CHARMING SHOPPES INC
Form 10-Q
June 08, 2007

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 May 5, 2007

Or

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

For the transition period from ______________ to _______________

Commission File No. 000-07258

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

PENNSYLVANIA (State or other jurisdiction of incorporation or organization)	**23-1721355** (I.R.S. Employer Identification No.)
450 WINKS LANE, BENSALEM, PA 19020 (Address of principal executive offices) (Zip Code)	**(215) 245-9100** (Registrant’s telephone number, including Area Code)

NOT APPLICABLE
(Former name, former address, and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (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 o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act):

Large Accelerated Filer x Accelerated Filer o Non-accelerated Filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes o No x

The number of shares outstanding of the issuer’s Common Stock (par value $.10 per share) as of June 4, 2007 was 128,605,982 shares.

CHARMING SHOPPES, INC. AND SUBSIDIARIES
TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

CHARMING SHOPPES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)	May 5, 2007 (Unaudited)	February 3, 2007
ASSETS		
Current assets		
Cash and cash equivalents	**$ 240,913**	$ 143,838
Available-for-sale securities	**300**	1,997
Accounts receivable, net of allowances of $5,627 and $5,083	**6,831**	33,366
Investment in asset-backed securities	**61,564**	60,643
Merchandise inventories	**469,508**	429,433
Deferred advertising	**20,701**	21,707
Deferred taxes	**5,573**	4,469
Prepayments and other	**139,010**	145,385
Total current assets	**944,400**	840,838
Property, equipment, and leasehold improvements – at cost	**1,026,396**	996,430
Less accumulated depreciation and amortization	**592,835**	573,984
Net property, equipment, and leasehold improvements	**433,561**	422,446
Trademarks and other intangible assets	**248,809**	249,490
Goodwill	**153,370**	153,370
Other assets	**54,789**	44,798
Total assets	**$ 1,834,929**	$ 1,710,942
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
4.75% Senior convertible notes	**$ 149,999**	$ 0
Accounts payable	**197,125**	178,629
Accrued expenses	**168,153**	190,702
Income taxes payable	**1,233**	0
Current portion – long-term debt	**10,134**	10,887
Total current liabilities	**526,644**	380,218
Deferred taxes	**56,944**	57,340
Other non-current liabilities	**164,492**	144,722
Long-term debt	**279,129**	181,124
Stockholders' equity		
Common Stock $.10 par value:		
Authorized – 300,000,000 shares		
Issued – 136,020,034 shares and 135,762,531 shares	**13,602**	13,576

Additional paid-in capital	**255,120**	285,159
Treasury stock at cost – 22,580,893 shares and 12,265,993 shares	**(215,238)**	(84,136)
Accumulated other comprehensive income/(loss)	**(2)**	1
Retained earnings	**754,238**	732,938
Total stockholders' equity	**807,720**	947,538
Total liabilities and stockholders' equity	**$ 1,834,929**	$ 1,710,942

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

See Notes to Condensed Consolidated Financial Statements

CHARMING SHOPPES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(Unaudited)

(In thousands, except per share amounts)	Thirteen Weeks Ended May 5, 2007	Thirteen Weeks Ended April 29, 2006
Net sales	**$ 784,712**	$ 734,922
Cost of goods sold, buying, catalog, and occupancy expenses	**546,197**	501,072
Selling, general, and administrative expenses	**195,620**	181,447
Total operating expenses	**741,817**	682,519
Income from operations	**42,895**	52,403
Other income	**1,330**	1,547
Interest expense	**(3,263)**	(4,124)
Income before income taxes	**40,962**	49,826
Income tax provision	**14,664**	17,765
Net income	**26,298**	32,061
Other comprehensive income, net of tax		
Unrealized (losses)/gains on available-for-sale securities, net of income tax benefit/(provision) of $1 in 2007 and ($2) in 2006	**(3)**	3
Comprehensive income	**$ 26,295**	$ 32,064
Basic net income per share	**$ .21**	$ .26
Diluted net income per share	**$ .20**	$ .24

