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MOVADO GROUP INC  
Form 10-Q  
December 07, 2006

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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 October 31, 2006

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-16497

MOVADO GROUP, INC.  
(Exact Name of Registrant as Specified in its Charter)

New York  
(State of Other Jurisdiction  
of Incorporation or Organization)

13-2595932  
(IRS Employer  
Identification No.)

650 From Road, Paramus, New Jersey  
(Address of Principal Executive Offices)

07652  
(Zip Code)

(201) 267-8000  
(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 that past 90 days. Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer" or "large accelerated filer" in Rule 12b-2 of the Exchange Act.  
Large accelerated filer  Accelerated filer  Non-accelerated filer

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

The number of shares outstanding of the registrant's common stock and class A common stock as of November 30, 2006 were 19,077,906 and 6,657,159, respectively.

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MOVADO GROUP, INC.

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October 31, 2006

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PART I - FINANCIAL INFORMATION  
Item 1. Financial Statements

MOVADO GROUP, INC.  
CONSOLIDATED BALANCE SHEETS  
(In thousands, except share and per share amounts)  
(Unaudited)

October 31,      January 31,      Oct

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	2006	2006	
	-----	-----	-----
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 79,908	\$123,625	\$
Trade receivables, net	159,010	106,619	1
Inventories	207,709	198,582	2
Other assets	33,740	26,319	
	-----	-----	-----
Total current assets	480,367	455,145	4
Property, plant and equipment, net	53,339	52,168	
Other assets	47,058	39,373	
	-----	-----	-----
Total assets	\$580,764	\$546,686	\$5
	=====	=====	==
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Loans payable to banks	\$ --	\$ --	\$
Current portion of long-term debt	5,000	5,000	
Accounts payable	35,948	33,120	
Accrued liabilities	52,465	42,268	
Current taxes payable	7,120	7,724	
Deferred taxes	514	503	
	-----	-----	-----
Total current liabilities	101,047	88,615	1
Long-term debt	82,435	104,955	
Deferred and non-current income taxes	11,050	11,947	
Other liabilities	21,714	19,491	
	-----	-----	-----
Total liabilities	216,246	225,008	2
	-----	-----	-----
Commitments and contingencies (Note 8)			
Minority interest	244	--	
Shareholders' equity:			
Preferred Stock, \$0.01 par value, 5,000,000 shares authorized; no shares issued	--	--	
Common Stock, \$0.01 par value, 100,000,000 shares authorized; 23,752,692, 23,215,836 and 23,178,828 shares issued, respectively	238	232	
Class A Common Stock, \$0.01 par value, 30,000,000 shares authorized; 6,657,159, 6,766,909 and 6,773,258 shares issued and outstanding, respectively	67	68	
Capital in excess of par value	115,168	107,965	1
Retained earnings	267,996	236,515	2
Accumulated other comprehensive income	33,291	27,673	
Treasury Stock, 4,676,117, 4,613,645 and 4,613,645 shares, respectively, at cost	(52,486)	(50,775)	(
	-----	-----	-----
Total shareholders' equity	364,274	321,678	3
	-----	-----	-----
Total liabilities and equity	\$580,764	\$546,686	\$5
	=====	=====	==

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See Notes to Consolidated Financial Statements

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MOVADO GROUP, INC.  
CONSOLIDATED STATEMENTS OF INCOME  
(In thousands, except per share amounts)  
(Unaudited)

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2006	2005	2006	2005
Net sales	\$166,272	\$141,736	\$390,604	\$344,818
Cost of sales	68,370	55,563	154,600	135,821
Gross profit	97,902	86,173	236,004	208,997
Selling, general and administrative	78,123	67,163	198,717	175,563
Operating income	19,779	19,010	37,287	33,434
Other income, net	374	1,008	374	1,008
Interest expense	(987)	(1,292)	(2,849)	(3,090)
Interest income	753	84	2,260	189
Minority interest	2	--	66	--
Income before income taxes	19,921	18,810	37,138	31,541
(Benefit) / Provision for income taxes	(1,964)	4,702	1,049	7,885
Net income	\$ 21,885	\$ 14,108	\$ 36,089	\$ 23,656
Earnings per share:				
Basic	\$ 0.85	\$ 0.56	\$ 1.41	\$ 0.94
Diluted	\$ 0.82	\$ 0.54	\$ 1.35	\$ 0.91
Weighted-average shares outstanding:				
Basic	25,758	25,328	25,620	25,209
Diluted	26,799	26,211	26,659	26,123

See Notes to Consolidated Financial Statements

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MOVADO GROUP, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In thousands)  
(Unaudited)

	Nine Months Ended October 31,	
	2006	2005
Cash flows from operating activities:		
Net income	\$ 36,089	\$ 23,656
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	11,945	11,158
Deferred income taxes	(10,342)	(1,860)
Provision for losses on accounts receivable	8,876	900
Provision for losses on inventory	463	450
Stock-based compensation	2,237	995
Excess tax benefit from stock-based compensation	(1,471)	--
Gain on sale of asset held for sale	(374)	(2,630)
Loss on hedge derivatives	--	1,622
Minority interest	(66)	--
Changes in assets and liabilities:		
Trade receivables	(51,762)	(42,498)
Inventories	(6,402)	(29,643)
Other current assets	(5,066)	(734)
Accounts payable	2,491	4,974
Accrued liabilities	12,012	5,486
Current taxes payable	872	1,721
Other non-current assets	(3,039)	(1,074)
Other non-current liabilities	2,219	442
Net cash used in operating activities	(1,318)	(27,035)
Cash flows from investing activities:		
Capital expenditures	(12,305)	(9,970)
Proceeds from sale of asset held for sale	686	4,000
Trademarks	(471)	(533)
Net cash used in investing activities	(12,090)	(6,503)
Cash flows from financing activities:		
Net (repayments) / proceeds of bank borrowings	(24,158)	44,000
Stock options exercised and other changes	1,788	655
Excess tax benefit from stock-based compensation	1,471	--
Dividends paid	(4,607)	(3,786)
Net cash (used in) / provided by financing activities	(25,506)	40,869
Effect of exchange rate changes on cash and cash equivalents	(4,803)	(15,049)

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Net decrease in cash and cash equivalents	(43,717)	(7,718)
Cash and cash equivalents at beginning of period	123,625	63,782
	-----	-----
Cash and cash equivalents at end of period	\$ 79,908	\$ 56,064
	=====	=====

See Notes to Consolidated Financial Statements

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### MOVADO GROUP, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared by Movado Group, Inc. (the "Company") in a manner consistent with that used in the preparation of the consolidated financial statements included in the Company's fiscal 2006 Annual Report filed on Form 10-K. In the opinion of management, the accompanying consolidated financial statements reflect all adjustments, consisting of only normal and recurring adjustments, necessary for a fair statement of the financial position and results of operations for the periods presented. These consolidated financial statements should be read in conjunction with the aforementioned Annual Report. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for the full year.

#### NOTE 1 - RECLASSIFICATIONS

Certain reclassifications were made to prior years' financial statement amounts and related note disclosures to conform to the fiscal 2007 presentation.

#### NOTE 2 - STOCK-BASED COMPENSATION

Effective concurrently with the consummation of the Company's public offering in the fourth quarter of fiscal 1994, the Board of Directors and the shareholders of the Company approved the adoption of the Movado Group, Inc. 1993 Employee Stock Option Plan (the "Employee Stock Option Plan") for the benefit of certain officers, directors and key employees of the Company. The Employee Stock Option Plan was amended in fiscal 1997 and restated as the Movado Group, Inc. 1996 Stock Incentive Plan (the "Plan"). Under the Plan, as amended and restated as of April 8, 2004, the Compensation Committee of the Board of Directors, which is comprised of four of the Company's outside directors, has the authority to grant incentive stock options and nonqualified stock options to purchase, as well as stock appreciation rights and stock awards, up to 9,000,000 shares of Common Stock. Options granted to participants under the Plan generally become exercisable in equal installments over three or five years and remain exercisable until the tenth anniversary of the date of grant. The option price may not be less than the fair market value of the stock at the time the options are granted.

