor Subsidiary, or the designation of any restricted subsidiary that is a Guarantor Subsidiary as an unrestricted subsidiary.

The following consolidating schedules present the condensed financial information on a combined basis.

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EXPRESS, INC.
 CONDENSED CONSOLIDATING BALANCE SHEET
 (Amounts in thousands)
 (Unaudited)

	November 1, 2014					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Assets						
Current assets						
Cash and cash equivalents	\$ 1,894	\$ 183,048	\$ 20,893	\$ 11,979	\$ —	\$ 217,814
Receivables, net	—	8,348	11,654	466	—	20,468
Inventories	—	23,346	321,218	5,705	—	350,269
Prepaid minimum rent	—	333	27,385	1,366	—	29,084
Intercompany receivable	—	36,604	—	5,784	(42,388)	—
Intercompany loan receivable	—	7,102	—	—	(7,102)	—
Other	346	34,872	7,012	500	(20,316)	22,414
Total current assets	2,240	293,653	388,162	25,800	(69,806)	640,049
Property and equipment, net	—	58,294	340,061	17,425	—	415,780
Tradename/domain name	—	197,822	—	—	—	197,822
Investment in subsidiary	508,879	443,155	—	503,094	(1,455,128)	—
Deferred tax assets	660	5,772	11,002	—	—	17,434
Other assets	—	6,172	807	6	—	6,985
Total assets	\$ 511,779	\$ 1,004,868	\$ 740,032	\$ 546,325	\$ (1,524,934)	\$ 1,278,070
Liabilities and stockholders' equity						
Current liabilities						
Accounts payable	\$ —	\$ 222,491	\$ 2,444	\$ 1,356	\$ —	\$ 226,291
Deferred revenue	—	840	19,225	183	—	20,248
Accrued expenses	—	42,468	63,166	1,036	(20,316)	86,354
Intercompany payable	—	5,784	36,604	—	(42,388)	—
Intercompany loan payable	—	—	—	7,102	(7,102)	—
Total current liabilities	—	271,583	121,439	9,677	(69,806)	332,893
Long-term debt	—	199,435	—	—	—	199,435
Deferred lease credits	—	4,664	116,335	7,162	—	128,161
Other long-term liabilities	—	26,092	79,704	6	—	105,802
Total liabilities	—	501,774	317,478	16,845	(69,806)	766,291
Commitments and contingencies (Note 10)						
Total stockholders' equity	511,779	503,094	422,554	529,480	(1,455,128)	511,779
Total liabilities and stockholders' equity	\$ 511,779	\$ 1,004,868	\$ 740,032	\$ 546,325	\$ (1,524,934)	\$ 1,278,070

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EXPRESS, INC.
CONDENSED CONSOLIDATING BALANCE SHEET
(Amounts in thousands)
(Unaudited)

	February 1, 2014					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Assets						
Current assets						
Cash and cash equivalents	\$ 1,984	\$ 283,707	\$ 19,631	\$ 6,562	\$ —	\$ 311,884
Receivables, net	—	10,410	5,880	1,094	—	17,384
Inventories	—	15,928	192,762	3,820	—	212,510
Prepaid minimum rent	—	689	26,658	1,207	—	28,554
Intercompany receivable	—	—	114,258	5,784	(120,042)	—
Intercompany loan receivable	—	28,080	—	—	(28,080)	—
Other	237	8,523	4,552	54	(237)	13,129
Total current assets	2,221	347,337	363,741	18,521	(148,359)	583,461
Property and equipment, net	—	56,922	301,684	17,516	—	376,122
Tradename/domain name	—	197,812	—	—	—	197,812
Investment in subsidiary	471,687	393,156	—	465,902	(1,330,745)	—
Deferred tax assets	661	6,637	10,182	78	—	17,558
Other assets	—	6,295	1,416	6	—	7,717
Total assets	\$ 474,569	\$ 1,008,159	\$ 677,023	\$ 502,023	\$ (1,479,104)	\$ 1,182,670
Liabilities and stockholders' equity						
Current liabilities						
Accounts payable	\$ —	\$ 150,420	\$ 2,873	\$ 1,443	\$ —	\$ 154,736
Deferred revenue	—	1,004	27,264	168	—	28,436
Accrued expenses	—	40,087	75,159	1,026	(237)	116,035
Intercompany payable	—	120,042	—	—	(120,042)	—
Intercompany loan payable	—	—	—	28,080	(28,080)	—
Total current liabilities	—	311,553	105,296	30,717	(148,359)	299,207
Long-term debt	—	199,170	—	—	—	199,170
Deferred lease credits	—	4,963	103,129	6,417	—	114,509
Other long-term liabilities	—	26,571	68,644	—	—	95,215
Total liabilities	—	542,257	277,069	37,134	(148,359)	708,101
Commitments and contingencies (Note 10)						
Total stockholders' equity	474,569	465,902	399,954	464,889	(1,330,745)	474,569
Total liabilities and stockholders' equity	\$ 474,569	\$ 1,008,159	\$ 677,023	\$ 502,023	\$ (1,479,104)	\$ 1,182,670