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

See Notes to Condensed Consolidated Financial Statements

CHARMING SHOPPES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	Thirteen Weeks Ended May 5, 2007	Thirteen Weeks Ended April 29, 2006
Operating activities		
Net income	**$ 26,298**	$ 32,061
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	**22,744**	20,158
Deferred income taxes	**(395)**	(1,665)
Stock-based compensation	**2,924**	2,551
Excess tax benefits related to stock-based compensation	**(636)**	(2,035)
Net loss from disposition of capital assets	**460**	353
Net gain from securitization activities	**(193)**	(152)
Changes in operating assets and liabilities		
Accounts receivable, net	**26,535**	30,118
Merchandise inventories	**(40,075)**	(72,206)
Accounts payable	**18,496**	49,720
Deferred advertising	**1,006**	(953)
Prepayments and other	**4,625**	(11,127)
Income taxes payable	**1,869**	18,274
Accrued expenses and other	**(3,476)**	(6,160)
Net cash provided by operating activities	**60,182**	58,937
Investing activities		
Investment in capital assets	**(37,511)**	(23,854)
Gross purchases of securities	**(1,598)**	(3,251)
Proceeds from sales of securities	**2,563**	9,463
Increase in other assets	**(3,523)**	(7,042)
Net cash used by investing activities	**(40,069)**	(24,684)
Financing activities		
Proceeds from short-term borrowings	**5,383**	96,418
Repayments of short-term borrowings	**(5,383)**	(106,418)
Proceeds from issuance of senior convertible notes	**250,000**	0
Repayments of long-term borrowings	**(2,749)**	(3,766)
Payments of deferred financing costs	**(6,250)**	0
Excess tax benefits related to stock-based compensation	**636**	2,035
Purchase of hedge on senior convertible notes	**(82,250)**	0
Sale of common stock warrants	**49,050**	0
Purchases of treasury stock	**(131,102)**	0
Net proceeds/(payments) from shares issued under employee stock plans	**(373)**	2,223
Net cash provided/(used) by financing activities	**76,962**	(9,508)
Increase in cash and cash equivalents	**97,075**	24,745
Cash and cash equivalents, beginning of period	**143,838**	130,132

Cash and cash equivalents, end of period	**$**	**240,913**	$	154,877

See Notes to Condensed Consolidated Financial Statements

4

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Condensed Consolidated Financial Statements

We have prepared our condensed consolidated balance sheet as of May 5, 2007, our condensed consolidated statements of operations and comprehensive income for the thirteen weeks ended May 5, 2007 and April 29, 2006, and our condensed consolidated statements of cash flows for the thirteen weeks ended May 5, 2007 and April 29, 2006 without audit. In our opinion, we have made all adjustments (which include only normal recurring adjustments) necessary to present fairly our financial position, results of operations and comprehensive income, and cash flows. Certain prior-year amounts in the condensed consolidated statements of operations and comprehensive income have been reclassified to conform to the current-year presentation. We have condensed or omitted certain information and footnote disclosures normally included in financial statements prepared in accordance with United States generally accepted accounting principles. These financial statements and related notes should be read in conjunction with our financial statements and related notes included in our February 3, 2007 Annual Report on Form 10-K. The results of operations for the thirteen weeks ended May 5, 2007 and April 29, 2006 are not necessarily indicative of operating results for the full fiscal year.

As used in these notes, the terms "Fiscal 2008" and "Fiscal 2007" refer to our fiscal year ending February 2, 2008 and our fiscal year ended February 3, 2007, respectively. The term "Fiscal 2009" refers to our fiscal year ending January 31, 2009. The terms "Fiscal 2008 First Quarter" and "Fiscal 2007 First Quarter" refer to our fiscal quarters ended May 5, 2007 and April 29, 2006, respectively. The term "Fiscal 2008 Second Quarter" refers to our fiscal quarter ending August 4, 2007. The terms "the Company," "we," "us," and "our" refer to Charming Shoppes, Inc. and, where applicable, our consolidated subsidiaries.

Segment Reporting

We operate and report in two segments: Retail Stores and Direct-to-Consumer. We determine our operating segments based on the way our chief operating decision-makers review our results of operations. We also consider the similarity of economic characteristics, production processes, and operations in aggregating our operating segments. Accordingly, we have aggregated our retail stores and store-related E-commerce operations into a single reporting segment (the "Retail Stores" segment). Our catalog and catalog-related E-commerce operations are reported under the Direct-to-Consumer segment. The Retail Stores segment derives its revenues from sales through retail stores and store-related E-commerce sales under our LANE BRYANT® (including LANE BRYANT OUTLET™)**,** FASHION BUG®, CATHERINES PLUS SIZES®, and PETITE SOPHISTICATE® brands. The Direct-to-Consumer segment derives its revenues from catalog sales and catalog-related E-commerce sales under our Crosstown Traders catalogs. See **"Note 10. Segment Reporting"** below for further information regarding our segment reporting.

