DOLLAR TREE

2006 ANNUAL REPORT

EXPANDING

THRILLING

EXCITING

STRIVING

PERFORMING

LEADING

EVOLVING

IMPROVING

SURPRISING

DELIVERING

COMPELLING

COMMITTED

INNOVATIVE

RESPONSIVE

CONVENIENT

EFFICIENT

FUN

FRESH

UNIQUE

VALUE

DOLLAR TREE

ABOUT THE COMPANY

Over twenty years ago, a unique concept was born as Dollar Tree opened its first store in Dalton, Georgia.

Today thanks to continued innovation and a dedicated vision, there are more than 3,200 locations throughout the contiguous United States.

All of our stores offer a compelling assortment of variety merchandise and basic consumable products to better serve our customers.

Shopping at Dollar Tree is fun, friendly, and exciting. Take a walk down our aisles and you will discover a clean and bright store full of private label and national brand products.

The things you want and need are all in one place, from affordable luxury bath items to dinnerware, stemware and toys, to our vast array of seasonal goods. From fresh flowers and candy at Valentine's Day to our "Build a Wreath" promotion, themed ornaments, holiday gift wrap and gift bags at Christmas, Dollar Tree is truly the store for all seasons.

Headquartered in Chesapeake, Virginia, with a nationwide logistics network, and more than 40,000 associates, there is plenty of runway ahead for Dollar Tree.

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3,219	48	$3.97
STORES	STATES	BILLION IN SALES

THRILLING

FINANCIAL HIGHLIGHTS

	2006[a]	2005	2004	2003[b]	2002
(in millions, except store and per share data)					
Net Sales	**$3,969.4**	$3,393.9	$3,126.0	$2,799.9	$2,329.2
Gross Profit	**1,357.2**	1,172.4	1,112.5	1,018.4	852.0
Operating Income	**310.8**	283.9	293.5	293.6	253.9
Net Income	**192.0**	173.9	180.3	177.6	154.6
Diluted Net Income Per Share	**1.85**	1.60	1.58	1.54	1.35
Working Capital	**$ 575.7**	$ 648.2	$ 675.5	$ 450.3	$ 509.6
Total Assets	**1,873.3**	1,798.4	1,792.7	1,501.5	1,116.4
Total Debt	**269.5**	269.9	281.7	185.1	54.4
Shareholders' Equity	**1,167.7**	1,172.3	1,164.2	1,014.5	855.4
Number of Stores Open	**3,219**	2,914	2,735	2,513	2,263
Total Selling Square Footage	**26.3**	23.0	20.4	16.9	13.0
Comparable Store Net Sales Increase/(Decrease)[c]	**4.6%**	(0.8%)	0.5%	2.9%	1.0%
Average Net Sales Per Store[c]	**$ 1.3**	$ 1.2	$ 1.2	$ 1.2	$ 1.1

(a) Fiscal 2006 includes 53 weeks, commensurate with the retail calendar, while all other fiscal years reported in the table contain 52 weeks.

(b) In January 2003, the Company changed its fiscal year from December 31 to the Saturday closest to January 31, effective for the year beginning February 2, 2003.

(c) Comparable store net sales compare net sales for stores open throughout each of the two periods being compared. Net sales per store are calculated for stores open throughout the entire period presented.

PERFORMING

Bob Sasser
President and
Chief Executive Officer

TO OUR SHAREHOLDERS

Last year, I ended my letter to you with the comment, "the best is yet to come." I am proud to report to you that 2006 lived up to those expectations. At Dollar Tree Stores, 2006 was a year of achieving new milestones and continued progress on our goals. We celebrated our 20th anniversary with a solid and consistent performance throughout the year. In true Dollar Tree fashion, we opened our 3,000th store and "blew" past that milestone ending the year with over 3,200 stores in our portfolio. Total revenues were just shy of $4 billion dollars, another milestone that we are sure to exceed in 2007. We leveraged our investments in new stores, retail technology and logistics by delivering increased merchandise excitement to our customers, with improved assortments, a higher in-stock position in basic products, and a more efficient flow of inventory. As a result, our comparable-store sales grew by 4.6%, and we achieved double-digit increases — and all-time record levels — in revenues, earnings per share and square footage. And yes, I believe "the best is still to come."