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EXPRESS, INC.

CONDENSED CONSOLIDATING STATEMENT OF INCOME AND COMPREHENSIVE INCOME

(Amounts in thousands)

(Unaudited)

	Thirteen Weeks Ended November 1, 2014					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Net sales	\$—	\$322,836	\$482,257	\$9,990	\$(317,475)	\$497,608
Cost of goods sold, buying and occupancy costs	—	255,582	394,738	7,205	(317,475)	340,050
Gross profit	—	67,254	87,519	2,785	—	157,558
Selling, general, and administrative expenses	139	46,338	76,685	3,364	—	126,526
Other operating income, net	—	(67)	) 544	31	—	508
Operating (loss) income	(139)	) 20,983	10,290	(610)	) —	30,524
Interest expense, net	—	5,150	892	—	—	6,042
(Income) loss in subsidiary	(14,665)	) (5,115)	) —	(14,665)	) 34,445	—
Other expense, net	—	(1)	) —	161	—	160
Income (loss) before income taxes	14,526	20,949	9,398	13,894	(34,445)	24,322
Income tax (benefit) expense	(59)	) 6,284	3,816	(304)	) —	9,737
Net income (loss)	\$14,585	\$14,665	\$5,582	\$14,198	\$(34,445)	\$14,585
Foreign currency translation	(600)	) (600)	) —	(1,200)	) 1,800	(600)
Comprehensive income (loss)	\$13,985	\$14,065	\$5,582	\$12,998	\$(32,645)	\$13,985

	Thirteen Weeks Ended November 2, 2013					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Net sales	\$—	\$319,989	\$487,697	\$8,902	\$(312,780)	\$503,808
Cost of goods sold, buying and occupancy costs	—	246,069	399,332	5,895	(312,753)	338,543
Gross profit	—	73,920	88,365	3,007	(27)	165,265
Selling, general, and administrative expenses	55	50,064	75,233	3,015	(1)	128,366
Other operating (income) expense, net	—	(180)	) 374	1	(26)	) 169
Operating (loss) income	(55)	) 24,036	12,758	(9)	) —	36,730
Interest expense (income), net	—	5,065	(208)	) 19	—	4,876
(Income) loss in subsidiary	(19,301)	) (7,775)	) —	(19,301)	) 46,377	—
Other expense, net	—	—	—	153	—	153
Income (loss) before income taxes	19,246	26,746	12,966	19,120	(46,377)	31,701
Income tax (benefit) expense	(21)	) 7,445	5,010	—	—	12,434
Net income (loss)	\$19,267	\$19,301	\$7,956	\$19,120	\$(46,377)	\$19,267
Foreign currency translation	26	26	—	54	(80)	26
Comprehensive income (loss)	\$19,293	\$19,327	\$7,956	\$19,174	\$(46,457)	\$19,293

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EXPRESS, INC.

CONDENSED CONSOLIDATING STATEMENT OF INCOME AND COMPREHENSIVE INCOME

(Amounts in thousands)

(Unaudited)

