CHRISTOPHER & BANKS CORP
Form 10-Q
July 07, 2005

# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

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# FORM 10-Q

**(Mark One)**

| | |
|---|---|
| ý | **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** |
| | **For the quarterly period ended May 28, 2005** |
| | **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. 0-19972**

# CHRISTOPHER & BANKS CORPORATION

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware**<br>(State or other jurisdiction of<br>incorporation or organization) | **06 - 1195422**<br>(I.R.S. Employer<br>Identification Number) |

**2400 Xenium Lane North, Plymouth, Minnesota**

(Address of principal executive offices)

**55441**

(Zip Code)

**(763) 551-5000**

(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** ý **NO** **o**

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

**YES** ý **NO** **o**

As of June 17, 2005, 35,847,176 shares of the registrant s common stock were outstanding.

**CHRISTOPHER & BANKS CORPORATION**

**FORM 10-Q QUARTERLY REPORT**

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**PART I**
**FINANCIAL INFORMATION**

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**CHRISTOPHER & BANKS CORPORATION**

**CONSOLIDATED CONDENSED BALANCE SHEET**

(Unaudited)

| | | May 28, 2005 | | February 26, 2005 | | May 29, 2004 (Restated) |
|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | |
| Current assets: | | | | | | |
| Cash and cash equivalents | $ | 31,535,282 | $ | 14,063,378 | $ | 6,891,470 |
| Short-term investments | | 34,765,866 | | 46,748,329 | | 80,754,522 |
| Accounts receivable | | 3,309,361 | | 3,744,488 | | 4,260,399 |
| Merchandise inventory, net | | 36,620,209 | | 40,525,008 | | 34,833,473 |
| Other current assets | | 7,968,002 | | 7,532,235 | | 3,395,084 |
| Total current assets | | 114,198,720 | | 112,613,438 | | 130,134,948 |
| | | | | | | |
| Property, equipment and improvements, net | | 112,758,722 | | 112,058,758 | | 99,694,838 |
| | | | | | | |
| Other assets: | | | | | | |
| Goodwill | | 3,587,052 | | 3,587,052 | | |
| Intangible assets | | 766,319 | | 793,611 | | |
| Other | | 208,472 | | 150,843 | | 144,525 |
| Total other assets | | 4,561,843 | | 4,531,506 | | 144,525 |
| | | | | | | |
| Total assets | $ | 231,519,285 | $ | 229,203,702 | $ | 229,974,311 |
| | | | | | | |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | | | | | |
| | | | | | | |
| Current liabilities: | | | | | | |
| Accounts payable | $ | 7,096,559 | $ | 12,323,298 | $ | 6,471,012 |
| Accrued salaries, wages and related expenses | | 6,745,549 | | 4,606,596 | | 5,612,559 |
| Other accrued liabilities | | 12,131,648 | | 14,125,942 | | 8,663,125 |
| Income taxes payable | | | | | | 5,768,246 |
| Total current liabilities | | 25,973,756 | | 31,055,836 | | 26,514,942 |
| | | | | | | |
| Other liabilities: | | | | | | |
| Deferred lease incentives | | 19,867,756 | | 20,648,042 | | 17,789,675 |
| Deferred rent obligations | | 8,595,966 | | 8,171,674 | | 6,991,909 |
| Other | | 5,125,930 | | 6,119,284 | | 3,915,918 |
| Total other liabilities | | 33,589,652 | | 34,939,000 | | 28,697,502 |
| | | | | | | |
| Commitments | | | | | | |
| | | | | | | |
| Stockholders equity: | | | | | | |
| Preferred stock $0.01 par value, 1,000,000 shares authorized, none outstanding | | | | | | |
| Common stock $0.01 par value, 74,000,000 shares authorized, 42,612,312, 42,503,590 and 42,287,696 shares issued and 35,827,576, 35,718,854 and 37,039,196 shares outstanding at May 28, 2005, February 26, 2005 and May 29, 2004, respectively | | 426,103 | | 425,047 | | 422,857 |
| Additional paid-in capital | | 61,900,296 | | 61,035,745 | | 59,785,881 |
| Retained earnings | | 170,205,572 | | 162,324,168 | | 149,645,243 |
| Common stock held in treasury, 6,784,736, 6,784,736 and 5,248,500 shares at cost at May 28, 2005, February 26, 2005 and May 29, 2004, respectively | | (60,576,094) | | (60,576,094) | | (35,092,114) |
| Total stockholders equity | | 171,955,877 | | 163,208,866 | | 174,761,867 |
| | | | | | | |
| Total liabilities and stockholders equity | $ | 231,519,285 | $ | 229,203,702 | $ | 229,974,311 |

The accompanying notes are an integral part of these unaudited consolidated condensed financial statements.