Dollar Tree is a unique and proven retail concept. We are a large company, national in scope and at each Dollar Tree store — Everything is $1! We have a long history of profitable growth, building a solid, scalable infrastructure and strong relationships along the way. This strong foundation, one that has been nurtured over the past 20 years, will provide leverage for continued profitable growth and will strengthen as we grow to an even higher scale. Our world-wide sourcing relationships, merchandising skills, logistics capabilities and retail technology, proven and improved over time, enable us to provide surprising value to our customers. We remain focused on our customers' needs and we believe that they want great value and a great shopping experience. That means we put a premium on running stores that are bright, clean and inviting. Our store associates are friendly and strive to thrill our customers every day by exceeding their expectations with products that represent surprising value. The more we deliver this "WOW factor," the more our customers will come back.

REVIEW OF 2006 GOALS AND ACCOMPLISHMENTS

Our primary goal for 2006, and indeed every year, is to grow the top line while delivering sector leading profitability. We accomplished this in 2006 through a combination of new store openings and improved productivity of existing stores. It's all about the stores and the merchandise; this is the key to the Dollar Tree extreme value proposition. A Dollar Tree store offers a wide assortment of variety merchandise at incredible values. Our merchandise strategy provides a mix of branded product, including well-known national brands, popular regional brands, exclusive Dollar Tree brands, and an ever-changing mix of exciting seasonal merchandise and high value closeouts. It is our prime goal to create merchandise excitement for our customers, every time they visit our store.

This year our merchants, working with our planning, allocations and replenishment department, did an outstanding job of planning assortments and giving the right amount of product to the stores as needed. Seasonal transitions were crisp.

New promotions, such as our "Build a Gift Basket" and "Build a Wreath" encouraged multiple purchases and exceeded our customers' expectations with high value for their $1 and a fun shopping experience.

We benefited from increased sales of basic products; items that people need everyday and are more frequently purchased. Our expanded product selection has been embraced by our customers who are making more frequent shopping trips to our stores. Improved replenishment methods are providing a better in-stock position on these products and we believe this has been a real driver of increases in both customer traffic and our average ticket.

Our initiative to expand frozen and refrigerated product to more stores continues to yield positive results. We added freezers and coolers to 392 stores in 2006, bringing our total to 632 stores at year-end, compared with 240 stores at the beginning of the year. The margins on this product are a bit lower than our average but this is a trade that we are willing to make. The fact is our customers love it! We are attracting more customers to our stores more frequently with this product and it is resulting in incremental sales. We are planning to roll freezers and coolers to an additional 250 stores in fiscal 2007.

We continue to refine our advertising, with increased emphasis on the holiday season. Using a combination of radio and television in target markets, and tabloid advertisements at key seasons we found a winning combination. The "Feature Item of the Week" program added energy and focus on key items. We believe we are honing in on the appropriate mix of advertising and promotion required to drive traffic and increased sales.

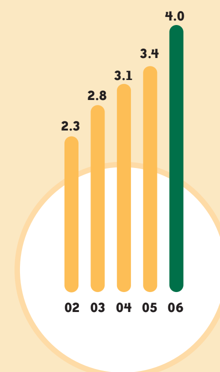
In 2005, we began to expand tender types for the added convenience of our customers. By the middle of 2006, we completed the rollout of debit card and Electronic Benefits Transfer acceptance to substantially all of our stores. This has provided a lift to our average ticket as well as traffic and will continue to do so in 2007 and beyond. In addition, with the rollout of frozen and refrigerated capability, at year end we were accepting Food Stamps in about 600 stores. Last, but with great promise, we launched a gift card program in the third quarter, just in time for the holidays.