Stock-based Compensation

We have various stock-based compensation plans under which we are currently granting awards, which are more fully described in **"Item 8. Financial Statements and Supplementary Data; Note 11. Stock-Based Compensation Plans"** in our February 3, 2007 Annual Report on Form 10-K.

5

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 1. Condensed Consolidated Financial Statements (Continued)

Our 2003 Non-Employee Directors Compensation Plan provides for the grant of stock options, stock appreciation rights (“SARs”), restricted stock awards, restricted stock units (“RSUs”), or deferred shares of up to an aggregate total of 600,000 shares of our common stock to members of our Board of Directors that are not employed by the Company, provided that in no event may more than 50% of such shares be delivered in connection with “full-value awards.” The exercise price of options or SARs granted under the plan may not be less than the fair market value of our common stock on the date of grant. Non-employee directors may also elect to receive deferred shares of common stock of an equivalent market value instead of cash director’s fees. The plan provides for a one-time restricted stock award of 10,000 shares of common stock that vest in equal amounts over three years to a newly elected or appointed non-employee director. The plan also provides for annual grants of options for 7,500 shares of common stock that vest in one year and annual grants of 7,500 RSUs that vest in one year to each non-employee director serving at the date of our Annual Meeting of Shareholders. As of May 5, 2007, 203,671 shares were available for future grants under this plan.

Our 2004 Stock Award and Incentive Plan (the “2004 Plan”) provides for the grant of options (including both incentive and non-qualified stock options), restricted stock, SARS, restricted stock units, and a variety of other types of awards of up to an aggregate of 6,500,000 shares of our common stock plus shares remaining available under certain of our previous plans. Of the aggregate shares available, up to 2,000,000 shares may be issued in connection with “full-value” awards. Additional shares may be used for full-value awards by reducing the number of shares that remain available for options, SARs, and other non-full-value awards at a three-to-one ratio. The aggregate number of shares subject to awards granted under the 2004 Plan in any fiscal year will not exceed 2% of our common stock on a fully diluted basis as of the last day of the preceding fiscal year. As of May 5, 2007, 3,696,850 shares were available for future grants under this plan.

Our 1988 Key Employee Stock Option Plan provides for the grant of options to our key employees to purchase up to an aggregate total of 3,000,000 shares of our common stock. The exercise price of options granted under this plan is $1.00 per share. As of May 5, 2007, 101,807 shares were available for future grants under this plan.

The table below summarizes stock option activity for the thirteen weeks ended May 5, 2007:

	Option Shares	**Average Option Price**	**Option Prices Per Share**		
Outstanding at February 3, 2007	2,217,790	$ 5.82	$ 1.00	–	$ 13.84
Granted – option price less than market price	18,000	1.00	1.00	–	1.00
Canceled/forfeited	(4,254)	7.72	1.00	–	11.28
Exercised	(62,377)	5.38	1.00	–	8.46
Outstanding at May 5, 2007	2,169,159	$ 5.79	$ 1.00	–	$ 13.84
Exercisable at May 5, 2007	2,040,863	$ 5.80	$ 1.00	–	$ 13.84

The aggregate intrinsic value of options outstanding and options exercisable at May 5, 2007 (aggregate market value on May 5, 2007 less aggregate exercise price) was $14,140,000, and $13,284,000, respectively. The aggregate intrinsic value of options exercised during the Fiscal 2008 First Quarter was $432,000.

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 1. Condensed Consolidated Financial Statements (Continued)

Our 1994 Employee Stock Purchase Plan permits employees to purchase shares of our common stock during quarterly offering periods at a price equal to 85% of the lower of the stock's market price on the first day of, or the fifth business day after the end of, the offering period. Employees purchase shares through accumulation of payroll deductions of up to 10% of the employee's compensation during each offering period. An aggregate total of 2,000,000 shares are reserved for grant under this plan. As of May 5, 2007, 1,133,547 shares were available for future purchases under this plan.

Stock-based compensation expense for the thirteen weeks ended May 5, 2007 and April 29, 2006 includes (i) compensation cost for all partially-vested stock-based awards granted prior to the beginning of Fiscal 2007, based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123, *"Accounting for Stock-Based Compensation"* ("SFAS No. 123"), and (ii) compensation cost for all stock-based awards granted subsequent to the beginning of Fiscal 2007, based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123 (revised 2004), *"Share-Based Payment"* ("SFAS No. 123R"), a revision of SFAS No. 123. Current grants of stock-based compensation consist primarily of restricted stock and restricted stock unit awards.