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**CHRISTOPHER & BANKS CORPORATION**

**CONSOLIDATED CONDENSED STATEMENT OF INCOME**

(Unaudited)

| | Three Months Ended | |
|---|---|---|
| | May 28, 2005 | May 29, 2004 (Restated) |
| Net sales | $ 122,678,256 | $ 102,625,442 |
| Cost of sales: | | |
| Merchandise, buying and occupancy, exclusive of depreciation and amortization shown separately below | 72,073,209 | 58,148,917 |
| Gross profit, exclusive of depreciation and amortization shown separately below | 50,605,047 | 44,476,525 |
| Selling, general and administrative | 31,292,276 | 24,652,970 |
| Depreciation and amortization | 4,476,474 | 3,735,973 |
| Operating income | 14,836,297 | 16,087,582 |
| Interest income | 326,815 | 257,680 |
| Income before income taxes | 15,163,112 | 16,345,262 |
| Income tax provision | 5,852,961 | 6,309,270 |
| Net income | $ 9,310,151 | $ 10,035,992 |
| Basic earnings per common share: | | |
| Net income | $ 0.26 | $ 0.27 |
| Basic shares outstanding | 35,746,372 | 37,506,305 |
| Diluted earnings per common share: | | |
| Net income | $ 0.26 | $ 0.26 |
| Diluted shares outstanding | 36,104,826 | 38,136,384 |
| Dividends per share | $ 0.04 | $ 0.04 |

The accompanying notes are an integral part of these unaudited consolidated condensed financial statements.

**CHRISTOPHER & BANKS CORPORATION**

**CONSOLIDATED CONDENSED STATEMENT OF CASH FLOWS**

(Unaudited)

| | Three Months Ended | |
|---|---|---|
| | **May 28, 2005** | **May 29, 2004 (Restated)** |
| Cash flows from operating activities: | | |
| Net income | $ 9,310,151 | $ 10,035,992 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 4,396,786 | 3,656,286 |
| Deferred income taxes | (969,319) | (85,828) |
| Income tax benefit on exercise of stock options | 449,248 | 92,255 |
| Stock-based compensation expense | 16,656 | |
| Loss on disposal of furniture, fixtures and equipment | 173,777 | 2,511 |
| Changes in operating assets and liabilities: | | |
| (Increase) decrease in merchandise inventory | 3,904,799 | (3,533,457) |
| (Increase) decrease in accounts receivable | 435,127 | (1,007,398) |
| Increase in other current assets | (380,114) | (405,031) |
| Increase in other assets | (57,629) | (62,250) |
| Decrease in accounts payable | (5,509,779) | (784,655) |
| Increase in accrued liabilities | 144,659 | 6,565,198 |
| Increase (decrease) in deferred lease incentives | (780,286) | 960,631 |
| Increase in deferred rent obligations | 424,292 | 487,926 |
| Net cash provided by operating activities | 11,558,368 | 15,922,180 |
| Cash flows from investing activities: | | |
| Purchases of property, equipment and improvements | (5,039,883) | (6,050,955) |
| Proceeds from sale of furniture, fixtures and equipment | | 1,300 |
| Purchases of short-term investments | (6,894,829) | (35,822,798) |
| Redemptions of short-term investments | 18,877,292 | 27,912,301 |
| Net cash provided by (used in) investing activities | 6,942,580 | (13,960,152) |
| Cash flows from financing activities: | | |
| Exercise of stock options | 399,703 | 386,969 |
| Dividends paid | (1,428,747) | (1,513,366) |
| Acquisition of common stock held in treasury | | (9,899,176) |
| Net cash used in financing activities | (1,029,044) | (11,025,573) |
| Net increase (decrease) in cash and cash equivalents | 17,471,904 | (9,063,545) |
| Cash and cash equivalents at beginning of period | 14,063,378 | 15,955,015 |
| Cash and cash equivalents at end of period | $ 31,535,282 | $ 6,891,470 |
| Supplemental cash flow information: | | |
| Income taxes paid | $ 7,013,687 | $ 445,300 |
| Purchases of equipment and improvements, included in accounts payable at end of period | $ 283,040 | $ 432,380 |

The accompanying notes are an integral part of these unaudited consolidated condensed financial statements.

**CHRISTOPHER & BANKS CORPORATION**

**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

(Unaudited)

**NOTE 1 BASIS OF PRESENTATION**

The unaudited consolidated condensed financial statements included in this Form 10-Q have been prepared by Christopher & Banks Corporation and subsidiaries (the Company ) pursuant to the rules and regulations of the United States Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed, or omitted, pursuant to such rules and regulations. These unaudited consolidated condensed financial statements should be read in conjunction with the financial statements and related notes included in the Company s Annual Report on Form 10-K for the fiscal year ended February 26, 2005.

The results of operations for the interim periods shown in this report are not necessarily indicative of results to be expected for the fiscal year. In the opinion of management, the information contained herein reflects all adjustments necessary to make the results of operations for the interim periods a fair statement of such operations. All such adjustments are of a normal recurring nature.

**NOTE 2 RESTATEMENT OF PRIOR YEAR FINANCIAL STATEMENTS**

As disclosed in Note 2 to the consolidated financial statements in Item 8 of the Company s fiscal 2005 Annual Report on Form 10-K, the Company restated its prior year financial statements to correct errors in certain lease-related accounting practices. The following tables present a summary of the effects of the restatement on the Company s consolidated condensed financial statements for the first quarter of fiscal 2005:

| | Consolidated Condensed Balance Sheet | | |
|---|---|---|---|
| | Previously Reported | Adjustments | Restated |
| **May 29, 2004** | | | |
| Property, equipment and improvements, net | $ 81,905,163 | $ 17,789,675 | $ 99,694,838 |
| Deferred lease incentives | | 17,789,675 | 17,789,675 |
| Deferred rent obligations | 3,279,673 | 3,712,236 | 6,991,909 |
| Deferred income taxes | 5,003,529 | (1,432,924) | 3,570,605 |
| Retained earnings | 151,924,555 | (2,279,312) | 149,645,243 |