We continue to grow our store base, and refine our real estate process. Our goal is to open stores earlier in the year, to maximize their productivity through improved site selection, improve the construction process and ultimately to increase our return on invested capital. In fiscal 2006 we opened 211 new stores, expanded and relocated 85 existing stores, and increased retail square footage 14%, including the Deal$ acquisition. Our new stores averaged 11,200 square feet, a size that is within our targeted range, and ideal from the customers' perspective, allowing them to see a full display of merchandise in an open and bright shopping environment, while keeping their shopping trip quick and convenient.

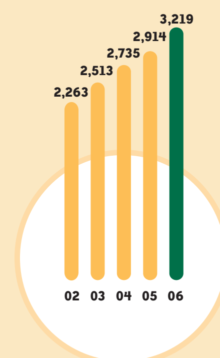
LEVERAGING OUR INFRASTRUCTURE

Significant investments in infrastructure over the past few years are contributing to improved performance. Our logistics network is highly automated, efficient and capable of delivering product to all 48 contiguous states and we have capacity to support growth to $5 billion without additional investment. Our technology infrastructure, and particularly our investment in point-of-sale applications, has given us the ability to improve our flow of product to stores, reduce back room inventory and improve operating efficiency. Our Automated Store Replenishment tool is improving our in stock of basics. Demand driven allocations of new product consistent with sales trends is driving store sales and our sell through of seasonal product is increasing. In combination, these investments enabled us to lower our inventory investment by 5% per store at fiscal 2006 year-end, following a 12% reduction in inventory per store in 2005. Inventory turns increased an amazing 50 basis points in 2006!

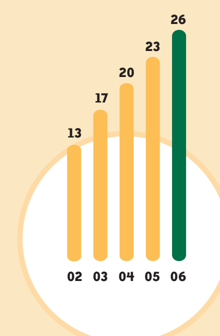
NET SALES
($ In Billions)



NUMBER OF STORES OPEN



TOTAL SELLING SQUARE FOOTAGE
(In Millions)



DEAL$

Last March, we acquired the Deal$ chain. Our intention is not to convert these stores to Dollar Trees but to use them as a platform to develop an additional format. Within six months we integrated the Deal$ stores into our back office processes and systems and in the fall, we lifted the restriction of the $1 price point and introduced a new store look and a high value, compelling general merchandise assortment. Our customers have responded favorably and we are encouraged by the results in terms of average ticket, store productivity and margin. This year we will begin to expand this concept with plans to open 25 new Deal$ stores. These new Deal$ stores will provide an additional opportunity to develop the sales potential and operating metrics of the new model.

CORPORATE GOVERNANCE

Dollar Tree is committed to responsible corporate governance. To strengthen that commitment, we continue to review best practices and respond with changes accordingly. We recently adopted a majority vote governance policy with respect to the election of directors who run unopposed, created an independent committee with responsibility for Corporate Governance, and established the position of Lead Independent Director on our Board. Most importantly we remain focused on our core values. We are very proud of our record and our history of honesty, integrity and transparency. We are uncompromising in these values and they will always be reflected in our strength of financial controls, our open and straight forward relationships with our customers, our suppliers, our associates and our shareholders.

We are committed to increasing total shareholder returns. As chronicled in this annual report, our stock has performed well over the past year, achieving an increase in share price of nearly 27%. In doing so, we outperformed the major indices with a larger increase than the S & P 500, the Dow Jones Industrial Average and the NASDAQ Composite. In addition to solid growth in revenue and earnings, in 2006 we returned over $248 million dollars to our shareholders in the form of share repurchase. We believe this to be a good use of cash and we will continue to examine strategies to build total shareholder returns.

THE FUTURE

As we enter our third decade, we can look back with pride at our accomplishments and look forward to even more exciting opportunities. We have grown from six stores in 1986 to more than 3,200 today, and we are positioned to expand to 5,000 – 7,000 stores over the long term. All of the tools are in place to achieve these goals while continuing to achieve sector leading profitability. At Dollar Tree, we have a concept that customers love, a rock-solid foundation on which to build, one that is proven and scalable, a solid, cash rich balance sheet and an experienced and focused management team. We believe the best is still to come!

