

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 May 5, 2007

OR

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 1-31340

THE CATO CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction
of incorporation or organization)

56-0484485

(I.R.S. Employer
Identification No.)

8100 Denmark Road, Charlotte, North Carolina 28273-5975

(Address of principal executive offices)
(Zip Code)

(704) 554-8510

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year,
if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes 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 and 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

As of May 22, 2007, there were 30,987,759 shares of Class A common stock and 690,525 shares of Class B common stock outstanding.

THE CATO CORPORATION
FORM 10-Q
Quarter Ended May 5, 2007
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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

THE CATO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND
COMPREHENSIVE INCOME

	Three Months Ended	
	May 5, 2007 (Unaudited)	April 29, 2006 (Unaudited)
	(Dollars in thousands, except per share data)	
REVENUES		
Retail sales	\$ 224,134	\$ 229,741
Other income (principally finance charges, late fees and layaway charges)	3,094	3,319
Total revenues	<u>227,228</u>	<u>233,060</u>
COSTS AND EXPENSES, NET		
Cost of goods sold (exclusive of depreciation shown below)	143,422	142,113
Selling, general and administrative	51,136	54,577
Depreciation	5,391	5,168
Interest and other income	(1,893)	(1,552)
	<u>198,056</u>	<u>200,306</u>
Income before income taxes	29,172	32,754
Income tax expense	10,502	11,955
Net Income	<u>\$ 18,670</u>	<u>\$ 20,799</u>
Basic earnings per share	<u>\$ 0.60</u>	<u>\$ 0.67</u>
Basic weighted average shares	31,352,592	31,084,206
Diluted earnings per share	<u>\$ 0.59</u>	<u>\$ 0.65</u>
Diluted weighted average shares	31,897,676	31,814,193
Dividends per share	<u>\$ 0.15</u>	<u>\$ 0.13</u>
Comprehensive income:		
Net income	\$ 18,670	\$ 20,799
Unrealized gains (losses) on available-for-sale securities, net of deferred income tax benefit	27	(22)
Net comprehensive income	<u>\$ 18,697</u>	<u>\$ 20,777</u>

See notes to condensed consolidated financial statements.

THE CATO CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

	May 5, 2007 <u>(Unaudited)</u>	April 29, 2006 <u>(Unaudited)</u>	February 3, 2007
	(Dollars in thousands)		
ASSETS			
Current Assets:			
Cash and cash equivalents	\$ 21,164	\$ 25,319	\$ 24,833
Short-term investments	132,450	95,752	98,709
Accounts receivable, net of allowance for doubtful accounts of \$3,243, \$3,606 and \$3,554 at May 5, 2007, April 29, 2006 and February 3, 2007, respectively	45,287	47,791	45,958
Merchandise inventories	117,037	103,145	115,918
Deferred income taxes	7,489	8,538	7,508
Prepaid expenses	6,940	2,841	6,587
Total Current Assets	330,367	283,386	299,513
Property and equipment — net	126,809	131,516	128,461
Other assets	4,361	10,799	4,348
Total Assets	\$ 461,537	\$ 425,701	\$ 432,322
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current Liabilities:			
Accounts payable	\$ 90,952	\$ 75,641	\$ 77,046
Accrued expenses	29,755	30,089	29,526
Accrued bonus and benefits	1,065	13,194	10,756
Accrued income taxes	15,692	16,591	5,721
Total Current Liabilities	137,464	135,515	123,049
Deferred income taxes	8,817	9,261	8,817
Other noncurrent liabilities (primarily deferred rent)	23,298	23,526	23,663
Commitments and contingencies:			
Stockholders' Equity:			
Preferred stock, \$100 par value per share, 100,000 shares authorized, none issued	—	—	—
Class A common stock, \$.033 par value per share, 50,000,000 shares authorized; issued 36,082,118 shares, 35,653,816 shares and 35,955,815 shares at May 5, 2007, April 29, 2006 and February 3, 2007, respectively	1,203	1,188	1,199
Convertible Class B common stock, \$.033 par value per share, 15,000,000 shares authorized; issued 690,525 shares, at May 5, 2007, April 29, 2006 and February 3, 2007, respectively	23	23	23
Additional paid-in capital	43,307	39,743	42,475
Retained earnings	341,986	311,202	327,684
Accumulated other comprehensive income	252	56	225
	386,771	352,212	371,606
Less Class A common stock in treasury, at cost (5,093,609 shares at May 5, 2007, April 29, 2006 and February 3, 2007, respectively)	(94,813)	(94,813)	(94,813)
Total Stockholders' Equity	291,958	257,399	276,793
Total Liabilities and Stockholders' Equity	\$ 461,537	\$ 425,701	\$ 432,322

See notes to condensed consolidated financial statements.

THE CATO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended	
	May 5, 2007 (Unaudited)	April 29, 2006 (Unaudited)
	(Dollars in thousands)	
OPERATING ACTIVITIES		
Net income	\$ 18,670	\$ 20,799
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	5,391	5,168
Provision for doubtful accounts	458	981
Share-based compensation	371	244
Excess tax benefits from share-based compensation	(62)	(80)
Deferred income taxes	—	(12)
Loss on disposal of property and equipment	133	136
Changes in operating assets and liabilities which provided (used) cash:		
Accounts receivable	213	872
Merchandise inventories	(1,119)	225
Prepaid and other assets	(366)	(467)
Accrued income taxes	10,396	11,681
Accounts payable, accrued expenses and other liabilities	4,539	(10,739)
Net cash provided by operating activities	<u>38,624</u>	<u>28,808</u>
INVESTING ACTIVITIES		
Expenditures for property and equipment	(3,930)	(12,765)
Purchases of short-term investments	(158,505)	(50,069)
Sales of short-term investments	124,810	40,380
Net cash used in investing activities	<u>(37,625)</u>	<u>(22,454)</u>
FINANCING ACTIVITIES		
Change in cash overdrafts included in accounts payable	(400)	805
Dividends paid	(4,734)	(4,059)
Proceeds from employee stock purchase plan	214	189
Excess tax benefits from share-based compensation	62	80
Proceeds from stock options exercised	190	216
Net cash used in financing activities	<u>(4,668)</u>	<u>(2,769)</u>
Net increase (decrease) in cash and cash equivalents	<u>(3,669)</u>	<u>3,585</u>
Cash and cash equivalents at beginning of period	24,833	21,734
Cash and cash equivalents at end of period	<u>\$ 21,164</u>	<u>\$ 25,319</u>

See notes to condensed consolidated financial statements.