| | Consolidated Condensed Statement of Income | | |
|---|---|---|---|
| | Previously Reported | Adjustments | Restated |
| **Three Months Ended May 29, 2004** | | | |
| Merchandise, buying and occupancy | $ 58,515,443 | $ (366,526) | $ 58,148,917 |
| Depreciation and amortization | 3,147,096 | 588,877 | 3,735,973 |
| Operating income | 16,309,933 | (222,351) | 16,087,582 |
| Income before income taxes | 16,567,613 | (222,351) | 16,345,262 |
| Income tax provision | 6,395,098 | (85,828) | 6,309,270 |
| Net income | 10,172,515 | (136,523) | 10,035,992 |
| | | | |
| Basic earnings per share | $ 0.27 | $ | $ 0.27 |
| Diluted earnings per share | $ 0.27 | $ (0.01) | $ 0.26 |

| | Consolidated Condensed Statement of Cash Flows | | |
|---|---|---|---|
| | Previously Reported | Adjustments | Restated |
| **Three Months Ended May 29, 2004** | | | |
| Net cash provided by operating activities | $ 14,372,672 | $ 1,549,508 | $ 15,922,180 |
| Net cash used in investing activities | (12,410,644) | (1,549,508) | (13,960,152) |

**NOTE 3 SHORT-TERM INVESTMENTS**

Short-term investments consisted of the following:

| Description | Maturity Dates | | May 28, 2005 | | February 26, 2005 | | May 29, 2004 |
|---|---|---|---|---|---|---|---|
| Corporate debt securities | Within one year | $ | 17,765,866 | $ | 25,748,329 | $ | 31,854,522 |
| Auction rate securities | Variable | | | | 4,000,000 | | 31,900,000 |
| U.S. Government debt securities | Two to three years, callable within one year | | 17,000,000 | | 17,000,000 | | 17,000,000 |
| | | $ | 34,765,866 | $ | 46,748,329 | $ | 80,754,522 |

**NOTE 4 MERCHANDISE INVENTORY, NET**

Merchandise inventory, net consisted of the following:

| Description | May 28, 2005 | February 26, 2005 | May 29, 2004 |
|---|---|---|---|
| Merchandise - in store | $ 29,850,748 | $ 31,950,213 | $ 25,891,369 |
| Merchandise - in transit | 7,222,527 | 9,400,419 | 9,206,120 |
| Allowance for permanent markdowns | (453,066) | (825,624) | (264,016) |
| | $ 36,620,209 | $ 40,525,008 | $ 34,833,473 |

The Company purchased approximately 22% and 30% of its merchandise from its largest overseas supplier during the first three months of fiscal 2006 and 2005, respectively.

**NOTE 5 PROPERTY, EQUIPMENT, AND IMPROVEMENTS, NET**

Property, equipment and improvements, net consisted of the following:

| Description | Estimated Useful Life | May 28, 2005 | February 26, 2005 | May 29, 2004 (Restated) |
|---|---|---|---|---|
| Land | | $ 1,596,898 | $ 1,596,898 | $ 1,596,898 |
| Corporate office, distribution center and related building improvements | 25 years | 10,783,627 | 10,783,627 | 8,742,060 |
| Store leasehold improvements | Term of related lease, typically 10 years | 67,279,026 | 67,175,045 | 57,273,795 |
| Store furniture and fixtures | Three to 10 years | 76,397,624 | 76,402,663 | 63,245,521 |
| Point of sale hardware and software | Five years | 7,189,361 | 7,028,545 | 6,455,204 |
| Corporate office and distribution center furniture, fixtures and equipment | Seven years | 2,640,722 | 2,352,583 | 2,248,672 |
| Computer hardware and software | Three to five years | 3,761,646 | 3,576,101 | 3,101,215 |
| Construction in progress | | 7,144,020 | 3,064,048 | 6,956,688 |
| | | 176,792,924 | 171,979,510 | 149,620,053 |
| Less accumulated depreciation and amortization | | 64,034,202 | 59,920,752 | 49,925,215 |
| Net property, equipment and improvements | | $ 112,758,722 | $ 112,058,758 | $ 99,694,838 |

**NOTE 6 GOODWILL**

The changes in the carrying amount of goodwill for the three months ended May 28, 2005 were as follows:

| | | |
|---|---|---|
| Balance as of February 26, 2005 | $ | 3,587,052 |
| Impairment charges | | |
| Balance as of May 28, 2005 | $ | 3,587,052 |

**The Company recognizes the excess cost of an acquired entity over the net amount assigned to assets acquired and liabilities assumed as goodwill. Goodwill will be tested for impairment on an annual basis in the fourth quarter and between annual tests whenever impairment is indicated. Fair values are calculated based on an estimate of future cash flows, compared to the corresponding carrying value of the acquired entity, including goodwill. Impairment losses will be recognized whenever the implied fair value is less than the carrying value of the related asset.**

**NOTE 7 INTANGIBLES**

**Intangible assets consisted of the following at May 28, 2005:**

| | | Amount |
|---|---|---|
| Customer lists | $ | 830,000 |
| Accumulated amortization | | (63,681) |
| | $ | 766,319 |

Aggregate amortization expense for the three months ended May 28, 2005 was $27,292. Estimated aggregate amortization expense for fiscal 2006 and the next five fiscal years is as follows:

| | | |
|---|---|---|
| Fiscal 2006 | $ | 109,167 |
| Fiscal 2007 | | 109,167 |
| Fiscal 2008 | | 100,278 |
| Fiscal 2009 | | 82,500 |
| Fiscal 2010 | | 82,500 |
| Fiscal 2011 | | 82,500 |