We use the Black-Scholes valuation model to estimate the fair value of stock options, and amortize stock-based compensation on a straight-line basis over the estimated life of a stock option or the vesting period of an award. Estimates or assumptions we used under the Black-Scholes model are more fully described in **"Item 8. Financial Statements and Supplementary Data; Note 1. Summary of Significant Accounting Policies; *Stock-based Compensation*"** in our February 3, 2007 Annual Report on Form 10-K.

Total stock-based compensation recognized in our results of operations for the thirteen weeks ended May 5, 2007 and April 29, 2006 was $2,924,000 and $2,551,000, respectively. Total stock-based compensation not yet recognized, related to the non-vested portion of stock options and awards outstanding, was $23,636,000 as of May 5, 2007. The weighted-average period over which we expect to recognize this compensation is approximately 3.0 years.

Crosstown Traders Integration Plan

Concurrent with our acquisition of Crosstown Traders (see **"Item 8. Financial Statements and Supplementary Data; Note 2. Acquisition of Crosstown Traders, Inc."** in our February 3, 2007 Annual Report on Form 10-K), we prepared a formal integration plan for Crosstown Traders' operations that included exiting and consolidating certain activities of Crosstown Traders, lease terminations, severance, and certain other exit costs. As of January 28, 2006, we finalized the plan and recorded a liability for the costs of the plan, which we recorded as a component of the purchase price of the acquisition in accordance with FASB Emerging Issues Task Force ("EITF") Issue 95-3, *"Recognition of Liabilities in Connection with a Purchase Business Combination."*

Liabilities recorded in connection with the integration plan outstanding as of February 3, 2007, payments or settlements of these liabilities for the thirteen weeks ended May 5, 2007, and the remaining accrual as of May 5, 2007 were as follows:

(In thousands)	Balance at February 3, 2007	Thirteen Weeks Ended May 5, 2007 Payments/Settlements	Balance at May 5, 2007
Lease termination and related costs	$ 1,820	$ (219)	$ 1,601
Other costs	239	(72)	167
Total	$ 2,059	$ (291)	$ 1,768

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 2. Accounts Receivable

Accounts receivable consist of trade receivables from sales through our FIGI'S® catalog. Details of our accounts receivable are as follows:

(In thousands)	May 5, 2007	February 3, 2007
Due from customers	$ 12,458	$ 38,449
Allowance for doubtful accounts	(5,627)	(5,083)
Net accounts receivable	$ 6,831	$ 33,366

Note 3. Trademarks and Other Intangible Assets

(In thousands)	May 5, 2007	February 3, 2007
Trademarks, tradenames, and internet domain names	$ 241,988	$ 241,850
Customer lists, customer relationships, and covenant not to compete	16,400	16,400
Total at cost	258,388	258,250
Less accumulated amortization of customer lists, customer relationships, and covenant not to compete	9,579	8,760
Net trademarks and other intangible assets	$ 248,809	$ 249,490

Note 4. Short-term Borrowings and Long-term Debt

(In thousands)	May 5, 2007	February 3, 2007
Short-term borrowings		
4.75% Senior Convertible Notes, due June 2012(1)	$ 149,999	$ 0
Long-term debt		
1.125% Senior Convertible Notes, due May 2014	$ 250,000	$ 0
4.75% Senior Convertible Notes, due June 2012(1)	0	149,999
Capital lease obligations	10,814	12,853
6.07% mortgage note, due October 2014	11,542	11,696

6.53% mortgage note, due November 2012		7,700		8,050
7.77% mortgage note, due December 2011		8,350		8,496
Other long-term debt		857		917
Total long-term debt		289,263		192,011
Less current portion		10,134		10,887
Long-term debt	$	279,129	$	181,124

*(1) On April 30, 2007, we called these notes for redemption on June 4, 2007. As of June 4, 2007, holders of $149,956,000 aggregate principal amount of these notes had exercised their right to convert their notes into an aggregate of 15,145,556 shares of our common stock and the remaining notes were redeemed for cash (see "**Note 12. Subsequent Events**" below).*

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 4. Short-term Borrowings and Long-term Debt (Continued)

On April 30, 2007, we issued $250,000,000 in aggregate principal amount of 1.125% Senior Convertible Notes due May 1, 2014 (the "1.125% Notes") in a private offering for resale to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended. We received proceeds of approximately $243,750,000 from the issuance, net of underwriting fees of approximately $6,250,000. We included the underwriting fees in "Other assets," and are amortizing them to interest expense on an effective interest rate basis over seven years. The 1.125% Notes were issued at par plus accrued interest, if any, from April 30, 2007, and interest is payable semiannually in arrears on May 1 and November 1, beginning November 1, 2007. The 1.125% Notes will mature on May 1, 2014, unless earlier converted or repurchased by us.