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 5, 2007 AND APRIL 29, 2006

NOTE 1 — GENERAL:

The condensed consolidated financial statements have been prepared from the accounting records of The Cato Corporation and its wholly-owned subsidiaries (the “Company”), and all amounts shown as of and for the periods ended May 5, 2007 and April 29, 2006 are unaudited. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. The results of the interim period may not be indicative of the results expected for the entire year.

The interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto, included in the Company’s Annual Report on Form 10-K for the fiscal year ended February 3, 2007.

Cash equivalents consist of highly liquid investments with original maturities of three months or less. Investments with original maturities beyond three months are classified as short-term investments. The fair values of short-term investments are based on quoted market prices.

Short-term investments are classified as available-for-sale. As they are available for current operations, they are classified in the Condensed Consolidated Balance Sheets as current assets. Available-for-sale securities are carried at fair value, with unrealized gains and temporary losses, net of income taxes, reported as a component of accumulated other comprehensive income. Other than temporary declines in fair value of investments are recorded as a reduction in the cost of the investments in the accompanying Condensed Consolidated Balance Sheets and a reduction of interest and other income in the accompanying Condensed Consolidated Statements of Income and Comprehensive Income. The cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. The amortization of premiums, accretion of discounts and realized gains and losses are included in interest and other income.

Merchandise inventories are stated at the lower of cost (first-in, first-out method) or market as determined by the retail inventory method.

On May 24, 2007, the Board of Directors increased the quarterly dividend by 10% from \$.15 per share to \$.165 per share, or an annualized rate of \$.66 per share.

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 5, 2007 AND APRIL 29, 2006

NOTE 2 — EARNINGS PER SHARE:

Basic EPS is computed as net income divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock options and other convertible securities. Unvested restricted stock is included in the computation of diluted EPS using the treasury stock method.

	Three Months Ended	
	May 5, 2007	April 29, 2006
Weighted-average shares outstanding	31,352,592	31,084,206
Dilutive effect of :		
Stock options	501,653	586,610
Restricted stock	43,431	143,377
Weighted-average shares and common stock equivalents outstanding	<u>31,897,676</u>	<u>31,814,193</u>

NOTE 3 — SUPPLEMENTAL CASH FLOW INFORMATION:

Income tax payments, net of refunds received, for the three months ended May 5, 2007 and April 29, 2006 were \$140,000 and \$277,000, respectively.

NOTE 4 — FINANCING ARRANGEMENTS:

At May 5, 2007, the Company had an unsecured revolving credit agreement, which provided for borrowings of up to \$35 million. The revolving credit agreement is committed until August 2008. The credit agreement contains various financial covenants and limitations, including the maintenance of specific financial ratios with which the Company was in compliance as of May 5, 2007. There were no borrowings outstanding under these credit facilities during the first three months ended May 5, 2007 or April 29, 2006, or the fiscal year ended February 3, 2007. Interest on any borrowings is based on LIBOR which was 5.32% at May 5, 2007.

At May 5, 2007 and April 29, 2006 the Company had approximately \$4,501,000 and \$2,236,000, respectively, of outstanding irrevocable letters of credit relating to purchase commitments.

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 5, 2007 AND APRIL 29, 2006

NOTE 5 — REPORTABLE SEGMENT INFORMATION:

The Company has two reportable segments: retail and credit. The Company operated its women's fashion specialty retail stores in 31 states at May 5, 2007, principally in the southeastern United States. The Company offers its own credit card to its customers and all related credit authorizations, payment processing, and collection efforts are performed by a separate subsidiary of the Company.

The following schedule summarizes certain segment information (in thousands):

Three Months Ended May 5, 2007	Retail	Credit	Total
Revenues	\$224,630	\$ 2,598	\$227,228
Depreciation	5,367	24	5,391
Interest and other income	(1,893)	—	(1,893)
Income before taxes	28,018	1,154	29,172
Total assets	395,385	66,152	461,537
Capital expenditures	3,917	13	3,930

Three Months Ended April 29, 2006	Retail	Credit	Total
Revenues	\$230,370	\$ 2,690	\$233,060
Depreciation	5,148	20	5,168
Interest and other income	(1,552)	—	(1,552)
Income before taxes	31,977	777	32,754
Total assets	357,683	68,018	425,701
Capital expenditures	12,748	17	12,765

The Company evaluates performance based on income before taxes. The Company does not allocate certain corporate expenses or income taxes to the credit segment.

The following schedule summarizes the direct expenses of the credit segment which are reflected in selling, general and administrative expenses (in thousands):

	Three Months Ended	
	May 5, 2007	April 29, 2006
Bad debt expense	\$ 458	\$ 981
Payroll	242	252
Postage	278	296
Other expenses	442	364
Total expenses	\$ 1,420	\$ 1,893

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 5, 2007 AND APRIL 29, 2006

NOTE 6 — STOCK BASED COMPENSATION:

Effective January 29, 2006, the Company began recording compensation expense associated with stock options and other forms of equity compensation in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 123R, *Share-Based Payment*, as interpreted by SEC Staff Accounting Bulletin No. 107. Prior to January 29, 2006, the Company had accounted for stock options according to the provisions of Accounting Principles Board (“APB”) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations, and therefore no related compensation expense was recorded for awards granted with no intrinsic value at the date of the grant. The Company adopted the modified prospective transition method provided under SFAS No. 123R, and, consequently, has not adjusted results from prior periods to retroactively reflect compensation expense. Under this transition method, compensation cost associated with stock options recognized in fiscal 2006 and 2007 includes quarterly amortization related to the remaining unvested portion of all stock option awards granted prior to January 29, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123.

