AEROPOSTALE INC
Form 10-Q
December 01, 2005

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

Form 10-Q

(Mark One)

þ	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the quarterly period ended October 29, 2005**
	OR
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission file number: 001-31314

Aéropostale, Inc.
(Exact name of registrant as specified in its charter)

Delaware	**31-1443880**
(State of incorporation)	*(I.R.S. Employer Identification No.)*
112 W. 34th Street, New York, NY	**10120**
(Address of Principal Executive Offices)	*(Zip Code)*

(646) 485-5398
(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 þ No o

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes þ No o

Indicate by check mark whether the Registrant is a shell company (as defined in Exchange Act Rule 12b-2). Yes o No þ

The Registrant had 54,355,588 shares of common stock outstanding as of November 19, 2005.

AÉROPOSTALE, INC.

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PART I

FINANCIAL INFORMATION

Item 1. *Financial Statements*

AÉROPOSTALE, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	October 29, 2005	January 29, 2005	October 30, 2004
		(In Thousands)	
ASSETS			
Current Assets:			
Cash and cash equivalents	$ 114,317	$ 106,128	$ 65,620
Short-term investments	20,062	76,224	55,040
Merchandise inventory	159,873	81,238	114,515
Tenant allowances receivable	10,712	4,809	11,411
Miscellaneous receivables	5,258	923	868
Prepaid expenses and other current assets	12,460	10,165	9,529
Total current assets	322,682	279,487	256,983
Fixtures, equipment and improvements, net	162,325	122,651	121,845
Intangible assets	2,529	2,529	1,400
Other assets	1,937	1,152	2,127
TOTAL ASSETS	$ 489,473	$ 405,819	$ 382,355
LIABILITIES AND STOCKHOLDERS EQUITY			
Current Liabilities:			
Accounts payable	$ 95,064	$ 44,858	$ 69,075
Accrued compensation	7,818	14,580	12,303
Income taxes payable	8,085	6,322	1,752
Accrued expenses	33,874	31,234	25,782
Total current liabilities	144,841	96,994	108,912
Deferred rent and tenant allowances	81,409	63,065	59,579
Retirement benefit plan liability	7,347	6,158	4,425
Deferred income taxes	4,321	1,351	
Commitments and contingent liabilities			

Stockholders Equity:			
Preferred stock par value, $0.01 per share; 5,000 shares authorized, no shares issued or outstanding			
Common stock par value, $0.01 per share; 200,000 shares authorized, 58,558, 58,115 and 58,168 shares issued	586	581	582
Additional paid-in capital	87,567	79,069	78,709
Accumulated other comprehensive loss	(817)	(817)	(672)
Deferred compensation	(2,968)	(1,271)	(1,441)
Retained earnings	266,463	224,315	189,047
Treasury stock at cost (4,203, 2,749 and 2,499 shares)	(99,276)	(63,626)	(56,789)
Total stockholders equity	251,555	238,251	209,439
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 489,473	$ 405,819	$ 382,355

See notes to unaudited condensed consolidated financial statements.

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AÉROPOSTALE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(Unaudited)

	13 weeks ended		39 weeks ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
	(In Thousands, Except Per Share Data)			
Net sales	$ 324,657	$ 274,616	$ 769,101	$ 637,122
Cost of sales (includes certain buying, occupancy and warehousing expenses)	229,938	176,415	552,584	430,328
Gross profit	94,719	98,201	216,517	206,794
Selling, general and administrative expenses	52,411	46,775	149,455	127,805
Income from operations	42,308	51,426	67,062	78,989
Interest income, net	781	336	2,362	796
Income before income taxes	43,089	51,762	69,424	79,785
Income taxes	17,004	20,076	27,276	30,941
Net income and comprehensive income	$ 26,085	$ 31,686	$ 42,148	$ 48,844
Basic earnings per share	$ 0.48	$ 0.57	$ 0.76	$ 0.88
Diluted earnings per share	$ 0.47	$ 0.55	$ 0.75	$ 0.85
Weighted average basic shares	54,913	55,894	55,243	55,792
Weighted average diluted shares	55,711	57,210	56,217	57,399

See notes to unaudited condensed consolidated financial statements.

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AÉROPOSTALE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	39 weeks ended	
	October 29, 2005	October 30, 2004
	(In Thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 42,148	$ 48,844
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	15,046	11,407
Other	3,446	(2,049)
Changes in operating assets and liabilities:		
Merchandise inventory	(78,635)	(52,708)
Accounts payable	50,206	38,598
Other assets and liabilities	3,070	18,412
Net cash from operating activities	35,281	62,504
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of fixtures, equipment and improvements	(48,783)	(40,674)
Purchase of short-term investments	(166,376)	(322,623)
Proceeds from sale of short-term investments	222,538	267,583
Purchase of intangible assets		(1,400)
Net cash from investing activities	7,379	(97,114)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Purchase of treasury stock	(35,650)	(39,091)
Proceed from exercise of stock options	1,179	965
Net cash from financing activities	(34,471)	(38,126)
Net increase (decrease) in cash and cash equivalents	8,189	(72,736)
Cash and cash equivalents, beginning of year	106,128	138,356
Cash and cash equivalents, end of period	$ 114,317	$ 65,620
Supplemental Disclosure of Cash Flow Information:		
Tax benefit related to exercise of stock options included in change in other assets and liabilities	$ 4,346	$ 12,597

See notes to unaudited condensed consolidated financial statements.

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AÉROPOSTALE, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

References to the Company, we, us, or our means Aéropostale, Inc. and its subsidiaries, except as expressly indicat to the contrary or unless the context otherwise requires. We are a mall-based, specialty retailer of casual apparel and accessories. We design, market and sell our own brand of merchandise principally targeting 11 to 18 year-old young women and men. Jimmy Z Surf Co., Inc., a wholly owned subsidiary of Aéropostale, Inc., is a California lifestyle-oriented brand targeting trend-aware young women and men aged 18-25. As of October 29, 2005, we operated 668 stores in 47 states, consisting of 655 Aeropostale stores and 13 Jimmy Z stores, and in May 2005 we launched our Aeropostale e-commerce website, www.aeropostale.com (this and any other references in this Quarterly Report on Form 10-Q to aeropostale.com is solely a reference to a uniform resource locator, or URL, and is an inactive textual reference only, not intended to incorporate the website into this Quarterly Report on Form 10-Q).

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with Rule 10-01 of Regulation S-X and do not include all of the information and footnotes required by accounting principles generally accepted in the United States. However, in the opinion of our management, all known adjustments necessary for a fair presentation of the results of the interim periods have been made. These adjustments consist primarily of normal recurring accruals and estimates that impact the carrying value of assets and liabilities. Actual results may materially differ from these estimates.