On February 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment" ("SFAS No. 123(R)"), electing to use the modified prospective application transition method, and accordingly, prior period financial statements have not been

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restated. Under this method, the fair value of all stock options granted after adoption and the unvested portion of previously granted awards must be recognized in the Consolidated Statements of Income. The Company utilizes the Black-Scholes option-pricing model to calculate the fair value of each option at the grant date which requires certain assumptions be made. The expected life of stock option grants is determined using historical data and represents the time period which the stock option is expected to be outstanding until it is exercised. The risk free interest rate is the yield on the grant date of U.S. Treasury constant maturities with a maturity date closest to the expected life of the stock option. The expected stock price volatility is derived from historical volatility and calculated based on the estimated term structure of the stock option grant. The expected dividend yield is

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calculated using the expected annualized dividend which remains constant during the expected term of the option.

The weighted-average assumptions used with the Black-Scholes option-pricing model for the calculation of the fair value of stock option grants during the nine months ended October 31, 2006 were: expected term of 5.5 years; risk-free interest rate of 4.97%; expected volatility of 31.78% and dividend yield of 1.26%. The weighted-average grant date fair value of options granted during the nine months ended October 31, 2006 was \$6.46.

Total compensation expense for unvested stock option grants recognized during the three and nine months ended October 31, 2006 was approximately \$0.2 million, net of a tax benefit of \$0.1 million and \$0.6 million, net of a tax benefit of \$0.3 million, respectively. Expense related to stock option compensation is recognized on a straight-line basis over the vesting term. As of October 31, 2006, there was approximately \$2.7 million of unrecognized compensation cost related to unvested stock options. These costs are expected to be recognized over a weighted-average period of 2.4 years. Total cash received for stock option exercises during the nine months ended October 31, 2006 amounted to approximately \$2.9 million. Windfall tax benefits realized on these exercises were approximately \$1.1 million.

Prior to February 1, 2006, employee stock options were accounted for under the intrinsic value method, which measures compensation cost as the excess, if any, of the quoted market price of the stock at grant date over the amount an employee must pay to acquire the stock. Accordingly, compensation expense had not been recognized for stock options granted at or above fair value. Had compensation expense been determined and recorded based upon the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", net income (in thousands) and net income per share would have been reduced to pro forma amounts for the three months and nine months ended October 31, 2005 as follows:

(In thousands, except per share data)	Three Months Ended October 31, 2005	Nine Months Ended October 31, 2005
	-----	-----
Net income as reported	\$14,108	\$23,656
Fair value based compensation expense, net of taxes	(277)	(1,788)
	-----	-----
Pro forma net income	\$13,831	\$21,868

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	=====	=====
Basic earnings per share:		
As reported	\$ 0.56	\$ 0.94
Pro forma under SFAS No. 123	\$ 0.55	\$ 0.87
Diluted earnings per share:		
As reported	\$ 0.54	\$ 0.91
Pro forma under SFAS No. 123	\$ 0.53	\$ 0.84

The weighted-average assumptions used with the Black-Scholes option-pricing model for the calculation of the fair value of stock option grants during the nine months ended October 31, 2005 were: expected term of 7.0 years; risk-free interest rate of 3.76%; expected volatility of 46.53% and dividend yield of 1.75%. The weighted-average grant date fair value of options granted during the nine months ended October 31, 2005 was \$8.10.

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Stock option activity for the nine months ended October 31, 2006 is summarized as follows:

	Number of Options	Weighted-Average Exercise Price
	-----	-----
January 31, 2006	3,169,613	\$12.96
Options granted	21,000	\$19.33
Options exercised	(42,564)	\$ 8.96
	-----	-----
April 30, 2006	3,148,049	\$13.06
Options granted	97,000	\$18.41
Options exercised	(242,015)	\$ 8.33
Options cancelled	(20,000)	\$14.32
	-----	-----
July 31, 2006	2,983,034	\$13.61
Options granted	11,000	\$25.99
Options exercised	(43,974)	\$12.09
Options cancelled	(1,200)	\$ 9.15
	-----	-----
October 31, 2006	2,948,860	\$13.68
	=====	=====

The total intrinsic value of stock options exercised for the nine months ended October 31, 2006 and 2005 was approximately \$4.6 million and \$6.9 million, respectively. The total fair value of the stock options vested for the nine months ended October 31, 2006 and 2005 was approximately \$2.1 million and \$10.5 million, respectively.

The following table summarizes outstanding and exercisable stock options as of October 31, 2006:

Weighted-



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Range of Exercise Prices	Number Outstanding	Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
\$3.12 - \$6.22	132,340	3.1	\$ 4.25	132,340	\$ 4.25
\$6.23 - \$9.34	150,898	4.0	\$ 7.27	150,898	\$ 7.27
\$9.35 - \$12.45	748,748	3.1	\$10.67	724,948	\$10.70
\$12.46 - \$15.57	1,167,127	4.3	\$14.55	877,327	\$14.68
\$15.58 - \$18.68	720,747	6.2	\$18.13	379,749	\$18.36
\$18.69 - \$21.80	18,000	9.0	\$19.76	2,001	\$18.85
\$21.81 - \$24.91	1,000	9.2	\$22.45	0	--
\$24.92 - \$28.04	10,000	9.3	\$26.34	0	--
	-----	---	-----	-----	-----
	2,948,860	4.3	\$13.68	2,267,263	\$12.93
	-----	---	-----	-----	-----

The total intrinsic value of outstanding and exercisable stock options as of October 31, 2006 was approximately \$35.6 million and \$29.1 million, respectively.

Under the 1996 Stock Incentive Plan, the Company has the ability to grant restricted stock to certain employees. Restricted stock grants generally vest three to five years from the date of grant. Expense for these grants is

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recognized on a straight-line basis over the vesting period. The fair value of restricted stock grants is equal to the closing price of the Company's publicly-traded common stock on the grant date.

On May 31, 2006, the Compensation Committee of the Board of Directors adopted the Executive Long Term Incentive Plan (the "LTIP") authorized by section 9 of the Plan. The LTIP provides for the award of "Performance Share Units" that are equivalent, one for one, to shares of the Company's common stock and that vest based on the Company's achievement of its operating margin goal for the fiscal year ending January 31, 2009. The number of actual shares earned by a participant is based on the Company's actual performance at the end of the award period and can range from 0% to 150% of the participant's target award. Total target awards of 189,500 Performance Share Units were granted by the Compensation Committee on May 31, 2006 that vest over three and five year periods.

Total compensation expense for restricted stock grants and for grants of Performance Share Units under the LTIP (together "restricted stock") recognized during the three months ended October 31, 2006 and 2005 was approximately \$0.3 million, net of a tax benefit of \$0.2 million, and \$0.2 million, net of a tax benefit of \$0.1 million, respectively. Total compensation expense for restricted stock grants recognized during the nine months ended October 31, 2006 and 2005 was approximately \$0.8 million, net of a tax benefit of \$0.5 million, and \$0.6 million, net of a tax benefit of \$0.4 million, respectively. Prior to February 1, 2006, compensation expense for restricted stock grants was reduced as actual forfeitures of the awards occurred. SFAS No. 123(R) requires forfeitures to be estimated at the time of grant in order to estimate the amount of share-based awards that will ultimately vest and thus, current period compensation expense has been adjusted for estimated forfeitures based on historical data. As of October 31, 2006, there was approximately \$4.4 million of unrecognized compensation cost related to unvested restricted stock. These costs are expected

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to be recognized over a weighted-average period of 2.8 years.

