DOLLAR GENERAL CORP
Form 10-Q
September 03, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended August 1, 2008

Commission File Number: 001-11421

DOLLAR GENERAL CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

TENNESSEE	**61-0502302**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

100 MISSION RIDGE
GOODLETTSVILLE, TN 37072
(Address of principal executive offices, zip code)

(615) 855-4000

(Registrant s telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

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

Large accelerated filer [ ]

Accelerated filer [ ]

Non-accelerated filer [X]

Smaller reporting company [ ]

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

The Registrant had 555,876,560 shares of common stock, $0.50 par value per share, outstanding as of August 29, 2008.

PART I FINANCIAL INFORMATION

ITEM 1.

FINANCIAL STATEMENTS.

DOLLAR GENERAL CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

	August 1, 2008 (Unaudited)	February 1, 2008 (see Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 261,630	$ 100,209
Short-term investments	2,597	19,611
Merchandise inventories	1,490,063	1,288,661
Income taxes receivable	12,829	32,501
Deferred income taxes	17,395	17,297
Prepaid expenses and other current assets	68,287	59,465
Total current assets	1,852,801	1,517,744
Net property and equipment	1,266,722	1,274,245
Goodwill	4,344,930	4,344,930
Intangible assets, net	1,347,948	1,370,557
Other assets, net	97,389	148,955
Total assets	$ 8,909,790	$ 8,656,431
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current portion of long-term obligations	$ 2,999	$ 3,246
Accounts payable	818,246	551,040
Accrued expenses and other	341,728	300,956
Income taxes payable	1,744	2,999

Total current liabilities	1,164,717	858,241
Long-term obligations	4,177,610	4,278,756
Deferred income taxes	483,867	486,725
Other liabilities	305,636	319,714
Redeemable common stock	11,157	9,122
Shareholders equity:		
Preferred stock	-	-
Common stock	277,712	277,741
Additional paid-in capital	2,484,606	2,480,062
Retained earnings (accumulated deficit)	28,816	(4,818)
Accumulated other comprehensive loss	(24,331)	(49,112)
Total shareholders equity	2,766,803	2,703,873
Total liabilities and shareholders equity	$ 8,909,790	$ 8,656,431

See notes to condensed consolidated financial statements.

DOLLAR GENERAL CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands)

	Successor		Predecessor
	13-weeks ended August 1, 2008	July 7, 2007 through August 3, 2007 (a)	May 5, 2007 through July 6, 2007
Net sales	$ 2,609,384	$ 699,078	$ 1,648,486
Cost of goods sold	1,851,349	514,355	1,209,971
Gross profit	758,035	184,723	438,515
Selling, general and administrative	614,980	190,440	388,839
Transaction and related costs	-	308	95,791
Operating profit (loss)	143,055	(6,025)	(46,115)
Interest income	(1,217)	(1,033)	(2,473)
Interest expense	99,434	36,520	4,132
Other (income) expense	292	(567)	-
Income (loss) before income taxes	44,546	(40,945)	(47,774)
Income tax expense (benefit)	16,828	(14,995)	(4,906)
Net income (loss)	$ 27,718	$ (25,950)	$ (42,868)

(a)

Includes the results of operations of Buck Acquisition Corp. for the period from May 5, 2007 through July 6, 2007, prior to its merger with and into Dollar General Corporation (reflecting the change in fair value of interest rate swaps), and the post-merger results of Dollar General Corporation for the period from July 7, 2007 through August 3, 2007. See Note 1.

See notes to condensed consolidated financial statements.

DOLLAR GENERAL CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands)

	Successor		Predecessor
	26-weeks ended August 1, 2008	July 7, 2007 through August 3, 2007 (a)	February 3, 2007 through July 6, 2007
Net sales	$ 5,012,882	$ 699,078	$ 3,923,753
Cost of goods sold	3,561,770	514,355	2,852,178
Gross profit	1,451,112	184,723	1,071,575
Selling, general and administrative	1,197,186	190,440	960,930
Transaction and related costs	-	308	101,397
Operating profit (loss)	253,926	(6,025)	9,248
Interest income	(2,174)	(1,033)	(5,046)
Interest expense	200,305	36,520	10,299
Other (income) expense	590	1,448	-
Income (loss) before income taxes	55,205	(42,960)	3,995
Income tax expense (benefit)	21,571	(15,785)	11,993
Net income (loss)	$ 33,634	$ (27,175)	$ (7,998)

(a)

Includes the results of operations of Buck Acquisition Corp. for the period from March 6, 2007 (its formation) through July 6, 2007, prior to its merger with and into Dollar General Corporation (reflecting the change in fair value of interest rate swaps), and the post-merger results of Dollar General Corporation for the period from July 7, 2007 through August 3, 2007. See Note 1.

See notes to condensed consolidated financial statements.

DOLLAR GENERAL CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

	Successor		Predecessor
	26-weeks ended August 1, 2008	July 7, 2007 through August 3, 2007 (a)	February 3, 2007 through July 6, 2007
Cash flows from operating activities:			
Net income (loss)	$ 33,634	$ (27,175)	$ (7,998)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	122,023	25,575	83,917
Deferred income taxes	(18,208)	(14,378)	(20,874)
Noncash LIFO charge	16,037	-	-
Noncash share-based compensation	4,516	1,170	45,433
Tax benefit from stock option exercises	(475)	-	(3,927)
Noncash unrealized gain on interest rate swap	-	(4,739)	-
Change in operating assets and liabilities:			
Merchandise inventories	(217,439)	(27,027)	16,424
Prepaid expenses and other current assets	(6,060)	(8,711)	(6,184)
Accounts payable	262,415	(28,439)	34,794
Accrued expenses and other liabilities	68,692	26,254	52,995
Income taxes	18,892	(2,188)	2,809
Other	12,497	15	4,557
Net cash provided by (used in) operating activities	296,524	(59,643)	201,946
Cash flows from investing activities:			
Merger, net of cash acquired	-	(6,724,370)	-
Purchases of property and equipment	(80,100)	(11,400)	(56,153)
Purchases of short-term investments	(9,903)	-	(5,100)
Sales of short-term investments	58,950	1,000	9,505
Purchases of long-term investments	-	(4,662)	(15,754)
	683	162	620

Proceeds from sale of property and equipment			
Net cash used in investing activities	(30,370)	(6,739,270)	(66,882)
Cash flows from financing activities:			
Issuance of common stock	-	2,765,443	-
Issuance of long-term obligations	-	4,176,817	-
Repayments of long-term obligations	(2,195)	(210,298)	(4,500)
Borrowings under revolving credit facilities	-	432,300	-
Repayments of borrowings under revolving credit facilities	(102,500)	(132,300)	-
Debt issuance costs	-	(109,379)	-
Payment of cash dividends	-	-	(15,710)
Proceeds from exercise of stock options	-	-	41,546
Repurchases of common stock	(513)	-	-
Tax benefit of stock options	475	-	3,927
Net cash provided by (used in) financing activities	(104,733)	6,922,583	25,263
Net increase in cash and cash equivalents	161,421	123,670	160,327
Cash and cash equivalents, beginning of period	100,209	-	189,288
Cash and cash equivalents, end of period	$ 261,630	$ 123,670	$ 349,615

Supplemental schedule of noncash investing and financing activities:			
Purchases of property and equipment awaiting processing for payment, included in Accounts payable	$ 25,240	$ 10,183	$ 13,544
Purchases of property and equipment under capital lease obligations	$ 2,314	$ 540	$ 1,036
Expiration of equity repurchase rights	$ 2,548	$ -	$ -
Exchange of shares and stock options in business combination	$ -	$ 7,685	$ -

(a)

Includes the results of operations of Buck Acquisition Corp. for the period from March 6, 2007 (its formation) through July 6, 2007, prior to its merger with and into Dollar General Corporation (reflecting the change in fair value of interest rate swaps), and the post-merger results of Dollar General Corporation for the period from July 7, 2007 through August 3, 2007. See Note 1.

See notes to condensed consolidated financial statements.

DOLLAR GENERAL CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1.

Basis of presentation

The accompanying unaudited condensed consolidated financial statements of Dollar General Corporation and its subsidiaries (the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and are presented in accordance with the requirements of Form 10-Q and Rule 10-01 of Regulation S-X. Such financial statements consequently do not include all of the disclosures normally required by U.S. GAAP or those normally made in the Company s Annual Report on Form 10-K. Accordingly, the reader of this Quarterly Report on Form 10-Q should refer to the Company s Annual Report on Form 10-K for the fiscal year ended February 1, 2008 for additional information.

The Company was acquired on July 6, 2007 through a merger with Buck Acquisition Corp. (Buck) accounted for as a reverse acquisition (the Merger). The Merger was funded primarily through debt financings and cash equity contributions from investment funds affiliated with Kohlberg Kravis Roberts & Co., L.P. (KKR), GS Capital Partners VI Fund, L.P. and affiliated funds (affiliates of Goldman, Sachs & Co.), Citi Private Equity, Wellington Management Company, LLP, CPP Investment Board (USRE II) Inc. and other equity co-investors (collectively, the Investors). Although the Company continued as the same legal entity after the Merger, the accompanying condensed consolidated financial statements are presented for the Predecessor and Successor relating to the periods preceding and succeeding the Merger, respectively, as follows:

- All periods presented for the Successor, including the 2008 periods, reflect the Merger of the Company and Buck, as a result of the Company applying purchase accounting and a new basis of accounting beginning on July 7, 2007.

- The 2007 13-week period presented includes the Predecessor period of the Company from May 5, 2007 to July 6, 2007 and the post-Merger Successor period from July 7, 2007 to August 3, 2007. The consolidated financial statements for the Predecessor periods have been prepared using the pre-merger historical basis of accounting for the Company. As a result of purchase accounting, the pre-Merger and post-Merger financial results are not comparable.

- The 2007 26-week period presented includes the Predecessor period of the Company from February 3, 2007 to July 6, 2007 and the post-Merger Successor period from July 7, 2007 to August 3, 2007.

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The results of operations of Buck for the period from March 6, 2007 (its formation) to July 6, 2007 (prior to its merger with and into the Company on July 6, 2007) also are included in the condensed consolidated financial statements of the Successor for the periods described above, where applicable, as a result of certain derivative financial instruments entered into by Buck prior to the Merger as further described in Note 3. Prior to the Merger, Buck had no assets, liabilities, or operations other than the derivatives.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the Company s customary accounting practices. In management s opinion, all adjustments (which are of a normal recurring nature) necessary for a fair presentation of the consolidated financial position for the accounting periods presented for the Predecessor, Successor and Buck as described above, have been made. Because the Company s business is moderately seasonal, the financial results for interim periods are not necessarily indicative of the results to be expected for the entire year.

The condensed consolidated balance sheet as of February 1, 2008 has been derived from the audited consolidated financial statements at that date but does not include all of the information and notes required by U.S. GAAP for complete financial statements.

The preparation of financial statements in conformity with U.S. GAAP requires the Company to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. The Company uses the last-in, first-out (LIFO) method of valuing inventory. An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management s estimates of expected year-end inventory levels, sales for the year and the expected rate of inflation/deflation for the year and are thus subject to adjustment in the final year-end LIFO inventory valuation. As a result of commodity-related inflationary cost pressures experienced by the Company in the 13-week period ended August 1, 2008, and its expectations of continued inflation, the Company recorded a $16.0 million LIFO charge in the 13-week period ended August 1, 2008. In addition, ongoing estimates of inventory shrinkage and initial markups and markdowns are included in the interim cost of goods sold calculation.

Certain financial statement amounts relating to prior periods have been reclassified to conform to the current period presentation.

As discussed in Note 3, effective February 2, 2008 the Company changed its accounting for the fair value of certain financial assets and liabilities in connection with the adoption of Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements. The adoption resulted in a $4.7 million decrease in liability balances associated with interest rate swaps that the Company uses to manage interest rate risk, with the offset reflected in other comprehensive income.

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles. SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with U.S. GAAP (the GAAP hierarchy). SFAS 162 will be effective 60 days following the approval by the Securities and Exchange Commission (the SEC) of the Public Company Accounting Oversight Board (the PCAOB) amendments to AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. The Company plans to adopt SFAS 162 once it is effective and does not expect this standard to materially impact its financial statements.

2.

Comprehensive income (loss)

Comprehensive income (loss) consists of the following:

	Successor		Predecessor
(in thousands)	13- weeks ended August 1, 2008	July 7, 2007 through August 3, 2007 (a)	May 5, 2007 through July 6, 2007
Net income (loss)	$ 27,718	$ (25,950)	$ (42,868)
Unrealized net gain on hedged transactions, net of income taxes (see Note 3)	6,308	-	-
Reclassification of net loss on derivatives	-	-	30
Comprehensive income (loss)	$ 34,026	$ (25,950)	$ (42,838)

	Successor		Predecessor
(in thousands)	26-weeks ended August 1, 2008	July 7, 2007 through August 3, 2007 (b)	February 3, 2007 through July 6, 2007
Net income (loss)	$ 33,634	$ (27,175)	$ (7,998)
Unrealized net gain on hedged transactions, net of income taxes (see Note 3)	24,781	-	-
Reclassification of net loss on derivatives	-	-	76
Comprehensive income (loss)	$ 58,415	$ (27,175)	$ (7,922)

(a) Includes results of operations for Buck from May 5, 2007 through July 6, 2007. See Note 1.