The initial purchasers of the 1.125% Notes had the option to purchase up to an additional $25,000,000 in principal amount of notes from us to cover over-allotments, which was exercised on May 11, 2007. See **"Note 12. Subsequent Events"** below for information regarding the exercise of the over-allotment option.

Holders of the 1.125% Notes may convert their notes based on a conversion rate of 65.0233 shares of our common stock per $1,000 principal amount of notes (the equivalent of $15.379 per share), subject to adjustment upon certain events, only under the following circumstances as described in the Indenture for the 1.125% Notes (the "Indenture"): (1) during specified periods, if the price of our common stock reaches specified thresholds; (2) if the trading price of the 1.125% Notes is below a specified threshold; (3) at any time after November 15, 2013; or (4) upon the occurrence of certain corporate transactions.

Upon conversion, we intend to deliver an amount in cash equal to the lesser of the aggregate principal amount of notes to be converted and our total conversion obligation. If our conversion obligation exceeds the aggregate principal amount of the 1.125% Notes, we will deliver shares of our common stock in respect of the excess. However, we have the option, subject to the approval of our Board of Directors, to elect to satisfy our conversion obligation entirely in shares of our common stock. In connection with a "Fundamental Change" as defined in the Indenture, we also will deliver upon conversion of the notes additional shares of common stock as described in the Indenture. In addition, if we undergo a Fundamental Change before maturity of the 1.125% Notes, we may be required to repurchase for cash all or a portion of the 1.125% Notes at a repurchase price of 100% of the principal amount of the notes being repurchased, plus accrued and unpaid interest, including additional amounts, if any, up to but excluding the date of purchase. As of May 5, 2007, none of the conditions allowing holders of the 1.125% Notes to convert had been met.

We are required to file a shelf registration statement covering resales of the 1.125% Notes and the shares of our common stock issuable on conversion of the notes with the Securities and Exchange Commission ("SEC"). If we are not eligible to use an automatic shelf registration statement, we are required to use our reasonable efforts to cause the shelf registration statement to become effective no later than 210 days after the first date of original issuance of the notes. If we fail to meet these terms, we will be required to pay additional interest on the 1.125% Notes in an amount of up to 0.50% per annum. As of May 5, 2007, we expect to meet the terms of the registration requirements.

We accounted for the issuance of the 1.125% Notes in accordance with the guidance in EITF Issue 90-19, *"Convertible Bonds with Issuer Option to Settle for Cash upon Conversion"* and EITF Issue 00-19, *"Accounting for*

Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock." Accordingly, we have recorded the 1.125% Notes as long-term debt in our condensed consolidated balance sheet as of May 5, 2007.

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 4. Short-term Borrowings and Long-term Debt (Continued)

Concurrently with the issuance of the 1.125% Notes, we entered into privately negotiated common stock call options with affiliates of the initial purchasers. The call options allow us to purchase up to approximately 16,256,000 shares of our common stock (17,881,000 shares including exercise of the over-allotment option) at an initial strike price of $15.379 per share. The call options expire on May 1, 2014 and must be net-share settled. The cost of the call options prior to exercise of the over-allotment option was approximately $82,250,000.

In addition, we sold warrants to affiliates of certain of the initial purchasers whereby they have the option to purchase up to approximately 17,069,000 shares of our common stock (18,775,000 shares including exercise of the over-allotment option) at an initial strike price of $21.607 per share. The warrants expire on various dates from July 30, 2014 through December 18, 2014 and must be net-share settled. We received approximately $49,050,000 in cash proceeds from the sale of these warrants prior to exercise of the over-allotment option.

The call options are intended to reduce the potential dilution to our common stock upon conversion of the 1.125% Notes by effectively increasing the initial conversion price of the notes to $21.607 per share, representing a 73.0% conversion premium over the closing price of our common stock on April 30, 2007 of $12.49 per share.