Restricted stock activity for the nine months ended October 31, 2006 is summarized as follows:

	Number of Restricted Stock Units -----	Weighted- Average Grant Date Fair Value -----
January 31, 2006	321,090	\$14.39
Units granted	46,400	\$20.43
Units vested	(92,390)	\$ 9.83
Units forfeited	(220)	\$13.27
	-----	-----
April 30, 2006	274,880	\$16.95
Units granted	194,000	\$18.20
Units vested	(4,550)	\$ 9.98
Units forfeited	(8,410)	\$16.64
	-----	-----
July 31, 2006	455,920	\$17.56
Units granted	50	\$20.80
Units forfeited	(570)	\$18.23
	-----	-----
October 31, 2006	455,400 =====	\$17.56 =====

Restricted stock units are exercised simultaneously when they vest and are issued from the pool of authorized shares. The total intrinsic value of restricted stock units that vested during the nine months ended October 31, 2006 was approximately \$1.9 million. The windfall tax benefits realized on the vested restricted stock grants for the nine months ended October 31, 2006 were \$0.3 million. The weighted-average grant date fair values for restricted stock grants for the nine months ended October 31, 2006 and 2005 were \$18.63 and \$17.94,

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respectively. Outstanding restricted stock units had a total intrinsic value of approximately \$11.7 million as of October 31, 2006.

### NOTE 3 - COMPREHENSIVE INCOME (LOSS)

The components of comprehensive income (loss) for the three months and nine months ended October 31, 2006 and 2005 are as follows (in thousands):

	Three Months Ended October 31, -----		Nine Months Ended October 31, -----	
	2006	2005	2006	2005
	-----	-----	-----	-----
Net income	\$21,885	\$14,108	\$36,089	\$ 23,656
Net unrealized gain (loss) on				

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investments, net of tax	71	(92)	90	62
Effective portion of unrealized (loss) gain				
on hedging contracts, net of tax	(568)	1,393	1,494	(3,734)
Foreign currency translation adjustment (1)	(1,024)	925	4,034	(20,812)
	-----	-----	-----	-----
Total comprehensive income (loss)	\$20,364	\$16,334	\$41,707	(\$828)
	=====	=====	=====	=====

(1) The currency translation adjustments are not adjusted for income taxes as they relate to permanent investments in international subsidiaries.

### NOTE 4 - SEGMENT INFORMATION

The Company conducts its business primarily in two operating segments: Wholesale and Retail. The Company's Wholesale segment includes the designing, manufacturing and distribution of quality watches. The Retail segment includes the Movado Boutiques and outlet stores.

The Company divides its business into two major geographic segments: Domestic, which includes the results of the Company's North American, Caribbean and Tommy Hilfiger South American operations, and International, which includes the results of the Company's operations in all other parts of the world. The Company's International operations are principally conducted in Europe, the Middle East and Asia. The Company's International assets are substantially located in Switzerland.

Operating Segment Data for the Three Months Ended October 31, 2006 and 2005 (in thousands):

	Net Sales		Operating Income (Loss)	
	2006	2005	2006	2005
	-----	-----	-----	-----
Wholesale	\$146,396	\$121,932	\$20,355	\$18,459
Retail	19,876	19,804	(576)	551
	-----	-----	-----	-----
Consolidated total	\$166,272	\$141,736	\$19,779	\$19,010
	=====	=====	=====	=====

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Operating Segment Data for the nine months ended October 31, 2006 and 2005 (in thousands):

	Net Sales		Operating Income (Loss)	
	2006	2005	2006	2005
	-----	-----	-----	-----
Wholesale	\$333,505	\$290,196	\$38,251	\$34,370
Retail	57,099	54,622	(964)	(936)
	-----	-----	-----	-----

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Consolidated total	\$390,604	\$344,818	\$37,287	\$33,434
	=====	=====	=====	=====

	Total Assets		
	October 31, 2006	January 31, 2006	October 31, 2005
Wholesale	\$509,842	\$481,561	\$459,897
Retail	70,922	65,125	67,240
Consolidated total	\$580,764	\$546,686	\$527,137
	=====	=====	=====

Geographic Segment Data for the three months ended October 31, 2006 and 2005 (in thousands):

	Net Sales		Operating Income	
	2006	2005	2006	2005
Domestic	\$134,418	\$113,128	\$ 3,072	\$12,463
International	31,854	28,608	16,707	6,547
Consolidated total	\$166,272	\$141,736	\$19,779	\$19,010
	=====	=====	=====	=====

Geographic Segment Data for the nine months ended October 31, 2006 and 2005 (in thousands):

	Net Sales		Operating Income	
	2006	2005	2006	2005
Domestic	\$301,330	\$270,435	\$ 3,800	\$16,132
International	89,274	74,383	33,487	17,302
Consolidated total	\$390,604	\$344,818	\$37,287	\$33,434
	=====	=====	=====	=====

Domestic and International net sales are net of intercompany sales of \$84.2 million and \$74.4 million for the three months ended October 31, 2006 and 2005, respectively.

Domestic and International net sales are net of intercompany sales of \$194.2 million and \$179.7 million for the nine months ended October 31, 2006 and 2005, respectively.

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	Total Assets		
	October 31, 2006	January 31, 2006	October 31, 2005
Domestic	\$379,441	\$388,104	\$311,521
International	201,323	158,582	215,616
Consolidated total	\$580,764	\$546,686	\$527,137

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	Long-Lived Assets		
	October 31, 2006	January 31, 2006	October 31, 2005
Domestic	\$39,431	\$37,903	\$38,091
International	13,908	14,265	13,615
Consolidated total	\$53,339	\$52,168	\$51,706

NOTE 5 - EXECUTIVE RETIREMENT PLAN

The Company has a number of employee benefit plans covering substantially all employees. Certain eligible executives of the Company have elected to defer a portion of their compensation on a pre-tax basis under a defined contribution, supplemental executive retirement plan (SERP) sponsored by the Company. The SERP was adopted effective June 1, 1995, and provides eligible executives with supplemental pension benefits in addition to amounts received under the Company's other retirement plans. The Company makes a matching contribution which vests over five years. For the three months ended October 31, 2006 and 2005, the Company recorded an expense related to the SERP of \$0.2 million for each period. For the nine months ended October 31, 2006 and 2005, the Company recorded an expense related to the SERP of \$0.5 million for each period.

NOTE 6 - INVENTORIES

Inventories consist of the following (in thousands):

	October 31, 2006	January 31, 2006	October 31, 2005
Finished goods	\$133,138	\$135,160	\$134,350
Component parts	64,746	59,325	69,046
Work-in-process	9,825	4,097	5,547
	\$207,709	\$198,582	\$208,943

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### NOTE 7 - EARNINGS PER SHARE

The Company presents net income per share on a basic and diluted basis. Basic earnings per share is computed using weighted-average shares outstanding during the period. Diluted earnings per share is computed using the weighted-average number of shares outstanding adjusted for dilutive common stock equivalents.

The weighted-average number of shares outstanding for basic earnings per share were 25,758,000 and 25,328,000 for the three months ended October 31, 2006 and 2005, respectively. For diluted earnings per share, these amounts were increased by 1,041,000 and 883,000 for the three months ended October 31, 2006 and 2005, respectively, due to potentially dilutive common stock equivalents issuable under the Company's stock option plan and restricted stock grants.

The weighted-average number of shares outstanding for basic earnings per share were 25,620,000 and 25,209,000 for the nine months ended October 31, 2006 and 2005, respectively. For diluted earnings per share, these amounts were increased by 1,039,000 and 914,000 for the nine months ended October 31, 2006 and 2005, respectively, due to potentially dilutive common stock equivalents issuable under the Company's stock option plan and restricted stock grants.

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### NOTE 8 - COMMITMENTS AND CONTINGENCIES

At October 31, 2006, the Company had outstanding letters of credit totaling \$1.2 million with expiration dates through August 31, 2007. One bank in the domestic bank group has issued irrevocable standby letters of credit for retail and operating facility leases to various landlords, for the administration of the Movado Boutique private-label credit card and Canadian payroll to the Royal Bank of Canada.

As of October 31, 2006, two European banks have guaranteed obligations to third parties on behalf of two of the Company's foreign subsidiaries in the amount of \$2.1 million in various foreign currencies.