(b) Includes results of operations for Buck from March 6, 2007 through July 6, 2007. See Note 1.

3.

Assets and liabilities measured at fair value

On February 2, 2008, the Company adopted components of SFAS No. 157, Fair Value Measurements . SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements. Accordingly, the standard does not require any new fair value measurements of reported balances.

SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, SFAS 157 establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity s own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs are inputs other than quoted prices included in Level 1 that are directly or indirectly observable for the asset or liability. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, which are typically based on an entity s own assumptions, as there is little, if any, related market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

In April 2007, Buck entered into interest rate swaps, contingent upon the completion of the Merger, on a portion of the loans anticipated to result from the Merger. These swaps were designated as cash flow hedges in October 2007. As a result of these swaps, the Company is paying an all-in fixed interest rate of 7.683% on a notional amount equal to $1.46 billion as of August 1, 2008. As of August 3, 2007, the instruments had not been designated as hedges and, therefore, unrealized gains of $6.8 million and $4.7 million for the respective Successor periods ended August 3, 2007 have been recognized in Other (income) expense in the condensed consolidated statements of operations, reflecting the changes in fair value of the swaps.

In February 2008, the Company entered into an additional interest rate swap, which was designated as a cash flow hedge at its inception, resulting in the Company paying an all-in fixed interest rate of 5.58% on a notional amount of $350.0 million as of August 1, 2008. The Company uses interest rate swaps to manage its interest rate risk.

The valuation of the Company s derivative financial instruments is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves. The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash payments (or receipts) and the discounted expected variable cash receipts (or payments). The variable cash receipts (or payments) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves.

To comply with the provisions of SFAS 157, the Company incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty s nonperformance risk in the fair value measurements. In adjusting the fair value of its derivative contracts for the effect of nonperformance risk, the Company has considered the impact of netting and any applicable credit enhancements, such as collateral postings, thresholds, mutual puts, and guarantees.

Although the Company has determined that the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. However, as of August 1, 2008, the Company has assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined that the credit valuation adjustments are not significant to the overall valuation of its derivatives. As a result, the Company has determined that its derivative valuations in their entirety are classified in Level 2 of the fair value hierarchy.

The table below presents the Company s assets and liabilities measured at fair value on a recurring basis as of August 1, 2008, aggregated by the level in the fair value hierarchy within which those measurements fall.

(In thousands)	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at August 1, 2008
Assets:				
Available-for-sale securities (a)	$ 9,497	$ -	$ -	$ 9,497
Trading securities (b)	12,915	-	-	12,915
Derivative financial instruments (c)	-	318	-	318
Liabilities:				
Derivative financial instruments (d)	-	43,078	-	43,078

(a)

Reflected in the condensed consolidated balance sheet as Cash and cash equivalents of $6,900 and Short-term investments of $2,597

(b)

Reflected in the condensed consolidated balance sheet as Other current assets of $1,972 and Other assets, net of $10,943.

(c)

Reflected in the condensed consolidated balance sheet as Other assets, net.

(d)

Reflected in the condensed consolidated balance sheet as Other (noncurrent) liabilities.

The Company does not have any fair value measurements using significant unobservable inputs (Level 3) as of August 1, 2008.

4.

Strategic initiatives

During 2006, the Company began implementing certain strategic initiatives related to its historical inventory management and real estate strategies, as more fully described below.

Inventory management

In 2006, the Company undertook an initiative to discontinue its historical inventory packaway model for virtually all merchandise by the end of fiscal 2007 and recorded a reserve for lower of cost or market inventory impairment estimates. This reserve was reduced by $13.8 million during 2007 prior to the Merger to account for sales of products with markdowns below cost, higher than anticipated shrink during the period, and adjustments to the estimates of the remaining below cost markdowns to be taken. In connection with this strategic change, the

Company incurred higher markdowns and writedowns on inventory in the 2007 Predecessor periods than in the comparable prior-year periods. As a result of the Merger and in accordance with SFAS 141, the Company s inventory balances, including the inventory associated with this strategic change, were adjusted to fair value and the related reserve was eliminated.

Exit and disposal activities

In 2006 and 2007, the Company implemented plans to close, in addition to those stores that might be closed in the ordinary course of business, approximately 460 stores, all of which were closed by the end of fiscal 2007. Approximately 400 of such stores were closed as of August 1, 2007, and the Company incurred pretax costs of $31.0 million in the Predecessor period from February 3, 2007 through July 6, 2007, including $17.8 million of lease contract termination costs, $3.9 million of asset impairment and accelerated depreciation, $2.8 million of inventory liquidation fees, $0.9 million of inventory markdowns below cost, and $5.6 million of other associated costs. Additional amounts associated with these store closings recorded as purchase price adjustments in connection with the Merger totaled $15.3 million, including $12.3 million of lease contract termination costs, $0.9 million of asset impairment and accelerated depreciation, $0.7 million of inventory markdowns below cost, and $1.4 million of other associated costs.

All pretax costs recorded as expenses associated with exit and disposal activities are included in selling, general and administrative (SG&A) expenses with the exception of the below-cost inventory adjustments which were included in cost of goods sold in 2007.

Liability balances related to exit activities discussed above are as follows (in millions):

	Balance, February 1, 2008	2008 Expenses	2008 Payments and Other	Balance, August 1, 2008
Lease contract termination costs	$ 20.1	$ 0.2	$ 6.6	$ 13.7
Other associated store closing costs	1.0	-	0.7	0.3
Total	$ 21.1	$ 0.2	$ 7.3	$ 14.0

5.

Commitments and contingencies

Leases

The Merger and certain of the related financing transactions may be interpreted as giving rise to certain trigger events (which may include events of default) under leases for three of the Company s distribution centers (DCs). While the Company does not believe such an interpretation would be appropriate under the terms of the leases, there is no guarantee that the Company will prevail on its position. In the event the Company does not prevail, the Company s net cost of acquiring the underlying assets could approximate $112 million. At this time, the Company does not believe the resolution of such issues would result in the purchase of these DCs; however, the payments associated with such an outcome would have a negative impact on the Company s liquidity. To minimize the uncertainty associated with such possible interpretations, the Company is negotiating the restructuring of these leases and the related

underlying debt. The ultimate resolution of these negotiations may result in additional losses, which may be material.

Legal proceedings

On August 7, 2006, a lawsuit entitled *Cynthia Richter, et al. v. Dolgencorp, Inc., et al.* was filed in the United States District Court for the Northern District of Alabama (Case No. 7:06-cv-01537-LSC) (Richter) in which the plaintiff alleges that she and other current and former Dollar General store managers were improperly classified as exempt executive employees under the Fair Labor Standards Act (FLSA) and seeks to recover overtime pay, liquidated damages, and attorneys fees and costs. On August 15, 2006, the Richter plaintiff filed a motion in which she asked the court to certify a nationwide class of current and former store managers. The Company opposed the plaintiff s motion. On March 23, 2007, the court conditionally certified a nationwide class of individuals who worked for Dollar General as store managers since August 7, 2003. The number of persons who will be included in the class has not been determined, and the court has not approved the Notice that will be sent to the class.

On May 30, 2007, the court stayed all proceedings in the case, including the sending of the Notice, to evaluate, among other things, certain appeals currently pending in the Eleventh Circuit involving claims similar to those raised in this action. That stay has been extended through September 15, 2008. During the stay, the statute of limitations will be tolled for potential class members. At its conclusion, the court will determine whether to extend the stay or to permit this action to proceed. If the court ultimately permits Notice to issue, the Company will have an opportunity at the close of the discovery period to seek decertification of the class, and the Company expects to file such a motion.

The Company believes that its store managers are and have been properly classified as exempt employees under the FLSA and that this action is not appropriate for collective action treatment. The Company intends to vigorously defend this action. However, at this time, it is not possible to predict whether the court ultimately will permit this action to proceed collectively, and no assurances can be given that the Company will be successful in the defense on the merits or otherwise. If the Company is not successful in its efforts to defend this action, the resolution could have a material adverse effect on the Company s financial statements as a whole.

On May 18, 2006, the Company was served with a lawsuit entitled *Tammy Brickey, Becky Norman, Rose Rochow, Sandra Cogswell and Melinda Sappington v. Dolgencorp, Inc. and Dollar General Corporation* (Western District of New York, Case No. 6:06-cv-06084-DGL, originally filed on February 9, 2006 and amended on May 12, 2006 (Brickey)). The Brickey plaintiffs seek to proceed collectively under the FLSA and as a class under New York, Ohio, Maryland and North Carolina wage and hour statutes on behalf of, among others, assistant store managers who claim to be owed wages (including overtime wages) under those statutes. At this time, it is not possible to predict whether the court will permit this action to proceed collectively or as a class. However, the Company believes that this action is not appropriate for either collective or class treatment and that the Company s wage and hour policies and practices comply with both federal and state law. The Company plans to vigorously defend this action; however, no assurances can be given that the Company will be successful in the defense on the

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merits or otherwise, and, if it is not successful, the resolution of this action could have a material adverse effect on the Company s financial statements as a whole.

On March 7, 2006, a complaint was filed in the United States District Court for the Northern District of Alabama (*Janet Calvert v. Dolgencorp, Inc.*, Case No. 2:06-cv-00465-VEH (Calvert)), in which the plaintiff, a former store manager, alleged that she was paid less than male store managers because of her sex, in violation of the Equal Pay Act and Title VII of the Civil Rights Act of 1964, as amended (Title VII). The complaint subsequently was amended to include additional plaintiffs, who also allege to have been paid less than males because of their sex, and to add allegations that the Company s compensation practices disparately impact females. Under the amended complaint, Plaintiffs seek to proceed collectively under the Equal Pay Act and as a class under Title VII, and request back wages, injunctive and declaratory relief, liquidated damages, punitive damages and attorney s fees and costs.

On July 9, 2007, the plaintiffs filed a motion in which they asked the court to approve the issuance of notice to a class of current and former female store managers under the Equal Pay Act. The Company opposed plaintiffs motion. On November 30, 2007, the court conditionally certified a nationwide class of females under the Equal Pay Act who worked for Dollar General as store managers between November 30, 2004 and November 30, 2007. The notice was issued on January 11, 2008, and persons to whom the notice was sent were required to opt into the suit by March 11, 2008. The Company will have an opportunity at the close of the discovery period to seek decertification of the Equal Pay Act class, and the Company expects to file such motion.

The plaintiffs have not yet moved for class certification relating to their Title VII claims. The Company expects such motion to be filed within the next several months, and will strenuously oppose such a motion.

At this time, it is not possible to predict whether the court ultimately will permit the Calvert action to proceed collectively under the Equal Pay Act or as a class under Title VII. However, the Company believes that the case is not appropriate for class or collective treatment and that its policies and practices comply with the Equal Pay Act and Title VII. The Company intends to vigorously defend the action; however, no assurances can be given that the Company will be successful in the defense on the merits or otherwise. If the Company is not successful in defending the Calvert action, its resolution could have a material adverse effect on the Company s financial statements as a whole.

Subsequent to the announcement of the agreement relating to the Merger, the Company and its directors were named in seven putative class actions alleging claims for breach of fiduciary duty arising out of the Company s proposed sale to KKR. Each of the complaints alleged, among other things, that the Company s directors engaged in self-dealing by agreeing to recommend the transaction to the Company s shareholders and that the consideration available to such shareholders in the transaction is unfairly low. On motion of the plaintiffs, each of these cases was transferred to the Sixth Circuit Court for Davidson County, Twentieth Judicial District, at Nashville. By order dated April 26, 2007, the seven lawsuits were consolidated in the court under the caption, In re: Dollar General, Case No. 07MD-1. On June 13, 2007, the court denied the Plaintiffs motion for a temporary injunction to block the shareholder vote that was

then held on June 21, 2007. On June 22, 2007, the Plaintiffs filed their amended complaint making claims substantially similar to those outlined above. The matter is currently in discovery.

The Company believes that the foregoing lawsuit is without merit and continues to defend the action vigorously; however, if the Company is not successful in that defense, its resolution could have a material adverse effect on the Company s financial statements as a whole.

From time to time, the Company is a party to various other legal actions involving claims incidental to the conduct of its business, including actions by employees, consumers, suppliers, government agencies, or others through private actions, class actions, administrative proceedings, regulatory actions or other litigation, including under federal and state employment laws and wage and hour laws. The Company believes, based upon information currently available, that such other litigation and claims, both individually and in the aggregate, will be resolved without a material adverse effect on the Company s financial statements as a whole. However, litigation involves an element of uncertainty. Future developments could cause these actions or claims to have a material adverse effect on the Company s results of operations or financial position. In addition, certain of these lawsuits, if decided adversely to the Company or settled by the Company, may result in liability material to the Company s financial position or may negatively affect operating results if changes to the Company s business operation are required.

6.

Income taxes

The Company reports income taxes in accordance with SFAS No. 109, Accounting for Income Taxes . Under SFAS 109, the asset and liability method is used for computing the future income tax consequences of events that have been recognized in the Company s consolidated financial statements or income tax returns.