**NOTE 8 ACCRUED LIABILITIES**

Other accrued liabilities consisted of the following:

| **Description** | **May 28, 2005** | **February 26, 2005** | **May 29, 2004** |
|---|---|---|---|
| Gift card, certificate and store credit liability | $ 6,511,219 | $ 8,523,420 | $ 4,917,176 |
| Accrued occupancy related expenses | 1,072,946 | 1,340,403 | 1,034,511 |
| Other accrued liabilities | 4,547,483 | 4,262,119 | 2,711,438 |
| | $ 12,131,648 | $ 14,125,942 | $ 8,663,125 |

**NOTE 9 LONG-TERM DEBT**

The Company maintains an Amended and Restated Revolving Credit and Security Agreement with Wells Fargo Bank, National Association (the Wells Fargo Revolver ) which expires on June 30, 2006. The Wells Fargo Revolver provides the Company with revolving credit loans and letters of credit of up to $40.0 million, subject to a borrowing base formula based on inventory levels.

Loans under the Wells Fargo Revolver bear interest at Wells Fargo s base rate, 6.0% as of May 28, 2005, plus 0.25%. Interest is payable monthly in arrears. The Wells Fargo Revolver carries a facility fee of 0.25% based on the unused portion as defined in the agreement. Facility fees totaled $1,305 for the three months ended May 28, 2005. The credit facility is collateralized by the Company s equipment, general intangibles, inventory, inventory letters of credit and letter of credit rights. The Company had no revolving credit loan borrowings under the Wells Fargo Revolver during the first three months of fiscal 2006. Historically, the Wells Fargo Revolver has been utilized by the Company only to open letters of credit to facilitate the import of merchandise. The borrowing base at May 28, 2005 was $29.3 million. As of May 28, 2005, the Company had outstanding letters of credit in the amount of $18.6 million. Accordingly, the availability of revolving credit loans under the Wells Fargo Revolver was $10.7 million at May 28, 2005.

The Wells Fargo Revolver contains certain restrictive covenants including restrictions on incurring additional indebtedness and limitations on certain types of investments, as well as requiring the maintenance of certain financial covenants. As of May 28, 2005, the most recent measurement date, the Company was in compliance with all covenants of the Wells Fargo Revolver.

**NOTE 10 NET INCOME PER SHARE**

Basic earnings per share ( EPS ) is computed based on the weighted average number of shares of common stock outstanding during the applicable periods, while diluted EPS is computed based on the weighted average number of common and common equivalent shares (dilutive stock options) outstanding.

The following is a reconciliation of the number of shares and per share amounts used in the basic and diluted EPS computations:

| | Three Months Ended | | | |
|---|---|---|---|---|
| | May 28, 2005 | | May 29, 2004 | |
| | Shares | Net Income | Shares | Net Income (Restated) |
| Basic EPS | 35,746,372 | $ 0.26 | 37,506,305 | $ 0.27 |
| Effect of dilutive stock options | 358,454 | 0.00 | 630,079 | (0.01) |
| Diluted EPS | 36,104,826 | $ 0.26 | 38,136,384 | $ 0.26 |

Stock options of 2,664,149 and 1,513,349 were excluded from the shares used in the computation of diluted EPS for the three months ended May 28, 2005 and May 29, 2004, respectively, as they were anti-dilutive.

**NOTE 11 STOCK-BASED COMPENSATION**

The Company discloses stock-based compensation information in accordance with Statement of Financial Accounting Standards No. 123 ( SFAS No. 123 ), Accounting for Stock Based Compensation, and No. 148 ( SFAS No. 148 ), Accounting for Stock Based Compensation Transition and Disclosure. SFAS No. 148, an amendment of SFAS No. 123, does not amend the provisions of SFAS No. 123 that permit entities to account for stock-based compensation under the intrinsic value method set forth by Accounting Principles Board Opinion No. 25 ( APB No. 25 ), Accounting for Stock Issued to Employees. The Company has elected to continue to recognize compensation cost for its stock-based compensation plans in accordance with APB No. 25. No compensation expense for stock options has been recognized as all options granted had an exercise price equal to the market value of the underlying stock on the date of grant. The Company recognizes compensation expense related to restricted stock awards on the basis of the fair value of the stock, amortized over the vesting period.

During the first quarter of fiscal 2006, the Company awarded 19,000 shares of restricted stock to an employee. A restricted stock award is an award of common stock shares that is subject to certain restrictions during a specified period. The Company holds the shares during the vesting period and the grantee cannot transfer the shares before the termination of that period. The grantee is, however, entitled to vote the common shares and to receive dividends and other distributions on the shares.