The Company is involved from time to time in legal claims involving trademarks and intellectual property, contracts, employee relations and other matters incidental to the Company's business. Although the outcome of such matters cannot be determined with certainty, the Company's general counsel and management believe that the final outcome would not have a material effect on the Company's consolidated financial position, results of operations or cash flows.

### NOTE 9 - OTHER INCOME, NET

The components of other income, net for the three months and nine months ended October 31, 2006 and 2005 are as follows (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2006	2005	2006	2005
	-----	-----	-----	-----
Gain on sale of building (a) (b)	\$374	\$ 2,630	\$374	\$ 2,630

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Discontinued cash flow hedges (c)	--	(1,622)	--	(1,622)
	----	-----	----	-----
Other income, net	\$374	\$ 1,008	\$374	\$ 1,008
	====	=====	====	=====

- (a) The Company recorded a pre-tax gain for the three months and nine months ended October 31, 2006 of \$0.4 million on the sale of a building acquired on March 1, 2004 in the acquisition of Ebel. The building was classified as an asset held for sale in other current assets.
- (b) The Company recorded a pre-tax gain for the three months and nine months ended October 31, 2005 of \$2.6 million on the sale of a building acquired on March 1, 2004 in the acquisition of Ebel. The building was classified as an asset held for sale in other current assets.
- (c) The Company recorded a pre-tax loss for the three months and nine months ended October 31, 2005 of \$1.6 million in other expense, representing the impact of the discontinuation of foreign currency cash flow hedges because it was not probable that the forecasted transactions would occur by the end of the originally specified time period.

### NOTE 10 - INCOME TAXES

At October 31, 2006, as a result of revised income projections, the Company recognized that it would be able to utilize a greater portion of the Swiss net operating loss carryforward acquired with the Ebel brand in fiscal year 2005. The taxes recorded during the three months and nine months ended October 31, 2006 reflect a discrete benefit of \$3.0 million as well as an adjustment to reflect the projected 11% annual effective tax rate.

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### NOTE 11 - RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48 "Accounting for Uncertainty in Income Taxes (an interpretation of FASB Statement No. 109)" which is effective for fiscal years beginning after December 15, 2006. This interpretation clarifies the accounting for uncertainty in income taxes recognized in the financial statements by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Company is currently evaluating the impact of this interpretation.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact of SFAS 157 on the Company's consolidated financial statements.

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

#### FORWARD-LOOKING STATEMENTS

Statements in this Quarterly Report on Form 10-Q, including, without limitation, statements under this Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this report, as well as statements in future filings by the Company with the Securities and Exchange Commission ("SEC"), in the Company's press releases and oral statements made by or with the approval of an authorized executive officer of the Company, which are not historical in nature, are intended to be, and are hereby identified as, "forward-looking statements" for purposes of the safe harbor provided by the Private Securities Litigation Reform Act of 1995. These statements are based on current expectations, estimates, forecasts and projections about the Company, its future performance, the industry in which the Company operates and management's assumptions. Words such as "expects", "anticipates", "targets", "goals", "projects", "intends", "plans", "believes", "seeks", "estimates", "may", "will", "should" and variations of such words and similar expressions are also intended to identify such forward-looking statements. The Company cautions readers that forward-looking statements include, without limitation, those relating to the Company's future business prospects, projected operating or financial results, revenues, working capital, liquidity, capital needs, plans for future operations, expectations regarding capital expenditures and operating expenses, effective tax rates, margins, interest costs, and income as well as assumptions relating to the foregoing. Forward-looking statements are subject to certain risks and uncertainties, some of which cannot be predicted or quantified. Actual results and future events could differ materially from those indicated in the forward-looking statements, due to several important factors herein identified, among others, and other risks and factors identified from time to time in the Company's reports filed with the SEC including, without limitation, the following: general economic and business conditions which may impact disposable income of consumers in the United States and the other significant markets where the Company's products are sold, general uncertainty related to possible terrorist attacks and the impact on consumer spending, changes in consumer preferences and popularity of particular designs, new product development and introduction, competitive products and pricing, seasonality, availability of alternative sources of supply in the case of the loss of any significant supplier, the loss of significant customers, the Company's dependence on key employees and officers, the ability to successfully integrate the operations of acquired businesses without disruption to other business activities, the continuation of licensing arrangements with third parties, the ability to secure and protect trademarks, patents and other intellectual property rights, the ability to lease new stores on suitable terms in desired markets and to complete construction on a timely basis, continued availability to the Company of financing and credit on favorable terms, business disruptions, disease, general risks associated with doing business outside the United States including, without limitation, import duties, tariffs, quotas, political and economic stability, and success of hedging strategies with respect to currency exchange rate fluctuations.

These risks and uncertainties, along with the risk factors discussed under Item 1A "Risk Factors" in the Company's Annual Report on Form 10-K, should be considered in evaluating any forward-looking statements contained in this Quarterly Report on Form 10-Q or incorporated by reference herein. All forward-looking statements speak only as of the date of this report or, in the case of any document incorporated by reference, the date of that document. All subsequent written and oral forward-looking statements attributable to the Company or any person acting on its behalf are qualified by the cautionary statements in this section. The Company undertakes no obligation to update or publicly release any revisions to forward-looking statements to reflect events, circumstances or changes in expectations after the date of this report.



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### Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial

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statements. These estimates and assumptions also affect the reported amounts of revenues and expenses. Estimates by their nature are based on judgments and available information. Therefore, actual results could materially differ from those estimates under different assumptions and conditions.

Critical accounting policies are those that are most important to the portrayal of the Company's financial condition and the results of operations and require management's most difficult, subjective and complex judgments as a result of the need to make estimates about the effect of matters that are inherently uncertain. The Company's most critical accounting policies have been discussed in the Company's Annual Report on Form 10-K for the year ended January 31, 2006. In applying such policies, management must use significant estimates that are based on its informed judgment. Because of the uncertainty inherent in these estimates, actual results could differ from estimates used in applying the critical accounting policies. Changes in such estimates, based on more accurate future information, may affect amounts reported in future periods.

As of October 31, 2006, except as noted below, there have been no material changes to any of the critical accounting policies as disclosed in its Annual Report on Form 10-K for the fiscal year ended January 31, 2006.

On February 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment" ("SFAS No. 123(R)"), electing to use the modified prospective application transition method, and accordingly, prior period financial statements have not been restated. Under this method, the fair value of all employee stock options granted after adoption and the unvested portion of previously granted awards must be recognized in the Consolidated Statements of Income. Prior to February 1, 2006, employee stock option grants were accounted for under the intrinsic value method, which measures compensation cost as the excess, if any, of the quoted market price of the stock at grant date over the amount an employee must pay to acquire the stock. Accordingly, compensation expense had not been recognized for employee stock options granted at or above fair value.

### Overview

The Company conducts its business primarily in two operating segments: Wholesale and Retail. The Company's Wholesale segment includes the designing, manufacturing and distribution of quality watches. The Retail segment includes the Movado Boutiques and outlet stores.

The Company divides its watch business into distinct categories. The luxury category is comprised of the Ebel and Concord brands. The accessible luxury category is comprised of the Movado and ESQ brands. The licensed brands category represents all brands distributed under license agreements and includes Coach, Hugo Boss, Juicy Couture and Tommy Hilfiger.

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Results of operations for the three months ended October 31, 2006 as compared to the three months ended October 31, 2005

Net Sales: Comparative net sales by business segment were as follows (in thousands):

	Three Months Ended October 31,	
	2006	2005
Wholesale:		
Domestic	\$114,542	\$ 93,324
International	31,854	28,608
Retail	19,876	19,804
	-----	-----
Net Sales	\$166,272	\$141,736

Net sales for the three months ended October 31, 2006 were \$166.3 million, above prior year by \$24.5 million or 17.3%. The liquidation of excess discontinued inventory accounted for approximately \$12.1 million of the increase. Net sales excluding the liquidation of excess discontinued inventory were \$154.2 million, representing an increase of \$12.5 million, or 8.8%, over the prior year. The Company is presenting net sales excluding the liquidation of excess discontinued inventory (and gross profit excluding liquidation sales) because the Company believes that it is useful to investors to eliminate the effect of these unusual sales in order to improve the comparability of the Company's results for the periods presented.