Income tax reserves are determined using the methodology established by FASB Interpretation 48, Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement 109 (FIN 48). FIN 48 requires companies to assess each income tax position taken using a two step approach. A determination is first made as to whether it is more likely than not that the position will be sustained, based upon the technical merits, upon examination by the taxing authorities. If the tax position is expected to meet the more likely than not criteria, the benefit recorded for the tax position equals the largest amount that is greater than 50% likely to be realized upon ultimate settlement of the respective tax position.

Subsequent to its February 3, 2007 adoption of FIN 48, the Company elected to record income tax related interest and penalties as a component of the provision for income tax expense.

In the 13-week period ended May 4, 2007, the Internal Revenue Service completed an examination of the Company s federal income tax returns through fiscal year 2003 resulting in a net income tax refund. There are no unresolved issues related to this examination. None of the Company s federal income tax returns are currently under examination; however, fiscal years 2004 and later are still subject to possible examination by the Internal Revenue Service. The

Company has various state income tax examinations that are currently in progress. The estimated liability related to these state income tax examinations is included in the Company s reserve for uncertain tax positions. Generally, the Company s tax years ended in 2004 and forward remain open for examination by the various state taxing authorities.

As of August 1, 2008, the total reserves for uncertain tax benefits, interest expense related to income taxes and potential income tax penalties were $104.2 million, $21.3 million and $1.8 million, respectively. Of this amount, $33.3 million and $92.7 million are reflected in current liabilities as accrued expenses and other and in noncurrent other liabilities, respectively, in the condensed consolidated balance sheet with the remaining $1.3 million reducing deferred tax assets related to net operating loss carry forwards. The Company believes that it is reasonably possible that the reserve for uncertain tax positions may be reduced by approximately $67.8 million in the upcoming twelve months principally as a result of the settlement of currently ongoing state income tax examinations and the anticipated filing of an income tax accounting method change request that is expected to resolve certain uncertainties related to accounting methods employed by the Company. The $67.8 million reasonably possible change is included in both current liabilities ($29.7 million) and other noncurrent liabilities ($38.1 million) in the condensed consolidated balance sheet as of August 1, 2008. Also, as of August 1, 2008, approximately $0.8 million of the reserve for uncertain tax positions would impact the Company s effective income tax rate if the Company were to recognize the tax benefit for these positions.

The effective income tax rates for the 13-week Successor period ended August 1, 2008, the Successor period ended August 3, 2007 and the Predecessor period ended July 6, 2007 were 37.8%, 36.6% (a benefit) and 10.3% (a benefit), respectively. The difference in the effective tax rate between the two Successor periods results principally from the inclusion of income tax related interest expense in income tax expense as reported on the financial statements. The effective tax rate for the Predecessor period is higher than the other periods presented due principally to non-deductible expenses incurred in association with the Merger.

The effective income tax rates for the 26-week Successor period ended August 1, 2008, the Successor period ended August 3, 2007 and the Predecessor period ended July 6, 2007 were 39.1%, 36.7% (a benefit) and 300.2%, respectively. The difference in the effective tax rate between the two Successor periods results principally from the inclusion of income tax related interest expense in income tax expense as reported on the financial statements. The effective tax rate for the Predecessor period is higher than the other periods presented due principally to non-deductible expenses incurred in association with the Merger.

7.

Segment reporting

The Company manages its business on the basis of one reportable segment. As of August 1, 2008, all of the Company s operations were located within the United States, with the exception of a Hong Kong subsidiary the assets and revenues of which are not material. The following net sales data is presented in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information .

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	Successor			Predecessor	
(In thousands)	13-weeks ended August 1, 2008	26-weeks ended August 1, 2008	July 7, 2007 through August 3, 2007	May 5, 2007 through July 6, 2007	February 3, 2007 through July 6, 2007
Categories of similar products:					
Highly consumable	$ 1,796,015	$ 3,476,910	$ 487,407	$ 1,091,316	$ 2,615,110
Seasonal	384,520	706,646	97,071	268,486	604,935
Home products	219,542	424,035	60,151	147,679	362,725
Basic clothing	209,307	405,291	54,449	141,005	340,983
Net sales	$ 2,609,384	$ 5,012,882	$ 699,078	$ 1,648,486	$ 3,923,753

8.

Related party transactions

Affiliates of certain of the Investors participated as (i) lenders in the Company s indebtedness incurred to finance the Merger; (ii) counterparties to certain interest rate swaps discussed in Note 3 and (iii) as advisors in the Merger. Certain fees were paid upon closing of the Merger to affiliates of certain of the Investors. These fees primarily included underwriting fees, advisory fees, equity commitment fees, syndication fees, merger and acquisition fees, sponsor fees, costs of raising equity, and out of pocket expenses. The aggregate fees paid to these related parties during the 13-week period ended August 3, 2007 totaled $134.9 million, portions of which were capitalized as debt financing costs or as direct acquisition costs.

The Company is party to a monitoring agreement with an affiliate of KKR and with Goldman Sachs & Co. pursuant to which those entities provide management and advisory services to the Company. Under the terms of the monitoring agreement, among other things, the Company is obligated to pay to those entities an aggregate annual management fee payable in arrears at the end of each calendar quarter plus all reasonable out of pocket expenses incurred in connection with the provision of services under the agreement upon request. The fees incurred for the 13-week and 26-week Successor periods ended August 1, 2008 totaled $1.7 million and $3.0 million, respectively, and $0.4 million for the 2007 Successor period.

The Company utilizes Capstone Consulting, LLC, a team of executives who work exclusively with KKR portfolio companies providing certain consulting services. The Chief Executive Officer of Capstone serves on the Company s Board. Although neither KKR nor any entity affiliated with KKR owns any of the equity of Capstone, KKR had provided financing to Capstone prior to January 1, 2007. The aggregate fees incurred for Capstone services for the 13-week and 26-week Successor periods ended August 1, 2008 totaled $0.8 million and $1.7 million, respectively.

9.

Investments in debt and equity securities

In recent years, pursuant to state regulatory requirements, the Company s South Carolina-based wholly owned captive insurance subsidiary, Ashley River Insurance Company (ARIC), has held cash and cash equivalents and investment balances to maintain a percentage of ARIC s liability and equity balances (primarily insurance liabilities) in the form of certain specified types of assets. As a result, these investments have not been available for general corporate purposes.

In May 2008, the Company received notice that the state of South Carolina had agreed to a change in these regulatory requirements for a portion of these assets. As a result the Company liquidated a substantial portion of these investments during the 13-weeks ended August 1, 2008 and $9.5 million of investment balances held by ARIC on the August 1, 2008 condensed consolidated balance sheet ($6.9 million of which are classified as cash and equivalents) are reflected as available-for-sale. These remaining investments matured or were liquidated during the third quarter of 2008.

10.

Guarantor subsidiaries

Certain of the Company s subsidiaries (the Guarantors) have fully and unconditionally guaranteed on a joint and several basis the Company's obligations under certain outstanding debt obligations. Each of the Guarantors is a direct or indirect wholly-owned subsidiary of the Company. The following consolidating schedules present condensed financial information on a combined basis, in thousands.

SUCCESSOR	August 1, 2008				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
BALANCE SHEET:					
ASSETS					
Current assets:					
Cash and cash equivalents	$ 163,628	$ 72,117	$ 25,885	$ -	$ 261,630
Short-term investments	-	-	2,597	-	2,597
Merchandise inventories	-	1,490,063	-	-	1,490,063
Income taxes receivable	79,184	-	-	(66,355)	12,829
Deferred income taxes	7,660	-	20,149	(10,414)	17,395
Prepaid expenses and other current assets	248,885	781,509	14,951	(977,058)	68,287
Total current assets	499,357	2,343,689	63,582	(1,053,827)	1,852,801
Net property and equipment	83,381	1,183,006	335	-	1,266,722
Goodwill	4,344,930	-	-	-	4,344,930
Intangible assets, net	8,689	1,339,259	-	-	1,347,948
Deferred income taxes	39,046	-	51,273	(90,319)	-
Other assets, net	2,927,928	7,435	250,117	(3,088,091)	97,389
Total assets	$ 7,903,331	$ 4,873,389	$ 365,307	$ (4,232,237)	$ 8,909,790
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					
Current portion of long-term obligations	$ -	$ 2,999	$ -	$ -	$ 2,999
Accounts payable	764,593	972,075	48,395	(966,817)	818,246
Accrued expenses and other	72,337	222,564	57,067	(10,240)	341,728

Income taxes payable	-	58,799	9,300	(66,355)	1,744
Deferred income taxes	-	10,414	-	(10,414)	-
Total current liabilities	836,930	1,266,851	114,762	(1,053,826)	1,164,717
Long-term obligations	4,155,747	2,060,735	57,031	(2,095,903)	4,177,610
Deferred income taxes	-	574,186	-	(90,319)	483,867
Other liabilities	132,694	27,835	145,107	-	305,636
Redeemable common stock	11,157	-	-	-	11,157
Shareholders equity:					
Preferred stock	-	-	-	-	-
Common stock	277,712	23,753	100	(23,853)	277,712
Additional paid-in capital	2,484,606	653,711	19,900	(673,611)	2,484,606
Retained earnings	28,816	266,318	28,407	(294,725)	28,816
Accumulated other comprehensive loss	(24,331)	-	-	-	(24,331)
Total shareholders equity	2,766,803	943,782	48,407	(992,189)	2,766,803
Total liabilities and shareholders equity	$ 7,903,331	$ 4,873,389	$ 365,307	$ (4,232,237)	$ 8,909,790

SUCCESSOR	February 1, 2008				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
BALANCE SHEET:					
ASSETS					
Current assets:					
Cash and cash equivalents	$ 8,320	$ 59,379	$ 32,510	$ -	$ 100,209
Short-term investments	-	-	19,611	-	19,611
Merchandise inventories	-	1,288,661	-	-	1,288,661
Income taxes receivable	102,273	-	-	(69,772)	32,501
Deferred income taxes	3,966	-	20,626	(7,295)	17,297
Prepaid expenses and other current assets	221,408	337,741	9,341	(509,025)	59,465
Total current assets	335,967	1,685,781	82,088	(586,092)	1,517,744
Net property and equipment	83,658	1,190,131	456	-	1,274,245
Goodwill	4,344,930	-	-	-	4,344,930
Intangible assets, net	10,911	1,359,646	-	-	1,370,557
Deferred income taxes	43,890	-	47,067	(90,957)	-
Other assets, net	2,629,967	1,652	111,597	(2,594,261)	148,955
Total assets	$ 7,449,323	$ 4,237,210	$ 241,208	$ (3,271,310)	$ 8,656,431
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					
Current portion of long-term obligations	$ -	$ 3,246	$ -	$ -	$ 3,246
Accounts payable	253,477	736,844	40	(439,321)	551,040
Accrued expenses and other	62,957	188,877	55,185	(6,063)	300,956
Income taxes payable	-	59,264	13,507	(69,772)	2,999
Total current liabilities	316,434	988,231	68,732	(515,156)	858,241

Long-term obligations	4,257,250	1,837,715	-	(1,816,209)	4,278,756
Deferred income taxes	-	584,976	-	(98,251)	486,725
Other liabilities	162,644	21,191	135,879	-	319,714
Redeemable common stock	9,122	-	-	-	9,122
Shareholders equity:					
Preferred stock	-	-	-	-	-
Common stock	277,741	23,753	100	(23,853)	277,741
Additional paid-in capital	2,480,062	653,711	19,900	(673,611)	2,480,062
Retained earnings (accumulated deficit)	(4,818)	127,633	16,597	(144,230)	(4,818)
Accumulated other comprehensive loss	(49,112)	-	-	-	(49,112)
Total shareholders equity	2,703,873	805,097	36,597	(841,694)	2,703,873
Total liabilities and shareholders equity	$ 7,449,323	$ 4,237,210	$ 241,208	$ (3,271,310)	$ 8,656,431

SUCCESSOR	For the 13-weeks ended August 1, 2008				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF OPERATIONS:					
Net sales	$ 50,582	$ 2,609,384	$ 25,498	$ (76,080)	$ 2,609,384
Cost of goods sold	-	1,851,349	-	-	1,851,349
Gross profit	50,582	758,035	25,498	(76,080)	758,035
Selling, general and administrative	46,854	624,268	19,938	(76,080)	614,980
Operating profit	3,728	133,767	5,560	-	143,055
Interest income	(19,140)	(8,673)	(3,683)	30,279	(1,217)
Interest expense	108,102	21,561	50	(30,279)	99,434
Other (income) expense	292	-	-	-	292
Income (loss) before income taxes	(85,526)	120,879	9,193	-	44,546
Income tax expense (benefit)	(29,614)	43,847	2,595	-	16,828
Equity in subsidiaries earnings, net of taxes	83,630	-	-	(83,630)	-
Net income	$ 27,718	$ 77,032	$ 6,598	$ (83,630)	$ 27,718

SUCCESSOR	July 7, 2007 to August 3, 2007 (including Buck from May 5, 2007 to July 6, 2007, see Note 1)				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF OPERATIONS:					
Net sales	$ 8,297	$ 699,078	$ 10,005	$ (18,302)	$ 699,078
Cost of goods sold	-	514,355	-	-	514,355
Gross profit	8,297	184,723	10,005	(18,302)	184,723
Selling, general and administrative	21,398	180,930	6,722	(18,302)	190,748
Operating profit (loss)	(13,101)	3,793	3,283	-	(6,025)
Interest income	(11,532)	(2,893)	(1,113)	14,505	(1,033)