	Thirty-Nine Weeks Ended November 1, 2014					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Net sales	\$—	\$772,931	\$1,396,433	\$27,094	\$(756,778)	\$1,439,680
Cost of goods sold, buying and occupancy costs	—	613,713	1,133,002	18,787	(756,778)	1,008,724
Gross profit	—	159,218	263,431	8,307	—	430,956
Selling, general, and administrative expenses	648	135,564	226,438	8,659	—	371,309
Other operating expense (income), net	—	(52)	(455)	31	—	(476)
Operating (loss) income	(648)	23,706	37,448	(383)	—	60,123
Interest expense, net	—	15,815	2,065	—	—	17,880
(Income) loss in subsidiary	(26,923)	(20,725)	—	(26,923)	74,571	—
Other expense (income), net	—	3	—	154	—	157
Income (loss) before income taxes	26,275	28,613	35,383	26,386	(74,571)	42,086
Income tax (benefit) expense	(260)	1,690	14,360	(239)	—	15,551
Net income (loss)	\$26,535	\$26,923	\$21,023	\$26,625	\$(74,571)	\$26,535
Foreign currency translation	(116)	(116)	—	(232)	348	(116)
Comprehensive income (loss)	\$26,419	\$26,807	\$21,023	\$26,393	\$(74,223)	\$26,419

	Thirty-Nine Weeks Ended November 2, 2013					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Net sales	—	779,996	1,461,197	24,307	(762,255)	1,503,245
Cost of goods sold, buying and occupancy costs	—	574,603	1,186,593	15,715	(762,255)	1,014,656
Gross profit	—	205,393	274,604	8,592	—	488,589
Selling, general, and administrative expenses	286	129,825	222,070	7,984	—	360,165
Other operating (income) expense, net	—	(180)	(250)	15	—	(415)
Operating (loss) income	(286)	75,748	52,784	593	—	128,839
Interest expense (income), net	—	15,612	(1,197)	42	—	14,457
(Income) loss in subsidiary	(68,788)	(32,627)	—	(68,788)	170,203	—
Other expense, net	—	—	—	958	—	958
Income (loss) before income taxes	68,502	92,763	53,981	68,381	(170,203)	113,424
Income tax (benefit) expense	(111)	23,975	20,947	—	—	44,811
Net income (loss)	68,613	68,788	33,034	68,381	(170,203)	68,613
Foreign currency translation	242	242	—	486	(728)	242
Comprehensive income (loss)	68,855	69,030	33,034	68,867	(170,931)	68,855

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EXPRESS, INC.

CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

(Amounts in thousands)

(Unaudited)

	Thirty-Nine Weeks Ended November 1, 2014					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Operating Activities						
Net cash (used in) provided by operating activities	\$(483)	\$(71,241)	\$68,271	\$1,460	\$—	\$(1,993)
Investing Activities						
Capital expenditures	—	(16,633)	(67,014)	(2,924)	—	(86,571)
Distributions received	3,874	—	—	3,874	(7,748)	—
Purchase of intangible assets	—	(1,010)	—	—	—	(1,010)
Net cash provided by (used in) investing activities	3,874	(17,643)	(67,014)	950	(7,748)	(87,581)
Financing Activities						
Payments on lease financing obligations	—	(1,105)	—	—	—	(1,105)
Excess tax benefit from share-based compensation	—	42	5	—	—	47
Repurchase of common stock	(3,481)	—	—	—	—	(3,481)
Repayment of intercompany loan	—	2,205	—	(2,205)	—	—
Borrowings under intercompany loan	—	(9,043)	—	9,043	—	—
Distributions paid	—	(3,874)	—	(3,874)	7,748	—
Net cash (used in) provided by financing activities	(3,481)	(11,775)	5	2,964	7,748	(4,539)
Effect of exchange rate on cash	—	—	—	43	—	43
Net (decrease) increase in cash and cash equivalents	(90)	(100,659)	1,262	5,417	—	(94,070)
Cash and cash equivalents, beginning of period	1,984	283,707	19,631	6,562	—	311,884
Cash and cash equivalents, end of period	\$1,894	\$183,048	\$20,893	\$11,979	\$—	\$217,814

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EXPRESS, INC.
 CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
 (Amounts in thousands)
 (Unaudited)