As of May 5, 2007, the Company had three long-term compensation plans pursuant to which stock-based compensation was outstanding or could be granted. The Company’s 1987 Non-Qualified Stock Option Plan authorized 5,850,000 shares for the granting of options to officers and key employees. The 1999 Incentive Compensation Plan and 2004 Incentive Compensation Plan authorized 1,000,000 and 1,350,000 shares, respectively, for the granting of various forms of equity-based awards, including restricted stock and stock options to officers and key employees. The 1999 Plan has expired as to the ability to grant new awards.

The following table presents the number of options and shares of restricted stock initially authorized and available for grant under each of the plans:

	1987 Plan	1999 Plan	2004 Plan	Total
Options and/or restricted stock initially authorized	5,850,000	1,000,000	1,350,000	8,200,000
Options and/or restricted stock available for grant:				
February 3, 2007	9,277	—	1,091,618	1,100,895
May 5, 2007	9,277	—	992,393	1,001,670

Stock option awards outstanding under the Company’s current plans were granted at exercise prices which were equal to the market value of the Company’s stock on the date of grant, vest over five years and expire no later than ten years after the grant date.

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 5, 2007 AND APRIL 29, 2006

NOTE 6 — STOCK BASED COMPENSATION (CONTINUED):

The following is a summary of the changes in stock options outstanding during the three months ended May 5, 2007:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (a)
Options outstanding at February 3, 2007	1,236,675	\$8.01	1.86 years	\$18,363,084
Granted	—	—	—	—
Forfeited or expired	(15,675)			
Exercised	(300)			
Outstanding at May 5, 2007	1,220,700	\$7.96	1.57 years	\$17,724,034
Vested and exercisable at May 5, 2007	1,157,900	\$7.59	1.26 years	\$17,243,726

(a) The intrinsic value of a stock option is the amount by which the market value of the underlying stock exceeds the exercise price of the option.

No options were granted in fiscal 2006 or the first quarter of fiscal 2007.

As of May 5, 2007, there was approximately \$262,000 of total unrecognized compensation cost related to nonvested options, which is expected to be recognized over a remaining weighted-average vesting period of 2.18 years. The total intrinsic value of options exercised during the first quarter ended May 5, 2007 was approximately \$172,000.

Effective with the adoption of FAS 123R, the Company began recognizing share-based compensation expense ratably over the vesting period, net of estimated forfeitures. The Company recognized share-based compensation expense of \$375,000 and \$244,000 for the first quarter ended May 5, 2007 and April 29, 2006, respectively, which was classified as a component of selling, general and administrative expenses.

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 5, 2007 AND APRIL 29, 2006

NOTE 6 — STOCK BASED COMPENSATION (CONTINUED):

Prior to the adoption of SFAS No. 123R, the Company presented all benefits of tax deductions resulting from the exercise of share-based compensation as operating cash flows in the Statements of Cash Flows. SFAS No. 123R requires the benefits of tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. For the three months ended May 5, 2007 and April 29, 2006, the Company reported \$62,000 and \$80,000 of excess tax benefits as a financing cash inflow in addition to \$404,000 and \$405,000 in cash proceeds received from the exercise of stock options and Employee Stock Purchase Plan purchases, respectively.

The Company's Employee Stock Purchase Plan allows eligible full-time employees to purchase a limited number of shares of the Company's Class A Common Stock during each semi-annual offering period at a 15% discount through payroll deductions. During the three months ended May 5, 2007 and April 29, 2006, the Company sold 11,403 shares and 11,075 shares to employees at an average discount of \$3.31 and \$3.01 per share, respectively under the Employee Stock Purchase Plan. The compensation expense recognized for the 15% discount given under the Employee Stock Purchase Plan was approximately \$38,000 and \$33,000 for the three months ended May 5, 2007 and April 29, 2006, respectively.

In accordance with SFAS No. 123R, the fair value of current restricted stock awards is estimated on the date of grant based on the market price of the Company's stock and is amortized to compensation expense on a straight-line basis over the related vesting periods net of estimated forfeitures. As of May 5, 2007 and April 29, 2006, there was \$6,234,123 and \$57,000 of total unrecognized compensation cost related to nonvested restricted stock awards, which is expected to be recognized over a remaining weighted-average vesting period of 4.3 years and 0.1 years, respectively. The total fair value of the shares recognized as compensation expense during the first quarter ended May 5, 2007 and April 29, 2006 was \$302,000 and \$171,000, respectively.

The following summary shows the changes in the shares of restricted stock outstanding during the three months ended May 5, 2007:

	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Vested and exercisable at February 3, 2007	214,882	\$ 22.92
Granted	99,885	21.87
Vested	—	N/A
Forfeited or expired	(660)	22.89
Outstanding at May 5, 2007	314,107	\$ 22.59

THE CATO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE MONTHS ENDED MAY 5, 2007 AND APRIL 29, 2006

NOTE 7 — INCOME TAXES:

In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes — an Interpretation of FASB Statement No. 109." This Interpretation prescribes the recognition threshold a tax position is required to meet before being recognized in the financial statements. The Interpretation also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods and disclosure of uncertain tax positions. The Interpretation is effective for fiscal years beginning after December 15, 2006. The Company adopted Financial Accounting Standards Board Interpretation No. 48, "Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109," on February 4, 2007. As a result of the implementation of FASB Interpretation No. 48, the Company recognized a transition adjustment increasing beginning retained earnings by \$362,000. At May 5, 2007, we had \$6,600,000 of unrecognized tax benefits, \$4,500,000 of which would affect the effective tax rate if recognized. The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. As of May 5, 2007, we had approximately \$4,000,000 of accrued interest and penalties related to uncertain tax positions. The tax years after 2003 remain open to examination by the major taxing jurisdictions to which the Company is subject.