Interest expense	38,587	12,437	1	(14,505)	36,520
Other (income) expense	(567)	-	-	-	(567)
Income (loss) before income taxes	(39,589)	(5,751)	4,395	-	(40,945)
Income tax expense (benefit)	(11,925)	(4,377)	1,307	-	(14,995)
Equity in subsidiaries earnings, net of taxes	1,714	-	-	(1,714)	-
Net income (loss)	$ (25,950)	$ (1,374)	$ 3,088	$ (1,714)	$ (25,950)

PREDECESSOR **May 5, 2007 to July 6, 2007**

	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF OPERATIONS:					
Net sales	$ 23,410	$ 1,648,486	$ 17,483	$ (40,893)	$ 1,648,486
Cost of goods sold	-	1,209,971	-	-	1,209,971
Gross profit	23,410	438,515	17,483	(40,893)	438,515
Selling, general and administrative	120,779	390,146	14,598	(40,893)	484,630
Operating profit (loss)	(97,369)	48,369	2,885	-	(46,115)
Interest income	(20,511)	(3,032)	(2,336)	23,406	(2,473)
Interest expense	6,612	20,921	5	(23,406)	4,132
Income (loss) before income taxes	(83,470)	30,480	5,216	-	(47,774)
Income tax expense (benefit)	(17,156)	10,552	1,698	-	(4,906)
Equity in subsidiaries earnings, net of taxes	23,446	-	-	(23,446)	-
Net income (loss)	$ (42,868)	$ 19,928	$ 3,518	$ (23,446)	$ (42,868)

SUCCESSOR	For the 26-weeks ended August 1, 2008				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF OPERATIONS:					
Net sales	$ 100,657	$ 5,012,882	$ 48,469	$ (149,126)	$ 5,012,882
Cost of goods sold	-	3,561,770	-	-	3,561,770
Gross profit	100,657	1,451,112	48,469	(149,126)	1,451,112
Selling, general and administrative	93,334	1,212,240	40,738	(149,126)	1,197,186
Operating profit	7,323	238,872	7,731	-	253,926
Interest income	(35,722)	(17,352)	(6,819)	57,719	(2,174)
Interest expense	217,297	40,673	54	(57,719)	200,305
Other (income) expense	590	-	-	-	590
Income (loss) before income taxes	(174,842)	215,551	14,496	-	55,205
Income tax (expense) benefit	(57,981)	76,866	2,686	-	21,571
Equity in subsidiaries earnings, net of taxes	150,495	-	-	(150,495)	-
Net income	$ 33,634	$ 138,685	$ 11,810	$ (150,495)	$ 33,634

SUCCESSOR	July 7, 2007 to August 3, 2007 (including Buck from March 5, 2007 to July 6, 2007, see Note 1)				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF OPERATIONS:					
Net sales	$ 8,297	$ 699,078	$ 10,005	$ (18,302)	$ 699,078
Cost of goods sold	-	514,355	-	-	514,355
Gross profit	8,297	184,723	10,005	(18,302)	184,723
Selling, general and administrative	21,398	180,930	6,722	(18,302)	190,748
Operating profit (loss)	(13,101)	3,793	3,283	-	(6,025)
Interest income	(11,532)	(2,893)	(1,113)	14,505	(1,033)

Interest expense	38,587	12,437	1	(14,505)	36,520
Other (income) expense	1,448	-	-	-	1,448
Income (loss) before income taxes	(41,604)	(5,751)	4,395	-	(42,960)
Income tax expense (benefit)	(12,715)	(4,377)	1,307	-	(15,785)
Equity in subsidiaries earnings, net of taxes	1,714	-	-	(1,714)	-
Net income (loss)	$ (27,175)	$ (1,374)	$ 3,088	$ (1,714)	$ (27,175)

PREDECESSOR **February 3, 2007 to July 6, 2007**

	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF OPERATIONS:					
Net sales	$ 76,945	$ 3,923,753	$ 44,206	$ (121,151)	$ 3,923,753
Cost of goods sold	-	2,852,178	-	-	2,852,178
Gross profit	76,945	1,071,575	44,206	(121,151)	1,071,575
Selling, general and administrative	166,224	982,321	34,933	(121,151)	1,062,327
Operating profit (loss)	(89,279)	89,254	9,273	-	9,248
Interest income	(53,278)	(11,472)	(5,626)	65,330	(5,046)
Interest expense	19,796	55,828	5	(65,330)	10,299
Income (loss) before income taxes	(55,797)	44,898	14,894	-	3,995
Income tax expense (benefit)	(4,814)	11,924	4,883	-	11,993
Equity in subsidiaries earnings, net of taxes	42,985	-	-	(42,985)	-
Net income (loss)	$ (7,998)	$ 32,974	$ 10,011	$ (42,985)	$ (7,998)

SUCCESSOR	For the 26-weeks ended August 1, 2008				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF CASH FLOWS:					
Cash flows from operating activities:					
Net income	$ 33,634	$ 138,685	$ 11,810	$ (150,495)	$ 33,634
Adjustments to reconcile net income to net cash provided by (used in) operating activities:					
Depreciation and amortization	17,310	104,585	128	-	122,023
Deferred income taxes	(14,102)	(377)	(3,729)	-	(18,208)
Noncash LIFO charge	-	16,037	-	-	16,037
Noncash share-based compensation	4,516	-	-	-	4,516
Tax benefit from stock option exercises	(475)	-	-	-	(475)
Equity in subsidiaries earnings, net	(150,495)	-	-	150,495	-
Change in operating assets and liabilities:					
Merchandise inventories	-	(217,439)	-	-	(217,439)
Prepaid expenses and other current assets	(671)	(3,906)	(1,483)	-	(6,060)
Accounts payable	20,633	241,677	105	-	262,415
Accrued expenses and other	21,218	36,364	11,110	-	68,692
Income taxes	23,564	(465)	(4,207)	-	18,892
Other	1,870	10,715	(88)	-	12,497
Net cash provided by (used in) operating activities	(42,998)	325,876	13,646	-	296,524

Cash flows from investing activities:					
Purchases of property and equipment	(5,699)	(74,394)	(7)	-	(80,100)
Purchases of short-term investments	-	-	(9,903)	-	(9,903)
Sales of short-term investments	-	-	58,950	-	58,950
Proceeds from sale of property and equipment	-	683	-	-	683
Net cash provided by (used in) investing activities	(5,699)	(73,711)	49,040	-	(30,370)
Cash flows from financing activities:					
Repayments of long-term obligations	-	(2,195)	-	-	(2,195)
Borrowings under revolving credit facility	-	-	-	-	-
Repayments of borrowings under revolving credit facility	(102,500)	-	-	-	(102,500)
Repurchases of common stock	(513)	-	-	-	(513)
Tax benefit from stock option exercises	475	-	-	-	475
Changes in intercompany note balances, net	306,543	(237,232)	(69,311)	-	-
Net cash provided by (used in) financing activities	204,005	(239,427)	(69,311)	-	(104,733)
Net increase (decrease) in cash and cash equivalents	155,308	12,738	(6,625)	-	161,421
Cash and cash equivalents, beginning of period	8,320	59,379	32,510	-	100,209
Cash and cash equivalents, end of	$ 163,628	$ 72,117	$ 25,885	$ -	$ 261,630

period

SUCCESSOR	July 7, 2007 to August 3, 2007				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF CASH FLOWS:					
Cash flows from operating activities:					
Net income (loss)	$ (27,175)	$ (1,374)	$ 3,088	$ (1,714)	$ (27,175)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:					
Depreciation and amortization	2,580	22,974	21	-	25,575
Deferred income taxes	1,865	(15,894)	(349)	-	(14,378)
Noncash share-based compensation	1,170	-	-	-	1,170
Noncash unrealized gain on interest rate swap	(4,739)	-	-	-	(4,739)
Equity in subsidiaries earnings, net	(1,714)	-	-	1,714	-
Change in operating assets and liabilities:					
Merchandise inventories	-	(27,027)	-	-	(27,027)
Prepaid expenses and other current assets	(7,930)	(683)	(98)	-	(8,711)
Accounts payable	(38,634)	23,191	(12,996)	-	(28,439)
Accrued expenses and other	87,597	(62,393)	1,050	-	26,254
Income taxes	(3,243)	(12,565)	13,620	-	(2,188)
Other	(3,275)	3,365	(75)	-	15
Net cash provided by (used in) operating activities	6,502	(70,406)	4,261	-	(59,643)

Cash flows from investing activities:					
Merger, net of cash acquired	(5,635,161)	(1,129,953)	40,744	-	(6,724,370)
Purchases of property and equipment	(78)	(11,322)	-	-	(11,400)
Sales of short-term investments	-	-	1,000	-	1,000
Purchases of long-term investments	-	-	(4,662)	-	(4,662)
Proceeds from sale of property and equipment	-	162	-	-	162
Net cash provided by (used in) investing activities	(5,635,239)	(1,141,113)	37,082	-	(6,739,270)
Cash flows from financing activities:					
Issuance of common stock	2,765,443	-	-	-	2,765,443
Issuance of long-term obligations	4,176,817	-	-	-	4,176,817
Repayments of long-term obligations	(209,698)	(600)	-	-	(210,298)
Borrowings under revolving credit facility	432,300	-	-	-	432,300
Repayments of borrowings under revolving credit facility	(132,300)	-	-	-	(132,300)
Debt issuance costs	(109,379)	-	-	-	(109,379)
Changes in intercompany note balances, net	(1,276,653)	1,291,789	(15,136)	-	-
Net cash provided by (used in) financing activities	5,646,530	1,291,189	(15,136)	-	6,922,583
Net increase in cash and cash equivalents	17,793	79,670	26,207	-	123,670
Cash and cash equivalents, beginning of period	-	-	-	-	-

Cash and cash equivalents, end of period	$ 17,793	$ 79,670	$ 26,207	$ -	$ 123,670

PREDECESSOR	February 3, 2007 through July 6, 2007				
	DOLLAR GENERAL CORPORATION	GUARANTOR SUBSIDIARIES	OTHER SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED TOTAL
STATEMENTS OF CASH FLOWS:					
Cash flows from operating activities:					
Net income (loss)	$ (7,998)	$ 32,974	$ 10,011	$ (42,985)	$ (7,998)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:					
Depreciation and amortization	9,051	74,770	96	-	83,917
Deferred income taxes	(7,982)	(9,194)	(3,698)	-	(20,874)
Noncash share-based compensation	45,433	-	-	-	45,433
Tax benefit from stock option exercises	(3,927)	-	-	-	(3,927)
Equity in subsidiaries earnings, net	(42,985)	-	-	42,985	-
Change in operating assets and liabilities:					
Merchandise inventories	-	16,424	-	-	16,424
Prepaid expenses and other current assets	5,758	(11,762)	(180)	-	(6,184)
Accounts payable	44,909	(23,103)	12,988	-	34,794
Accrued expenses and other	7,897	36,021	9,077	-	52,995
Income taxes	(24,998)	31,741	(3,934)	-	2,809
Other	21	4,726	(190)	-	4,557
Net cash provided by operating activities	25,179	152,597	24,170	-	201,946
Cash flows from investing activities:					
Purchases of property and equipment	(5,321)	(50,737)	(95)	-	(56,153)
Purchases of short-term investments	-	-	(5,100)	-	(5,100)
	-	-	9,505	-	9,505

Sales of short-term investments					
Purchases of long-term investments	-	-	(15,754)	-	(15,754)
Proceeds from sale of property and equipment	-	620	-	-	620
Net cash used in investing activities	(5,321)	(50,117)	(11,444)	-	(66,882)
Cash flows from financing activities:					
Repayments of long-term obligations	(148)	(4,352)	-	-	(4,500)
Payment of cash dividends	(15,710)	-	-	-	(15,710)
Proceeds from exercise of stock options	41,546	-	-	-	41,546
Tax benefit of stock options	3,927	-	-	-	3,927
Changes in intercompany note balances, net	75,840	(86,988)	11,148	-	-
Net cash provided by (used in) financing activities	105,455	(91,340)	11,148	-	25,263
Net increase in cash and cash equivalents	125,313	11,140	23,874	-	160,327
Cash and cash equivalents, beginning of period	114,310	58,107	16,871	-	189,288
Cash and cash equivalents, end of period	$ 239,623	$ 69,247	$ 40,745	$ -	$ 349,615

ITEM 2.

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL

CONDITION AND RESULTS OF OPERATIONS.

General

Accounting Periods. We follow the concept of a 52-53 week fiscal year that ends on the Friday nearest to January 31. The following text contains references to years 2008 and 2007, which represent 52-week fiscal years ending or ended January 30, 2009 and February 1, 2008, respectively. Consequently, references to quarterly accounting periods for 2008 and 2007 contained herein refer to 13-week accounting periods.

Seasonality. The nature of our business is seasonal to a certain extent. Primarily because of sales of holiday-related merchandise, sales in the fourth quarter have historically been higher than sales achieved in each of the first three quarters of the fiscal year. Expenses and, to a greater extent, operating income, vary by quarter. Results of a period shorter than a full year may not be indicative of results expected for the entire year. Furthermore, the seasonal nature of our business may affect comparisons between periods.