Our business is highly seasonal, and historically we have realized a significant portion of our sales, net income, and cash flow in the second half of the year, driven by the impact of the back-to-school selling season in the third quarter and the holiday selling season in the fourth quarter. Therefore, our interim period consolidated financial statements will not be indicative of our full-year results of operations, financial condition or cash flows. These financial statements should be read in conjunction with our Annual Report on Form 10-K for our fiscal year ended January 29, 2005.

References to 2005 mean the 52-week period ending January 28, 2006, and references to 2004 mean the 52-week period ended January 29, 2005. References to the third quarter of 2005 mean the thirteen-week period ended October 29, 2005, and references to the third quarter of 2004 mean the thirteen-week period ended October 30, 2004.

2. Stock Based Compensation

We periodically grant stock options to our employees and directors, and we account for these stock options in accordance with the provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, or APB No. 25 . We have also adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*, or SFAS No. 148 . In accordance with the provisions of SFAS No. 148 and APB No. 25, since all options were issued at market value, we have not recognized compensation expense related to stock options in our consolidated financial statements. If we would have elected to recognize compensation expense

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AÉROPOSTALE, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

based on the fair value of options at grant date, as prescribed by SFAS No. 148, our net income and earnings per share would have been reduced to the pro forma amounts indicated in the following table:

	13 weeks ended		39 weeks ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
	(In Thousands, Except Per Share Data)			
Net income:				
As reported	$ 26,085	$ 31,686	$ 42,148	$ 48,844
Add: Restricted stock amortization net of taxes	306	101	782	261
Deduct: Total stock based compensation expense determined under the fair value method, net of taxes	(746)	(380)	(2,054)	(1,024)
Pro-forma	$ 25,645	$ 31,407	$ 40,876	$ 48,081
Basic earnings per share:				
As reported	$ 0.48	$ 0.57	$ 0.76	$ 0.88
Pro-forma	$ 0.47	$ 0.56	$ 0.74	$ 0.86
Diluted earnings per share:				
As reported	$ 0.47	$ 0.55	$ 0.75	$ 0.85
Pro-forma	$ 0.46	$ 0.55	$ 0.73	$ 0.84

The weighted average fair value of stock options was calculated using the Black-Scholes Option Pricing Model with the following weighted average assumptions used for grants in their respective periods. For periods ended in 2005: no dividend yield; expected volatility of 40%; risk free interest rate of 4.10%; and expected life of 5 years. For periods ended in 2004: no dividend yield; expected volatility of 69%; risk free interest rate of 2.79%; and expected life of 5 years. There were 6,000 options granted during the third quarter of 2005, with a weighted average fair value of $0.1 million, and 294,000 options granted during the thirty-nine weeks ended October 29, 2005 with a weighted average fair value of $4.0 million. There were 19,000 options granted during the third quarter of 2004, with a weighted average fair value of $0.3 million, and 521,000 options granted during the thirty-nine weeks ended October 30, 2004 with a weighted average fair value of $7.4 million.

Certain of our employees and all of our directors have been awarded restricted stock, pursuant to restricted stock agreements. There were 165,000 outstanding shares of restricted stock as of October 29, 2005. The restricted stock awarded to employees vests at the end of three years of continuous service with us. Initial grants of restricted stock awarded to directors vest, pro-rata, over a three-year period, based upon continuous service. Subsequent grants of restricted stock awarded to directors vest in full one year after the grant date. Total compensation expense is being amortized over the vesting period. Amortization expense was $0.5 million for the third quarter of 2005 and $1.3 million for the thirty-nine weeks ended October 29, 2005. Amortization expense was $0.1 million for the third

quarter of 2004 and $0.4 million for the thirty-nine weeks ended October 30, 2004.

3. Reclassification of Auction Rate Securities

Auction rate securities, which were previously recorded in cash and cash equivalents in our interim 2004 condensed consolidated financial statements, have been included in short-term investments in the

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AÉROPOSTALE, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

accompanying consolidated financial statements due to their liquidity and pricing reset feature. There was no impact on net income, stockholders equity, debt covenants or cash flow from operations as a result of this reclassification. The condensed consolidated financial statements for the first thirty-nine weeks of 2004 have been reclassified as follows:

	As Previously Reported	As Reclassified
	(In Thousands)	
Cash and cash equivalents	$ 120,660	$ 65,620
Short-term investments	$	$ 55,040
Cash flows from investing activities	$ (42,074)	$ (97,114)

4. Cost of Sales and Selling, General and Administrative Expenses

Cost of sales includes costs related to: merchandise sold, distribution and warehousing, freight from the distribution center and warehouse to the stores, payroll for our design, buying and merchandising departments, and occupancy costs. Occupancy costs include: rent, contingent rents, common area maintenance, real estate taxes, utilities, repairs, maintenance and all depreciation.

Selling, general and administrative expenses, or SG&A , include costs related to: selling expenses, store management and corporate expenses such as payroll and employee benefits, marketing expenses, employment taxes, maintenance costs and expenses, insurance and legal expenses, and store pre-opening and other corporate level expenses. Store pre-opening expenses include store level payroll, grand opening event marketing, travel, supplies and other store pre-opening expenses.

5. Recent Accounting Developments

In May 2005, the Financial Accounting Standards Board, or FASB, issued SFAS No. 154, *Accounting Changes and Error Corrections*. This statement replaces APB No. 20 and SFAS No. 3, and changes the requirements for the accounting for and reporting of a change in accounting principle. SFAS No. 154 requires retrospective application to prior period s financial statements of changes in accounting principle. The statement defines retrospective application as the application of a different accounting principle to prior accounting periods as if that principle had always been used or as the adjustment of previously issued financial statements to reflect a change in the reporting entity. This statement shall be effective for accounting changes and correction of errors made in years beginning after December 15, 2005.

In April 2005, the Securities and Exchange Commission delayed the date of compliance with SFAS No. 123(R), *Share-Based Payment, a revision of SFAS No. 123, Accounting for Stock Based Compensation*, for publicly held companies until the company s first fiscal year beginning on or after June 15, 2005. Accordingly, we will adopt the

provisions of SFAS No. 123(R) at the beginning of our 2006 fiscal year. SFAS No. 123(R) was issued in December 2004, and supersedes APB No. 25, and its related implementation guidance. Under SFAS No. 123(R), all forms of share-based payment to employees and directors, including stock options, must be treated as compensation and recognized in the income statement. As discussed in Note 2, we currently account for stock options under APB No. 25 and, accordingly, do not recognize compensation expense in our consolidated financial statements. Also as prescribed by SFAS No. 148, we have disclosed the pro-forma impact of expensing options in Note 2. We expect that the adoption of SFAS No. 123(R) will not have a material impact on our consolidated financial statements or cash flows.

In March 2005, the FASB issued Statement of Financial Accounting Standards Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations , or FIN 47. FIN 47 provides clarification

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AÉROPOSTALE, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

regarding the meaning of the term conditional asset retirement obligation as used in FASB Statement No. 143, Accounting for Asset Retirement Obligations . FIN 47 is effective for fiscal years beginning after December 15, 2005. We expect that the adoption of FIN 47 will not have a material impact on our consolidated financial statements or cash flows.