If stock-based compensation cost had been determined based on the fair value methodology prescribed by SFAS No. 123 and SFAS No. 148, the Company s net earnings and earnings per share would have been reduced to the pro forma amounts indicated in the following table.

| | Three Months Ended | | | |
|---|---|---|---|---|
| | | May 28, 2005 | | May 29, 2004 (Restated) |
| Net income - as reported | $ | 9,310,151 | $ | 10,035,992 |
| Add stock-based compensation expense included in net income, net of related tax effects | | 10,227 | | |
| Less total stock-based compensation expense determined under fair value method, net of related tax effects | | 710,252 | | 816,723 |
| Net income - pro forma | $ | 8,610,126 | $ | 9,219,269 |
| | | | | |
| Basic earnings per common share: | | | | |
| As reported | $ | 0.26 | $ | 0.27 |
| Pro forma | $ | 0.24 | $ | 0.25 |
| | | | | |
| Diluted earnings per common share: | | | | |
| As reported | $ | 0.26 | $ | 0.26 |
| Pro forma | $ | 0.24 | $ | 0.24 |

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. Option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. As the Company s employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management s opinion the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

**NOTE 12 RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

In December 2004, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standard ( SFAS ) No. 123R, Share-Based Payment, which is a revision of SFAS No. 123, Accounting for Stock-Based Compensation. The original effective date for adoption of SFAS No. 123R for the Company was August 28, 2005. However, in April 2005 the SEC announced the adoption of a new rule that amends the effective date for SFAS No. 123R. The SEC s new rule allows companies to implement SFAS No. 123R at the beginning of their next fiscal year, instead of the next reporting period, that begins after June 15, 2005. Therefore, the Company plans to adopt SFAS No. 123R effective for its 2007 fiscal year, which commences on February 26, 2006.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections. SFAS No. 154 replaces Accounting Principles Board Opinion No. 20, Accounting Changes, and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements, and changes the requirements for the accounting for and reporting of a change in accounting principle. SFAS No. 154 applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. When a pronouncement includes specific transition provisions, those provisions should be followed. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Company will adopt SFAS No. 154 effective for its 2007 fiscal year, which commences on February 26, 2006. The adoption of SFAS No. 154 is expected to have no impact on the Company s financial position or results of operations.

**ITEM 2.**
**MANAGEMENT S DISCUSSION AND ANALYSIS OF**

**FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

(Unaudited)

**The following management s discussion and analysis of financial condition and results of operations ( MD&A ) should be read in conjunction with the consolidated financial statements and notes included in Item 1 of this Form 10-Q. As discussed in Note 2 to the consolidated condensed financial statements, the Consolidated Condensed Balance Sheet as of May 29, 2004 and the Consolidated Condensed Statements of Income and of Cash Flows for the three months ended May 29, 2004 have been restated for the effects of an error in the Company s method of accounting for leases. This MD&A gives effect to the restatement.**

**Executive Summary - Key Performance Indicators**

The Company s management evaluates the following items, which are considered key performance indicators, in assessing the Company s performance:

*Same-store sales*

The Company s same-store sales data is calculated based on the change in net sales for stores that have been open for more than 13 full months and includes stores, if any, that have been relocated within the same mall. The Company typically does not expand or relocate stores within a mall. Stores where square footage has been changed by more than 25 percent are excluded from the same-store sales calculation. Stores closed during the year are included in the same-store sales calculation only for the full months of the year the stores were open.

Management considers same-store sales to be an important indicator of the Company s performance. Same-store sales results are important in achieving leveraging of costs, including store payroll, store occupancy, depreciation and other general and administrative expenses. Positive same-store sales contribute to greater leveraging of costs while negative same-store sales contribute to deleveraging of costs. Same-store sales also have a direct impact on the Company s total net sales, cash and cash equivalents and working capital.

*Gross profit*

Gross profit measures whether the Company is appropriately optimizing the price of its merchandise. Gross profit is the difference between net sales and costs of sales. Cost of sales include the cost of merchandise, markdowns, shrink, freight into and out from the Company s distribution center, buyer and distribution center salaries, buyer travel, rent and other occupancy related costs, miscellaneous merchandise expenses and other costs related to the Company s distribution network. Any inability to obtain acceptable levels of initial markups or any significant increase in the Company s markdowns could have an adverse effect on the Company s gross profit and results of operations.

*Operating income*

The Company s management views operating income as a key indicator of the Company s success. The key drivers of operating income are same-store sales, gross profit and the Company s ability to control operating costs.

*Store productivity*

Store productivity, including sales per square foot, average unit retail price, number of transactions per store and number of units per transaction, is evaluated by management in assessing the operational performance of the Company.

*Inventory turnover*

The Company s management evaluates inventory turnover as a measure of how productively inventory is bought and sold. Inventory turnover is important as it can signal slow moving inventory, which can be critical in determining the need to take markdowns on merchandise.

*Cash flow and liquidity*

Management evaluates cash flow from operations, investing activities and financing activities in determining the sufficiency of the Company s cash position. Cash flow from operations has historically been sufficient to cover the Company s uses of cash. Management believes that cash flow from operations will be sufficient to fund anticipated capital expenditures and working capital requirements in fiscal 2006.

**Executive Overview**

Christopher & Banks Corporation is a Minneapolis-based retailer of women s specialty apparel, which operates stores through its wholly-owned subsidiaries; Christopher & Banks, Inc., Christopher & Banks Company and Christopher & Banks Services Company, collectively referred to as the Company. As of June 17, 2005, the Company operated 660 stores in 45 states including 478 Christopher & Banks stores, 161 C.J. Banks stores and 21 Acorn stores. The Company s Christopher & Banks stores offer distinctive fashions featuring exclusively designed, coordinated assortments of sportswear and sweaters in sizes four to 16. The Company s C.J. Banks stores offer similar assortments of women s specialty apparel in sizes 14W and up. Acorn offers upscale women s fashions along with complementary jewelry and accessories under private and branded labels.