Merger with KKR. We were acquired on July 6, 2007 through a merger accounted for as a reverse acquisition (the Merger) with Buck Acquisition Corp. (Buck). As a result of the Merger, we are a subsidiary of Buck Holdings, L.P. (Parent), a Delaware limited partnership controlled by investment funds affiliated with Kohlberg Kravis Roberts & Co., L.P. (KKR). KKR, GS Capital Partners VI Fund, L.P. and affiliated funds (affiliates of Goldman, Sachs & Co.), Citi Private Equity, Wellington Management Company, LLP, CPP Investment Board (USRE II) Inc. and other equity co-investors (collectively, the Investors) indirectly own a substantial portion of our capital stock through their investment in Parent. The Company continued as the same legal entity after the Merger.

The Merger was consummated on July 6, 2007, the end of the ninth week of our 13-week second quarter period in 2007. The 2007 13-week and 26-week periods presented include the 9-week Predecessor period from May 5, 2007 to July 6, 2007, and the 22-week Predecessor period from February 3, 2007 to July 6, 2007, respectively, combined with the four-week Successor periods from July 7, 2007 to August 3, 2007. The Predecessor periods reflect the historical basis of accounting while the Successor periods reflect the impact of the preliminary purchase price allocation associated with the Merger as well as pre-Merger operations of Buck associated with the change in fair value of interest rate swaps.

For comparison purposes, the discussion of operations included below is generally based on the Successor 13-week and 26-week periods ended August 1, 2008, compared to the mathematical combination of the Successor and Predecessor periods in the 13-week and 26-week periods ended August 3, 2007, which we believe provides a more meaningful understanding of the underlying business. Transactions relating to or resulting from the Merger are discussed separately. The combined results have not been prepared as pro forma results and may not reflect the actual results we could have achieved absent the Merger and in addition, may not be indicative of future results of

operations.

Purpose of Discussion. We intend for this discussion to provide the reader with information that will assist in understanding our company and the critical economic factors that affect us. This discussion further explains our financial statements, the changes in certain key items in those financial statements from period to period, and the primary factors that accounted for those changes, as well as how certain accounting principles affect our financial statements.

This discussion and analysis is based on, should be read with, and is qualified in its entirety by, the accompanying condensed consolidated financial statements and related notes, as well as our consolidated financial statements and the related Management s Discussion and Analysis of Financial Condition and Results of Operations as contained in our Annual Report on Form 10-K for the year ended February 1, 2008. It also should be read in conjunction with the disclosure under Cautionary Disclosure Regarding Forward-Looking Statements in this report.

Executive Overview

We are the largest discount retailer in the United States by number of stores, with over 8,300 stores located in 35 states, primarily in the southern, southwestern, midwestern and eastern United States. We serve a broad customer base and offer a focused assortment of everyday items, including basic consumable merchandise and other home, apparel and seasonal products. We seek to offer a compelling value proposition for our customers based on convenient store locations, easy in and out shopping and quality merchandise at highly competitive prices. We believe our combination of value and convenience distinguishes us from other discount, convenience and drugstore retailers, who typically focus on either value or convenience. Our business model has proven to be resilient in both strong and challenging economic environments, as evidenced by our historical annual and 2008 year-to-date same store sales growth. Consumers are currently being challenged by higher energy prices, food and healthcare inflation and uncertainty in the economy. We are committed to serving our customers needs for value and convenience in this challenging environment.

In late 2006, we launched certain strategic operating initiatives aimed at improving our long-term financial performance. Our actions included the closing of approximately 400 under-performing stores, a slowdown in our new store growth plans, and the elimination of our longtime practice of packing away inventories at the end of each season to be sold in future years. In fiscal 2007, we completed the implementation of these initial actions. Working with new ownership, we further developed our merchandising and real estate strategies, including the closing of an additional 60 stores, and clearly defined our go-forward operating priorities. Our first half 2007 operating results included significant transition costs as we closed stores and eliminated packaway inventories. In 2008, we have been keenly focused on executing our four operating priorities, which are to:

-

Drive productive sales growth;

-

Increase gross margins;

•

Leverage process improvements and information technology to reduce costs; and

•

Strengthen and expand Dollar General s culture of serving others.

Each of our key financial metrics for the second quarter of 2008 reflects improved performance over the comparable combined Successor and Predecessor 2007 periods as follows:

- Same-store sales for the quarter increased 10.1% compared with the prior year period.

- Gross profit, as a percentage of sales, increased to 29.1% compared to 26.5% in the 2007 period as a result of improvements in shrink and damages, lower markdowns and leverage of our distribution costs, including the impact of higher sales volumes as well as logistics efficiencies and other cost savings in the supply chain which substantially mitigated the impact of higher than anticipated fuel costs, all of which were partially offset by a LIFO charge primarily related to commodity cost increases.

- Inventory turnover improved to 5.0 times on a rolling four-quarter basis compared to 4.5 times for the corresponding previous year period.

- Cash flow from operating activities for the year-to-date period was $296.5 million, compared to $142.3 million in the 2007 year-to-date period, primarily reflecting improved accounts payable terms and increased net income, partially offset by inventory purchases associated with our merchandising initiatives.

We believe that our merchandising and operating initiatives, in addition to aiding improvement in our financial performance (including shrink), have contributed to a decrease in employee turnover and an improvement in the overall appearance of our stores. We continue to move forward with our pricing and private label initiatives, and our enhanced merchandising analysis tools are giving us a better platform for decision-making. With new pricing tools, we have been able to react faster to recent cost increases from our vendors, including making changes to our retail prices as necessary. As a result of our efforts to respond to our consumers need for convenience and value, we have extended store hours and continue to add new convenience and national name brand items in our stores.

In the first half of 2008, we opened 125 new stores, relocated 48 stores, remodeled 201 stores and closed 11 stores. We remain on track to open approximately 200 new stores and to remodel or relocate 400 stores in fiscal 2008. As of August 1, 2008, we operated 8,308 stores in 35 states.

The above discussion is only a summary. Readers should refer to the detailed discussion below for the full analysis of our financial performance in the current year periods as compared with the prior year periods.

Results of Operations

The following discussion of our financial performance is based on the Condensed Consolidated Financial Statements set forth herein. The following table contains results of operations data for the 13-week and 26-week periods ended August 1, 2008 and August 3, 2007 (including a combination of the relevant Predecessor and Successor periods), and the dollar and percentage variances among those periods:

	Successor	Combined (a)	Successor (b)	Predecessor	2008 vs. Combined 2007	
	13-weeks ended August 1, 2008	13-weeks ended August 3, 2007	July 7, 2007 through August 3, 2007	May 5, 2007 through July 6, 2007	*Amount change*	*% change*
(amounts in millions)						
Net sales by category:						
Highly consumable	$ 1,796.0	$ 1,578.7	$ 487.4	$ 1,091.3	*217.3*	*13.8* %
% of net sales	*68.83%*	*67.25%*				
Seasonal	384.5	365.6	97.1	268.5	*19.0*	*5.2*
% of net sales	*14.74%*	*15.57%*				
Home products	219.5	207.8	60.2	147.7	*11.7*	*5.6*
% of net sales	*8.41%*	*8.85%*				
Basic clothing	209.3	195.5	54.4	141.0	*13.9*	*7.1*
% of net sales	*8.02%*	*8.33%*				
Net sales	2,609.4	2,347.6	699.1	1,648.5	*261.8*	*11.2*
Cost of goods sold	1,851.3	1,724.3	514.4	1,210.0	*127.0*	*7.4*
% of net sales	*70.95%*	*73.45%*				
Gross profit	758.0	623.2	184.7	438.5	*134.8*	*21.6*
% of net sales	*29.05%*	*26.55%*				
Selling, general and administrative	615.0	579.3	190.4	388.8	*35.7*	*6.2*
% of net sales	*23.57%*	*24.68%*				
Transaction and related costs	-	96.1	0.3	95.8	*(96.1)*	-
% of net sales	-	*4.09%*				
Operating profit (loss)	143.1	(52.1)	(6.0)	(46.1)	*195.2*	-
% of net sales	*5.48%*	*(2.22)%*				
Interest income	(1.2)	(3.5)	(1.0)	(2.5)	*2.3*	*(65.3)*
% of net sales	*(0.05)%*	*(0.15)%*				
Interest expense	99.4	40.7	36.5	4.1	*58.8*	*144.6*
% of net sales	*3.81%*	*1.73%*				
	0.3	(0.6)	(0.6)	-	*0.9*	-

Other (income) expense						
% of net sales	*0.01%*	*(0.02)%*				
Income (loss) before income taxes	44.5	(88.7)	(40.9)	(47.8)	*133.3*	-
% of net sales	*1.71%*	*(3.78)%*				
Income tax expense (benefit)	16.8	(19.9)	(15.0)	(4.9)	*36.7*	-
% of net sales	*0.64%*	*(0.85)%*				
Net income (loss)	$ 27.7	$ (68.8)	$ (26.0)	$ (42.9)	$ *96.5*	- %
% of net sales	*1.06%*	*(2.93)%*				

(a)

The combined results are the mathematical combination of the Predecessor and Successor periods included in the condensed consolidated financial statements for the 2007 periods presented. The presentation does not comply with generally accepted accounting principles, but we believe this combination provides a more meaningful method of comparison.

(b)

Includes the results of operations of Buck for the period prior to the Merger from May 5, 2007 through July 6, 2007 (reflecting the change in fair value of interest rate swaps), and the post-Merger results of Dollar General Corporation for the period from July 7, 2007 through August 3, 2007.

	Successor	Combined (a)	Successor (b)	Predecessor	*2008 vs. Combined 2007*	
	26-weeks ended August 1, 2008	26-weeks ended August 3, 2007	July 7, 2007 through August 3, 2007	February 3, 2007 through July 6, 2007	*Amount change*	*% change*
(amounts in millions)						
Net sales by category:						
Highly consumable	$ 3,476.9	$ 3,102.5	$ 487.4	$ 2,615.1	$ *374.4*	*12.1* %
% of net sales	*69.36%*	*67.11%*				
Seasonal	706.6	702.0	97.1	604.9	*4.6*	*0.7*
% of net sales	*14.10%*	*15.19%*				
Home products	424.0	422.9	60.2	362.7	*1.2*	*0.3*
% of net sales	*8.46%*	*9.15%*				
Basic clothing	405.3	395.4	54.4	341.0	*9.9*	*2.5*
% of net sales	*8.08%*	*8.55%*				
Net sales	5,012.9	4,622.8	699.1	3,923.8	*390.1*	*8.4*
Cost of goods sold	3,561.8	3,366.5	514.4	2,852.2	*195.2*	*5.8*
% of net sales	*71.05%*	*72.82%*				
Gross profit	1,451.1	1,256.3	184.7	1,071.6	*194.8*	*15.5*
% of net sales	*28.95%*	*27.18%*				
Selling, general and administrative	1,197.2	1,151.4	190.4	960.9	*45.8*	*4.0*
% of net sales	*23.88%*	*24.91%*				
Transaction and related costs	-	101.7	0.3	101.4	*(101.7)*	-
% of net sales	-	*2.20%*				
Operating profit (loss)	253.9	3.2	(6.0)	9.2	*250.7*	-
% of net sales	*5.07%*	*0.07%*				
Interest income	(2.2)	(6.1)	(1.0)	(5.0)	*3.9*	*(64.2)*
% of net sales	*(0.04)%*	*(0.13)%*				
Interest expense	200.3	46.8	36.5	10.3	*153.5*	*327.8*
% of net sales	*4.00%*	*1.01%*				

Other (income) expense	0.6	1.4	1.4	-	*(0.9)*	*(59.3)*	
% of net sales	*0.01%*	*0.03%*					
Income (loss) before income taxes	55.2	(39.0)	(43.0)	4.0	*94.2*	-	
% of net sales	*1.10%*	*(0.84)%*					
Income tax expense (benefit)	21.6	(3.8)	(15.8)	12.0	*25.4*	-	
% of net sales	*0.43%*	*(0.08)%*					
Net income (loss)	$ 33.6	$ (35.2)	$ (27.2)	$ (8.0)	$ *68.8*	-	%
% of net sales	*0.67%*	*(0.76)%*					

(a)

The combined results are the mathematical combination of the Predecessor and Successor periods included in the condensed consolidated financial statements for the 2007 periods presented. The presentation does not comply with generally accepted accounting principles, but we believe this combination provides a more meaningful method of comparison.

(b)

Includes the results of operations of Buck for the period prior to the Merger from March 6, 2007 (its formation) through July 6, 2007 (reflecting the change in fair value of interest rate swaps), and the post-Merger results of Dollar General Corporation for the period from July 7, 2007 through August 3, 2007.

13 WEEKS ENDED AUGUST 1, 2008 AND AUGUST 3, 2007

Net Sales. The 11.2% net sales increase over the 2007 period primarily was attributable to our 10.1% same-store sales increase. Same-store sales, which includes those stores that have been open at least 13 full fiscal months and remain open at the end of the reporting period, were positively impacted by increases in the number of customer transactions and the average dollar value of transactions during the period. We believe the increase in sales resulted from our merchandising and store operations initiatives, including extended store hours, and from favorable customer response to our convenience and value during the current challenging economic environment. Sales of merchandise in our highly consumables category were the largest contributor to our net sales increase, although sales in our home, seasonal and basic clothing categories also improved over recent past performance. We believe that our overall mix of sales has been impacted unfavorably by economic pressures on discretionary consumer spending. We continue to focus our efforts on meeting our customers consumables needs and increasing sales in our home, basic clothing and seasonal categories by improving our merchandising to be more relevant to our customers.