	Thirty-Nine Weeks Ended November 2, 2013					
	Express, Inc.	Subsidiary Issuers	Guarantor Subsidiaries	Other Subsidiaries	Consolidating Adjustments	Consolidated Total
Operating Activities						
Net cash provided by (used in) operating activities	\$(86)	\$(15,994)	\$52,240	\$1,480	\$—	\$37,640
Investing Activities						
Capital expenditures	—	(21,497)	(51,651)	(5,624)	—	(78,772)
Distributions received	34,325	—	—	34,325	(68,650)	—
Purchase of intangible assets	—	(69)	—	—	—	(69)
Net cash provided by (used in) investing activities	34,325	(21,566)	(51,651)	28,701	(68,650)	(78,841)
Financing Activities						
Payments on leased financing obligations	—	(45)	—	—	—	(45)
Excess tax benefit from share-based compensation	—	201	—	—	—	201
Proceeds from exercise of stock options	4,426	—	—	—	—	4,426
Repayment of intercompany loan	—	5,806	—	(5,806)	—	—
Borrowings under intercompany loan	—	(11,459)	—	11,459	—	—
Repurchase of common stock	(37,905)	—	—	—	—	(37,905)
Distributions paid	—	(34,325)	—	(34,325)	68,650	—
Net cash (used in) provided by financing activities	(33,479)	(39,822)	—	(28,672)	68,650	(33,323)
Effect of exchange rate on cash	—	—	—	(220)	—	(220)
Net increase (decrease) in cash and cash equivalents	760	(77,382)	589	1,289	—	(74,744)
Cash and cash equivalents, beginning of period	938	230,174	22,924	2,261	—	256,297
Cash and cash equivalents, end of period	\$1,698	\$152,792	\$23,513	\$3,550	\$—	\$181,553

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12. Stockholders' Equity

Share Repurchase Programs

On May 28, 2014, the Company's Board of Directors (the "Board") authorized the repurchase of up to \$100.0 million of common stock (the "2014 Repurchase Program"). The 2014 Repurchase Program will be funded using available cash. For the thirteen and thirty-nine weeks ended November 1, 2014 there were no purchases made under the 2014 Repurchase Program.

On May 24, 2012, the Board authorized the repurchase of up to \$100.0 million of common stock (the "2012 Repurchase Program"). During the thirteen and thirty-nine weeks ended November 2, 2013, the Company repurchased 1.0 million and 1.6 million shares of its common stock under the 2012 Repurchase Program for a total of \$21.2 million and \$35.1 million, respectively, including commissions.

Stockholder Rights Plan

On June 12, 2014, the Board adopted a Stockholder Rights Plan (the "Rights Plan"). Under the Rights Plan, one right was distributed for each share of common stock outstanding at the close of business on June 23, 2014 and one right will be issued for each new share of common stock issued thereafter. If any person or group acquires 10% or more of the Company's outstanding common stock without the approval of the Board, there would be a triggering event entitling a registered holder to purchase from the Company one one-hundredth of a share of Participating Preferred Stock, par value \$0.01 per share, for \$70.00 subject to adjustment. Existing 10% or greater stockholders are grandfathered to the extent of their June 12, 2014 ownership levels. The Rights Plan will continue in effect until June 12, 2015, unless ratified by a majority vote of the Company's stockholders (in which case the Rights Plan will expire on June 12, 2017) or unless earlier redeemed or terminated by the Company, as provided in the Rights Plan. The rights have no voting or dividend privileges, and, unless and until they become exercisable, have no dilutive effect on the earnings of the Company.

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

The following discussion summarizes the significant factors affecting the consolidated operating results, financial condition, liquidity, and cash flows of the Company as of the dates and for the periods presented below. The following discussion and analysis should be read in conjunction with our Annual Report on Form 10-K for the year ended February 1, 2014 and our unaudited Consolidated Financial Statements and the related notes included in Item 1 of this Quarterly Report. This discussion contains forward-looking statements that are based on the beliefs of our management, as well as assumptions made by, and information currently available to, our management. Actual results could differ materially from those discussed in or implied by forward-looking statements as a result of various factors. See "Forward-Looking Statements."

Overview

Express is a specialty apparel and accessories retailer offering both women's and men's merchandise. We have over 30 years of experience offering a distinct combination of style and quality at an attractive value, targeting women and men between 20 and 30 years old. We offer our customers an assortment of fashionable apparel and accessories to address fashion needs across multiple wearing occasions, including work, casual, jeanswear, and going-out occasions.

The challenging retail environment, which included decreased traffic at retail stores and heightened promotional activity, continued into the third quarter of 2014. Comparable sales decreased 5% and earnings per share decreased by

approximately 26% compared to the third quarter of 2013. We believe that a portion of this can be attributed to the difficult macro retail environment, but there were also certain product offerings that did not resonate with our customers in both our women's and men's business. Looking forward, the Holiday season will be very important to us, as it is for many retailers, and we are committed to delivering compelling fashion with an appealing price/value proposition, maintaining high levels of discipline around our test and react strategy, and working to preserve our merchandise margins in the expected highly promotional environment.