Net sales in the domestic wholesale segment were \$114.5 million for the three months ended October 31, 2006 representing a 22.7% increase above prior year sales of \$93.3 million. The increase in net sales was primarily attributed to higher sales in the accessible luxury brands of \$11.0 million and in the licensed brand category of \$6.6 million. In the accessible luxury category, Movado was above prior year by \$9.3 million, which includes the sale of approximately \$5.0 million of excess discontinued inventory. In the licensed brand category, Tommy Hilfiger was above prior year by \$2.4 million, primarily as a result of increased business in Latin America. In addition, Juicy Couture, which was launched during the quarter, contributed \$2.2 million of net sales. The liquidation of excess discontinued inventory accounted for approximately \$12.1 million of the increase in domestic wholesale net sales. Net sales excluding the liquidation of excess discontinued inventory were \$102.4 million, representing an increase of \$9.1 million, or 9.8%, over the \$93.3 million of net sales in the prior year. Excluding excess discontinued inventory sales, the luxury category recorded a decline in net sales for the three months ended October 31, 2006 of \$3.7 million. This primarily reflects the re-positioning of the Concord brand.

Net sales in the international wholesale segment were \$31.9 million for the three months ended October 31, 2006 representing an 11.3% increase above prior year sales of \$28.6 million. The increase of \$3.3 million was attributed to higher sales volume in the licensed brand category of \$3.7 million. In the licensed brands, the sales increase was driven by growth in Hugo Boss of \$3.4

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million, which was primarily the result of new market expansion.

Net sales in the retail segment were \$19.9 million for the three months ended October 31, 2006 representing a 0.4% increase above prior year sales of \$19.8 million. The increase was driven by an overall 1.3% increase in Movado Boutique sales, resulting from a 0.5% comparable store sales increase in the Movado Boutiques along with sales from non-comparable stores. Sales by the Company's outlet stores were below prior year by 0.2%, resulting from a 5.6% comparable store sales decrease. The Company operated 30 Movado Boutiques and 30 outlet stores at October 31, 2006, compared to 27 Movado Boutiques and 29 outlet stores at October 31, 2005.

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The Company considers comparable store sales to be sales of stores that were open as of February 1st of the last year through January 31st of the current year. The Company had 24 comparable Movado Boutiques and 26 comparable outlet stores for the three months ended October 31, 2006. The sales from stores that have been relocated, renovated or refurbished are included in the calculation of comparable store sales. The method of calculating comparative store sales varies across the retail industry. As a result, the calculation of comparable store sales may not be the same as measures reported by other companies.

Gross Profit. Gross profit for the three months ended October 31, 2006 was \$97.9 million or 58.9% of net sales as compared to \$86.2 million or 60.8% of net sales for the three months ended October 31, 2005. The increase in dollar gross profit of \$11.7 million was primarily the result of the higher sales volume. Gross margin percentage excluding the liquidation of excess discontinued inventory was 63.5%, above the 60.8% margin recorded in the prior year. The increase in gross margin percentage was driven by higher margins in the Movado Boutiques due to both product mix and improved jewelry margins. In addition, increases were recorded across most brands largely due to higher margin percentages on new product introductions.

Selling, General and Administrative ("SG&A"). SG&A expenses for the three months ended October 31, 2006 were \$78.1 million or 47.0% of net sales as compared to \$67.2 million or 47.4% of net sales for the three months ended October 31, 2005. The increase of \$10.9 million includes higher bad debt expense of approximately \$6.0 million as a result of a change in estimate to provide for aged customer receivables. The increase is also attributed to higher payroll and related costs of \$4.2 million, reflecting salary and benefit cost increases, increased headcount to support the growth for both new and existing brands and higher equity compensation costs. In addition, increased spending of \$1.4 million was made to support the retail expansion and increased spending of \$0.6 million occurred as a result of the consolidation of the Company's majority owned joint venture with TWC established to distribute the licensed brands in France and Germany. The increase in SG&A was partially offset by a \$2.2 million out-of-period adjustment recorded in the third quarter of fiscal 2007 related to foreign currency transactions.

Wholesale Operating Income. Operating income in the wholesale segment increased by \$1.9 million to \$20.4 million. The increase was the net result of higher gross profit of \$11.3 million, partially offset by the increase in SG&A expenses attributable to the wholesale segment of \$9.4 million. The higher gross profit of \$11.3 million was the result of the increase in net sales of \$24.5 million. The increase in SG&A expenses allocable to the wholesale segment in fiscal 2007 related principally to higher bad debt expense of approximately \$6.0 million, \$4.2 million of increased salary and benefits, \$0.6 million of increased TWC-related spending, offset partially by the \$2.2 million out-of-period

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adjustment, each as described above under "Selling, General and Administrative".

**Retail Operating (Loss) Income.** Operating loss of \$0.6 million and operating income of \$0.6 million were recorded in the retail segment for the three months ended October 31, 2006 and 2005, respectively. The operating loss was the net result of higher gross profit of \$0.4 million more than offset by higher SG&A expenses of \$1.6 million. The increased gross profit was primarily attributed to an increase in the gross profit percentage primarily due to product mix as well as higher gross profit on jewelry. The increase in SG&A expenses was primarily the result of increased spending for the non-comparable door expansion. These results reflect the seasonality of the business.

**Other Income.** The Company recorded other income for the three months ended October 31, 2006 and 2005 of \$0.4 million and \$1.0 million, respectively. As of October 31, 2006, the Company recorded a pre-tax gain of \$0.4 million on the sale of a building acquired on March 1, 2004 in the acquisition of Ebel. As of October 31, 2005, the Company recorded a pre-tax gain of \$2.6 million on the sale of another building acquired in the acquisition of Ebel. Both buildings were classified as assets held for sale in other current assets. Additionally, as of October 31, 2005, the Company recorded a pre-tax loss of \$1.6 million representing the impact of the

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discontinuation of foreign currency cash flow hedges because it was not probable that the forecasted transactions would occur by the end of the originally specified time period.

**Interest Expense.** Interest expense for the three months ended October 31, 2006 and 2005 was \$1.0 million and \$1.3 million, respectively. Average borrowings were \$96.3 million at an average borrowing rate of 3.9% for the three months ended October 31, 2006 compared to average borrowings of \$88.8 million at an average rate of 5.2% for the three months ended October 31, 2005. The lower average borrowing rate was due to the shifting of debt from the U.S. to Switzerland, which has a more favorable borrowing rate.

**Interest Income.** Interest income was approximately \$0.8 million for the three months ended October 31, 2006 as compared to approximately \$0.1 million for the three months ended October 31, 2005. The repatriated foreign earnings of \$150.0 million in the fourth quarter of fiscal year 2006 under the American Jobs Creation Act of 2004 resulted in significantly higher cash balances in the United States. The cash invested in the United States generated interest income at the rate of 5.2%.

**Income Taxes.** The Company recorded a tax benefit of \$2.0 million for the three months ended October 31, 2006 as compared to a tax expense of \$4.7 million for the three months ended October 31, 2005. At October 31, 2006, as a result of revised income projections, the Company recognized that it would be able to utilize a greater portion of the Swiss net operating loss carryforward. The taxes recorded during the three months ended October 31, 2006 reflect a discrete benefit of \$3.0 million as well as an adjustment to reflect the projected 11% annual effective tax rate. For the three months ended October 31, 2005, the annual effective tax rate was 25%.

**Net Income.** For the three months ended October 31, 2006, the Company recorded net income of \$21.9 million as compared to \$14.1 million for the three months ended October 31, 2005.