Gross Profit. Improvements in shrink, lower markdowns and improved distribution and transportation logistics efficiencies, which more than offset increased fuel costs, along with the leverage impact of higher sales volumes were responsible for the 2008 gross profit increase as a percentage of sales. We recorded a LIFO charge of $16.0 million in the 2008 period as a result of inflationary pressures we began experiencing during the period (related primarily to commodity cost increases). In the 2007 period, net markdowns were higher than the historical rate as the result of markdowns taken in connection with the inventory reduction strategies discussed above.

SG&A Expense. SG&A decreased as a percentage of sales to 23.6% in the 2008 period from 24.7% in the 2007 period. The following items represent the more significant changes in SG&A, as a percentage of sales, between the periods. The 2008 period includes $10.0 million related to amortization of leasehold intangibles capitalized in connection with purchase accounting and approximately $7.1 million resulting from the Company s new ownership structure, primarily including monitoring fees, consulting, executive recruiting and legal expenses. SG&A in the 2007 period includes approximately $17.7 million relating to strategic real estate initiatives, estimated losses of approximately $8.6 million relating to the probable loss associated with the restructuring of three distribution center leases, $3.4 million of leasehold intangibles amortization and $0.8 million relating to the Company s new ownership structure, primarily monitoring and consulting fees. We leveraged occupancy costs resulting from higher net sales and experienced lower depreciation, advertising, workers compensation and employee benefits expense as a percentage of sales, partially offset by higher incentive compensation expense associated with our 2008 financial performance.

Transaction and Related Costs. Transaction and related costs of $96.1 million for the 2007 period reflect $56.7 million of expenses related to the Merger, such as investment banking and legal fees, as well as $39.4 million of compensation expense related to the accelerated vesting of stock options, restricted stock and restricted stock units.

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Interest Expense. The interest expense increase was due to interest on long-term obligations incurred to finance the Merger. See further discussion under Liquidity and Capital Resources below.

Other (Income) Expense. During the 2007 period, we recorded $6.2 million in expenses related to consent fees and other costs associated with a tender offer for our previously outstanding 8 5/8% unsecured notes due June 15, 2010 (the 2010 Notes). Approximately 99% of the 2010 Notes were retired in 2007 as a result of the tender offer. Also during the 2007 period, we recorded an unrealized gain of $6.8 million related to the change in the fair value of interest rate swaps.

Income Taxes. The effective income tax rates for the 13-week Successor period ended August 1, 2008, the Successor period ended August 3, 2007 and the Predecessor period ended July 6, 2007 were 37.8%, 36.6% (a benefit) and 10.3% (a benefit), respectively. The difference in the effective tax rate between the two Successor periods results principally from the inclusion of income tax related interest expense in income tax expense as reported on the financial statements. The effective tax rate for the Predecessor period is higher than the other periods presented due principally to non-deductible expenses incurred in association with the Merger.

26 WEEKS ENDED AUGUST 1, 2008 AND AUGUST 3, 2007

Net Sales. The 8.4% net sales increase over the 2007 period was primarily attributable to our 7.8% same-store sales increase. Same-store sales were positively impacted by increases in the number of customer transactions and the average dollar value of transactions during the period. We believe the increase in sales resulted from our merchandising and store operations initiatives, including extended store hours, and from favorable customer response to our convenience and value during the current challenging economic environment. While sales in all four categories increased year-to-date and we believe our overall sales benefited during the period as customers sought to save money as a result of the current economic downturn, we also believe our mix of sales was impacted unfavorably by economic pressure on discretionary consumer spending.

Gross Profit. Lower markdowns and improvements in shrink primarily were responsible for the 2008 gross profit increase as a percentage of sales. Additionally, improved distribution and transportation logistics efficiencies mitigated increased fuel costs in the 2008 period. We recorded a LIFO charge of $16.0 million in the 2008 period as a result of inflationary pressures we began experiencing during the second quarter of 2008 (related primarily to commodity cost increases). In the 2007 period, net markdowns were higher than the historical rate as the result of markdowns taken in connection with the inventory reduction strategies discussed above.

SG&A Expense. SG&A decreased as a percentage of sales to 23.9% in the 2008 period from 24.9% in the 2007 period. The following items represent the more significant changes in SG&A, as a percentage of sales, between the periods. The 2008 period includes $20.3 million related to amortization of leasehold intangibles capitalized in connection with purchase accounting, approximately $7.1 million of severance and related costs, and approximately $10.0 million resulting from the Company s new ownership structure, primarily including monitoring

fees, consulting, executive recruiting and legal expenses. SG&A in the 2007 period includes approximately $47.3 million relating to strategic real estate initiatives, estimated losses of approximately $8.6 million relating to the probable loss associated with the restructuring of three distribution center leases, $3.4 million of leasehold intangibles amortization and $1.5 million relating to the Company s new ownership structure, including monitoring and consulting fees. We leveraged occupancy costs resulting from higher net sales and experienced reduced advertising, depreciation, workers compensation, and employee benefits expenses as a percentage of sales, partially offset by significantly higher incentive compensation expense associated with our 2008 financial performance.

Transaction and Related Costs. The $101.7 million of expenses recorded in the 2007 period reflect $62.3 million of expenses related to the Merger, such as investment banking and legal fees, as well as $39.4 million of compensation expense related to stock options, restricted stock and restricted stock units.

Interest Expense. The interest expense increase was due to interest on long-term obligations incurred to finance the Merger. See further discussion under Liquidity and Capital Resources below.

Other (Income) Expense. During the 2007 period, we recorded $6.2 million in expenses related to consent fees and other costs associated with a tender offer for our previously outstanding 2010 Notes. Approximately 99% of the 2010 Notes were retired in 2007 as a result of the tender offer. Also during the 2007 period, we recorded an unrealized gain of $4.7 million related to the change in the fair value of interest rate swaps.

Income Taxes. The effective income tax rates for the 26-week Successor period ended August 1, 2008, the Successor period ended August 3, 2007 and the Predecessor period ended July 6, 2007 were 39.1%, 36.7% (a benefit) and 300.2%, respectively. The difference in the effective tax rate between the two Successor periods results principally from the inclusion of income tax related interest expense in income tax expense as reported on the financial statements. The effective tax rate for the Predecessor period is higher than the other periods presented due principally to non-deductible expenses incurred in association with the Merger.

Accounting Pronouncements

In May 2008, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 162, The Hierarchy of Generally Accepted Accounting Principles. SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States (the GAAP hierarchy). SFAS 162 will be effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board (PCAOB) amendments to AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. We plan to adopt SFAS 162 once it is effective, and do not believe this standard will have a material impact on our financial statements.

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Recently Adopted Accounting Standard

We adopted the provisions of SFAS 157, Fair Value Measurements effective February 2, 2008. The adoption resulted in a $4.7 million decrease in liability balances associated with interest rate swaps that we use to manage interest rate risk, with the offset reflected in other comprehensive income.

Liquidity and Capital Resources

Credit Facilities

We have two senior secured credit facilities (the Credit Facilities) which provide financing of up to $3.425 billion. The Credit Facilities consist of a $2.3 billion senior secured term loan facility and a senior secured asset-based revolving credit facility of up to $1.125 billion (of which up to $350.0 million is available for letters of credit), subject to borrowing base availability. The asset-based revolving credit facility includes borrowing capacity available for letters of credit and for short-term borrowings referred to as swingline loans.

The agreements governing the Credit Facilities provide that we have the right at any time to request up to $325.0 million of incremental commitments under one or more incremental term loan facilities and/or asset-based revolving credit facilities. The lenders under these facilities are not under any obligation to provide any such incremental commitments and any such addition of or increase in commitments will be subject to our not exceeding certain senior secured leverage ratios and certain other customary conditions precedent. Our ability to obtain extensions of credit under these incremental commitments also will be subject to the same conditions as extensions of credit under the Credit Facilities.

The amount from time to time available under the asset-based revolving credit facility (including in respect of letters of credit) is subject to certain borrowing base limitations. The asset-based revolving credit facility includes a last out tranche in respect of which we may borrow up to a maximum amount of $125.0 million.

Borrowings under the Credit Facilities bear interest at a rate equal to an applicable margin plus, at our option, either (a) LIBOR or (b) a base rate (which is usually equal to the prime rate). The applicable margin for borrowings is (i) under the term loan facility, 2.75% with respect to LIBOR borrowings and 1.75% with respect to base-rate borrowings and (ii) as of August 1, 2008 under the asset-based revolving credit facility (except in the last out tranche described above), 1.50% with respect to LIBOR borrowings and 0.50% with respect to base-rate borrowings and for any last out borrowings, 2.25% with respect to LIBOR borrowings and 1.25% with respect to base-rate borrowings. The applicable margins for borrowings under the asset-based revolving credit facility (except in the case of last out borrowings) are subject to adjustment each quarter based on average daily excess availability under the asset-based revolving credit facility. We also are required to pay a commitment fee to the lenders under the asset-based revolving

credit facility in respect of the unutilized commitments thereunder. At August 1, 2008, the commitment fee rate was 0.375% per annum. We also must pay customary letter of credit fees.

The senior secured credit agreement for the term loan facility requires us to prepay outstanding term loans, subject to certain exceptions, with up to 50% of our annual excess cash flow (as defined in the credit agreement), the net cash proceeds of certain non-ordinary course asset sales or other dispositions of property, and the net cash proceeds of any incurrence of debt other than proceeds from debt permitted under the senior secured credit agreement.

In addition, the senior secured credit agreement for the asset-based revolving credit facility requires us to prepay the asset-based revolving credit facility, subject to certain exceptions, with the net cash proceeds of all non-ordinary course asset sales or other dispositions of revolving facility collateral (as defined in the senior secured credit agreement); and to the extent such extensions of credit exceed the then current borrowing base.

We may be obligated to pay a prepayment premium on the amount repaid under the term loan facility if the term loans are voluntarily repaid in whole or in part before July 6, 2009. We may voluntarily repay outstanding loans under the asset-based revolving credit facility at any time without premium or penalty, other than customary breakage costs with respect to LIBOR loans.

At August 1, 2008, we had no borrowings, $51.8 million of commercial letters of credit, and $82.4 million of standby letters of credit outstanding under our asset-based revolving credit facility.

Senior Notes due 2015 and Senior Subordinated Toggle Notes due 2017

We have $1,175.0 million aggregate principal amount of 10.625% senior notes due 2015 (the senior notes) outstanding, which mature on July 15, 2015, pursuant to an indenture dated as of July 6, 2007 (the senior indenture), and $700 million aggregate principal amount of 11.875%/12.625% senior subordinated toggle notes due 2017 (the senior subordinated notes) outstanding, which mature on July 15, 2017, pursuant to an indenture dated as of July 6, 2007 (the senior subordinated indenture). The senior notes and the senior subordinated notes are collectively referred to herein as the notes. The senior indenture and the senior subordinated indenture are collectively referred to herein as the indentures. We may redeem some or all of the notes at any time at redemption prices described or set forth in the indentures.

Interest on the notes is payable on January 15 and July 15 of each year. Interest on the senior notes is payable in cash. Cash interest on the senior subordinated notes accrues at a rate of 11.875% per annum, and PIK interest (as that term is defined below) accrues at a rate of 12.625% per annum, if applicable. The initial interest payment on the senior subordinated notes was payable in cash. For any interest period thereafter through July 15, 2011, we may elect to pay interest on the senior subordinated notes (i) in cash, (ii) by increasing the principal amount of the senior subordinated notes or issuing new senior subordinated notes (PIK interest) or (iii) by paying interest on half of the principal amount of the senior subordinated notes in cash interest and half in PIK interest. After July 15, 2011, all interest on the senior subordinated notes will be payable in cash.

Adjusted EBITDA

Under the agreements governing the Credit Facilities and the indentures, certain limitations and restrictions could arise if we are not able to satisfy and remain in compliance with specified financial ratios. Management believes the most significant of such ratios is the senior secured incurrence test under the Credit Facilities. This test measures the ratio of the senior secured debt to Adjusted EBITDA. This ratio would need to be no greater than 4.25 to 1 to avoid such limitations and restrictions. As of August 1, 2008, this ratio was 2.6 to 1. Senior secured debt is defined as our total debt secured by liens or similar encumbrances less cash and cash equivalents. EBITDA is defined as income (loss) from continuing operations before cumulative effect of change in accounting principle plus interest and other financing costs, net, provision for income taxes, and depreciation and amortization. Adjusted EBITDA is defined as EBITDA, further adjusted to give effect to adjustments required in calculating this covenant ratio under our Credit Facilities. EBITDA and Adjusted EBITDA are not presentations made in accordance with U.S. GAAP, are not measures of financial performance or condition, liquidity or profitability, and should not be considered as an alternative to (i) net income, operating income or any other performance measures determined in accordance with U.S. GAAP or (ii) operating cash flows determined in accordance with U.S. GAAP. Additionally, EBITDA and Adjusted EBITDA are not intended to be measures of free cash flow for management s discretionary use, as they do not consider certain cash requirements such as interest payments, tax payments and debt service requirements and replacements of fixed assets.