Bob Sasser

Bob Sasser
President and Chief Executive Officer

FROM THE CFO

We firmly believe our responsibility, as a publicly-held company, is driving shareholder value through solid financial performance and prudent capital management, with an unwavering commitment to financial integrity. We also pride ourselves on having a sound framework of financial reporting controls allowing us to provide the public markets and our shareholders honest, transparent and complete financial information in a timely fashion. These values are the foundation on which our business was built, and to which we remain committed.

Kent Kleeberger
Chief Financial Officer

2006 FINANCIAL PERFORMANCE

We experienced improved financial performance in 2006. Sales increased 16.9% to a record $3.97 billion. Earnings per share grew 15.6% to $1.85. Our operating margin was 7.8%, among the highest of retailers in the value sector, but lower than previous years and less than we would like. Therefore, we are keenly focused on this opportunity for improvement.

We continue to generate significant Cash Flow through improved asset management. For example, our total inventory investment grew only 4.9% over last year, to $605 million, despite increasing our store base 10%. Thus, inventory per store declined by 5%, and inventory turns increased from 3.1 to 3.6. Further, our ratio of accounts payable to inventory at year-end increased to 31.3% from 23.5% at the end of 2005, representing nearly a $50 million positive impact on cash flow.

Cash and Investments at year-end totaled $307 million, a surprisingly high number after spending $54 million on the Deal$ acquisition and $248 million for share repurchases. In November 2006, the Board approved a new $500 million Share Repurchase Program, reflecting confidence in our ability to generate significant cash flow and our commitment to building shareholder value. We continued to repurchase shares under this authorization, facilitated by $250 million of Accelerated Buyback Programs starting in December 2006 and continuing through the first half of 2007. As of April 2007, we have $273 million available for repurchase against this authorization.

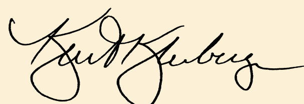
Also, we self-funded our $175 million capital expenditures in 2006. We are planning $170-$190 million for 2007 capital expenditures including expansions of our Briar Creek Distribution Center and home office in Chesapeake, Virginia. All of this will be funded from internally generated cash with significant free cash flow remaining after these investments.

For 2006, we once again earned a "clean bill of health" with no material weakness noted in our assessment of controls supporting the accounting and reporting processes, in compliance with the requirements of Sarbanes-Oxley legislation. You can be assured that, in 2007, we will continue to operate our Company with a strong commitment to financial integrity and the related internal controls while driving to a cost efficient infrastructure that delivers shareholder value.

2007 OUTLOOK

Looking ahead to the balance of 2007 and beyond, we are absolutely committed to improving our operating margins facilitated by gross margin improvement and lower expense rates, in addition to sales growth. We will also continue to build on our asset management performance and challenge ourselves for the appropriate capital structure to build value for our shareholders. Therefore, we believe 2007 will be another year of improved financial performance.

I look forward to serving you in 2007.



Kent Kleeberger
Chief Financial Officer

Dollar Tree features a great selection of variety products, including toys that delight children and their parents.

SURPRISING

Dollar Tree stores are full of energy and excitement and it all begins with the merchandise.

Our stores create merchandise excitement through a mix of private label and national brands along with the unexpected “Thrill of the Hunt” that has become a hallmark of our stores.

We offer a broad variety of more than 40 private label products that are marketed exclusively at Dollar Tree, including our sugar-free Icy Breeze® gum and mints and our Royal Norfolk® housewares line.

We offer a complete assortment of hand-painted genuine stoneware in great styles and colors, with coordinating linens. At a dollar price-point, they are perfect for students and families alike.

We expanded our signature line of Breck® shampoo products to include Breck for Kids and launched The Ana Grace Collection™, which features a complete line of social stationery and accessories. These are amazing values, available only at Dollar Tree!