Our third quarter 2014 results and near term plans with respect to our growth pillars are described below.

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Improve Productivity of Our Stores

For the third quarter of 2014, comparable sales (excluding e-commerce sales) declined 7% compared to an increase of 2% in the third quarter of 2013. Net sales per average gross square foot decreased from \$346 for the twelve months ended November 2, 2013 to \$321 for the twelve months ended November 1, 2014. Net sales per average gross square foot is determined by dividing net sales (excluding e-commerce sales, shipping and handling revenue related to e-commerce, gift card breakage, sell-off revenue, and franchise revenue) for the period by average gross square feet in operation during the period. Reversing these declines remains a primary focus for us and we plan to do this through targeted marketing and continued improvements in our product assortment. See "Results of Operations" below for additional information.

Optimization and Strategic Expansion of Our Store Base

In the third quarter of 2014, we opened four new Company-operated retail stores, all in the United States. We also opened nine factory outlet stores in the United States. As previously announced, we plan to close approximately 50 retail stores over the next 36 months, primarily when these stores' leases expire. We expect those closures to result in additional annual operating income of \$5 to \$8 million beginning in 2015, depending upon the amount of sales that transfer to other stores and e-commerce.

As of November 1, 2014, we operated 638 stores, including 29 factory outlet stores, compared to 628 stores at November 2, 2013 (which included no factory outlet stores). During the remainder of 2014, we expect to open five factory outlet stores in the United States. In addition, we expect to convert seven existing retail locations to factory outlet stores, while also closing three retail stores in the United States.

Expand Our e-Commerce Platform

In the third quarter of 2014, our e-commerce sales increased 11% compared to the third quarter of 2013. Looking ahead, we will continue to focus on improving our overall customer shopping experience. We plan to accomplish this through additional capabilities in our mobile app experience, and by making significant enhancements to our website with a focus on the shopping cart and checkout. We have already implemented several upgrades to our website designed to enhance the customer experience and drive incremental sales. We believe these improvements will make it easier for customers to find and buy the fashion looks and basics they desire. E-commerce sales represented 16% of our total net sales in the third quarter of 2014 compared to 14% in the third quarter of 2013.

Expand Internationally

At quarter end, we were earning revenue from 30 franchise locations, a net increase of seven stores from the third quarter of 2013. These included three shop-in-shop locations inside Edgars' department stores in South Africa. During the fourth quarter of 2014, we expect to open three to five additional franchise locations.

How We Assess the Performance of Our Business

In assessing the performance of our business, we consider a variety of performance and financial measures. These key measures include net sales, comparable sales and other individual store performance factors, gross profit, and selling, general, and administrative expenses.

Net Sales. Net sales reflects revenues from the sale of our merchandise, less returns and discounts, as well as sell-off revenue, shipping and handling revenue related to e-commerce, gift card breakage, and revenue earned from our franchise agreements.

Comparable Sales and Other Individual Store Performance Factors. Comparable sales are calculated based upon stores that were open at least thirteen full months as of the end of the reporting period and includes e-commerce sales and

store conversions that do not meet any of the criteria for exclusion that follow. A store is not considered a part of the comparable sales base if the square footage of the store changed by more than 20% due to remodel or relocation activities, or if we execute a phased remodel whereby a portion of the store is under construction and, therefore, that portion of the store is not productive selling space. Under the latter scenario, the store is excluded from comparable sales during the construction period only, and is then considered a comparable store when construction is complete. We also review sales per gross square foot, average unit retail price, units per transaction, average dollar sales per transaction, traffic, and conversion, among other things, to evaluate the performance of individual stores and on a company-wide basis.

Gross Profit. Gross profit is equal to net sales minus cost of goods sold, buying and occupancy costs. Gross margin measures gross profit as a percentage of net sales. Cost of goods sold, buying and occupancy costs includes the direct cost of purchased merchandise, inventory shrinkage, inventory adjustments, inbound freight to our distribution center, and outbound freight to our stores. It also includes merchandising, design, planning and allocation, manufacturing/production costs, occupancy costs

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related to store operations (such as rent, real estate taxes, landlord charges, common area maintenance, utilities, and depreciation on assets), and all logistics costs associated with our e-commerce business.