Paragraph 11(a) of SFAS No. 133, *"Accounting for Derivative Instruments and Hedging Activities,"* provides that contracts issued or held by an entity that are both (1) indexed to the entity's own common stock and (2) classified in stockholders' equity in its statement of financial position are not considered to be derivative instruments under SFAS No. 133 if the provisions of EITF Issue 00-19 are met.

We accounted for the call options and warrants in accordance with the guidance in EITF Issue 00-19. The call options and warrants meet the requirements of EITF Issue 00-19 to be accounted for as equity instruments. Accordingly, the cost of the call options and the proceeds from the sale of the warrants are included in additional paid-in capital in our accompanying condensed consolidated balance sheet as of May 5, 2007. We used a portion of the net proceeds from the 1.125% Notes to pay the $33,200,000 net cost of the call options and warrants.

In accordance with SFAS No. 128, *"Earnings Per Share,"* the 1.125% Notes will have no impact on our diluted net income per share until the price of our common stock exceeds the conversion price of $15.379 per share because the principal amount of the 1.125% Notes will be settled in cash upon conversion. Prior to conversion, we will include the effect of the additional shares that may be issued if our common stock price exceeds $15.379 per share using the treasury stock method. For the first $1.00 by which the price of our common stock exceeds $15.379 per share, there would be dilution of approximately 1,093,000 shares. Further increases in the share price would result in additional dilution at a declining rate, such that a price of $21.607 per share would result in cumulative dilution of approximately 5,156,000 shares. Should the stock price exceed $21.607 per share, we would also include the dilutive effect of the additional potential shares that may be issued related to the warrants, using the treasury stock method. The 1.125% Notes and warrants would have a combined dilutive effect such that, for the first $1.00 by which the stock price exceeds $21.607 per share, there would be cumulative dilution of approximately 6,552,000 shares prior to conversion. Further increases in the share price would result in additional dilution at a declining rate.

The call options are not considered for purposes of the diluted net income per share calculation as their effect would be anti-dilutive. Upon conversion of the 1.125% Notes, the call options will serve to neutralize the dilutive effect of the notes up to a stock price of $21.607 per share. For the first $1.00 by which the stock price exceeds $21.607 per share, the call options would reduce the cumulative dilution of approximately 6,552,000 shares in the example above to approximately 833,000 shares upon conversion of the notes.

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 4. Short-term Borrowings and Long-term Debt (Continued)

The preceding calculations assume the exercise of the over-allotment option and assume that the average price of our common stock exceeds the respective conversion prices during the period for which diluted net income per share is calculated, and exclude any potential adjustments to the conversion ratio provided under the terms of the 1.125% Notes.

During the Fiscal 2008 First Quarter, we used $131,102,000 of the net proceeds from the issuance of the 1.125% Notes to repurchase approximately 10,315,000 shares of our common stock. We expect to use the remaining proceeds to repurchase additional shares of our common stock in the open market or in privately negotiated transactions, or for general corporate purposes.

On April 30, 2007, we called for redemption on June 4, 2007 our $149,999,000 outstanding aggregate principal amount of 4.75% Senior Convertible Notes Due 2012 (the "4.75% Notes"). As a result of the call for redemption, we classified the 4.75% Notes as short-term borrowings in our accompanying condensed consolidated balance sheet as of May 5, 2007. See **"Note 12. Subsequent Events"** below for information regarding the redemption of the 4.75% Notes.

Note 5. Stockholders' Equity

(Dollars in thousands)		**Thirteen Weeks Ended May 5, 2007**
Total stockholders' equity, beginning of period	$	947,538
Cumulative effect of adoption of FIN No. 48[1]		(4,998)
Net income		26,298
Issuance of common stock (149,808 shares), net of shares withheld for payroll taxes		(373)
Purchase of treasury shares (10,314,900 shares)		(131,102)
Sale of common stock warrants[2]		49,050
Purchase of common stock call options[2]		(82,250)
Stock-based compensation expense		2,924
Excess tax benefits related to stock-based compensation		636
Unrealized losses on available-for-sale securities, net of tax		(3)
Total stockholders' equity, end of period	$	807,720

*(1) See **"Note 8. Income Taxes"*** below.

(2) See ***"Note 4. Short-term Borrowings and Long-term Debt"*** above.