NOTE 8 — RECENT ACCOUNTING PRONOUNCEMENTS:

In September 2006, FASB issued SFAS 157, "Fair Value Measurements." SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements and, accordingly does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is in the process of evaluating the impact that the adoption of SFAS 157 will have on its financial statements.

THE CATO CORPORATION

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS**

FORWARD LOOKING INFORMATION:

The following information should be read along with the Unaudited Condensed Consolidated Financial Statements, including the accompanying Notes appearing in this report. Any of the following are "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended: (1) statements in this Form 10-Q that reflect projections or expectations of our future financial or economic performance; (2) statements that are not historical information; (3) statements of our beliefs, intentions, plans and objectives for future operations, including those contained in "Management's Discussion and Analysis of Financial Condition and Results of Operations"; (4) statements relating to our operations or activities for fiscal 2007 and beyond, including, but not limited to, statements regarding expected amounts of capital expenditures and store openings, relocations, remodelings and closures; and (5) statements relating to our future contingencies. When possible, we have attempted to identify forward-looking statements by using words such as "expects," "anticipates," "approximates," "believes," "estimates," "hopes," "intends," "may," "plans," "should" and variations of such words and similar expressions. We can give no assurance that actual results or events will not differ materially from those expressed or implied in any such forward-looking statements. Forward-looking statements included in this report are based on information available to us as of the filing date of this report, but subject to known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from those contemplated by the forward-looking statements. Such factors include, but are not limited to, the following: general economic conditions; competitive factors and pricing pressures; our ability to predict fashion trends; consumer apparel buying patterns; adverse weather conditions; inventory risks due to shifts in market demand; and other factors discussed under "Risk Factors" in Part I, Item 1A of our annual report on Form 10-K for the fiscal year ended February 3, 2007 (fiscal 2006), as amended or supplemented, and in other reports we file with or furnish to the SEC from time to time. We do not undertake, and expressly decline, any obligation to update any such forward-looking information contained in this report, whether as a result of new information, future events, or otherwise.

As used herein, the terms "we," "our," "us" (or similar terms), the "Company" or "Cato" include The Cato Corporation and its subsidiaries, except that when used with reference to common stock or other securities described herein and in describing the positions held by management of the Company, such terms include only The Cato Corporation. Our website is located at www.catocorp.com. We make available free of charge, through our website, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and other reports (including amendments to these reports) filed or furnished pursuant to Section 13(a) or 15(d) under the Securities Exchange Act of 1934. These reports are available as soon as reasonably practicable after we electronically file those materials with the SEC. We also post on our website the charters of our Audit, Compensation and Corporate Governance and Nominating Committees; our Corporate Governance Guidelines, Code of Business Conduct and Ethics; and any amendments or waivers thereto; and any other corporate governance materials contemplated by SEC or New York Stock Exchange regulations. The documents are also available in print to any shareholder who requests by contacting our corporate secretary at our Company offices at 8100 Denmark Road, Charlotte, North Carolina 28273-5975.

**THE CATO CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS (CONTINUED)**

CRITICAL ACCOUNTING POLICIES:

The Company's accounting policies are more fully described in Note 1 to the Consolidated Financial Statements. As disclosed in Note 1 of Notes to Consolidated Financial Statements, the preparation of the Company's financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions about future events that affect the amounts reported in the financial statements and accompanying notes. Future events and their effects cannot be determined with absolute certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements. The most significant accounting estimates inherent in the preparation of the Company's financial statements include the allowance for doubtful accounts receivable, reserves relating to workers' compensation, general and auto insurance liabilities, reserves for inventory markdowns, calculation of asset impairment, shrinkage accrual and reserves for uncertain tax positions.

The Company's critical accounting policies and estimates are discussed with the Audit Committee.

RESULTS OF OPERATIONS:

The following table sets forth, for the periods indicated, certain items in the Company's unaudited Condensed Consolidated Statements of Income and Comprehensive Income as a percentage of total retail sales:

	Three Months Ended	
	May 5, 2007	April 29, 2006
Total retail sales	100.0%	100.0%
Total revenues	101.4	101.5
Cost of goods sold	64.0	61.8
Selling, general and administrative	22.8	23.8
Depreciation	2.4	2.3
Interest and other income	(0.8)	(0.7)
Income before income taxes	13.0	14.3
Net income	8.3	9.1

**THE CATO CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS (CONTINUED)**

RESULTS OF OPERATIONS — (CONTINUED):

Comparison of First Quarter of 2007 with 2006.

Total retail sales for the first quarter were \$224.1 million compared to last year's first quarter sales of \$229.7 million, a 2% decrease. Same-store sales declined 5% in the first quarter of fiscal 2007 compared to the first quarter of fiscal 2006. Total revenues, comprised of retail sales and other income (principally, finance charges and late fees on customer accounts receivable and layaway fees), were \$227.2 million for the first quarter ended May 5, 2007 compared to \$233.1 million for the first quarter ended April 29, 2006. The Company operated 1,286 stores at May 5, 2007 compared to 1,252 stores at the end of last year's first quarter. In the first quarter of fiscal 2007, the Company opened 10 stores and relocated 6 stores. The Company plans to open approximately 80 stores and close approximately 10 stores during fiscal 2007.

Credit revenue of \$2.6 million represented 1.1% of total revenues in the first quarter of fiscal 2007, compared to 2006 credit revenue of \$2.7 million or 1.2% of total revenues. The reduction in credit revenue was due to lower finance charge and late fee income from lower sales under the Company's proprietary credit card and improved collections compared to the prior year. Credit revenue is comprised of interest earned on the Company's private label credit card portfolio and related fee income. Related expenses include principally bad debt expense, payroll, postage and other administrative expenses and totaled \$1.4 million in the first quarter of 2007 compared to last year's first quarter expenses of \$1.9 million. The decrease in costs was principally due to lower bad debt expense.

Other income in total, as included in total revenues was \$3.1 million for the first quarter of fiscal 2007, compared to \$3.3 million for the prior year's comparable first quarter. The decrease resulted primarily from lower finance charges and late fee income.