6. Earnings Per Share

The following table sets forth the computations of basic and diluted earnings per share:

	13 weeks ended		39 weeks ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
	(In Thousands, Except Per Share Data)			
Net income	$ 26,085	$ 31,686	$ 42,148	$ 48,844
Weighted average basic shares	54,913	55,894	55,243	55,792
Impact of dilutive securities	798	1,316	974	1,607
Weighted average diluted shares	55,711	57,210	56,217	57,399
Earnings per basic share	$ 0.48	$ 0.57	$ 0.76	$ 0.88
Earnings per diluted share	$ 0.47	$ 0.55	$ 0.75	$ 0.85

Options to purchase 765,000 shares during the third quarter of 2005, and 411,000 shares during the thirty-nine weeks ended October 29, 2005 were not included in the computation of diluted earnings per share because the exercise price of the options was greater than the average market price of the common shares.

7. Revolving Credit Facility

In April 2005, we amended our revolving credit facility (the credit facility) with Bank of America, N.A., formerly Fleet Retail Finance, Inc. As amended, the credit facility allows us to borrow or obtain letters of credit up to an aggregate of $50.0 million, with letters of credit having a sub-limit of $15.0 million. The amount of available credit can be increased to an aggregate of $75.0 million if we so request. The credit facility matures in April 2010, and our assets collateralize indebtedness under the credit facility. Borrowings under the credit facility bear interest at our option, either at (a) the lender s prime rate or (b) the Euro Dollar Rate plus 0.75% to 1.25%, dependent upon our financial performance. There are no covenants in the credit facility requiring us to achieve certain earnings levels and there are no capital spending limitations. There are certain negative covenants under the credit facility, including but not limited to, limitations on our ability to incur other indebtedness, encumber our assets, or undergo a change of control. Additionally, we are required to maintain a ratio of 2:1 for the value of our inventory to the amount of the loans under the credit facility. As of October 29, 2005, we were in compliance with all covenants under the credit facility. Events of default under the credit facility include, subject to grace periods and notice provisions in certain

circumstances, failure to pay principal amounts when due, breaches of covenants, misrepresentation, default of leases or other indebtedness, excess uninsured casualty loss, excess uninsured judgment or restraint of business, business failure or application for bankruptcy, indictment of or institution of any legal process or proceeding under federal, state, municipal or civil statutes, legal challenges to loan documents, and a change in control. If an event of default occurs, the lenders under the credit facility will be entitled to take various actions, including the acceleration of amounts due there under and requiring that all such amounts be immediately paid in full as well as possession and sale of all assets that have been used as collateral. At October 29, 2005, we had no amount outstanding under the credit facility, and no stand-by or commercial letters of credit issued under the credit facility. In addition, we have not had outstanding borrowings under the credit facility since November 2002.

AÉROPOSTALE, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Retirement Benefit Plans

We have a qualified, defined contribution retirement plan with a 401(k) salary deferral feature that covers substantially all of our employees who meet certain requirements. Under the terms of the plan, employees may contribute up to 14% of gross earnings and we will provide a matching contribution of 50% of the first 5% of gross earnings contributed by the participants. We also have the option to make additional contributions. Matching contributions vest over a five-year service period with 20% vesting after two years and 50% vesting after year three. Vesting increases thereafter at a rate of 25% per year so that participants will be fully vested after year five. Contribution expense was $0.1 million for the third quarter of 2005 and $0.4 million for the first thirty-nine weeks of 2005. Contribution expense was $0.2 million for the third quarter of 2004 and $0.5 million for the first thirty-nine weeks of 2004.

We maintain a supplemental executive retirement plan, which is a nonqualified defined benefit plan for certain officers. The plan is non-contributory and not funded and provides benefits based on years of service and compensation during employment. Participants are vested upon entrance in the plan. Pension expense is determined using various actuarial cost methods to estimate the total benefits ultimately payable to officers and this cost is allocated to service periods. The actuarial assumptions used to calculate pension costs are reviewed annually.

The components of net periodic pension benefit cost are as follows:

	13 weeks ended		39 weeks ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
	(In Thousands)			
Service cost	$ 106	$ 70	$ 316	$ 209
Interest cost	183	140	549	486
Amortization of prior service cost	19	19	56	56
Amortization of net loss	138	66	413	254
Loss recognized due to settlement				1,396
Net periodic pension benefit cost	$ 446	$ 295	$ 1,334	$ 2,401

The loss recognized due to settlement in 2004 resulted from the early retirement of our former President and Chief Operating Officer, and we made a contribution of $2.4 million in August 2004 in connection with this early retirement.

During 2004, we adopted a long-term incentive deferred compensation plan for the purpose of providing long-term incentive to a select group of management. The plan is a non-qualified, defined contribution plan and is not funded. Participants in this plan include all employees designated by us as Vice President, or other higher-ranking position that are not participants in the SERP. Annual monetary credits are recorded to each participant s account based on compensation levels and years as a participant in the plan. Annual interest credits are applied to the balance of each

participant s account based upon established benchmarks. Each annual credit is subject to a three-year cliff-vesting schedule, and participant s accounts will be fully vested upon retirement after completing five years of service and attaining age 55.

In 2004, we adopted a postretirement benefit plan for certain officers. At October 29, 2005, we had a liability of $70,000 in connection with this plan.

9. Stock Repurchase Program

We repurchase our common stock from time to time under a stock repurchase program. In November 2005, our Board of Directors approved an additional $50.0 million of repurchase availability, thereby increasing the total amount of repurchase availability under this program to $150.0 million. The repurchase

AÉROPOSTALE, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

program may be modified or terminated by the Board of Directors at any time, and there is no expiration date for the program. The extent and timing of repurchases will depend upon general business and market conditions, stock prices, and liquidity and capital resource requirements going forward. We repurchased 1,454,000 shares for $35.6 million during the first thirty-nine weeks of 2005. Since the inception of the repurchase program, we have repurchased a total of 4.2 million shares of our common stock for total consideration of $99.3 million. At October 29, 2005 we would have had $50.7 million of repurchase availability remaining, after including the additional $50 million of availability approved in November 2005.

10. Commitments and Contingent Liabilities

We are party to various litigation matters and proceedings in the ordinary course of business. In the opinion of our management, dispositions of these matters are not expected to have a material adverse affect on our financial position, results from operations or cash flows. We have not provided any financial guarantees as of October 29, 2005.