Our cost of goods sold, buying and occupancy costs increase in higher volume quarters because the direct cost of purchased merchandise is tied to sales. Buying and occupancy costs are largely fixed and do not necessarily increase as volume increases. Changes in the mix of our products, such as changes in the proportion of accessories, which are higher margin, may impact our overall cost of goods sold, buying and occupancy costs. We review our inventory levels on an on-going basis in order to identify slow-moving merchandise and generally use markdowns to clear such merchandise. The timing and level of markdowns are driven primarily by seasonality and customer acceptance of our merchandise. We primarily use third-party vendors to dispose of mark-out-of-stock merchandise. The primary drivers of merchandise costs are raw materials, labor in the countries where our merchandise is sourced, and logistics costs associated with transporting our merchandise.

Selling, General, and Administrative Expenses. Selling, general, and administrative expenses include all operating costs not included in cost of goods sold, buying and occupancy costs, except for certain items which are included in other operating (income) expense, net, such as proceeds received from insurance claims and gain/loss on disposal of assets. These costs include payroll and other expenses related to operations at our corporate home office, store expenses other than occupancy, and marketing expenses, which primarily include production, direct mail programs, media/print advertising costs, digital video marketing, and e-commerce expenses. With the exception of store payroll, certain marketing expenses, and incentive compensation, these expenses generally are fixed and do not vary proportionally with net sales. As a result, selling, general, and administrative expenses as a percentage of net sales is typically higher in lower volume quarters and lower in higher volume quarters.

Results of Operations

The Third Quarter of 2014 Compared to the Third Quarter of 2013

The table below sets forth the various line items in the unaudited Consolidated Statements of Income and Comprehensive Income as a percentage of net sales for the third quarter of 2014 and the third quarter of 2013.

	Thirteen Weeks Ended		
	November 1, 2014	November 2, 2013	
Net sales	100	% 100	%
Cost of goods sold, buying and occupancy costs	68	% 67	%
Gross profit	32	% 33	%
Selling, general, and administrative expenses	25	% 25	%
Other operating expense (income), net	—	% —	%
Operating income	6	% 7	%
Interest expense, net	1	% 1	%
Other expense, net	—	% —	%
Income before income taxes	5	% 6	%
Income tax expense	2	% 2	%
Net income	3	% 4	%

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Net Sales

	Thirteen Weeks Ended		
	November 1, 2014	November 2, 2013	
Net sales (in thousands)	\$497,608	\$503,808	
Comparable sales percentage change	(5	)% 5	%
Comparable sales percentage change (excluding e-commerce sales)	(7	)% 2	%
Gross square footage at end of period (in thousands)	5,611	5,494	
Number of:			
Stores open at beginning of period	628	621	
New retail stores	4	7	
New outlet stores	9	—	
Retail stores converted to outlets	—	—	
Closed stores	(3)	—
Stores open at end of period	638	628	

Net sales decreased approximately \$6.2 million, or 1%, compared to the third quarter of 2013. Comparable sales decreased 5% in the third quarter of 2014 compared to the third quarter of 2013. The decrease in comparable sales resulted from decreased store transactions and a decrease in average dollar sales per transaction. We attribute the decrease in store transactions to a continued decline in traffic at our retail stores and weakness in certain product categories, while the decrease in average dollar sales per transaction can be attributed to deeper discounting to sell through slower moving inventory. Non-comparable sales increased \$16.5 million, driven primarily by new outlet store openings.

Gross Profit

The following table shows cost of goods sold, buying and occupancy costs and gross profit in dollars for the stated periods:

	Thirteen Weeks Ended	
	November 1, 2014	November 2, 2013
	(in thousands)	
Cost of goods sold, buying and occupancy costs	\$340,050	\$338,543
Gross profit	\$157,558	\$165,265

The 110 basis point decrease in gross margin, or gross profit as a percentage of net sales, in the third quarter of 2014 compared to the third quarter of 2013 was comprised of a 140 basis point increase in buying and occupancy costs as a percentage of net sales partially offset by an increase in merchandise margin of 30 basis points. The increase in buying and occupancy costs was primarily the result of increased depreciation expense, which was impacted by the two flagship stores, as well as impairment charges of \$2.3 million related to leasehold improvements at certain underperforming stores. In addition, there was an increase in rent expense during the quarter primarily related to our new outlet stores, which was partially offset by store closures. The increase in merchandise margin was primarily driven by progress against our inventory related initiatives, specifically more prudent management of our fabric commitments resulting in fewer cancellation charges and reduced shrink.