Cost of goods sold was \$143.4 million, or 64.0% of retail sales for the first quarter of fiscal 2007, compared to \$142.1 million, or 61.8% of retail sales in the first quarter of fiscal 2006. The overall increase in cost of goods sold as a percent of retail sales for the first quarter of fiscal 2007 resulted primarily from higher markdowns and occupancy costs, partially offset by lower procurement costs. The reduction in procurement cost was primarily the result of increased direct sourcing. The increase in markdowns was primarily attributable to lower sell-throughs of regular priced merchandise. Cost of goods sold includes merchandise costs, net of discounts and allowances, buying costs, distribution costs, occupancy costs, freight and inventory shrinkage. Net merchandise costs and in-bound freight are capitalized as inventory costs. Buying and distribution costs include payroll, payroll-related costs and operating expenses for the buying departments and distribution center. Occupancy expenses include rent, real estate taxes, insurance, common area maintenance, utilities and maintenance for stores and distribution facilities. Total gross margin dollars (retail sales less cost of goods sold)

**THE CATO CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS (CONTINUED)**

RESULTS OF OPERATIONS — (CONTINUED):

decreased by 7.9% to \$80.7 million for the first quarter of fiscal 2007 compared to \$87.6 million in the first quarter of fiscal 2006. Gross margin as presented may not be comparable to those of other entities.

Selling, general and administrative expenses ("SG&A") primarily include corporate and store payroll, related payroll taxes and benefits, insurance, supplies, advertising, bank and credit card processing fees and bad debts. SG&A expenses were \$51.1 million, or 22.8% of retail sales for the first quarter of fiscal 2007, compared to \$54.6 million, or 23.8% of retail sales in the first quarter of fiscal 2006. SG&A expenses as a percentage of retail sales decreased 100 basis points for the first quarter of fiscal 2007 as compared to the prior year. The decline in SG&A expenses as a percentage of retail sales for the first quarter of fiscal 2007 was primarily attributable to a decrease in incentive based compensation expenses. The overall dollar decrease in SG&A expenses for the first quarter of fiscal 2007 resulted primarily from decreased incentive based compensation expenses, legal fees and bad debts.

Depreciation expense was \$5.4 million, or 2.4% of retail sales for the first quarter of fiscal 2007, compared to \$5.2 million, or 2.3% of retail sales in the first quarter of fiscal 2006.

Interest and other income was \$1.9 million, or 0.8% of retail sales for the first quarter of fiscal 2007, compared to \$1.6 million, or 0.7% of retail sales for the first quarter of fiscal 2006. The increase in the first quarter of fiscal 2007 resulted primarily from higher interest rates and higher balances.

Income tax expense was \$10.5 million or 4.7% of retail sales for the first quarter of fiscal 2007, compared to \$12.0 million, or 5.2% of retail sales for the first quarter of fiscal 2006. The first quarter decrease resulted from lower pre-tax income and a lower effective tax rate. The effective income tax rate for the first quarter of fiscal 2007 was 36.0% compared to 36.5% for the first quarter of fiscal 2006.

LIQUIDITY, CAPITAL RESOURCES AND MARKET RISK:

The Company has consistently maintained a strong liquidity position. Cash provided by operating activities during the first three months of fiscal 2007 was \$38.6 million as compared to \$28.8 million in the first three months of fiscal 2006. These amounts enable the Company to fund its regular operating needs, capital expenditure program, cash dividend payments and purchase of treasury stock. In addition, the Company maintains \$35 million of unsecured revolving credit facilities for short-term financing of seasonal cash needs. There were no outstanding borrowings on these facilities at May 5, 2007.

**THE CATO CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS (CONTINUED)**

LIQUIDITY, CAPITAL RESOURCES AND MARKET RISK (CONTINUED):

Cash provided by operating activities for the first three months of fiscal 2007 was primarily generated by earnings adjusted for depreciation and changes in working capital. The increase of \$9.8 million for the first three months of fiscal 2007 as compared to the first three months of fiscal 2006 was primarily due to an increase in accounts payables in fiscal 2007 compared to a reduction in accounts payable in fiscal 2006, offset by lower net income and a smaller increase in accrued income taxes in fiscal 2007.

The Company believes that its cash, cash equivalents and short-term investments, together with cash flows from operations and borrowings available under its revolving credit agreement, will be adequate to fund the Company's planned capital expenditures, dividends, purchase of treasury stock and other operating requirements for fiscal 2007 and for the foreseeable future.

At May 5, 2007, the Company had working capital of \$192.9 million compared to \$147.9 million at April 29, 2006. Additionally, the Company had \$1.9 million invested in privately managed investment funds at May 5, 2007, which are included in other assets on the Condensed Consolidated Balance Sheets.

At May 5, 2007, the Company had an unsecured revolving credit agreement, which provides for borrowings of up to \$35 million. The revolving credit agreement is committed until August 2008. The credit agreement contains various financial covenants and limitations, including the maintenance of specific financial ratios with which the Company was in compliance as of May 5, 2007. There were no borrowings outstanding under these credit facilities during the first quarter ended May 5, 2007 or the fiscal year ended February 3, 2007.

At May 5, 2007 and April 29, 2006, the Company had approximately \$4.5 million and \$2.2 million, respectively, of outstanding irrevocable letters of credit relating to purchase commitments.

Expenditures for property and equipment totaled \$3.9 million in the first quarter of fiscal 2007, compared to \$12.8 million in last year's first fiscal quarter. The expenditures for the first three months of 2007 were primarily for the development of 10 new stores, relocating 6 stores, and additional investments in new technology. In fiscal 2007, the Company is planning to invest approximately \$24.0 to \$27.0 million for capital expenditures. This includes expenditures to open 80 new stores, relocate 20 stores and remodel 15 stores.

Net cash used in investing activities totaled \$37.6 million in the first quarter of fiscal 2007 compared to \$22.5 million used for the comparable period of 2006. The increase was due primarily to the net increase in purchases over sales of short-term investments.