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

Introduction

Aéropostale, Inc. is a mall-based specialty retailer of casual apparel and accessories in the United States. Our target customers are both young women and young men from age 11 to 18, and we provide our customers with a selection of high-quality, active-oriented, fashion basic merchandise at compelling values in a high-energy store environment. Jimmy Z Surf Co., Inc., a wholly owned subsidiary of Aéropostale, Inc., is a California lifestyle-oriented brand targeting trend-aware young women and men aged 18-25. We opened our first Jimmy Z stores in July 2005. In addition, we launched our Aeropostale e-commerce business in May 2005. As of October 29, 2005, we operated 668 stores in 47 states, consisting of 655 Aeropostale stores and 13 Jimmy Z stores, in addition to our e-commerce website, www.aeropostale.com.

Management s Discussion and Analysis of Financial Condition and Results of Operations, or MD&A, is intended to provide information to help you better understand our financial condition and results of operations. Our business is highly seasonal, and historically we realize a significant portion of our sales, net income, and cash flow in the second half of the year, driven by the impact of the back-to-school selling season in our third quarter and the holiday selling season in our fourth quarter. Therefore, our interim period consolidated financial statements will not be indicative of our full-year results of operations, financial condition or cash flows. We recommend that you read this section along with our condensed consolidated financial statements included in this report and along with our Annual Report on Form 10-K for the year ended January 29, 2005.

Overview

We achieved net sales of $324.7 million for the third quarter of 2005, an 18.2% increase over the third quarter of 2004. This increase was driven by total square footage growth of 20%, and was partially offset by a 1.5% decline in comparable store sales. On a year-to-date basis, we achieved net sales of $769.1 million for the first thirty-nine weeks of 2005, or a 20.7% increase over the same period in 2004. This increase was driven by total square footage growth of 20%. On a year-to-date basis comparable store sales decreased 0.1%. Gross profit, as a percentage of net sales, decreased by 6.6 percentage points for the third quarter of 2005 and by 4.3 percentage points for the year-to-date period. The decline in gross profit, as a percentage of net sales, was primarily due to decreased merchandise margins driven by significantly higher promotional activity, which was intended to stimulate demand for our merchandise offerings. SG&A, as a percentage of net sales, decreased by 0.9 percentage points for the third quarter of 2005, and decreased by 0.7 percentage points for the year-to-date period. A decrease in incentive compensation and a retirement plan charge recorded in 2004 drove these reductions. Net income for the third quarter of 2005 declined to $26.1 million, or $0.47 per diluted share, from $31.7 million, or $0.55 per diluted share for the third quarter of last year. Net income for the first thirty-nine weeks of 2005 declined to $42.1 million, or $0.75 per diluted share, from $48.8 million, or $0.85 per diluted share, for the first thirty-nine weeks of last year.

As of October 29, 2005, we had working capital of $177.8 million, cash and cash equivalents of $114.3 million, short-term investments of $20.1 million, and no third party debt outstanding. Our merchandise inventories increased by 40% at October 29, 2005, compared to the same period last year, and by 17% on a square foot basis. Cash flows from operating activities were $35.3 million for the first thirty-nine weeks of 2005. We operated 668 stores at October 29, 2005, an increase of 19% from the same period last year.

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We use a number of key indicators of financial condition and operating performance to evaluate the performance of our business, some of which are set forth in the following table:

	13 weeks ended		39 weeks ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
Net sales (in millions)	$ 324.7	$ 274.6	$ 769.1	$ 637.1
Total store count at end of period	668	560	668	560
Comparable store sales count at end of period	508	413	508	413
Net sales growth	18.2%	24.8%	20.7%	37.8%
Comparable store sales (decrease) increase	(1.5)%	5.4%	(0.1)%	12.8%
Net sales per average square foot	$ 140	$ 144	$ 351	$ 356
Gross profit (in millions)	$ 94.7	$ 98.2	$ 216.5	$ 206.8
Income from operations (in millions)	$ 42.3	$ 51.4	$ 67.1	$ 79.0
Diluted earnings per share	$ 0.47	$ 0.55	$ 0.75	$ 0.85
Square footage growth	20%	22%	20%	22%
Increase in total inventory over comparable period	40%	1%	40%	1%
Increase (decrease) in inventory per square foot over comparable period	17%	(17)%	17%	(17)%
Percentages of net sales by category:				
Women s	66%	65%	62%	62%
Men s	23%	23%	25%	25%
Accessories	11%	12%	13%	13%

The following table sets forth our results of operations as a percentage of net sales. We also use this information to evaluate the performance of our business:

	13 weeks ended		39 weeks ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
Net sales	100.0%	100.0%	100.0%	100.0%
Gross profit	29.2%	35.8	28.2%	32.5
Selling, general and administrative expenses	16.1%	17.0	19.4%	20.1
Income from operations	13.1%	18.8	8.8%	12.4
Interest income, net	0.1%	0.1	0.2%	0.1
Income before income taxes	13.2%	18.9	9.0%	12.5
Income taxes	5.2%	7.4	3.5%	4.8
Net income	8.0%	11.5	5.5%	7.7

Results of Operations

Sales Net sales consist of sales from comparable stores and non-comparable stores. A store is included in comparable store sales after fourteen months of operation. We consider a remodeled or relocated store with more than a 25% change in square feet to be a new store. Prior period sales from stores that have closed are not included in comparable store sales, nor are sales from our temporary arrangements with colleges and universities.

Net sales for the third quarter of 2005 increased by $50.1 million, or by 18.2% versus the same period last year. New store sales drove the net sales increase for the quarter, and were partially offset by a decrease in comparable store sales. Comparable store sales decreased by $3.8 million, or by 1.5% for the third quarter of 2005, versus a comparable store sales increase of 5.4% for the third quarter of 2004. Comparable sales increased in our young men s category, but decreased in our women s and accessories categories. The

comparable store sales decline reflected an 11.1% decrease in average dollar per unit sold, a 1.5% increase in units per transaction, and a 9.2% increase in the number of sales transactions. Due to lower than expected sales performance during the third quarter of 2005, we increased our promotional cadence in an effort to stimulate customer demand for our merchandise offerings. Non-comparable store sales increased by $46.3 million, or by 19.7%, primarily due to 108 more stores open at the end of the third quarter of 2005 versus the end of the third quarter of 2004.

Net sales for the first thirty-nine weeks of 2005 increased by $132.0 million, or by 20.7% versus the same period last year, driven by new store sales. Comparable store sales decreased by $0.7 million, or by 0.1% for the year-to-date period, versus a comparable store sales increase of 12.8% for the first thirty-nine weeks of 2004. Non-comparable store sales increased by $132.7 million, or by 20.8%, primarily due to the new store openings discussed above.

Gross profit Cost of sales includes costs related to: merchandise sold, distribution and warehousing, freight from the distribution center and warehouse to the stores, payroll for our design, buying and merchandising departments, and occupancy costs. Occupancy costs include: rent, contingent rents, common area maintenance, real estate taxes, utilities, repairs, maintenance and all depreciation.