Our presentation of EBITDA and Adjusted EBITDA has limitations as an analytical tool, and should not be considered in isolation or as a substitute for analysis of our results as reported under U.S. GAAP. Because not all companies use identical calculations, these presentations of EBITDA and Adjusted EBITDA may not be comparable to other similarly titled measures of other companies. We believe that the presentation of EBITDA and Adjusted EBITDA is appropriate to provide additional information about the calculation of this financial ratio in the Credit Facilities. Adjusted EBITDA is a material component of this ratio. Specifically, non-compliance with the senior secured indebtedness ratio contained in our Credit Facilities could prohibit us from making investments, incurring liens, making certain restricted payments and incurring additional secured indebtedness (other than the additional funding provided for under the senior secured credit agreement and pursuant to specified exceptions).

The calculation of Adjusted EBITDA under the Credit Facilities is as follows:

	13-weeks ended		26-weeks ended		52-weeks ended	
	August 1, 2008	August 3, 2007	August 1, 2008	August 3, 2007	August 1, 2008	February 1, 2008
Net income (loss)	$ 27.7	$ (68.8)	$ 33.6	$ (35.2)	$ 56.0	$ (12.8)
Add (subtract):						
Interest income	(1.2)	(3.5)	(2.2)	(6.1)	(4.9)	(8.8)
Interest expense	99.4	40.7	200.3	46.8	416.7	263.2
Depreciation and amortization	57.4	57.3	115.7	107.9	234.2	226.4
Income taxes	16.8	(19.9)	21.5	(3.8)	35.5	10.2
EBITDA	200.1	5.8	368.9	109.6	737.5	478.2
Adjustments:						
Transaction and related costs	-	96.1	-	101.7	0.9	102.6
Loss on debt retirements, net	-	6.2	-	6.2	(5.0)	1.2
(Gain) loss on interest rate swaps	0.3	(6.8)	0.6	(4.7)	7.7	2.4
Contingent loss on distribution center leases	-	8.6	-	8.6	3.4	12.0
Impact of markdowns related to inventory clearance activities, including LCM adjustments, net of purchase accounting adjustments	-	9.0	1.3	5.1	(4.2)	(0.4)
SG&A related to store closing and inventory clearance activities	-	17.6	-	46.9	7.1	54.0
Operating losses (cash) of stores to be closed	-	4.1	-	9.4	1.1	10.5
Monitoring and consulting fees to affiliates	2.5	0.8	4.7	0.8	8.7	4.8
Stock option and restricted stock unit	2.2	3.8	4.5	3.8	7.2	6.5

expense						
Indirect merger-related costs	4.6	-	12.4	-	17.0	4.6
Other non-cash charges (LIFO)	16.0	-	16.0	-	22.1	6.1
Other	-	-	-	0.7	0.3	1.0
Total Adjustments	25.6	139.4	39.5	178.5	66.3	205.3
Adjusted EBITDA	$ 225.7	$ 145.2	$ 408.4	$ 288.1	$ 803.8	$ 683.5

Current Financial Condition / Recent Developments

At August 1, 2008, we had total outstanding debt (including the current portion of long-term obligations) of approximately $4.18 billion. We had $898.4 million available for borrowing under our senior secured asset-based revolving credit facility at that date. Our liquidity needs are significant, primarily due to our debt service and other obligations. However, we believe our cash flow from operations and existing cash balances, combined with availability under the Credit Facilities, will provide sufficient liquidity to fund our current obligations, projected working capital requirements and capital spending for a period that includes the next twelve months.

Our inventory balance represented approximately 46% of our total assets exclusive of goodwill and other intangible assets as of August 1, 2008. Our proficiency in managing our inventory balances can have a significant impact on our cash flows from operations during a given fiscal year. Inventory purchases are often somewhat seasonal in nature, such as the purchase of warm-weather or Christmas-related merchandise. See additional discussion below regarding changes in inventory balances.

In recent years, pursuant to state regulatory requirements, our South Carolina-based wholly owned captive insurance subsidiary, Ashley River Insurance Company (ARIC), has held cash and cash equivalents and investment balances to maintain a percentage of ARIC s liability and equity balances (primarily insurance liabilities) in the form of certain specified types of assets. As a result, these investments have not been available for general corporate purposes. In May 2008, we received notice that the state of South Carolina had agreed to a change in these regulatory requirements for a portion of these assets. As a result we have liquidated a substantial portion of our investment balances and remaining investments of $9.5 million held at August 1, 2008 are classified as available-for-sale. These remaining investments matured or were liquidated during the third quarter of 2008.

As described in Note 5 to the condensed consolidated financial statements, we are involved in the restructuring of certain leases as well as a number of legal actions and claims, some of which could potentially result in material cash payments. Adverse developments in those restructuring efforts or actions could materially and adversely affect our liquidity. We also have certain income tax-related contingencies as more fully described below under Critical Accounting Policies and Estimates. Future negative developments could have a material adverse effect on our liquidity.

We may seek, from time to time, to retire the notes (as defined above) through cash purchases on the open market, in privately negotiated transactions or otherwise. Such repurchases, if any, will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. The amounts involved may be material.

Cash flows from operating activities. A significant component of the change in cash flows from operating activities in the 2008 period as compared to the 2007 period was our strong operating performance due to greater sales, higher gross margins and lower SG&A expenses as a percentage of sales, partially offset by significantly higher interest expense, as described in more detail above under Results of Operations. In addition, we experienced increased inventory

turns and improved merchandise payment terms in the 2008 period as compared to the 2007 period. Accounts payable balances increased by $262.4 million in the 2008 period compared to an increase of $6.4 million in the 2007 period as a result of our implementation of initiatives to aggressively manage our payables. Partially offsetting the changes in accounts payable were changes in inventory balances, which increased by 16% overall during the first half of 2008 compared to a 2% overall decline during the first half of 2007. Inventory levels in the highly consumable category increased by 21% in the 2008 period compared to a 4% increase in the 2007 period; the seasonal category increased by 13% in the 2008 period compared to a 8% decrease in the 2007 period; the home products category was essentially unchanged in the 2008 period compared to an 11% decline in the 2007 period; and basic clothing increased by 16% in the 2008 period compared to a decline of 5% in the 2007 period. These changes in inventory balances are primarily attributable to new merchandising initiatives and the timing of certain product purchases as compared to the prior year period.

Cash flows from investing activities. Significant components of property and equipment purchases in the 2008 period included the following approximate amounts: $41 million for improvements and upgrades to existing stores; $16 million for remodels and relocations of existing stores; $10 million for new stores; $6 million for distribution and transportation-related capital expenditures; and $5 million for systems-related capital projects. During the 2008 period, we opened 125 new stores and remodeled or relocated 249 stores.

The Merger, as discussed in more detail above, resulted in cash payments of approximately $6.7 billion, net of cash acquired of $350 million, in the 2007 period. Significant components of property and equipment purchases in the 2007 period included the following approximate amounts: $30 million for new stores; $17 million for improvements, upgrades, remodels and relocations of existing stores; $7 million for distribution and transportation-related capital expenditures; and $4 million for systems-related capital projects. During the 2007 period, we opened 240 new stores, and remodeled or relocated 87 stores.

Purchases and sales of short-term investments of $9.9 million and $59.0 million, respectively, during the 2008 period, and sales of short-term investments of $10.5 million and purchases of short-term and long-term investments totaling $25.5 million during the 2007 period relate primarily to ARIC.

Capital expenditures for the entire 2008 fiscal year are projected to be approximately $200 to $220 million. We anticipate funding our 2008 capital requirements with cash flows from operations and our asset-based revolving credit facility, if necessary.

Cash flows from financing activities. We repaid $102.5 million under our asset-based revolving credit facility in the 2008 period. In the 2007 period we issued long-term debt of approximately $4.2 billion and issued common stock in the amount of approximately $2.8 billion to finance the Merger. We completed a cash tender offer in the 2007 period for our 2010 Notes. Approximately 99% of the 2010 Notes were validly tendered resulting in repayments of long-term debt in the amount of $210.3 million. Borrowings, net of repayments, under our asset-based revolving credit facility in the 2007 period totaled $300.0 million. Also in the 2007 Predecessor period, we paid cash dividends of $15.7 million, or $0.05 per share, on outstanding common

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stock during the 2007 period, offset by proceeds from the exercise of stock options of $41.5 million.

Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect reported amounts and related disclosures. In addition to the estimates presented below, there are other items within our financial statements that require estimation, but are not deemed critical as defined below. We believe these estimates are reasonable and appropriate. However, if actual experience differs from the assumptions and other considerations used, the resulting changes could have a material effect on the financial statements taken as a whole.

Management believes the following policies and estimates are critical because they involve significant judgments, assumptions, and estimates. Management has discussed the development and selection of the critical accounting estimates with the Audit Committee of our Board of Directors, and the Audit Committee has reviewed the disclosures presented below relating to those policies and estimates.

Merchandise Inventories. Merchandise inventories are stated at the lower of cost or market with cost determined using the retail last-in, first-out (LIFO) method. Under our retail inventory method (RIM), the calculation of gross profit and the resulting valuation of inventories at cost are computed by applying a calculated cost-to-retail inventory ratio to the retail value of sales. The RIM is an averaging method that has been widely used in the retail industry due to its practicality. Also, it is recognized that the use of the RIM will result in valuing inventories at the lower of cost or market (LCM) if markdowns are currently taken as a reduction of the retail value of inventories.

Inherent in the RIM calculation are certain significant management judgments and estimates including, among others, initial markups, markdowns, and shrinkage, which significantly impact the gross profit calculation as well as the ending inventory valuation at cost. These significant estimates, coupled with the fact that the RIM is an averaging process, can, under certain circumstances, produce distorted cost figures. Factors that can lead to distortion in the calculation of the inventory balance include:

- applying the RIM to a group of products that is not fairly uniform in terms of its cost and selling price relationship and turnover;

- applying the RIM to transactions over a period of time that include different rates of gross profit, such as those relating to seasonal merchandise;

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inaccurate estimates of inventory shrinkage between the date of the last physical inventory at a store and the financial statement date; and

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inaccurate estimates of LCM and/or LIFO reserves.

Factors that reduce potential distortion include the use of historical experience in estimating the shrink provision (see discussion below) and recent improvements in the annual LIFO analysis whereby all SKUs are considered in the index formulation. An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management s estimates of expected year-end inventory levels, sales for the year and the expected rate of inflation/deflation for the year and are thus subject to adjustment in the final year-end LIFO inventory valuation. We also perform interim inventory-aging analysis for determining obsolete inventory. Our policy is to write down inventory to an LCM value based on various management assumptions including estimated markdowns and sales required to liquidate such aged inventory in future periods. Inventory is reviewed on a quarterly basis and adjusted as appropriate to reflect write-downs determined to be necessary.

Factors such as slower inventory turnover due to changes in competitors tactics, consumer preferences, consumer spending and unseasonable weather patterns, among other factors, could cause excess inventory requiring greater than estimated markdowns to entice consumer purchases, resulting in an unfavorable impact on our consolidated financial statements. Sales shortfalls due to the above factors could cause reduced purchases from vendors and associated vendor allowances that would also result in an unfavorable impact on our consolidated financial statements.

We calculate our shrink provision based on actual physical inventory results during the fiscal period and an accrual for estimated shrink occurring subsequent to a physical inventory through the end of the fiscal reporting period. This accrual is calculated as a percentage of sales at each retail store, at a department level, and is determined by dividing the book-to-physical inventory adjustments recorded during the previous twelve months by the related sales for the same period for each store. To the extent that subsequent physical inventories yield different results than this estimated accrual, our effective shrink rate for a given reporting period will include the impact of adjusting the estimated results to the actual results. Although we perform physical inventories in virtually all of our stores on an annual basis, the same stores do not necessarily get counted in the same reporting periods from year to year, which could impact comparability in a given reporting period.

Goodwill and Indefinite-Lived Intangible Assets. Under SFAS 142, Goodwill and Other Intangible Assets, we are required to test goodwill and intangible assets with indefinite lives for impairment annually, or more frequently if impairment indicators occur. Significant judgments required in this testing process may include projecting future cash flows, determining appropriate discount rates and other assumptions. Projections are based on management s best estimates given recent financial performance, market trends, strategic plans and other available information. Changes in these estimates and assumptions could materially affect the determination of fair value or impairment. Future indicators of impairment could result in an asset impairment charge.

Purchase Accounting. The Merger was accounted for as a reverse acquisition in accordance with the purchase accounting provisions of SFAS 141, Business Combinations, under which our assets and liabilities have been accounted for at their estimated fair values as of the date of the Merger. The aggregate purchase price was allocated to the tangible and intangible

assets acquired and liabilities assumed, based upon an assessment of their relative fair values as of the date of the Merger. These estimates of fair values, the allocation of the purchase price and other factors related to the accounting for the Merger are subject to significant judgments and the use of estimates.

Property and Equipment. Property and equipment are recorded at cost. We group our assets into relatively homogeneous classes and generally provide for depreciation on a straight-line basis over the estimated average useful life of each asset class, except for leasehold improvements, which are amortized over the shorter of the applicable lease term or the estimated useful life of the asset. Certain store and warehouse fixtures, when fully depreciated, are removed from the cost and related accumulated depreciation and amortization accounts. The valuation and classification of these assets and the assignment of useful depreciable lives involves significant judgments and the use of estimates.