COMPELLING

Leveraging our skills enables us to exceed customer expectations each and every day and provide a great assortment of merchandise like coordinating winter hats and gloves in fashion colors.

Our selection of brand name values continues to expand. We offer over 75 brand name values that our customers know and trust on a regular basis. Health and Beauty is a signature category for Dollar Tree and it is full of brands our customers expect like Crest® toothpaste and Alberto VO5® shampoo.

At Dollar Tree, it's best to shop NOW, and nowhere is that more evident than in our "WOW Zone." Customers continue to enjoy "The Thrill of the Hunt" in this landmark section. Promotions like our weekly "Featured Item" make this a frequently shopped area.

CONVENIENT

Dollar Tree is a variety retailer, providing a unique shopping experience with value that is second to none.

Our stores are clean, bright, and conveniently located where middle America lives and works.

At Dollar Tree, shopping is fast and fun! Our average store size is ideal from the customer's perspective. Shoppers can find an ever-changing assortment of extreme value merchandise each time they visit.

FUN
FRESH
UNIQUE

We continue to feature our flagship categories like Party, Seasonal, and Toys. This year we launched a great selection of coordinating wedding favors and accessories available only at Dollar Tree.

In our fast-paced society, time is valuable and convenience is a must. With more than 3,200 stores in 48 states, Dollar Tree provides a unique combination of convenience, extreme value and a fun, fresh, exciting shopping experience to customers throughout the contiguous United States.

Dollar Tree offers frozen and refrigerated products in over 630 stores. Shop for a dozen eggs or a quart of orange juice and check out quickly as Debit Cards and EBT are accepted chain-wide, and food stamps are accepted in over 600 locations. Gift cards are now available, so share the convenient Dollar Tree shopping experience with someone you know!

EVOLVING

COMMITTED

Dollar Tree is committed to providing value and never has this been more evident than in the past year.

In 2006, we celebrated the opening of our 3,000th store and neared the $4 billion sales threshold. We continue to make a little magic each day by proving that there is still value in a dollar.

Our stores are conveniently located and easy to shop. Our merchandise is an ever-evolving mix of variety and consumable products including toys, health and beauty aids, household supplies, candy, snacks, stationery, greeting cards, crafts, gift bags, electronic accessories, home decor, party supplies, books, DVDs, dinnerware, seasonal favorites and much, much more.

At Dollar Tree stores, customers can find the unexpected every day. Where else can you find items like our April Bath & Shower® bath products, or speciality consumable products like organic tomato sauce along with gourmet spices and staples like bread, jam or marmalade all for just a dollar? That's value. **That's Dollar Tree.**

VALUE

Dollar Tree acquired the Deal$ chain in March 2006, and began offering multi-price merchandise at 122 of these stores in the fall.

DOLLAR TREE LOGISTICS NETWORK

Distribution Center Square Footage

Ridgefield, Washington
(665,000 sq. ft.)

Stockton, California
(525,000 sq. ft.)

Salt Lake City, Utah
(252,000 sq. ft.)

Briar Creek, Pennsylvania
(603,000 sq. ft.)

Joliet, Illinois
(1,200,000 sq. ft.)

Chesapeake, Virginia
(400,000 sq. ft.)

Savannah, Georgia
(603,000 sq. ft.)

Olive Branch, Mississippi
(425,000 sq. ft.)

Marietta, Oklahoma
(603,000 sq. ft.)

Dollar Tree has the infrastructure to support continued profitable growth, as a result of investments made over the past several years. We have built a national network of stores supported by efficient logistics and solid, scalable technology across the country.

Our network of nine Distribution Centers allows us to open new stores and efficiently deliver product to stores anywhere in the contiguous United States. As the map below illustrates, each Distribution Center serves a dedicated area of the country. We have worked diligently toward this goal and are now able to leverage this capability.

This year, we are expanding our Distribution Center in Briar Creek, PA, to meet the growing demands in the Northeast.

Shading indicates service area for each Distribution Center.