Gross profit, as a percentage of net sales, decreased by 6.6 percentage points for the third quarter of 2005 versus the same period last year. This decrease was primarily due to a 5.2 percentage point decrease in merchandise margin. The decrease in merchandise margin was driven by significantly higher promotional activity. Gross profit, as a percentage of net sales, decreased by 4.3 percentage points for the first thirty-nine weeks of 2005 versus the same period last year, driven by decreased merchandise margin.

SG&A SG&A includes costs related to: selling expenses, store management and corporate expenses such as payroll and employee benefits, marketing expenses, employment taxes, maintenance costs and expenses, insurance and legal expenses, and store pre-opening and other corporate level expenses. Store pre-opening expenses include store level payroll, grand opening event marketing, travel, supplies and other store pre-opening expenses.

SG&A increased by $5.6 million, and decreased by 0.9 percentage points, as a percentage of net sales for the third quarter of 2005 versus the same period last year. The decrease, as a percentage of sales, was primarily due to the reversal of $2.4 million of previously accrued incentive compensation in the third quarter of 2005, since certain performance thresholds were not expected to be achieved, compared to incentive compensation expense of $2.6 million in the third quarter of 2004.

SG&A increased by $21.7 million, and decreased by 0.7 percentage points, as a percentage of sales for the first thirty-nine weeks of 2005 versus the same period last year. The decrease in year-to-date SG&A, as a percentage of sales, reflects the decrease in incentive compensation, as well as a retirement plan charge of $1.4 million recorded in 2004, which did not reoccur in 2005.

Interest income and income taxes Interest income, net of interest expense, increased by $0.4 million for the third quarter of 2005 and by $1.6 million for the first thirty-nine weeks of 2005 versus the same periods last year. These increases were driven primarily by higher interest rates this year.

The effective tax rate was 39.5% for the third quarter of 2005 and 39.2% for the first thirty-nine weeks of 2005, compared with 38.8% for the same periods last year.

Net income Net income was $26.1 million, or $0.47 per diluted share, for the third quarter of 2005, or a decrease of $5.6 million, or $0.08 per diluted share, versus the same period last year. Net income was $42.1 million, or $0.75 per diluted share, for the first thirty-nine weeks of 2005, or a decreased of $6.7 million, or $0.10 per diluted share, versus the same periods last year.

Liquidity and Capital Resources

Our cash requirements are primarily for working capital, construction of new stores, remodeling of existing stores, and the improvement and enhancement of our information technology systems. Due to the seasonality of our business, we have historically realized a significant portion of our cash flows from

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operations during the second half of the year. Most recently, our cash requirements have been met primarily through cash and cash equivalents on hand during the first half of the year, and through cash flows from operations during the second half of the year. We expect to continue to meet our cash requirements for the next twelve months primarily through cash flows from operations and existing cash and cash equivalents. In addition, we have recently amended our revolving credit facility (the credit facility), and have expanded our borrowing availability to provide for a $50.0 million base borrowing availability with $25.0 million of additional borrowing availability (see note 7 to the Notes to Unaudited Condensed Consolidated Financial Statements for a further description). We have not had outstanding borrowings under the credit facility since November 2002. At October 29, 2005, we had working capital of $177.8 million, cash and cash equivalents of $114.3 million, short-term investments of $20.1 million, and no third party debt outstanding.

The following table sets forth our cash flows for the period indicated:

	39 weeks ended	
	October 29, 2005	October 30, 2004
	(In Thousands)	
Net cash from operating activities	$ 35,281	$ 62,504
Net cash from investing activities	7,379	(97,114)
Net cash from financing activities	(34,471)	(38,126)
Net increase (decrease) in cash and cash equivalents	$ 8,189	$ (72,736)

Operating activities Cash flows from operating activities, our primary form of liquidity on a full-year basis, decreased by $27.2 million for the thirty-nine weeks of 2005, as compared to the same period in 2004. On a period-over-period basis, cash used for merchandise inventories, net of accounts payable, increased by $14.3 million, and the tax benefit related to exercise of stock options decreased by $8.3 million. Miscellaneous receivables increased by $4.4 million at October 29, 2005, compared to October 30, 2004.

Merchandise inventories increased by 40% as of October 29, 2005, as compared to the same period last year. On a square foot basis, merchandise inventories increased by 17% as of October 29, 2005, as compared to the same period in 2004, and decreased, by 17% per square foot as of October 30, 2004, as compared to the same period in 2003. We increased our inventory levels during 2005 in an effort to better capitalize upon perceived sales opportunities. However, sales fell significantly below our expectations. We anticipate that we will continue to utilize increased promotional activities throughout 2005 in an effort to increase customer demand for our merchandise offerings, and thereby reduce our inventory levels. We expect that this strategy will have an unfavorable impact on our gross margin through the remainder of 2005 and possibly into the first quarter of 2006, depending on the level of sales activity in the fourth quarter of 2005.

Due to the seasonality of our business, we have historically generated a significant portion of our cash flows from operating activities in the second half of the year, and we expect this trend to continue through the balance of this year.

Capital requirements Investments in capital expenditures are principally for the construction of new stores, remodeling of existing stores, and investments in information technology. Our future capital requirements will depend primarily on the number of new stores we open, the number of existing stores we remodel and the timing of these expenditures. We opened 101 new Aeropostale stores during the first thirty-nine weeks of 2005, and have opened 4

more during November 2005. We also opened our first 13 Jimmy Z stores, and have opened one more in November 2005. Capital expenditures for the full year of 2005 are expected to approximate $54 million to open the new stores discussed above, to remodel certain existing stores, and to improve and enhance our information technology systems. We plan to open approximately 65 new Aeropostale stores and approximately 5 new Jimmy Z stores in 2006.

We had $20.1 million in short-term investments at October 29, 2005, consisting of auction rate debt and preferred stock securities. Auction rate securities are term securities that earn income at a rate that is periodically reset, typically within 35 days, to reflect current market conditions through an auction process. These securities have long-term contractual maturities and are classified as available-for-sale securities in

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the current asset section of our condensed consolidated balance sheet as of October 29, 2005. These securities were previously recorded in cash and cash equivalents in our interim 2004 condensed consolidated financial statements, and have been reclassified accordingly in the accompanying consolidated financial statements. There was no impact on net income, stockholders equity, debt covenants or cash flow from operations as a result of this reclassification.

Financing activities and capital resources We repurchase our common stock from time to time under a stock repurchase program. In November 2005, our Board of Directors approved an additional $50.0 million repurchase availability, thereby increasing the total amount of repurchase availability under this program to $150.0 million. The repurchase program may be modified or terminated by the Board of Directors at any time, and there is no expiration date for the program. The extent and timing of repurchases will depend upon general business and market conditions, stock prices, and liquidity and capital resource requirements going forward. We repurchased 1,454,000 shares for $35.6 million during the first thirty-nine weeks of 2005, versus 1,554,000 shares for $39.1 million during the same period last year. Since the inception of the repurchase program, we have repurchased a total of 4.2 million shares of our common stock for total consideration of $99.3 million. At October 29, 2005 we would have had $50.7 million of repurchase availability remaining, after including the additional $50 million of availability approved in November 2005.