11

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 6. Customer Loyalty Card Programs

We offer our customers various loyalty card programs. Customers that join these programs are entitled to various benefits, including discounts and rebates on purchases during the membership period. Customers generally join these programs by paying an annual membership fee. We recognize revenue from these loyalty programs as sales over the life of the membership period based on when the customer earns the benefits and when the fee is no longer refundable. We recognize costs in connection with administering these programs as cost of goods sold when incurred. During the thirteen weeks ended May 5, 2007 and April 29, 2006, we recognized revenues of $5,702,000 and $4,070,000, respectively, in connection with our loyalty card programs.

Note 7. Net Income Per Share

	Thirteen Weeks Ended			
(In thousands, except per share amounts)		**May 5, 2007**		**April 29, 2006**
Basic weighted average common shares outstanding		123,003		121,813
Dilutive effect of assumed conversion of 4.75% Senior Convertible Notes		15,182		15,182
Dilutive effect of stock options and awards		1,753		2,432
Diluted weighted average common shares and equivalents outstanding		139,938		139,427
Net income	$	26,298	$	32,061
Decrease in interest expense from assumed conversion of 4.75% Senior Convertible Notes, net of income taxes		1,128		1,128
Net income used to determine diluted net income per share	$	27,426	$	33,189
Options with weighted average exercise price greater than market price, excluded from computation of net income per share:				
Number of shares		1		0
Weighted average exercise price per share	$	13.84	$	0.00

Our 1.125% Notes have no impact on our diluted net income per share until the price of our common stock exceeds the conversion price of $15.379 per share because we expect to settle the principal amount of the 1.125% Notes in cash upon conversion. The call options are not considered for purposes of the diluted net income per share calculation as their effect would be anti-dilutive. Should the price of our common stock exceed $21.607 per share, we would also include the dilutive effect of the additional potential shares that may be issued related to the warrants, using the treasury stock method. See **"Note 4. Short-term Borrowings and Long-term Debt"** above and **"Note 12. Subsequent**

Events" below for further information regarding the 1.125% Notes and related call options and warrants. and the conversion of our 4.75% Notes.

Note 8. Income Taxes

The effective income tax rate was 35.8% for the thirteen weeks ended May 5, 2007, as compared to 35.7% for the thirteen weeks ended April 29, 2006.

In July 2006, the FASB issued FASB Interpretation ("FIN") No. 48, *"Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109."* FIN No. 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN No. 48 also provides guidance on de-recognition, measurement, classification, interest and penalties, accounting in interim periods, expanded disclosures regarding tax uncertainties, and transition.

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 8. Income Taxes (Continued)

FIN No. 48 applies to all tax positions related to income taxes subject to SFAS No. 109, *"Accounting for Income Taxes."* Under FIN No. 48, recognition of a tax benefit occurs when a tax position is more-likely-than-not to be sustained upon examination, based solely on its technical merits. The recognized benefit is measured as the largest amount of benefit which is more-likely-than-not to be realized on ultimate settlement, based on a cumulative probability basis. A tax position failing to qualify for initial recognition is recognized in the first interim period in which it meets the FIN No. 48 recognition standard, or is resolved through negotiation, litigation, or upon expiration of the statute of limitations. De-recognition of a previously recognized tax position would occur if it is subsequently determined that the tax position no longer meets the more-likely-than-not threshold of being sustained. Differences between amounts recognized in balance sheets prior to the adoption of FIN No. 48 and amounts reported after adoption (except for items not recognized in earnings) are accounted for as a cumulative effect adjustment to retained earnings as of the date of adoption of FIN No. 48, if material.

We adopted the provisions of FIN No. 48 effective as of February 4, 2007. In accordance with FIN No. 48, we recognized a cumulative effect adjustment of $4,998,000, increasing our liability for unrecognized tax benefits, interest, and penalties and reducing the February 4, 2007 balance of retained earnings.

As of February 4, 2007, we had $44,203,000 of gross unrecognized tax benefits. If recognized, the portion of the liabilities for gross unrecognized tax benefits that would decrease our provision for income taxes and increase our net income is $15,106,000. We record interest and penalties related to unrecognized tax benefits in income tax expense. As of the date of adoption of FIN No. 48, we had accrued interest and penalties of $7,412,000. During the Fiscal 2008 First Quarter, there was no material change in either the unrecognized tax benefits or accrued interest and penalties. We do not expect that any of the previously unrecognized tax benefits or interest and penalties will materially increase or decrease within the next 12 months.