On May 24, 2007, the Board of Directors increased the quarterly dividend by 10% from \$.15 per share to \$.165 per share, or an annualized rate of \$.66 per share.

**THE CATO CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS (CONTINUED)**

LIQUIDITY, CAPITAL RESOURCES AND MARKET RISK (CONTINUED):

The Company does not use derivative financial instruments. At May 5, 2007, the Company's investment portfolio was primarily invested in governmental and other debt securities with maturities less than 36 months. These securities are classified as available-for-sale and are recorded on the balance sheet at fair value, with unrealized gains and temporary losses reported net of taxes as accumulated other comprehensive income. Other than temporary declines in fair value of investments are recorded as a reduction in the cost of investments in the accompanying Condensed Consolidated Balance Sheets.

THE CATO CORPORATION
QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK:

The Company is subject to market rate risk from exposure to changes in interest rates based on its financing, investing and cash management activities, but the Company does not believe such exposure is material.

ITEM 4. CONTROLS AND PROCEDURES:

We carried out an evaluation, with the participation of our principal executive officer and principal financial officer, of the effectiveness of our disclosure controls and procedures as of May 5, 2007. Based on this evaluation, our principal executive officer and principal financial officer concluded that, as of May 5, 2007, our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act"), were effective to ensure that information we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING:

No change in the Company's internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) has occurred during the Company's fiscal quarter ended May 5, 2007 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

THE CATO CORPORATION

ITEM 1. LEGAL PROCEEDINGS

Not Applicable

ITEM 1A. RISK FACTORS

In addition to the other information in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for our fiscal year ended February 3, 2007. These risks could materially affect our business, financial condition or future results; however, they are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also materially adversely affect our business, financial condition or results of operations.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not Applicable

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not Applicable

ITEM 5. OTHER INFORMATION

Not Applicable

ITEM 6. EXHIBITS

<u>Exhibit No.</u>	<u>Item</u>
10.1	Separation and Confidentiality Agreement and General Release, between the Registrant and Reynolds C. Faulkner, dated April 18, 2007.
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer.
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer.
32.1	Section 1350 Certification of Chief Executive Officer.
32.2	Section 1350 Certification of Chief Financial Officer.

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PART II OTHER INFORMATION

THE CATO CORPORATION

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.

THE CATO CORPORATION

June 13, 2007

Date

/s/ John P. D. Cato

John P. D. Cato
Chairman, President and
Chief Executive Officer

June 13, 2007

Date

/s/ Thomas W. Stoltz

Thomas W. Stoltz
Executive Vice President
Chief Financial Officer

June 13, 2007

Date

/s/ John R. Howe

John R. Howe
Senior Vice President
Controller

SEPARATION AND CONFIDENTIALITY AGREEMENT AND GENERAL RELEASE

THIS SEPARATION AND CONFIDENTIALITY AGREEMENT AND GENERAL RELEASE ("Agreement"), dated April 18, 2007, is made between The Cato Corporation ("Cato") and Reynolds C. Faulkner, his heirs, executors, administrators, successors, and assigns ("Faulkner"). (Cato and Faulkner are referred to as "Parties"). This Agreement shall be effective on the date Faulkner and Cato sign, subject to the revocation rights set forth below.

WHEREAS, Faulkner previously was employed by Cato as its Executive Vice-President and Chief Financial Officer under a letter agreement dated March 6, 2006 ("Employment Agreement");

WHEREAS, upon being told by Cato that he would be terminated without cause and given the option to do so, Faulkner resigned rather than be terminated without cause, with such resignation effective October 30, 2006;

WHEREAS, the Parties wish to settle and resolve all possible controversies between them amicably and expeditiously;

NOW THEREFORE, in consideration of the mutual promises set forth herein and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged by Faulkner, the Parties agree as follows:

1. **Last Day of Employment.** Faulkner's last day of active employment with Cato was October 30, 2006. Faulkner is not eligible to participate in Cato's 401(k) Retirement and Savings Plan or any other Cato-sponsored employee benefit plan after October 30, 2006, except as set forth below.

2. **Consideration.** In consideration for signing this Agreement, Cato will do the following:

- (a) Pay to Faulkner on the next business day after the Revocation Period described in Paragraph 15, in a lump sum, \$750,000, less (i) \$29,196.12 already paid in November 2006, or \$720,803.88, and (ii) less \$3,357.86 as described in Section 2(b) below. Of the \$720,803.88 lump sum amount, \$583,303.88 shall be deemed to be compensation in settlement of any wage, bonus, stock, severance, or employment claims and will be subject to withholding for Federal and North Carolina income tax purposes and for which Faulkner will be issued a Form W-2 for the year 2007 at the time provided for under existing governmental regulations. For the balance of the lump sum amount, or \$137,500 paid in settlement of other claims, including in tort or any other basis, that Faulkner releases herein, Faulkner will be issued a Form 1099 for the year 2007 with respect thereto at the time provided for under existing governmental regulations.
 - (b) Continue Faulkner's health insurance coverage (on the same basis and at the same level it is provided to current Cato associates) from October 31, 2006 through October 31, 2007 or until Faulkner becomes eligible for another employer's group
-

health insurance benefits, whichever occurs first. Faulkner's share of the health insurance premiums will be \$3,357.86. Faulkner agrees that this \$3,357.86 amount will be withheld by Cato from the \$720,803.88 lump sum payment above. From the \$3,357.86 amount, Cato will deduct any amounts needed to pay prior months of coverage, and going forward, Cato will deduct \$306.07 each month for Faulkner's share of the health insurance premiums. In the event Faulkner becomes eligible for another employer's group health insurance benefits before October 31, 2007, Faulkner will notify Cato and Cato will pay to Faulkner any amount of the \$3,357.86 that has not already been applied to Faulkner's monthly share of the health insurance premiums.