DELIVERING

A WARNING ABOUT FORWARD-LOOKING STATEMENTS: This Annual Report contains "forward-looking statements" as that term is used in the Private Securities Litigation Reform Act of 1995. Forward-looking statements address future events, developments and results. They include statements preceded by, followed by or including words such as "believe," "anticipate," "expect," "intend," "plan," "view," "target" or "estimate." For example, our forward-looking statements include statements regarding:

- our anticipated sales, including comparable store net sales, net sales growth and earnings growth;
- our growth plans, including our plans to add, expand or relocate stores, our anticipated square footage increase, and our ability to renew leases at existing store locations;
- the average size of our stores to be added in 2007 and beyond;
- the effect of a slight shift in merchandise mix to consumables and the increase of freezers and coolers on gross profit margin and sales;
- the effect that expanding tender types accepted by our stores will have on sales;
- the net sales per square foot, net sales and operating income attributable to smaller and larger stores and store-level cash payback metrics;
- the possible effect of inflation and other economic changes on our costs and profitability, including the possible effect of future changes in minimum wage rates, shipping rates, domestic and foreign freight costs, fuel costs and wage and benefit costs;
- our cash needs, including our ability to fund our future capital expenditures and working capital requirements;
- our gross profit margin, earnings, inventory levels and ability to leverage selling, general and administrative and other fixed costs;
- our seasonal sales patterns including those relating to the length of the holiday selling seasons;
- the capabilities of our inventory supply chain technology and other new systems;
- the future reliability of, and cost associated with, our sources of supply, particularly imported goods such as those sourced from China;
- the capacity, performance and cost of our distribution centers, including opening and expansion schedules;
- our expectations regarding competition and growth in our retail sector;
- costs of pending and possible future legal claims;
- management's estimates associated with our critical accounting policies, including inventory valuation, accrued expenses, and income taxes;
- the possible effect on our financial results of changes in generally accepted accounting principles relating to accounting for income tax uncertainties.

You should assume that the information appearing in this annual report is accurate only as of the date it was issued. Our business, financial condition, results of operations and prospects may have changed since that date.

For a discussion of the risks, uncertainties and assumptions that could affect our future events, developments or results, you should carefully review the risk factors summarized below and the more detailed discussions in the "Risk Factors" and "Business" sections in our Annual Report on Form 10-K filed on April 4, 2007. Also see our "Management's Discussion and Analysis of Financial Condition and Results of Operations" which begins on the next page.

- Our profitability is especially vulnerable to cost increases.
- Our profitability is affected by the mix of products we sell.
- We may be unable to expand our square footage as profitably as planned.
- A downturn in economic conditions could adversely affect our sales.
- Our sales and profits rely on imported merchandise, which may increase in cost or become unavailable.
- We could encounter disruptions or additional costs in receiving and distributing merchandise.
- Sales below our expectations during peak seasons may cause our operating results to suffer materially.
- Pressure from competitors may reduce our sales and profits.

- The resolution of certain legal matters could have a material adverse effect on our results of operations, accrued liabilities and cash.
- Certain provisions in our articles of incorporation and bylaws could delay or discourage a takeover attempt that may be in a shareholder's best interest.

Our forward-looking statements could be wrong in light of these and other risks, uncertainties and assumptions. The future events, developments or results described in this report could turn out to be materially different. We have no obligation to publicly update or revise our forward-looking statements after the date of this annual report and you should not expect us to do so.

Investors should also be aware that while we do, from time to time, communicate with securities analysts and others, we do not, by policy, selectively disclose to them any material, nonpublic information or other confidential commercial information. Accordingly, shareholders should not assume that we agree with any statement or report issued by any securities analyst regardless of the content of the statement or report. We generally do not issue financial forecasts or projections and we do not, by policy, confirm those issued by others. Thus, to the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are not our responsibility.