In April 2005, we amended our revolving credit facility to allow us to borrow or obtain letters of credit up to at least an aggregate of $50 million (see note 7 to the Notes to Unaudited Condensed Consolidated Financial Statements for a further discussion). At October 29, 2005, we had no amounts outstanding under the credit facility, and no stand-by or commercial letters of credit issued under the credit facility. As of October 29, 2005, we were in compliance with all covenants under the credit facility. In addition, we have not had outstanding borrowings under the credit facility since November 2002.

Contractual Obligations

The following table summarizes our contractual obligations as of October 29, 2005:

	Payments Due				
	Total	**Balance of 2005**	**In 2006 and 2007**	**In 2008 and 2009**	**After 2009**
	(In Thousands)				
Contractual Obligations					
Employment agreements	$ 3,807	$ 603	$ 3,204	$	$
Event sponsorship agreement	1,810		1,810		
Operating leases	482,139	15,855	124,440	122,797	219,047
Total contractual obligations	$ 487,756	$ 16,458	$ 129,454	$ 122,797	$ 219,047

Annual computed bonuses in excess of capped amounts for certain members of our senior management are carried forward to the following year. As of October 29, 2005, $3.3 million was available for carry forward, and is payable dependant on the achievement of certain financial performance criteria. This carry forward amount was not accrued at October 29, 2005, and is not included in the above table, since we did not expect the payment criteria to be achieved. The operating leases included in the above table do not include contingent rent based upon sales volume, which represented approximately 17% of minimum lease obligations in 2004, or variable costs such as maintenance, insurance and taxes, which represented approximately 53% of minimum lease obligations in 2004. Our open purchase

orders are cancelable without penalty and are therefore not included in the above table. We have not provided any financial guarantees as of October 29, 2005.

Off-Balance Sheet Arrangements

We have not created, and are not party to, any special-purpose or off-balance sheet entities for the purpose of raising capital, incurring debt or operating our business. We do not have any arrangements or relationships with entities that are not consolidated into the financial statements that are reasonably likely to

materially affect our liquidity or the availability of capital resources. As of October 29, 2005, we have not issued any letters of credit for the purchase of merchandise inventory or any capital expenditures.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the appropriate application of certain accounting policies, many of which require us to make estimates and assumptions about future events and their impact on amounts reported in our financial statements and related notes. We believe the application of our accounting policies, and the estimates inherently required therein, are reasonable. These accounting policies and estimates are constantly reevaluated, and adjustments are made when facts and circumstances dictate a change. However, since future events and their impact cannot be determined with certainty, actual results may differ from our estimates, and such differences could be material to the consolidated financial statements. Historically, we have found our application of accounting policies to be appropriate, and actual results have not differed materially from those determined using necessary estimates. A summary of our significant accounting policies and a description of accounting policies that we believe are most critical may be found in the MD&A included in our Annual Report on Form 10-K for the year ended January 29, 2005.

Item 3. ***Quantitative and Qualitative Disclosures About Market Risk***

At October 29, 2005, we had no borrowings outstanding under our credit facility and we have not had any borrowings outstanding under our credit facility since November 2002. To the extent that we may borrow pursuant to our credit facility in the future, we may be exposed to market risk related to interest rate fluctuations. Additionally, we have not entered into financial instruments for hedging purposes.

Item 4. ***Controls and Procedures***

(a) *Evaluation of Disclosure Controls and Procedures:* Pursuant to Exchange Act Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (the Exchange Act), our management carried out an evaluation, under the supervision and with the participation of our Chairman and Chief Executive Officer along with our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls (as defined in Rule 13a-15(e) of the Exchange Act) and procedures. Based upon that evaluation, our Chief Executive Officer along with our Chief Financial Officer concluded that as of the end of our 2005 third quarter, ended October 29, 2005, our disclosure controls and procedures (1) are effective in timely alerting them to material information relating to our company (including its consolidated subsidiaries) required to be included in our periodic SEC filings and (2) are adequate to ensure that information required to be disclosed by us in the reports filed or submitted by us under the Exchange Act is recorded, processed and summarized and reported within the time periods specified in the SEC s rules and forms. It should be noted, however, that the design of any system of controls is limited in its ability to detect errors and therefore there can be no assurance that any design of system controls will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

(b) *Changes in internal controls:* During the period covered by this quarterly report, there have been no significant changes in our internal controls over our financial reporting that have materially affected, or are reasonably likely to materially affect, our internal controls over our financial reporting.

Cautionary Note Regarding Forward-Looking Statements and Risk Factors

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Such forward-looking statements involve certain risks and uncertainties, including statements regarding the company s strategic direction, prospects and

future results. Certain factors, including factors outside of our control, may cause actual results to differ materially from those contained in the forward-looking statements. The following risk factors should be read in connection with evaluating the Company s business and future prospects. All forward looking statements included in this report are based on information available to us as of

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the date hereof, and we assume no obligation to update or revise such forward-looking statements to reflect events or circumstances that occur after such statements are made. Such uncertainties include, among others, the following factors:

Fluctuations in comparable store sales and quarterly results of operations may cause the price of our common stock to decline substantially.

Our comparable store sales and quarterly results of operations have fluctuated in the past and are likely to continue to fluctuate in the future. In addition, there can be no assurance that we will be able to maintain or increase our recent levels of comparable store sales as our business continues to expand. Our comparable store sales and quarterly results of operations are affected by a variety of factors, including:

- fashion trends;
- changes in our merchandise mix;
- the effectiveness of our inventory management;
- actions of competitors or mall anchor tenants;
- calendar shifts of holiday or seasonal periods;
- the timing of promotional events;
- weather conditions; and
- changes in general economic conditions and consumer spending patterns.

If our future comparable store sales fail to meet the expectations of investors, then the market price of our common stock could decline substantially. You should refer to the section entitled Management s Discussion and Analysis of Financial Condition and Results of Operations for more information.

If we are unable to identify and respond to consumers fashion preferences in a timely manner, our profitability would decline.

We may not be able to keep pace with the rapidly changing fashion trends and consumer tastes inherent in the apparel industry. Our current design philosophy is based on the belief that our target customers prefer clothing that suits the demands of their active lifestyles and that they like to identify with a logo. Accordingly, we produce casual, comfortable apparel, a majority of which displays either the Aéropostale or Aéro logo. There can be no assurance that fashion trends will not move away from casual clothing or that we will not have to alter our design strategy to reflect a consumer change in logo preference. Failing to anticipate, identify or react appropriately to changes in styles, trends, desired images or brand preferences, could have a material adverse effect on the Company s sales, financial condition and results of operations.