Results of operations for the nine months ended October 31, 2006 as compared to

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the nine months ended October 31, 2005

Net Sales: Comparative net sales by business segment were as follows (in thousands):

	Nine Months Ended October 31,	
	2006	2005
	-----	-----
Wholesale:		
Domestic	\$244,231	\$215,813
International	89,274	74,383
Retail	57,099	54,622
	-----	-----
Net Sales	\$390,604	\$344,818
	=====	=====

Net sales for the nine months ended October 31, 2006 were \$390.6 million, above prior year by \$45.8 million or 13.3%. The liquidation of excess discontinued inventory accounted for approximately \$12.1 million of that increase. Net sales excluding the liquidation of excess discontinued inventory were \$378.5 million, above prior year by \$33.7 million, or 9.8%.

Net sales in the domestic wholesale segment were \$244.2 million for the nine months ended October 31, 2006 representing a 13.2% increase above prior year sales of \$215.8 million. The increase in net sales was primarily attributed to higher sales in the accessible luxury brands of \$20.1 million and in the licensed brand category of \$8.2 million. In the accessible luxury category, Movado was above prior year by \$16.5 million, which includes

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the sale of approximately \$5.0 million of excess discontinued inventory. In the licensed brand category, Tommy Hilfiger was above prior year by \$3.5 million, primarily as a result of increased business in Latin America. In addition, Juicy Couture, which was launched during the third quarter, contributed \$2.2 million of net sales. Hugo Boss was above prior year by \$1.5 million also reflecting the impact of the launch of the Hugo Boss business in the domestic segment. The liquidation of excess discontinued inventory accounted for approximately \$12.1 million of the increase in domestic wholesale net sales. Net sales excluding the liquidation of excess discontinued inventory were \$232.1 million, representing an increase of \$16.3 million, or 7.6%, over the \$215.8 million of net sales in the prior year. Excluding excess discontinued inventory sales, the luxury category recorded a decline in net sales for the nine months ended October 31, 2006 of \$7.3 million. This primarily reflects the re-positioning of the Concord brand.

Net sales in the international wholesale segment were \$89.3 million for the nine months ended October 31, 2006 representing a 20.0% increase above prior year sales of \$74.4 million. The increase of \$14.9 million was attributed to higher sales volume in the licensed brand category of \$12.3 million. In the licensed brands, the sales increase was driven by growth in Hugo Boss of \$9.5 million and increases in Tommy Hilfiger of \$3.1 million, which was primarily as a result of new market expansion. The luxury category was above prior year by \$5.0 million. This was due to the new product introductions for the Ebel brand which recorded

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sales increases over last year of \$7.7 million.

Net sales in the retail segment were \$57.1 million for the nine months ended October 31, 2006 representing a 4.5% increase above prior year sales of \$54.6 million. The increase was driven by an overall 11.6% increase in Movado Boutique sales, resulting from a 5.0% comparable store sales increase in the Movado Boutiques along with sales from non-comparable stores. Net sales by the Company's outlet stores were below prior year by 0.6%, resulting from a 3.7% comparable store sales decrease, somewhat offset by sales from non-comparable stores. The Company operated 30 Movado Boutiques and 30 outlet stores at October 31, 2006, compared to 27 Movado Boutiques and 29 outlet stores at October 31, 2005.

Gross Profit. Gross profit for the nine months ended October 31, 2006 was \$236.0 million or 60.4% of net sales as compared to \$209.0 million or 60.6% of net sales for the nine months ended October 31, 2005. The increase in dollar gross profit of \$27.0 million was primarily the result of the higher sales volume. Gross margin percentage excluding the liquidation of excess discontinued inventory was 62.4%, above the 60.6% margin recorded in the prior year. The increase in gross margin percentage was driven by higher margins in the Movado Boutiques due to both product mix and improved jewelry margins. In addition, increases were recorded across most brands largely due to higher margin percentages on new product introductions.

Selling, General and Administrative. SG&A expenses for the nine months ended October 31, 2006 were \$198.7 million or 50.9% of net sales as compared to \$175.6 million or 50.9% of net sales for the nine months ended October 31, 2005. The increase of \$23.1 million includes the adjustment recorded in the third quarter for bad debt expense of approximately \$6.0 million to provide for aged customer receivables. The increase is also attributed to higher payroll and related costs of \$10.0 million reflecting salary and benefit cost increases, increased headcount to support the growth for both new and existing brands and higher equity compensation costs. In addition, increased spending of \$9.2 million was made to support the sales growth initiatives, including higher marketing spending of \$2.9 million, increased costs associated with the retail expansion of \$2.6 million, higher sales support activities of \$2.0 million and higher costs of \$1.7 million as a result of the consolidation of the Company's majority owned joint venture with TWC. The increase in SG&A was partially offset by a \$2.2 million out-of-period adjustment recorded in the third quarter of fiscal 2007 related to foreign currency transactions.

Wholesale Operating Income. Operating income in the wholesale segment increased by \$3.9 million to \$38.3 million. The increase was the net result of higher gross profit of \$24.3 million, partially offset by the increase in SG&A expenses attributable to the wholesale segment of \$20.4 million. The higher gross profit of \$24.3

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million was primarily due to the result of the increase in net sales of \$43.3 million. The increase in SG&A expenses allocable to the wholesale segment in fiscal 2007 related principally to higher bad debt expense of approximately \$6.0 million, \$10.0 million of increased salary and benefits, \$2.7 of marketing-related expenses and \$1.7 million of increased TWC-related spending, offset partially by the \$2.2 million out-of-period adjustment, each as described above under "Selling, General and Administrative".

Retail Operating Loss. Operating losses of \$1.0 million and \$0.9 million were recorded in the retail segment for the nine months ended October 31, 2006 and 2005, respectively. The operating loss was the net result of higher gross profit

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of \$2.7 million offset by higher SG&A expenses of \$2.8 million. The increased gross profit was primarily attributable to higher net sales of \$2.5 million and an increase in the gross profit percentage primarily due to product mix as well as higher gross profit on jewelry. The increase in SG&A expenses was primarily the result of increased spending for the non-comparable door expansion. These results reflect the seasonality of the business.

Other Income. The Company recorded other income for the nine months ended October 31, 2006 and 2005 of \$0.4 million and \$1.0 million, respectively. As of October 31, 2006, the Company recorded a pre-tax gain of \$0.4 million on the sale of a building acquired on March 1, 2004 in the acquisition of Ebel. As of October 31, 2005, the Company recorded a pre-tax gain of \$2.6 million on the sale of another building acquired in the acquisition of Ebel. Both buildings were classified as assets held for sale in other current assets. Additionally, as of October 31, 2005, the Company recorded a pre-tax loss of \$1.6 million representing the impact of the discontinuation of foreign currency cash flow hedges because it was not probable that the forecasted transactions would occur by the end of the originally specified time period.

Interest Expense. Interest expense for the nine months ended October 31, 2006 and 2005 was \$2.8 million and \$3.1 million, respectively. Average borrowings were \$100.6 million at an average borrowing rate of 3.7% for the nine months ended October 31, 2006 compared to average borrowings of \$71.0 million at an average rate of 5.3% for the nine months ended October 31, 2005. The lower average borrowing rate was due to the shifting of debt from the U.S. to Switzerland, which has a more favorable borrowing rate.

Interest Income. Interest income was \$2.3 million for the nine months ended October 31, 2006 as compared to \$0.2 million for the nine months ended October 31, 2005. The repatriated foreign earnings of \$150.0 million in the fourth quarter of fiscal year 2006 under the American Jobs Creation Act of 2004 resulted in significantly higher cash balances in the United States. The cash invested in the United States generated interest income at the rate of 4.9%.

Income Taxes. The Company recorded a tax expense of \$1.0 million for the nine months ended October 31, 2006 as compared to a tax expense of \$7.9 million for the nine months ended October 31, 2005. At October 31, 2006, as a result of revised income projections, the Company recognized that it would be able to utilize a greater portion of the Swiss net operating loss carryforward. The taxes recorded during the nine months ended October 31, 2006 reflect a discrete benefit of \$3.0 million as well as an adjustment to reflect the projected 11% annual effective tax rate. For the three months ended October 31, 2005, the annual effective tax rate was 25%.