Selling, General, and Administrative Expenses

The following table shows selling, general, and administrative expenses in dollars for the stated periods:

	Thirteen Weeks Ended	
	November 1, 2014	November 2, 2013
	(in thousands)	
Selling, general, and administrative expenses	\$126,526	\$128,366

The \$1.8 million decrease in selling, general, and administrative expenses in the third quarter of 2014 as compared to the third quarter of 2013 was primarily the result of decreased payroll related expenses of approximately \$3.8 million resulting from a

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decrease in performance related payroll costs and previously announced cost saving initiatives. These decreases were partially offset by a \$2.5 million increase in marketing expense primarily related to the LED sign at our Times Square store.

Interest Expense, Net

The following table shows interest expense, net in dollars for the stated periods:

	Thirteen Weeks Ended	
	November 1, 2014	November 2, 2013
	(in thousands)	
Interest expense, net	\$6,042	\$4,876

The \$1.2 million increase in interest expense results from the accounting rules related to our flagship stores in New York and San Francisco. These rules require a portion of the rent payments to be allocated to interest expense. We expect the interest expense related to our flagship stores to be approximately \$4.0 to \$5.0 million in the aggregate for 2014. Refer to Note 7 of the unaudited Consolidated Financial Statements for additional information.

Income Tax Expense

The following table shows income tax expense in dollars for the stated periods:

	Thirteen Weeks Ended	
	November 1, 2014	November 2, 2013
	(in thousands)	
Income tax expense	\$9,737	\$12,434

The effective tax rate was 40.0% for the third quarter of 2014 compared to 39.2% for the third quarter of 2013. We anticipate that our effective tax rate will be approximately 39% in 2014.

The Thirty-Nine Weeks Ended November 1, 2014 Compared to the Thirty-Nine Weeks Ended November 2, 2013
The table below sets forth the various line items in the unaudited Consolidated Statements of Income and Comprehensive Income as a percentage of net sales for the thirty-nine weeks ended November 1, 2014 and the thirty-nine weeks ended November 2, 2013.

	Thirty-Nine Weeks Ended		
	November 1, 2014	November 2, 2013	
Net sales	100	% 100	%
Cost of goods sold, buying and occupancy costs	70	% 67	%
Gross profit	30	% 33	%
Selling, general, and administrative expenses	26	% 24	%
Other operating (income) expense, net	—	% —	%
Operating income	4	% 9	%
Interest expense, net	1	% 1	%
Other expense, net	—	% —	%
Income before income taxes	3	% 8	%
Income tax expense	1	% 3	%
Net income	2	% 5	%

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Net Sales

	Thirty-Nine Weeks Ended			
	November 1, 2014	November 2, 2013		
Net sales (in thousands)	\$1,439,680	\$1,503,245		
Comparable sales percentage change	(7	)% 3		%
Comparable sales percentage change (excluding e-commerce sales)	(8)% —		%
Gross square footage at end of period (in thousands)	5,611	5,494		
Number of:				
Stores open at beginning of period	632	625		
New retail stores	9	12		
New outlet stores	29	—		
Retail stores converted to outlets	(15)	—	
Closed stores	(17	)	(9)
Stores open at end of period	638	628		

Net sales decreased approximately \$63.6 million, or 4%. Comparable sales decreased 7% for the thirty-nine weeks ended November 1, 2014 compared to the thirty-nine weeks ended November 2, 2013. The decrease in comparable sales resulted from decreases in store transactions, along with a slight decrease in in-store average dollar sales per transaction. We attribute these declines to a continued decrease in traffic, a heavily promotional retail environment, and weakness in certain product categories. Non-comparable sales increased \$30.6 million, driven primarily by new store openings, including outlets and flagship stores.

Gross Profit

The following table shows cost of goods sold, buying and occupancy costs and gross profit in dollars for the stated periods:

	Thirty-Nine Weeks Ended	
	November 1, 2014	November 2, 2013
Cost of goods sold, buying and occupancy costs	(in thousands) \$1,008,724	