INTRODUCTORY NOTE: *Unless otherwise stated, references to "we," "our" and "Dollar Tree" generally refer to Dollar Tree Stores, Inc. and its direct and indirect subsidiaries on a consolidated basis. Unless specifically indicated otherwise, any references to "2007" or "fiscal 2007", "2006" or "fiscal 2006," "2005" or "fiscal 2005," and "2004" or fiscal 2004," relate to as of or for the years ended February 2, 2008, February 3, 2007, January 28, 2006 and January 29, 2005, respectively.*

AVAILABLE INFORMATION

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act are available free of charge on our website at www.dollartree.com as soon as reasonably practicable after electronic filing of such reports with the SEC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In Management's Discussion and Analysis, we explain the general financial condition and the results of operations for our company, including:

- what factors affect our business;
- what our earnings, gross margins and costs were in 2006 and 2005;
- why those earnings, gross margins and costs were different from the year before;
- how all of this affects our overall financial condition;
- what our expenditures for capital projects were in 2006 and what we expect them to be in 2007; and
- where funds will come from to pay for future expenditures.

As you read Management's Discussion and Analysis, please refer to our consolidated financial statements, included in this Annual Report, which present the results of operations for the fiscal years ended February 3, 2007, January 28, 2006 and January 29, 2005. In Management's Discussion and Analysis, we analyze and explain the annual changes in some specific line items in the consolidated financial statements for the fiscal year 2006 compared to the comparable fiscal year 2005 and the fiscal year 2005 compared to the comparable fiscal year 2004.

Key Events and Recent Developments

Several key events have had or are expected to have a significant effect on our results of operations. You should keep in mind that:

- In November 2006, our Board of Directors authorized the repurchase of up to $500 million of our common stock. This amount was in addition to the $26.7 million remaining on the $300.0 million March 2005 authorization. As of

February 3, 2007, we had approximately $427.0 million remaining under this authorization.

- In March 2006, we completed our acquisition of 138 Deal$ stores and related assets. We paid approximately $32.0 million for store related assets and $22.1 million for inventory.
- On December 15, 2005, the Compensation Committee of our Board of Directors approved the acceleration of the vesting date of all previously issued, outstanding and unvested options under all current stock option plans, effective as of December 15, 2005. This decision eliminated non-cash compensation expense that would have been recorded in future periods following our adoption of Statement of Financial Accounting Standards No. 123, *Share-Based Payment (revised 2004)* (FAS 123R), on January 29, 2006. Compensation expense has been reduced by approximately $14.9 million over a period of four years during which the options would have vested, as a result of the option acceleration program.
- In 2004, we completed construction and began operations in two new distribution centers. In June 2004, we began operations in our new distribution center in Joliet, Illinois. The Joliet distribution center is a 1.2 million square foot, fully automated facility. In February 2004, we began operations in our Ridgefield, Washington distribution center. The Ridgefield distribution center is a 665,000 square foot facility that can be expanded to accommodate future growth needs. In 2007, we are planning to expand our Briar Creek distribution center by 400,000 square feet. Upon completion of this expansion, our nine distribution centers will support approximately $5.0 billion in sales annually.
- In March 2004, we entered into a five-year $450.0 million Unsecured Revolving Credit Facility (Facility). We used availability under this Facility to repay variable rate debt. This Facility also replaced our previous $150.0 million revolving credit facility.

Overview

Our net sales are derived from the sale of merchandise. Two major factors tend to affect our net sales trends. First is our success at opening new stores or adding new stores through acquisitions. Second, sales vary at our existing stores from one year to the next. We refer to this change as a change in comparable store net sales, because we compare only those stores that are open throughout both of the periods being compared. We include sales from stores expanded during the year in the calculation of comparable store net sales, which has the effect of increasing our comparable store net sales. The term ‘expanded’ also includes stores that are relocated.