Our business could suffer as a result of a manufacturer s inability to produce merchandise on time and to specifications.

We do not own or operate any manufacturing facilities and therefore we depend upon independent third parties for the manufacture of all of our merchandise. We utilize both domestic and international manufacturers to produce our

merchandise. The inability of a manufacturer to ship orders in a timely manner or meet our quality standards could cause delivery date requirements to be missed, which could result in lost sales.

Our business could suffer if a manufacturer fails to use acceptable labor practices.

Our sourcing agents and independent manufacturers are required to operate in compliance with all applicable foreign and domestic laws and regulations. While our vendor operating guidelines promote ethical business practices for our vendors and suppliers, we do not control these manufacturers or their labor practices. The violation of labor or other laws by an independent manufacturer, or by one of the sourcing agents, or the divergence of an independent manufacturer s or sourcing agent s labor practices from those generally accepted

as ethical in the United States, could interrupt, or otherwise disrupt the shipment of finished products or damage the Company s reputation. Any of these, in turn, could have a material adverse effect on the Company s financial condition and results of operations.

We rely on a small number of vendors to supply a significant amount of our merchandise.

In 2004, we sourced 35% of our merchandise from our top three vendors; one company supplied 15% of our merchandise, and two others each supplied 10% of our merchandise. In addition, approximately 68% of our merchandise was directly sourced from our top ten vendors, and one company acted as our agent with respect to the sourcing of 21% of our merchandise. Our relationships with our vendors generally are not on a contractual basis and do not provide assurances on a long-term basis as to adequate supply, quality or acceptable pricing. Most of our vendors could discontinue selling to us at any time. If one or more of our significant vendors were to sever their relationship with us, we could be unable to obtain replacement products in a timely manner, which could cause our sales to decrease.

Failure of a new business concept could have a material adverse effect on our results of operations and our business

We expect that the introduction of new brand concepts and other business opportunities will play an important role in our growth strategy. In particular, we have and will continue to open our Jimmy Z brand stores. The operation of the Jimmy Z stores and the sale of Aéropostale, and potentially Jimmy Z, merchandise over the Internet through our e-commerce business, are subject to numerous risks, including unanticipated operating problems; lack of prior experience; lack of customer acceptance; new vendor relationships; competition from existing and new retailers; and diversion of management s attention from the Company s core Aéropostale business. The Jimmy Z concept involves, among other things, implementation of a retail apparel concept which is subject to many of the same risks as Aéropostale, as well as additional risks inherent with a more fashion driven concept, including risks of difficulty in merchandising, uncertainty of customer acceptance, fluctuations in fashion trends and customer tastes, as well as the attendant mark-down risks. Risks inherent in any new concept are particularly acute with respect to Jimmy Z because this is the first significant new venture by us, and the nature of the Jimmy Z business differs in certain respects from that of our core Aéropostale business. There can be no assurance that the Jimmy Z stores or our e-commerce business will achieve sales and profitability levels justifying our investments in these businesses. If those sales levels are not achieved we may be forced to impair the carrying value of our investments, which may have a material adverse effect on our results of operations.

Foreign suppliers manufacture most of our merchandise and the availability and costs of these products may be negatively affected by risks associated with international trade.

Trade restrictions such as increased tariffs or quotas, or both, could affect the importation of apparel generally and increase the cost and reduce the supply of merchandise available to us. Much of our merchandise is sourced directly from foreign vendors in Europe, Asia and Central America. In addition, many of our domestic vendors maintain production facilities overseas. Some of these facilities are also located in regions that may be affected by political instability that could cause a disruption in trade. Any reduction in merchandise available to us or any increase in its cost due to tariffs, quotas or local political issues could have a material adverse effect on our results of operations.

Our storeline growth strategy relies on the continued addition of a significant number of new stores each year, which could strain our resources and cause the performance of our existing stores to suffer.

Our growth will largely depend on our ability to open and operate new stores successfully. We opened 103 stores in 2004, 95 stores in 2003 and 93 stores in 2002. Additionally, we opened 105 new Aéropostale stores and 14 new

Jimmy Z stores during 2005. We expect to continue to open a significant number of new stores in future years while also remodeling a portion of our existing store base. Our planned expansion will place increased demands on our operational, managerial and administrative resources. These increased

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demands could cause us to operate our business less effectively, which in turn could cause deterioration in the financial performance of our individual stores. In addition, to the extent that our new store openings are in existing markets, we may experience a reduction in net sales volume, in previously existing stores in those same markets.

Our continued expansion plan is dependent on a number of factors which, if not implemented, could delay or prevent the successful opening of new stores and penetration into new markets.

Unless we continue to do the following, we may be unable to open new stores successfully and, if so, our continued growth would be impaired:

- identify suitable markets and sites for new store locations;
- negotiate acceptable lease terms;
- hire, train and retain competent store personnel;
- foster current relationships and develop new relationships with vendors that are capable of supplying a greater volume of merchandise;
- manage inventory effectively to meet the needs of new and existing stores on a timely basis;
- expand our infrastructure to accommodate growth; and
- generate sufficient operating cash flows or secure adequate capital on commercially reasonable terms to fund our expansion plans.

In addition, we will open new stores in markets in the United States in which we currently have few or no stores. Our experience in these markets is limited and there can be no assurance that we will be able to develop our brand in these markets or adapt to competitive, merchandising and distribution challenges that may be different from those in our existing markets. Our inability to open new stores successfully and/or penetrate new markets would have a material adverse effect on our revenue and earnings growth.

The loss of the services of key personnel could have a material adverse effect on our business.

The Company s key executive officers have substantial experience and expertise in the retail business and have made significant contributions to the growth and success of the Company s brands. The unexpected loss of the services of one or more of these individuals could adversely affect the Company. Specifically, if we were to lose the services of Julian R. Geiger, our Chairman and Chief Executive Officer, and/or Christopher L. Finazzo, our Executive Vice President-Chief Merchandising Officer, our business could be adversely affected. In addition, Mr. Geiger and Mr. Finazzo maintain many of our vendor relationships, and the loss of either of them could negatively impact present vendor relationships.

Our net sales and inventory levels fluctuate on a seasonal basis.

Our net sales and net income are disproportionately higher from August through January each year due to increased sales from back-to-school and holiday shopping. Sales during this period cannot be used as an accurate indicator for our annual results. Our net sales and net income from February through July are typically lower due to, in part, the traditional retail slowdown immediately following the winter holiday season. Any significant decrease in sales during the back-to-school and winter holiday seasons would have a material adverse effect on our financial condition and

results of operations. In addition, in order to prepare for the back-to-school and holiday shopping seasons, we must order and keep in stock significantly more merchandise than we would carry during other parts of the year. Any unanticipated decrease in demand for our products during these peak shopping seasons could require us to sell excess inventory at a substantial markdown, which could reduce our net sales and gross margins and negatively impact our profitability.