In the first three months of fiscal 2006, the Company opened 12 new Christopher & Banks stores, six new C.J. Banks stores and one new Acorn store. The Company closed one store during the first quarter. In the second and third quarters of fiscal 2006, the Company anticipates it will open approximately 56 additional new stores for a total of approximately 75 new store openings in fiscal 2006. The Company plans to grow its store base by 12 to 15% in fiscal 2007.

**Critical Accounting Policies and Estimates**

The Company s critical accounting policies are more fully described in Note 1 of the notes to consolidated financial statements contained within the Company s Annual Report on Form 10-K. Management s discussion and analysis of the Company s financial condition and results of operations are based upon the Company s consolidated condensed financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America.

On an ongoing basis, the Company evaluates its estimates, including those related to customer product returns, inventories, income taxes, medical claims and contingencies. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. There have been no material changes in the Company s critical accounting policies during the quarter ended May 28, 2005.

**Results of Operations**

The following table sets forth, for the periods indicated, certain items from the Company s consolidated condensed statement of income expressed as a percentage of net sales:

| | Three Months Ended | |
|---|---|---|
| | May 28, 2005 | May 29, 2004 (Restated) |
| Net sales | 100.0% | 100.0% |
| Cost of sales, exclusive of depreciation and amortization | 58.7 | 56.7 |
| Gross profit, exclusive of depreciation and amortization | 41.3 | 43.3 |
| Selling, general and administrative expenses | 25.5 | 24.0 |
| Depreciation and amortization | 3.7 | 3.6 |
| Operating income | 12.1 | 15.7 |
| Interest income | 0.3 | 0.3 |
| Income before income taxes | 12.4 | 16.0 |
| Income tax provision | 4.8 | 6.2 |
| Net income | 7.6% | 9.8% |

**Three Months Ended May 28, 2005 Compared to Three Months Ended May 29, 2004**

***Net Sales.*** Net sales for the three months ended May 28, 2005 were $122.7 million, an increase of $20.1 million or 19.6%, from $102.6 million for the three months ended May 29, 2004. The increase in net sales resulted from an increase in the number of stores operated by the Company, as well as a 4% increase in same-store sales. The Company operated 660 stores at May 28, 2005, compared to 566 stores at May 29, 2004. The Company s increase in same-store sales was partially driven by aggressive markdowns taken in the first quarter of fiscal 2006. Strong customer response to the Company s assortment of woven tops also contributed to the increase. The Company s newer stores, opened in fiscal 2003, 2004 and 2005, reported a high single-digit increase in same-store sales, while the Company s mature base of stores, opened in fiscal 2002 and earlier, posted a low single-digit same-store sales increase.

The Company s same-store sales data is calculated based on the change in net sales for stores that have been open for more than 13 full months and includes stores, if any, that have been relocated within the same mall. The Company typically does not expand or relocate stores within a mall. Stores where the square footage has been changed by more than 25 percent are excluded from the same-store sales calculation. Stores closed during the year are included in the calculation of same-store sales only for the full months of the year the stores were open.

Sales from the Acorn stores acquired by the Company in fiscal 2005 will be excluded from the calculation of same-store sales until the Company has operated the stores for 13 full months.

***Gross Profit, exclusive of depreciation and amortization.*** Gross profit, which is net sales less the cost of merchandise, buying expenses and occupancy costs, exclusive of depreciation and amortization, was $50.6 million, or 41.3% of net sales, during the first three months of fiscal 2006, compared to $44.5 million, or 43.3% of net sales, during the same period in fiscal 2005. The decline in gross margin as a percent of net sales was mainly attributable to lower merchandise margins resulting from a higher level of markdowns taken in the first quarter of fiscal 2006 than in the first quarter of fiscal 2005. Gross margin was positively affected by modest leveraging of occupancy expenses.

The Company s gross profit may not be comparable to that of other entities. The Company includes all costs related to its distribution network in cost of sales, while other entities exclude a portion of these expenses from cost of sales and include them in selling, general and administrative expenses. Please see the *Key Performance Indicators* section of this MD&A for further detail regarding which expenses the Company includes in cost of sales.

***Selling, General and Administrative Expenses.*** Selling, general and administrative expenses for the three months ended May 28, 2005 were $31.3 million, or 25.5% of net sales, compared to $24.7 million, or 24.0% of net sales, for the three months ended May 29, 2004. The approximate 150 basis point increase in selling, general and administrative expenses as a percent of net sales was primarily the result of negative leverage related to Acorn stores as well as other expenses which contributed lesser amounts of negative leverage. These expenses included store-level incentives, store supplies, professional fees, insurance and medical claims and certain other store-level costs.

***Depreciation and Amortization.*** Depreciation and amortization was $4.5 million, or 3.7% of net sales, in the first three months of fiscal 2006, compared to $3.7 million, or 3.6% of net sales, in the first three months of fiscal 2005. The increase in the amount of depreciation and amortization expense was a result of capital expenditures made during the past year. The Company operated 660 stores at May 28, 2005 compared to 566 stores at May 29, 2004.

***Operating Income.*** As a result of the foregoing factors, operating income for the three months ended May 28, 2005 was $14.8 million, or 12.1% of net sales, compared to operating income of $16.1 million, or 15.7% of net sales, for the three months ended May 29, 2004.