Net Income. For the nine months ended October 31, 2006, the Company recorded net income of \$36.1 million as compared to \$23.7 million for the nine months ended October 31, 2005.

### LIQUIDITY AND CAPITAL RESOURCES

Cash used in operating activities was \$1.3 million for the nine months ended October 31, 2006 as compared to \$27.0 million cash used for the nine months ended October 31, 2005. The cash used in operating activities reflects the historic pattern of the Company to fund its working capital needs in the first nine months of the year due to the seasonal nature of the business. For the nine months ended October 31, 2006, the most significant

changes in operating assets were the increases in accounts receivable of \$51.8

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million, primarily resulting from the growth in sales and an increase of \$6.4 million in inventory levels, primarily in anticipation of the upcoming holiday selling season. These were offset by cash provided from net earnings of \$36.1 million for the nine months ended October 31, 2006 and \$15.4 million of cash provided from the increase of total current liabilities. For the nine months ended October 31, 2005, the most significant changes in operating assets were the increases in accounts receivable of \$42.5 million, primarily resulting from the growth in sales and an increase of \$29.6 million in inventory levels. This was partially offset by net earnings of \$23.7 million for the nine months ended October 31, 2005.

Cash used in investing activities amounted to \$12.1 million and \$6.5 million for the nine months ended October 31, 2006 and 2005, respectively. The cash used during both periods consisted of the capital expenditures primarily related to the expansion and renovations of retail stores and computer hardware and software enhancements. Capital expenditures in the 2006 period also included the acquisition of tooling for new product introductions. Capital expenditures in the 2005 period also included the acquisition of machinery and equipment to further automate distribution activities.

Cash used in financing activities amounted to \$25.5 million for the nine months ended October 31, 2006 compared to cash provided of \$40.9 million for the nine months ended October 31, 2005. Cash used in financing activities for the nine months ended October 31, 2006 was primarily to pay down long-term debt, while cash provided in the nine months ended October 31, 2005 resulted primarily from short-term borrowings required to fund the Company's working capital needs.

During fiscal 1999, the Company issued \$25.0 million of Series A Senior Notes under a Note Purchase and Private Shelf Agreement dated November 30, 1998. These notes bear interest of 6.90% per annum, mature on October 30, 2010 and are subject to annual repayments of \$5.0 million commencing October 31, 2006. These notes contain certain financial covenants including an interest coverage ratio and maintenance of consolidated net worth and certain non-financial covenants that restrict the Company's activities regarding investments and acquisitions, mergers, certain transactions with affiliates, creation of liens, asset transfers, payment of dividends and limitation of the amount of debt outstanding. At October 31, 2006, the Company was in compliance with all financial and non-financial covenants and \$20.0 million of these notes were issued and outstanding.

As of March 21, 2004, the Company amended its Note Purchase and Private Shelf Agreement, originally dated March 21, 2001, to expire on March 21, 2007. This agreement allows for the issuance, for up to three years after the date thereof, of senior promissory notes in the aggregate principal amount of up to \$40.0 million with maturities up to 12 years from their original date of issuance. On October 8, 2004, the Company issued, pursuant to the Note Purchase Agreement, 4.79% Senior Series A-2004 Notes due 2011 (the "Senior Series A-2004 Notes"), in an aggregate principal amount of \$20.0 million, which will mature on October 8, 2011 and are subject to annual repayments of \$5.0 million commencing on October 8, 2008. Proceeds of the Senior Series A-2004 Notes have been used by the Company for capital expenditures, repayment of certain of its debt obligations and general corporate purposes. These notes contain certain financial covenants, including an interest coverage ratio and maintenance of consolidated net worth and certain non-financial covenants that restrict the Company's activities regarding investments and acquisitions, mergers, certain transactions with affiliates, creation of liens, asset transfers, payment of dividends and limitation of the amount of debt outstanding. As of October 31, 2006, the Company was in compliance with all financial and non-financial covenants and \$20.0 million of these notes were issued and outstanding.

On December 15, 2005, the Company as parent guarantor, and its Swiss subsidiaries, MGI Luxury Group S.A. and Movado Watch Company SA as borrowers,



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entered into a credit agreement with JPMorgan Chase Bank, N.A., JPMorgan Securities, Inc., Bank of America, N.A., PNC Bank and Citibank, N.A. (the "Swiss Credit Agreement") which provides for a revolving credit facility of 90.0 million Swiss francs and matures on December 15, 2010. The obligations of the Company's two Swiss subsidiaries under this credit agreement are

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guaranteed by the Company under a Parent Guarantee, dated as of December 15, 2005, in favor of the lenders. The Swiss Credit Agreement contains financial covenants, including an interest coverage ratio, average debt coverage ratio and limitations on capital expenditures and certain non-financial covenants that restrict the Company's activities regarding investments and acquisitions, mergers, certain transactions with affiliates, creation of liens, asset transfers, payment of dividends and limitation of the amount of debt outstanding. Borrowings under the Swiss Credit Agreement bear interest at a rate equal to the LIBOR (as defined in the Swiss Credit Agreement) plus a margin ranging from .50% per annum to .875% per annum (depending upon a leverage ratio). As of October 31, 2006, the Company was in compliance with all financial and non-financial covenants and had 59.0 million Swiss francs, with a dollar equivalent of \$47.4 million, outstanding under this revolving credit facility.

On December 15, 2005, the Company and its Swiss subsidiaries, MGI Luxury Group S.A. and Movado Watch Company SA, entered into a credit agreement with JPMorgan Chase Bank, N.A., JPMorgan Securities, Inc., Bank of America, N.A., PNC Bank and Citibank, N.A. (the "US Credit Agreement") which provides for a revolving credit facility of \$50.0 million (including a sublimit for borrowings in Swiss francs of up to \$25.0 million) with a provision to allow for an increase of an additional \$50.0 million subject to certain terms and conditions. The US Credit Agreement will mature on December 15, 2010. The obligations of MGI Luxury Group S.A. and Movado Watch Company SA are guaranteed by the Company under a Parent Guarantee, dated as of December 15, 2005, in favor of the lenders. The obligations of the Company are guaranteed by certain domestic subsidiaries of the Company under subsidiary guarantees, in favor of the lenders. The US Credit Agreement contains financial covenants, including an interest coverage ratio, average debt coverage ratio and limitations on capital expenditures and certain non-financial covenants that restrict the Company's activities regarding investments and acquisitions, mergers, certain transactions with affiliates, creation of liens, asset transfers, payment of dividends and limitation of the amount of debt outstanding. Borrowings under the US Credit Agreement bear interest, at the Company's option, at a rate equal to the Adjusted LIBOR (as defined in the US Credit Agreement) plus a margin ranging from .50% per annum to .875% per annum (depending upon a leverage ratio), or the Alternate Base Rate (as defined in the US Credit Agreement). As of October 31, 2006, the Company was in compliance with all financial and non-financial covenants, and there were no outstanding borrowings against this line.

On June 16, 2006, the Company renewed a line of credit letter agreement with Bank of America and an amended and restated promissory note in the principal amount of up to \$20.0 million payable to Bank of America, originally dated December 12, 2005. Pursuant to the line of credit letter agreement, Bank of America will consider requests for short-term loans and documentary letters of credit for the importation of merchandise inventory, the aggregate amount of which at any time outstanding shall not exceed \$20.0 million. The Company's obligations under the agreement are guaranteed by its subsidiaries, Movado Retail Group, Inc. and Movado LLC. Pursuant to the amended and restated promissory note, the Company promised to pay to Bank of America \$20.0 million, or such lesser amount as may then be the unpaid balance of all loans made by Bank of America to the Company thereunder, in immediately available funds upon the maturity date of June 16, 2007. The Company has the right to prepay all or

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part of any outstanding amounts under the promissory note without penalty at any time prior to the maturity date. The amended and restated promissory note bears interest at an annual rate equal to either (i) a floating rate equal to the prime rate or (ii) such fixed rate as may be agreed upon by the Company and Bank of America for an interest period which is also then agreed upon. The amended and restated promissory note contains various representations and warranties and events of default that are customary for instruments of that type. As of October 31, 2006, there were no outstanding borrowings against this line.