Our U.S. Federal income tax returns for Fiscal 2004 and beyond remain subject to examination by the U.S. Internal Revenue Service ("IRS"). The IRS is not currently examining any of our tax returns. We file returns in numerous state jurisdictions, with varying statutes of limitations. Our state tax returns for Fiscal 2003 and beyond, depending upon the jurisdiction, remain subject to examination. The statute of limitations on a limited number of returns for years prior to Fiscal 2003 has been extended by agreement between us and the particular state jurisdiction. The earliest year still subject to examination by state tax authorities is Fiscal 1999.

Note 9. Asset Securitization

Our FASHION BUG, CATHERINES, and PETITE SOPHISTICATE proprietary credit card receivables are originated by Spirit of America National Bank (the "Bank"), our wholly-owned credit card bank, which transfers its interest in the receivables to the Charming Shoppes Master Trust (the "Trust") through a separate and distinct special-purpose entity. The Trust is an unconsolidated qualified special-purpose entity ("QSPE"). Through Fiscal 2007, our Crosstown Traders apparel-related catalog proprietary credit card receivables, which we securitized subsequent to our acquisition of Crosstown Traders, were originated in a non-bank program by Crosstown Traders. Crosstown

Traders transferred its interest in the receivables to Catalog Receivables LLC, a separate and distinct unconsolidated QSPE, through a separate and distinct special-purpose entity. On February 5, 2007, the Bank acquired the account relationships of the Crosstown Traders catalog proprietary credit cards and all subsequent new receivables are originations of the Bank. This acquisition did not cause a change in the securitization entities used by the Crosstown Traders proprietary credit card program.

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 9. Asset Securitization (Continued)

The QSPEs can sell interests in these receivables on a revolving basis for a specified term. At the end of the revolving period, an amortization period begins during which the QSPEs make principal payments to the parties that have entered into the securitization agreement with the QSPEs. All assets of the QSPEs (including the receivables) are isolated and support the securities issued by those entities. Our asset securitization program is more fully described in **"Item 8. Financial Statements and Supplementary Data; Note 16. Asset Securitization"** in our February 3, 2007 Annual Report on Form 10-K.

Note 10. Segment Reporting

We operate and report in two segments, Retail Stores and Direct-to-Consumer. We determine our operating segments based on the way our chief operating decision-makers review our results of operations. We also consider the similarity of economic characteristics, production processes, and operations in aggregating our operating segments. Accordingly, we have aggregated our retail stores and store-related E-commerce operations into a single reporting segment (the "Retail Stores" segment). Our catalog and catalog-related E-commerce operations are separately reported under the Direct-to-Consumer segment.

The accounting policies of the segments are generally the same as those described in **"Item 8. Financial Statements and Supplementary Data; Note 1. Summary of Significant Accounting Policies"** in our February 3, 2007 Annual Report on Form 10-K. Our chief operating decision-makers evaluate the performance of our operating segments based on a measure of their contribution to operations, which consists of net sales less the cost of merchandise sold and certain directly identifiable and allocable operating costs. We do not allocate certain corporate costs, such as shared service costs, information systems support costs, and insurance costs to our Retail Stores or Direct-to-Consumer segments. For our Retail Stores segment, operating costs consist primarily of store selling, buying, and occupancy costs. For our Direct-to-Consumer segment, operating costs consist primarily of catalog development, production, and circulation costs, E-commerce advertising costs, and order processing costs. Other costs that are currently allocated to the segments include warehousing costs.

Corporate and Other includes unallocated general and administrative costs, shared service center costs, insurance costs, information systems support costs, corporate depreciation and amortization, corporate occupancy costs, the results of our proprietary credit card operations, and other non-routine charges. Operating contribution for the Retail Stores and Direct-to-Consumer segments less Corporate and Other net expenses equals income before interest and taxes.

Operating segment assets are those directly used in, or allocable to, that segment's operations. For the Retail Stores segment, operating assets consist primarily of inventories; the net book value of store facilities; and goodwill and intangible assets. For the Direct-to-Consumer segment, operating assets consist primarily of trade receivables; inventories; deferred advertising costs; the net book value of catalog operating facilities; and goodwill and intangible assets. Corporate and Other assets include corporate cash and cash equivalents; the net book value of corporate facilities; deferred income taxes; and other corporate long-lived assets.

CHARMING SHOPPES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Note 10. Segment Reporting (Continued)

Selected financial information for our operations by reportable segment and a reconciliation of the information by segment to our consolidated totals is as follows:

(In thousands)	Retail Stores	Direct-to-Consumer	Corporate and Other	Consolidated