- (c) Faulkner may convert the existing group life insurance coverage to an individual plan upon request to Cato's Director of Benefits and Cato will provide the necessary paperwork and information upon Faulkner's request.
- (d) As of November 1, 2007, Faulkner will be eligible to continue group health and major medical coverage pursuant to the Consolidated Omnibus and Reform Act (COBRA), at the applicable COBRA rate for his coverage (excluding Life Insurance, Short Term Disability and Long Term Disability coverage), provided that Faulkner pays his monthly COBRA charges on or before the first day of each month of continuing coverage. Faulkner will be responsible for premium increases should any occur. Unless Faulkner informs Cato that he has become eligible for another employer's group health insurance benefits before October 31, 2007, Cato's Human Resources Department will send information to Faulkner for such continuation election prior to October 31, 2007.

3. **General Release of All Claims.** In consideration of the provisions of this Agreement running to Faulkner's benefit, Faulkner knowingly and voluntarily releases and forever discharges Cato, its affiliates, subsidiaries, divisions, predecessors, insurers, benefit plans, successors, and assigns as well as their current and former employees, attorneys, officers, directors, and agents thereof, both individually and in their official capacities (collectively, the "Cato Affiliates"), of and from any and all claims, known and unknown, asserted or unasserted, which Faulkner has or may have against Cato or the Cato Affiliates as of the effective date of this Agreement, including, but not limited to, any alleged violation of:

- Title VII of the Civil Rights Act of 1964;
- Sections 1981 through 1988 of Title 42 of the United States Code;
- The Employee Retirement Income Security Act of 1974 (except for any vested benefits under any tax qualified benefit plan);
- The Immigration Reform and Control Act;
- The Americans with Disabilities Act of 1990;
- The Age Discrimination in Employment Act of 1967;

- The Workers Adjustment and Retraining Notification Act;
- The Fair Credit Reporting Act;
- The Sarbanes-Oxley Act of 2002;
- All North Carolina statutes, laws, and regulations;
- Any other federal, state, or local law, rule, regulation, or ordinance;
- Any public policy, contract, tort, or common law; or
- Any basis for recovering costs, fees, or other expenses including attorneys' fees incurred in any such matters.

4. **Covenant Not to Sue.** Faulkner agrees that he will never institute a claim released above in Paragraph 3 against Cato or the Cato Affiliates. If Faulkner violates this agreement by suing Cato or any of the Cato Affiliates for any claims released herein, Faulkner agrees that he will pay all costs and expenses of defending any such suit incurred by Cato or any of the Cato Affiliates, including reasonable attorneys' fees.

5. **Affirmations.** Faulkner makes the following affirmations:

- (a) He has not filed, nor caused to be filed, nor is he presently a party to, any claim against Cato or any Cato Affiliate that (i) is not being released by this instrument, and (ii) if filed, has not been withdrawn or dismissed.
- (b) He has been paid for and/or has received all leaves (paid or unpaid), compensation, wages, bonuses, stock awards, commissions, and/or benefits to which he may be entitled other than those provided to be paid under the terms of this Agreement.
- (c) He has no known workplace injuries or occupational diseases.
- (d) He will not apply in the future for employment, or accept employment, with Cato or any of its subsidiaries.

6. **Confidentiality and Return of Property.** (a) Faulkner agrees not to disclose any information regarding the existence or substance of this Agreement, except to his immediate family, tax and financial advisor, and/or an attorney with whom Faulkner chooses to consult regarding his consideration of this Agreement. Furthermore, to the extent Faulkner is permitted to disclose and does disclose such information, Faulkner agrees to require, and he warrants, that the person receiving such information will maintain its confidentiality. Faulkner warrants and represents that from March 2, 2007 through his execution of this Agreement, he has not breached the confidentiality provisions of this Agreement.

- (b) Faulkner acknowledges the highly competitive nature of Cato's business and affirms that he has not divulged, and will not divulge, to anyone outside of Cato

any proprietary or confidential information of Cato. "Confidential Information" means any information (i) which is, or is designed to be or may be used in Cato's business, (ii) which is private or confidential in that it is not generally known or available to the public, and (iii) which gives or may give Cato an opportunity to obtain an advantage over competitors or possible competitors, or which, if obtained by a competitor or possible competitor, would give or may give that competitor or possible competitor an advantage over Cato that a competitor may not otherwise have. Faulkner further acknowledges and affirms that he has not divulged, and will not divulge, to anyone outside of Cato any non-public information about Cato's company performance, future plans, or performance of Cato Affiliates, whether "Confidential Information" or not, that Faulkner learned in the course of and because of his employment with Cato. Faulkner also acknowledges that he will not divulge to anyone outside of Cato any non-public information about Cato's internal business practices, whether "Confidential Information" or not, that Faulkner learned in the course of and because of his employment with Cato. Provided, however, that Faulkner shall be entitled, subject to Paragraph 7 below, to respond to questions by a prospective employer with respect to his business relationship as Chief Financial Officer with John Cato as Chief Executive Officer that led to Faulkner's resignation from the company.

- (c) At Cato's reasonable advance request, and at mutually convenient times, Faulkner will make himself available to answer factual questions or provide factual information on subjects related to business matters of Cato of which he has knowledge arising from his former employment with Cato. In any legal proceeding to which he is not a party, his sworn testimony, including testimony in discovery, shall, however, be procured by subpoena.
- (d) The Parties agree that nothing in this Paragraph is intended to limit or prohibit, or shall be construed as limiting or prohibiting, either Party from providing information in response to a lawfully issued subpoena or otherwise complying with any legal requirement, or from participating in any investigation if requested to do so by a federal, state or local agency. The Parties further agree that the existence and substance of this Agreement may be disclosed in order to enforce its terms.
- (e) Faulkner affirms that he has returned all of Cato's property, documents, and/or any confidential information in whatever form, and any duplicates thereof, in his possession or control. Faulkner also affirms that he is in possession of all of his property and that Cato is not in possession of any of his property.