Impairment of Long-lived Assets. We review the carrying value of all long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. In accordance with Statement of Financial Accounting Standards (SFAS) 144, Accounting for the Impairment or Disposal of Long-Lived Assets, we review for impairment stores open more than two years for which current cash flows from operations are negative. Impairment results when the carrying value of the assets exceeds the undiscounted future cash flows over the life of the lease. Our estimate of undiscounted future cash flows over the lease term is based upon historical operations of the stores and estimates of future store profitability which encompasses many factors that are subject to variability and are difficult to predict. If a long-lived asset is found to be impaired, the amount recognized for impairment is equal to the difference between the carrying value and the asset s fair value. The fair value is estimated based primarily upon future cash flows (discounted at our credit adjusted risk-free rate) or other reasonable estimates of fair market value in accordance with U.S. GAAP.

Insurance Liabilities. We retain a significant portion of the risk for our workers compensation, employee health insurance, general liability, property loss and automobile coverage. These costs are significant primarily due to the large employee base and number of stores. At the date of the Merger this liability was discounted in accordance with purchase accounting standards. Subsequent to the Merger, provisions are made to this insurance liability on an undiscounted basis based on actual claim data and estimates of incurred but not reported claims developed using actuarial methodologies based on historical claim trends. If future claim trends deviate from recent historical patterns, we may be required to record additional expenses or expense reductions, which could be material to our future financial results.

Contingent Liabilities Income Taxes. Income tax reserves are determined using the methodology established by the Financial Accounting Standards Board (FASB) Interpretation 48, Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement 109 (FIN 48). FIN 48, which we adopted on February 3, 2007, requires companies to assess each income tax position taken using a two step process. A determination is first made as to whether it is more likely than not that the position will be sustained, based upon the technical merits, upon examination by the taxing authorities. If the tax position is expected to meet the more likely than not criteria, the benefit recorded for the tax position equals the largest amount that is

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greater than 50% likely to be realized upon ultimate settlement of the respective tax position. Uncertain tax positions require determinations and estimated liabilities to be made based on provisions of the tax law which may be subject to change or varying interpretation. If our determinations and estimates prove to be inaccurate, the resulting adjustments could be material to our future financial results.

Contingent Liabilities - Legal Matters. We are subject to legal, regulatory and other proceedings and claims. We establish liabilities as appropriate for these claims and proceedings based upon the probability and estimability of losses and to fairly present, in conjunction with the disclosures of these matters in our financial statements and SEC filings, management s view of our exposure. We review outstanding claims and proceedings with external counsel to assess probability and estimates of loss. We re-evaluate these assessments on a quarterly basis or as new and significant information becomes available to determine whether a liability should be established or if any existing liability should be adjusted. The actual cost of resolving a claim or proceeding ultimately may be substantially different than the amount of the recorded liability. In addition, because it is not permissible under U.S. GAAP to establish a litigation liability until the loss is both probable and estimable, in some cases there may be insufficient time to establish a liability prior to the actual incurrence of the loss (upon verdict and judgment at trial, for example, or in the case of a quickly negotiated settlement). See Note 5 to the condensed consolidated financial statements.

Lease Accounting and Excess Facilities. The majority of our stores are subject to short-term leases (usually with initial or primary terms of 3 to 5 years) with multiple renewal options when available. We also have stores subject to build-to-suit arrangements with landlords, which typically carry a primary lease term of 10 years with multiple renewal options. Approximately half of our stores have provisions for contingent rentals based upon a percentage of defined sales volume. We recognize contingent rental expense when the achievement of specified sales targets is considered probable. We recognize rent expense over the term of the lease. We record minimum rental expense on a straight-line basis over the base, non-cancelable lease term commencing on the date that we take physical possession of the property from the landlord, which normally includes a period prior to store opening to make necessary leasehold improvements and install store fixtures. When a lease contains a predetermined fixed escalation of the minimum rent, we recognize the related rent expense on a straight-line basis and record the difference between the recognized rental expense and the amounts payable under the lease as deferred rent. We also receive tenant allowances, which we record as deferred incentive rent and amortize as a reduction to rent expense over the term of the lease. We reflect as a liability any difference between the calculated expense and the amounts actually paid. Improvements of leased properties are amortized over the shorter of the life of the applicable lease term or the estimated useful life of the asset.

For store closures (excluding those associated with a business combination) where a lease obligation still exists, we record the estimated future liability associated with the rental obligation on the date the store is closed in accordance with SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities. Based on an overall analysis of store performance and expected trends, management periodically evaluates the need to close underperforming stores. Liabilities are established at the point of closure for the present value of any remaining

operating lease obligations, net of estimated sublease income, and at the communication date for severance and other exit costs, as prescribed by SFAS 146. Key assumptions in calculating the liability include the timeframe expected to terminate lease agreements, estimates related to the sublease potential of closed locations, and estimation of other related exit costs. If actual timing and potential termination costs or realization of sublease income differ from our estimates, the resulting liabilities could vary from recorded amounts. These liabilities are reviewed periodically and adjusted when necessary.

Share-Based Payments. Our share-based stock option awards are valued on an individual grant basis using the Black-Scholes-Merton closed form option pricing model. The application of this valuation model involves assumptions that are judgmental and highly sensitive in the valuation of stock options, which affects compensation expense related to these options. These assumptions include the term that the options are expected to be outstanding, an estimate of the volatility of our stock price (which is based on a peer group of publicly traded companies), applicable interest rates and the dividend yield of our stock. Other factors involving judgments that affect the expensing of share-based payments include estimated forfeiture rates of share-based awards. If our estimates differ materially from actual experience, we may be required to record additional expense or reductions of expense, which could be material to our future financial results.

Derivative Financial Instruments. The valuation of our derivative financial instruments is determined using valuation techniques including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves. The fair values of interest rate swaps are determined using a methodology of netting the discounted future fixed cash payments (or receipts) and the discounted expected variable cash receipts (or payments). The variable cash receipts (or payments) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves. In addition, we incorporate credit valuation adjustments to appropriately reflect both our own nonperformance risk and the respective counterparty s nonperformance risk. To adjust the fair value of derivative contracts for the effect of nonperformance risk, we consider the impact of netting and any applicable credit enhancements, such as collateral postings, thresholds, mutual puts, and guarantees. These valuation techniques and the related inputs include estimates and assumptions which are judgmental, and in some cases, based on forecasts of future events. If these estimates and assumptions differ materially from actual experience, the resulting adjustments could be material to our future financial results.

ITEM 3.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

There have been no material changes to the disclosures relating to this item from those set forth in our Annual Report on Form 10-K for the fiscal year ended February 1, 2008.

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ITEM 4T.

CONTROLS AND PROCEDURES.

(a)

Disclosure Controls and Procedures. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) or 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act). Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

(b)

Changes in Internal Control Over Financial Reporting. There have been no changes in our internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) during the quarter ended August 1, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1.

LEGAL PROCEEDINGS.

The information contained under the heading Legal proceedings in Note 5 to the condensed consolidated financial statements included in Part I, Item 1 of this Form 10-Q is incorporated herein by this reference.

ITEM 1A.

RISK FACTORS.

There have been no material changes to the disclosures relating to this item from those set forth in our Annual Report on Form 10-K for the fiscal year ended February 1, 2008.

ITEM 4.

SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

Pursuant to the terms of a Management Stockholder s Agreement with us and Buck Holdings, L.P., each of our shareholders agreed that shareholder action may be taken without a meeting, without prior notice and without a vote if a written consent setting forth the action taken is signed by shareholders having not less than the minimum number of votes that would be necessary to authorize the action at a meeting, and consented to the taking of any action in such manner. On May 29, 2008, acting by written consent without a meeting in reliance upon this provision, Buck Holdings, L.P., which owns 553,400,020 shares of our common stock (or approximately 99% of our then outstanding common stock), voted all of its shares to:

- Re-elect each member of our Board of Directors (namely, Michael M. Calbert, Raj Agrawal, Richard W. Dreiling, Adrian Jones and Dean B. Nelson) for a term of one year or until the election of each such director s successor.

- Approve and authorize an amendment to the 2007 Stock Incentive Plan for Key Employees of Dollar General Corporation and its Affiliates to increase the number of

shares available for grant under that Plan to 27.5 million from the previously authorized 24 million.

In addition, pursuant to the terms of the Management Stockholder s Agreement, each of our shareholders appointed Buck Holdings, L.P. and its authorized representatives and designees as proxy and attorney-in-fact to exercise the shareholder s right to vote all of his or her shares of our common stock for the purpose of electing any one or more members to our Board. Pursuant to this proxy, Buck Holdings, L.P., must vote on behalf of each such shareholder in the same manner as Buck Holdings, L.P., votes its own shares for the purpose of electing any one or more members to our Board. As of May 29, 2008, 2,079,877 shares of our common stock were outstanding and subject to this proxy.

ITEM 6.

EXHIBITS.

See the Exhibit Index immediately following the signature page hereto, which Exhibit Index is incorporated by reference as if fully set forth herein.

CAUTIONARY DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

Forward-looking statements within the meaning of the federal securities laws are included throughout this report, particularly under the heading Management s Discussion and Analysis of Financial Condition and Results of Operations, among others. You can identify these statements because they are not solely statements of historical fact or they use words such as may, will, should, expect, believe, anticipate, project, plan, expect, estim forecast, goal, intend, will likely result, or will continue and similar expressions that concern our strategy, plans intentions, among other things. For example, all statements relating to our estimated or projected earnings, costs, expenditures, cash flows, financial results and liquidity, our plans and objectives for future operations, growth or initiatives, the expected outcome or impact of pending or threatened litigation, and expectations regarding a possible reduction in the reserve for uncertain tax positions are forward-looking statements.

All forward-looking statements are subject to risks and uncertainties that may change at any time, so our actual results may differ materially from those that we expected. We derive many of these statements from our operating budgets and forecasts, which are based on many detailed assumptions that we believe are reasonable. However, it is very difficult to predict the impact of known factors, and we cannot anticipate all factors that could affect our actual results. Important factors that could cause actual results to differ materially from the expectations expressed in our forward-looking statements include, without limitation, increased competition; consumer demand, spending patterns and debt levels; changing wages, health care, other benefit, and insurance costs; inflation and general economic conditions; fluctuations in the costs of gasoline, diesel fuel and other energy, transportation, and utilities costs; the ability to hire and retain effective employees; our ability to timely open, remodel or relocate stores; interest rate fluctuations; capital market conditions; risks and challenges in connection with sourcing merchandise from domestic and international vendors; disruptions in the supply chain; the level of success of our initiatives; the outbreak of war or pandemics; geopolitical events or conditions; natural disasters; weather conditions; regulatory matters; the cost of goods; seasonality; the

factors disclosed under Risk Factors in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended February 1, 2008; the factors disclosed elsewhere in this document (including, without limitation, in conjunction with the forward-looking statements themselves and under the heading Critical Accounting Policies and Estimates); and other factors. All written and oral forward-looking statements are qualified in their entirety by these cautionary statements as well as other cautionary statements that we make from time to time in our other SEC filings and public communications. You should evaluate all of our forward-looking statements in the context of these risks and uncertainties.

The important factors referenced above may not contain all of the material factors that are important to you. In addition, we cannot assure you that we will realize the results or developments we expect or anticipate or, even if substantially realized, that they will result in the consequences or affect us or our operations in the way we expect. The forward-looking statements included in this report are made only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events or otherwise, except as otherwise required by law.

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, both on behalf of the Registrant and in his capacity as principal financial and accounting officer of the Registrant.

DOLLAR GENERAL CORPORATION

Date: September 3, 2008	By:	/s/ David M. Tehle David M. Tehle Executive Vice President and Chief Financial Officer

EXHIBIT INDEX

10.1

First Amendment to Employment Agreement with David M. Tehle, dated as of May 9, 2008 (incorporated by reference to Exhibit 99.1 to the Company s Current Report on Form 8-K dated May 9, 2008, filed with the SEC on May 15, 2008 (file no. 001-11421)).

10.2

First Amendment to Employment Agreement with Kathleen R. Guion, dated as of May 9, 2008 (incorporated by reference to Exhibit 99.2 to the Company s Current Report on Form 8-K dated May 9, 2008, filed with the SEC on May 15, 2008 (file no. 001-11421)).

10.3

First Amendment to Employment Agreement with Challis M. Lowe, dated as of May 9, 2008 (incorporated by reference to Exhibit 99.3 to the Company s Current Report on Form 8-K dated May 9, 2008, filed with the SEC on May 15, 2008 (file no. 001-11421)).

10.4

Addendum to Employment Agreement with Challis M. Lowe, dated as of May 14, 2008 (incorporated by reference to Exhibit 99.4 to the Company s Current Report on Form 8-K dated May 9, 2008, filed with the SEC on May 15, 2008 (file no. 001-11421)).

10.5

Amendment No. 1 to the 2007 Stock Incentive Plan for Key Employees of Dollar General Corporation and its Affiliates (incorporated by reference to Exhibit 99 to the Company s Current Report on Form 8-K dated May 29, 2008, filed with the SEC on June 2, 2008 (file no. 001-11421)).

10.6

Second Amendment to the Dollar General Corporation CDP/SERP Plan (as amended and restated effective December 31, 2007), dated as of June 3, 2008.

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Certifications of CEO and CFO under Exchange Act Rule 13a-14(a).

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Certifications of CEO and CFO under 18 U.S.C. 1350.