***Interest Income.*** For the three months ended May 28, 2005, interest income increased to $326,815 from $257,680 for the three months ended May 29, 2004. The increase was a result of higher interest rates on short-term investments, partially offset by a lower average cash and short-term investment balance, in the first quarter of fiscal 2006 compared to the first quarter of fiscal 2005.

***Income Taxes.*** Income tax expense in the first three months of fiscal 2006 was $5.9 million, with an effective tax rate of 38.6%, compared to $6.3 million, with an effective tax rate of 38.6%, in the first three months of fiscal 2005.

***Net Income.*** As a result of the foregoing factors, net income for the three months ended May 28, 2005 was $9.3 million, or 7.6% of net sales and $0.26 per diluted share, compared to $10.0 million, or 9.8% of net sales and $0.26 per diluted share, for the three months ended May 29, 2004.

**Liquidity and Capital Resources**

The Company s principal on-going cash requirements are to finance the construction of new stores and the remodeling of certain existing stores, to purchase merchandise inventory and to fund other working capital requirements. Merchandise purchases vary on a seasonal basis, peaking in the fall. As a result, the Company s cash requirements historically reach their peak in October or November. Conversely, cash balances reach their peak in January after the holiday season is completed.

Net cash provided by operating activities totaled $11.6 million in the first three months of fiscal 2006, down from $15.9 million in the first three months of fiscal 2005. The reduction was primarily due to a decrease in accounts payable, partially offset by a decrease in merchandise inventory. Net cash provided by investing activities included net redemptions of short-term investments of approximately $12.0 million, partially offset by $5.0 million of capital expenditures. The Company opened 19 new stores and completed six store remodels during the three months ended May 28, 2005.

Net cash of $1.0 million was used by the Company for financing activities during the first three months of fiscal 2006. In April 2005, the Company paid a quarterly cash dividend which totaled approximately $1.4 million. The Company received approximately $400,000 in cash as certain of the Company s officers, directors and key employees exercised stock options during the first three months of fiscal 2006.

The Company plans to fund approximately $17 million of capital expenditures during the last nine months of fiscal 2006 to open approximately 56 new stores, to complete 12 store remodels and to make various capital improvements at its headquarters and distribution center facility. Additionally, management anticipates a portion of these capital expenditures will pertain to stores which the Company plans to open in the first quarter of fiscal 2007. The Company expects its cash and short-term investments, combined with cash flows from operations, to be sufficient to meet its capital expenditure, working capital and other requirements for liquidity during the remainder of fiscal 2006 and throughout fiscal 2007.

The Company maintains an Amended and Restated Revolving Credit and Security Agreement with Wells Fargo Bank, National Association (the Wells Fargo Revolver ) which expires on June 30, 2006. The Wells Fargo Revolver provides the Company with revolving credit loans and letters of credit of up to $40.0 million, subject to a borrowing base formula based on inventory levels.

Loans under the Wells Fargo Revolver bear interest at Wells Fargo s base rate, 6.0% as of May 28, 2005, plus 0.25%. Interest is payable monthly in arrears. The Wells Fargo Revolver carries a facility fee of 0.25% based on the unused portion as defined in the agreement. Facility fees totaled $1,305 for the three months ended May 28, 2005. The credit facility is collateralized by the Company s equipment, general intangibles, inventory, inventory letters of credit and letter of credit rights. The Company had no revolving credit loan borrowings under the Wells Fargo Revolver during the first three months of fiscal 2006. Historically, the Wells Fargo Revolver has been utilized by the Company only to open letters of credit to facilitate the import of merchandise. The borrowing base at May 28, 2005 was $29.3 million. As of May 28, 2005, the Company had outstanding letters of credit in the amount of $18.6 million. Accordingly, the availability of revolving credit loans under the Wells Fargo Revolver was $10.7 million at May 28, 2005.

**Merchandise Sourcing**

The Company directly imports approximately 95% of its total merchandise purchases. This reliance on sourcing from foreign countries may cause the Company to be exposed to certain risks. Import restrictions, including tariffs and quotas, and changes in such restrictions, could affect the import of apparel and might result in increased costs, delays in merchandise receipts or reduced supplies of apparel available to the Company and could possibly have an adverse effect on the Company s business, financial condition and results of operations.

The Company s merchandise flow could also be adversely affected by political instability in any of the countries where its merchandise is manufactured or by changes in the United States governmental policies toward such foreign countries. In addition, merchandise receipts could be delayed due to interruptions in air, ocean and ground shipments.

Substantially all of the Company s directly imported merchandise is manufactured in Southeast Asia. The majority of these goods are produced in China, Hong Kong, Indonesia and Singapore. The Company is not currently importing merchandise produced in the Middle East.

The Company purchased approximately 22% and 30% of its merchandise from its largest overseas supplier during the first three months of fiscal 2006 and 2005, respectively. Although the Company believes that its relationship with this particular vendor is good, there can be no assurance that this relationship can be maintained in the future or that the vendor will continue to supply merchandise to the Company. If there should be any significant disruption in the supply of merchandise from this vendor, management believes that it can shift production to other suppliers so as to continue to secure the required volume of product. Nevertheless, there is some potential that any such disruption in supply could have a material adverse impact on the Company s financial position and results of operations.

**Quota Restrictions**

On December 31, 2004, quota restrictions expired on the importing of apparel in the United States from foreign countries which are members of the World Trade Organization. The effect this quota expiration will have on global sourcing patterns is uncertain, but is likely to cause further retail price deflation. Management believes it can adjust to potential shifts in the availability of apparel following the expiration of these quotas.