7. **Non-Disparagement.** Faulkner and Cato agree that Faulkner and Cato's Senior Executives (President, Executive Vice Presidents, Senior Vice Presidents, and Assistant to the President) will refrain from making negative, disparaging, defamatory or slanderous comments, references, criticism or characterizations concerning Faulkner, Cato, or the Cato Affiliates, either verbally, in writing, or in any other manner, to any third party for any purpose whatsoever, unless a legal duty to do so is imposed. Faulkner further agrees not to make any other statement, written or oral (including but not limited to any media source or to any other party), that would

disrupt, impair or affect adversely the reputation, business interests, or profitability of Cato or any of the Cato Affiliates, unless a legal duty to do so is imposed.

8. **Neutral Reference.** In the event that any outside entities seek input from Cato for purposes of hiring Faulkner, Cato will provide a neutral reference limited to his dates of employment, position, and annual salary.

9. **No Solicitation.** Faulkner agrees that for a period of one year from the effective date of his resignation, he will not solicit any Cato employee to leave Cato's employment, initiate such a solicitation by a third party, allow himself to be listed as a reference by a Cato employee, or hire or recommend for hire by any entity by whom he is employed anyone employed by Cato.

10. **Governing Law and Interpretation.** This Agreement shall be governed and conformed in accordance with the laws of the State of North Carolina without regard to its conflict of laws provisions. In the event of a breach of any provision of this Agreement, either Party may institute an action specifically to enforce any term or terms of this Agreement and/or seek any damages for breach. Should any provision of this Agreement be declared illegal or unenforceable by any court of competent jurisdiction, and should such provision be unable to be modified to be enforceable, excluding the general release language, such provision shall immediately become null and void, leaving the remainder of this Agreement in full force and effect.

11. **No Wrongdoing.** The Parties agree that neither this Agreement nor the furnishing of the consideration for this Agreement shall be deemed or construed at any time for any purpose as an admission by Cato of wrongdoing or evidence of any liability or unlawful conduct of any kind.

12. **Amendment.** This Agreement may not be modified, altered, or changed except in writing and signed by both Parties.

13. **Notices.** Any delivery of funds or notices required under this Agreement shall be served upon the Parties via hand delivery, certified mail, or overnight priority mail through a commercial third-party carrier (such as UPS or FedEx) as follows:

Notices to Cato:	Robert C. Brummer Senior Vice President The Cato Corporation 8100 Denmark Road Charlotte, NC 28273
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Notices to Faulkner:	Reynolds C. Faulkner C/O E. Osborne Ayscue, Jr. Helms Mullis & Wicker 201 North Tryon Street Charlotte, North Carolina 28202
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14. **Entire Agreement.** This Agreement sets forth the entire agreement between the Parties and replaces any prior agreements or understandings between the Parties, including without limitation the Employment Agreement. Faulkner acknowledges that he has not relied on any representations, promises, or agreements of any kind made to him in connection with his decision to accept this Agreement, except for those set forth in this Agreement.

15. **ADEA Waiver and Acknowledgement.** Faulkner acknowledges that he knowingly and voluntarily waives any rights he has under the Age Discrimination in Employment Act ("ADEA"), 29 U.S.C. 621 et seq., except those that may arise under the ADEA after the date this Agreement is executed. Faulkner further acknowledges that the consideration he is receiving under this Agreement is in addition to anything of value to which Faulkner already is entitled. Faulkner acknowledges that he may, if desired, have a period of twenty-one (21) calendar days to consider this Agreement, including its reference to the ADEA contained here and in Paragraph 3 (the "Consideration Period"). In addition, Faulkner may revoke this Agreement within a period of seven (7) calendar days following its execution (the "Revocation Period"). If Faulkner does not revoke the Agreement and Release during the Revocation Period, it will become fully effective upon expiration of the Revocation Period. Faulkner acknowledges that he has been advised by Cato that he can and should consult with an attorney.

FAULKNER AND CATO FREELY AND KNOWINGLY, AND AFTER DUE CONSIDERATION, ENTER INTO THIS AGREEMENT INTENDING TO WAIVE, SETTLE AND RELEASE ALL CLAIMS THEY HAVE OR MIGHT HAVE AGAINST ONE ANOTHER.

The Parties knowingly and voluntarily sign this Agreement as of the date(s) set forth below:

REYNOLDS C. FAULKNER

**THE CATO CORPORATION, a
Delaware corporation**

By: /s/ Reynolds C. Faulkner
Reynolds C. Faulkner

By: /s/ Robert C. Brummer
Robert C. Brummer
Senior Vice President

Date: April 18, 2007

Date: April 18, 2007

**CHIEF EXECUTIVE OFFICER CERTIFICATION PURSUANT TO
SECURITIES EXCHANGE ACT OF 1934 RULE 13a-14(a)/15d-14(a), AS ADOPTED
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, John P. D. Cato, certify that:

1. I have reviewed this report on Form 10-Q of The Cato Corporation (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: June 13, 2007

/s/ John P. D. Cato

John P. D. Cato

Chairman, President and
Chief Executive Officer

**CHIEF FINANCIAL OFFICER CERTIFICATION PURSUANT TO
SECURITIES EXCHANGE ACT OF 1934 RULE 13a-14(a)/15d-14(a), AS ADOPTED
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Thomas W. Stoltz, certify that:

1. I have reviewed this report on Form 10-Q of The Cato Corporation (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: June 13, 2007

/s/ Thomas W. Stoltz

Thomas W. Stoltz
Executive Vice President
Chief Financial Officer

CERTIFICATION OF PERIODIC REPORT

I, John P. D. Cato, Chairman, President and Chief Executive Officer of The Cato Corporation, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that on the date of this Certification:

1. the Form 10-Q of the Company for the quarter ended May 5, 2007 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: June 13, 2007

/s/ John P. D. Cato

John P. D. Cato
Chairman, President and
Chief Executive Officer

CERTIFICATION OF PERIODIC REPORT

I, Thomas W. Stoltz, Executive Vice President, Chief Financial Officer of The Cato Corporation, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that on the date of this Certification:

1. the Form 10-Q of the Company for the quarter ended May 5, 2007 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: June 13, 2007

/s/ Thomas W. Stoltz

Thomas W. Stoltz
Executive Vice President
Chief Financial Officer