On July 31, 2006, the Company renewed a promissory note, originally dated December 13, 2005, in the principal amount of up to \$37.0 million, at a revised amount of up to \$7.0 million, payable to JPMorgan Chase Bank, N.A. ("Chase"). Pursuant to the promissory note, the Company promised to pay to Chase \$7.0 million, or such lesser amount as may then be the unpaid balance of each loan made or letter of credit issued by Chase to

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the Company thereunder, upon the maturity date of July 31, 2007. The Company has the right to prepay all or part of any outstanding amounts under the promissory note without penalty at any time prior to the maturity date. The promissory note bears interest at an annual rate equal to either (i) a floating rate equal to the prime rate, (ii) a fixed rate equal to an adjusted LIBOR plus 0.625% or (iii) a fixed rate equal to a rate of interest offered by Chase from time to time on any single commercial borrowing. The promissory note contains various events of default that are customary for instruments of that type. In addition, it is an event of default for any security interest or other encumbrance to be created or imposed on the Company's property, other than as permitted in the lien covenant of the US Credit Agreement. Chase issued 11 irrevocable standby letters of credit for retail and operating facility leases to various landlords, for the administration of the Movado Boutique private-label credit card and Canadian payroll to the Royal Bank of Canada totaling \$1.2 million with expiration dates through August 31, 2007. As of October 31, 2006, there were no outstanding borrowings against this promissory note.

A Swiss subsidiary of the Company maintains unsecured lines of credit with an unspecified length of time with a Swiss bank. Available credit under these lines totaled 8.0 million Swiss francs, with dollar equivalents of \$6.4 million and \$6.2 million at October 31, 2006 and 2005, respectively. As of October 31, 2006, two European banks have guaranteed obligations to third parties on behalf of two of the Company's foreign subsidiaries in the amount of \$2.1 million in various foreign currencies. As of October 31, 2006, there were no outstanding borrowings against these lines.

The Company paid dividends per share of \$0.06 quarterly or approximately \$4.6 million, for the nine months ended October 31, 2006 and \$0.05 per share quarterly or approximately \$3.8 million for the nine months ended October 31, 2005.

Cash and cash equivalents at October 31, 2006 amounted to \$79.9 million compared to \$56.1 million at October 31, 2005. The increase in cash and cash equivalents primarily relates to the Company's borrowings in the fourth quarter of fiscal 2006 to repatriate foreign earnings to the United States under the American Jobs Creation Act of 2004.

Management believes that the cash on hand in addition to the expected cash flow from operations and the Company's short-term borrowing capacity will be sufficient to meet its working capital needs for at least the next 12 months.

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### Off-Balance Sheet Arrangements

The Company does not have off-balance sheet financing or unconsolidated special-purpose entities.

### RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48 "Accounting for Uncertainty in Income Taxes (an interpretation of FASB Statement No. 109)" which is effective for fiscal years beginning after December 15, 2006. This interpretation clarifies the accounting for uncertainty in income taxes recognized in the financial statements by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Company is currently evaluating the impact of this interpretation.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact of SFAS 157 on the Company's consolidated financial statements.

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### Item 3. Quantitative and Qualitative Disclosure about Market Risks

#### Foreign Currency and Commodity Price Risks

A significant portion of the Company's purchases are denominated in Swiss francs. The Company reduces its exposure to the Swiss franc exchange rate risk through a hedging program. Under the hedging program, the Company manages most of its foreign currency exposures on a consolidated basis, which allows it to net certain exposures and take advantage of natural offsets. The Company uses various derivative financial instruments to further reduce the net exposures to currency fluctuations, predominately forward and option contracts. These derivatives either (a) are used to hedge the Company's Swiss franc liabilities and are recorded at fair value with the changes in fair value reflected in earnings or (b) are documented as cash flow hedges with the gains and losses on this latter hedging activity first reflected in other comprehensive income, and then later classified into earnings in accordance with Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133"), as amended by SFAS No. 137, SFAS No. 138 and SFAS No. 149. In both cases, the earnings impact is partially offset by the effects of currency movements on the underlying hedged transactions. If the Company did not engage in a hedging program, any change in the Swiss franc to local currency would have an equal effect on the Company's cost of sales. In addition, the Company hedges its Swiss franc payable exposure with forward contracts. As of October 31, 2006, the Company's entire net forward contracts hedging portfolio consisted of 141.0 million Swiss francs equivalent for various expiry dates ranging through September 28, 2007. If the Company were to settle its Swiss franc forward contracts at October 31, 2006, the net result would have been a loss of \$0.2 million, net of tax benefit of \$0.1 million. As of October 31, 2006, the Company had 24.0 million Swiss franc option contracts related to cash flow hedges for various expiry dates ranging through October 31, 2007. If the

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Company were to settle its Swiss franc option contracts at October 31, 2006, the net result would have been a loss of \$0.1 million, net of tax benefit of \$0.1 million.

The Company's Board of Directors authorized the hedging of the Company's Swiss franc denominated investment in its wholly-owned Swiss subsidiaries using purchase options under certain limitations. These hedges are treated as net investment hedges under SFAS No. 133. As of October 31, 2006, the Company did not hold a purchased option hedge portfolio related to net investment hedging.

### Commodity Risk

Additionally, the Company has a hedging program related to gold used in the manufacturing of the Company's watches. Under this hedging program, the Company purchases various commodity derivative instruments, primarily future contracts. These derivatives are documented as SFAS No. 133 cash flow hedges, and gains and losses on these derivative instruments are first reflected in other comprehensive income, and later reclassified into earnings, partially offset by the effects of gold market price changes on the underlying actual gold purchases. If the Company did not engage in a gold hedging program, any changes in the gold price would have an equal effect on the Company's cost of sales. The Company did not hold any futures contracts in its gold hedge portfolio related to cash flow hedges as of October 31, 2006.

### Debt and Interest Rate Risk

In addition, the Company has certain debt obligations with variable interest rates, which are based on Swiss LIBOR plus a fixed additional interest rate. The Company does not hedge these interest rate risks. The Company also has certain debt obligations with fixed interest rates. The differences between the market based interest rates at October 31, 2006, and the fixed rates were unfavorable. The Company believes that a 1% change in interest rates would affect the Company's net income by approximately \$0.5 million.

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## Item 4. Controls and Procedures

### Evaluation of Disclosure Controls and Procedures

The Company, under the supervision and with the participation of its management, including the Chief Executive Officer and the Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures, as such terms are defined in Rule 13a-15(e) under the Securities Exchange Act, as amended. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective as of the end of the period covered by this report.

It should be noted that while the Company's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the Company's disclosure controls and procedures or internal control over financial reporting will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

### Changes in Internal Control Over Financial Reporting

There has been no change in the Company's internal control over financial

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reporting during the three months ended October 31, 2006, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II - OTHER INFORMATION

Item 1A. Risk Factors

As of October 31, 2006, there have been no material changes to any of the risk factors previously reported in the Annual Report on Form 10-K for the fiscal year ended January 31, 2006.

Item 6. Exhibits

- 31.1 Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURE

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

MOVADO GROUP, INC.  
(Registrant)

Dated: December 7, 2006

By: /s/ Eugene J. Karpovich

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Eugene J. Karpovich  
Senior Vice President and  
Chief Financial Officer  
(Chief Financial Officer)  
(Duly Authorized Officer)

/s/ Ernest R. LaPorte  
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Ernest R. LaPorte  
Vice President of Finance  
(Principal Accounting Officer)