However, the Company s sourcing operations may be adversely affected by trade limits or political and financial instability resulting in the disruption of trade from exporting countries.

**Quarterly Results and Seasonality**

The Company s sales reflect seasonal variation as sales in the third and fourth quarters, which include the fall and holiday seasons, generally have been higher than sales in the first and second quarters. Sales and gross profit generated during the fall and holiday seasons have a significant impact on the Company s annual results of operations. Quarterly results may fluctuate significantly depending on a number of factors including adverse weather conditions, shifts in the timing of certain holidays, timing of new store openings and customer response to the Company s seasonal merchandise mix.

**Inflation**

Although the operations of the Company are influenced by general economic conditions, the Company does not believe that inflation had a material effect on the results of operations during the quarters ended May 28, 2005 and May 29, 2004.

**Forward Looking Information and Risk**

Information contained in this Form 10-Q contains certain forward-looking statements which reflect the current view of the Company with respect to future events and financial performance. Wherever used, terminology such as may , will , expect , intend , plan , anticipate , estir continue , or the negative thereof, or other variations thereon or comparable terminology reflect such forward-looking statements. There are certain important factors that could cause results to differ materially from those anticipated by some of these forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those matters discussed below and beginning on page 21 of the Company s most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission on May 12, 2005. Investors are cautioned that all forward-looking statements involve risks and uncertainty. The factors, among others, that could cause actual results to differ materially include: changes in general economic conditions, including recessionary effects which may affect consumers spending and debt levels; the Company s ability to execute its business plan including the successful expansion of its Christopher & Banks, C.J. Banks and Acorn concepts; the Company s ability to open new stores on favorable terms and the timing of such store openings; the acceptance of the Company s merchandising strategies by its target customers; the ability of the Company to anticipate fashion trends and consumer preferences; the loss of one or more of the Company s key executives; continuity of a relationship with or purchases from major vendors, particularly those from whom the Company imports merchandise; timeliness of vendor production and deliveries; competitive pressures on sales and pricing; increases in other costs which cannot be recovered through improved pricing of merchandise; and the adverse effect of weather conditions from time to time on consumers ability or desire to purchase new clothing. Since the Company relies heavily on sourcing from foreign vendors, there are risks and uncertainties including transportation delays related to ocean, air and ground shipments, political instability, work stoppages, changes in import and export controls including quota restrictions and the expiration thereof. The Company assumes no obligation to publicly update or revise its forward looking statements to reflect events or circumstances that may arise after the date of this Form 10-Q.

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

The market risk inherent in the Company s financial instruments and in its financial position represents the potential loss arising from adverse changes in interest rates. The Company s results of operations could be negatively impacted by decreases in interest rates on its short-term investments.

The Company is potentially exposed to market risk from changes in interest rates relating to its Wells Fargo Revolver. Loans under the Wells Fargo Revolver bear interest at Wells Fargo s fluctuating base rate, 6.0% as of May 28, 2005, plus 0.25%. However, the Company had no revolving credit loan borrowings under the Wells Fargo Revolver during the first three months of fiscal 2006 and, given its existing liquidity position, does not expect to utilize the Wells Fargo Revolver in the near future except for its continuing use of the import letter of credit facility.

All of the Company s purchase obligations with foreign suppliers are denominated in U.S. dollars. Therefore, the Company has only minimal exposure to foreign currency exchange risks. The Company does not hedge against foreign currency risks and believes that its foreign currency exchange risk is not significant.

The Company does not have any derivative financial instruments and does not hold any such instruments for trading purposes.

## ITEM 4.
## CONTROLS AND PROCEDURES

### *(a)* Evaluation of Disclosure Controls and Procedures.

The Company s management, with the participation of its Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company s disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act )) as of the end of the period covered by this report. These disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed by the Company in its Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms, and that such information is accumulated and communicated to the Company s management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Based upon the foregoing, the Company s Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures were effective as of May 28, 2005.

### *(b)* Internal Control Over Financial Reporting.

There have not been any changes in the Company s internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the three months ended May 28, 2005 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

## PART II.

## ITEM 1.

## LEGAL PROCEEDINGS

There are no material legal proceedings pending against the Company.

## ITEM 2.

## UNREGISTERED SALES OF EQUITY

## SECURITIES AND USE OF PROCEEDS

The Company did not repurchase any shares during the quarter ended May 28, 2005.

## ITEM 3.

## DEFAULTS UPON

## SENIOR SECURITIES

There has been no default with respect to any indebtedness of the Company.

## ITEM 4.

## SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

There were no matters submitted to a vote of security holders during the quarter ended May 28, 2005.

## ITEM 5.

## OTHER INFORMATION

None.

## ITEM 6.

## EXHIBITS

(a) Exhibits:

31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**CHRISTOPHER & BANKS CORPORATION**

| | |
|---|---|
| Dated: July 7, 2005 | By /S/ WILLIAM J. PRANGE |
| | William J. Prange<br>Chairman and<br>Chief Executive Officer |
| | Signing on behalf of the<br>Registrant as principal<br>executive officer. |
| Dated: July 7, 2005 | By /S/ ANDREW K. MOLLER |
| | Andrew K. Moller<br>Senior Vice President and<br>Chief Financial Officer |
| | Signing on behalf of the<br>Registrant as principal<br>financial officer. |