A downturn in the United States economy may affect consumer spending habits.

Consumer purchases of discretionary items and retail products, including the Company s products, may decline during recessionary periods and also may decline at other times when disposable income or consumer confidence is lower. A downturn in the economy may adversely affect our sales.

Our ability to attract customers to our stores depends heavily on the success of the shopping malls in which we are located.

In order to generate customer traffic, we must locate our stores in prominent locations within successful shopping malls. We cannot control the development of new shopping malls, the availability or cost of appropriate locations within existing or new shopping malls, or the success of individual shopping malls. A significant decrease in shopping mall traffic would have a material adverse effect on our results of operations.

We rely on a single distribution center.

We maintain one distribution center to receive, store and distribute merchandise to all of our stores. Any significant interruption in the operation of the distribution center due to natural disasters, accidents, system failures or other unforeseen causes could have a material adverse effect on the Company s financial condition and results.

We rely on a third party to manage our distribution center.

The efficient operation of our stores is dependent on our ability to distribute, in a timely manner, merchandise to our store locations throughout the United States. An independent third party operates our distribution and warehouse facility. We depend on this third party to receive, sort, pack and distribute substantially all of our merchandise. This third party employs personnel represented by a labor union. Although there have been no work stoppages or disruptions since the inception of our relationship with this third party provider beginning in 1991, there can be no assurance that work stoppages or disruptions will not occur in the future. We also use a separate third party transportation company to deliver our merchandise from our warehouse to our stores. Any failure by either of these third parties to respond adequately to our warehousing and distribution needs would disrupt our operations and negatively impact our profitability.

We rely on a third party to administer to certain aspects of our e-commerce business.

Under an e-commerce agreement with GSI Commerce, Inc. (GSI), GSI operates the retail potion of our website, www.aeropostale.com. Under this agreement, GSI owns certain content and technology related to the website, hosts and maintains the website, and fulfills orders through the website, as well as furnishing all other back-end operations required to operate the website. Any significant interruption of operations at GSI due to natural disasters, accidents, system failures or other unforeseen causes would have a material adverse effect on the Company s e-commerce business.

Failure to protect our trademarks adequately could negatively impact our brand image and limit our ability to penetrate new markets.

We believe that our key trademarks AÉROPOSTALE®, JIMMY Z and, to a lesser extent, AERO® and the Woody Car Design are integral to our logo-driven design strategy. We have obtained a federal registration of the AÉROPOSTALE® and JIMMY Z trademarks and the Woody Car Design in the United States and, with regard to the AÉROPOSTALE® trademark, have applied for or obtained registrations in most foreign countries in which our vendors are located. We use the AERO mark in many constantly changing designs and logos even though we have not

applied to register every variation or combination thereof for adult clothing. We have also expanded the scope of our filings in the United States Patent and Trademark Office for a greater number of apparel and accessory categories. There can be no assurance that the registrations we own and have obtained will prevent the imitation of our products or infringement of our intellectual property rights by others. If any third party imitates our products in a manner that projects lesser quality or carries a negative connotation, our brand image could be materially adversely affected. Because we have not registered the

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AERO mark in all forms and categories and have not registered the AÉROPOSTALE , JIMMY Z and Woody Car Design marks in all categories or in all foreign countries in which we now or may in the future source or offer our merchandise, international expansion and our merchandising of non-apparel products using these marks could be limited.

In addition, there can be no assurance that others will not try to block the manufacture, export or sale of our products as violation of their trademarks or other proprietary rights. Other entities may have rights to trademarks that contain the word AERO or may have registered similar or competing marks for apparel and accessories in foreign countries in which our vendors are located. Our applications for international registration of the AÉROPOSTALE® mark have been rejected in several countries in which our products are manufactured because third parties have already registered the mark for clothing in those countries. There may also be other prior registrations in other foreign countries of which we are not aware. In addition, we do not own the Jimmy Z brand outside of the United States and Canada. Accordingly, it may be possible, in those foreign countries where we were not been able to register the AÉROPOSTALE® mark, or in the countries where the Jimmy Z brand is owned by a third party, for a third party owner of the national trademark registration for AÉROPOSTALE , JIMMY Z or the Woody Car Design to enjoin the manufacture, sale or exportation of Aéropostale or Jimmy Z branded goods to the United States. If we were unable to reach a licensing arrangement with these parties, our vendors may be unable to manufacture our products in those countries. Our inability to register our trademarks or purchase or license the right to use our trademarks or logos in these jurisdictions could limit our ability to obtain supplies from or manufacture in less costly markets or penetrate new markets should our business plan change to include selling our merchandise in those jurisdictions outside the United States.

The effects of war or acts of terrorism could have a material adverse effect on our operating results and financial condition.

The continued threat of terrorism, heightened security measures and military action in response to an act of terrorism has disrupted commerce and has intensified the uncertainty of the U.S. economy. Any further acts of terrorism or a future war may disrupt commerce and undermine consumer confidence, which could negatively impact our sales revenue by causing consumer spending and/or mall traffic to decline. Furthermore, an act of terrorism or war, or the threat thereof, could negatively impact our business by interfering with our ability to obtain merchandise from foreign vendors. Inability to obtain merchandise from our foreign vendors or substitute other vendors, at similar costs and in a timely manner, could adversely affect our operating results and financial condition.

PART II

OTHER INFORMATION

Item 1. *Legal Proceedings*

We are party to various litigation matters and proceedings in the ordinary course of business. In the opinion of our management, dispositions of these matters are not expected to have a material adverse affect on our financial position, results from operations or cash flows.

Item 2. ***Unregistered Sales of Equity Securities and Use of Proceeds***

Our Board of Directors has authorized a share repurchase program of our outstanding common stock in the amount of $150.0 million. Our purchases of treasury stock for the third quarter ended October 29, 2005 pursuant to the share repurchase program, and remaining repurchase availability at that date, were as follows:

Period	Total Number of Shares (or Units) Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (In Thousands)
August 2005	270,000	$ 24.57	270,000	$ 68,551
September 2005	540,000	$ 23.88	540,000	$ 55,655
October 2005	259,000	$ 19.04	259,000	$ 50,724
Total	1,069,000	$ 22.88	1,069,000	$ 50,724

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

Not applicable.

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

Not applicable.

Item 5. ***Other Information***

Not applicable.

Item 6. ***Exhibits***

31.1	Certification by Julian R. Geiger, Chairman and Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by Michael J. Cunningham, Executive Vice President and Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by Julian R. Geiger pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification by Michael J. Cunningham pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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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.

Aeropostale, Inc.

/s/ Julian R. Geiger
Julian R. Geiger
Chairman of the Board and Chief Executive Officer
(Principal Executive Officer)

/s/ Michael J. Cunningham
Michael J. Cunningham
Executive Vice President Chief Financial Officer
(Principal Financial Officer)

Dated: December 1, 2005