At February 3, 2007, we operated 3,219 stores in 48 states, with 26.3 million selling square feet compared to 2,914 stores with 23.0 million selling square feet at January 28, 2006. During fiscal 2006, we opened 211 stores, expanded 85 stores and closed 44 stores, compared to 232 new stores opened, 93 stores expanded and 53 stores closed during fiscal 2005. In addition, we acquired 138 Deal$ stores on March 25, 2006. Including the Deal$ acquisition, we achieved the high end of our square footage growth target of 12%–14% for the fiscal year. In fiscal 2006, we increased our selling square footage by approximately 3.3 million square feet, or approximately 14%. Of the 3.3 million selling square foot increase in 2006, approximately 1.2 million resulted from the acquisition of the Deal$ stores and 0.4 million was added by expanding existing stores. The average size of our stores opened in 2006 was approximately 9,000 selling square feet (or about 11,000 gross square feet). The average new store size decreased in 2006 from approximately 10,000 selling square feet (or about 12,400 gross square feet) for new stores in 2005. For 2007, we continue to plan to open stores around 9,000 selling square feet (or about 11,000 gross square feet). We believe that the 11,000–12,500 gross square foot store size is our optimal size operationally and that this size also gives the customer an improved shopping environment that invites them to shop longer and buy more. We expect the substantial majority of our future net sales growth to come from the square footage growth resulting from new store openings and expansion of existing stores.

Fiscal 2006 ended on February 3, 2007 and included 53 weeks, commensurate with the retail calendar. The 53rd week in 2006 added approximately

$70 million in sales. Fiscal 2005 ended on January 28, 2006 and included 52 weeks.

In fiscal 2006, comparable store net sales increased by 4.6%. This increase was based on 53 weeks for both periods. The comparable store net sales increase was the result of increases of 1.9% in the number of transactions and 2.7% in transaction size, compared to fiscal 2005. We believe comparable store net sales were positively affected by the initiatives we began putting in place in 2005, including expansion of forms of payment accepted by our stores and the roll-out of freezers and coolers to more of our stores. During 2006, we completed the roll-out of debit card acceptance to all of our stores, which has enabled us to accept Electronic Benefit Transfer cards and we now accept food stamps in approximately 600 qualified stores. We believe the expansion of forms of payment accepted by our stores has helped increase the average transaction size in our stores.

In 2006, we continued to experience a slight shift in the mix of merchandise sold to more consumables, which we believe increases the traffic in our stores but have lower margin. The planned shift in mix to more consumables is the result of the roll-out of freezers and coolers to more stores in 2005 and 2006. At February 3, 2007, we had freezers and coolers in approximately 700 stores, compared to approximately 250 stores at January 28, 2006. We plan to add freezers and coolers to approximately 250 more stores in 2007, which we believe will continue to pressure margins, as a percentage of sales, in 2007. However, we believe that this will enable us to increase sales and earnings in the future by increasing the number of shopping trips made by our customers.

Our point-of-sale technology is now in all of our stores, and this technology provides us with valuable sales and inventory information to assist our buyers and improve our merchandise allocation to our stores. We believe that this has enabled us to better control our inventory, resulting in more efficient distribution and store operations and increased inventory turnover. Using the data captured at the point-of-sale has enabled us to better plan our inventory purchases and helped us reduce our inventory investment per store by approximately 5.0% at February 3, 2007 compared to January 28, 2006. In addition, inventory turnover has increased 70 basis points in 2006 as compared to 2005.

We must continue to control our merchandise costs, inventory levels and our general and administrative expenses. Increases in these expenses could negatively impact our operating results.

Our plans for fiscal 2007 anticipate comparable store net sales increases of approximately 1% to 3% yielding net sales in the $4.22 billion to $4.33 billion range and diluted earnings per share of $1.96 to $2.10. This guidance for 2007 is predicated on selling square footage growth of approximately 10%.

On March 25, 2006, we completed our acquisition of 138 Deal$ stores. These stores are located primarily in the Midwest part of the United States and we have existing logistics capacity to service these stores. This acquisition also included a few "combo" stores that offer an expanded assortment of merchandise including items that sell for more than $1. Substantially all Deal$ stores acquired continue to operate under the Deal$ banner while providing us an opportunity to leverage our Dollar Tree infrastructure in the testing of new merchandise concepts, including higher price points, without disrupting the single-price point model in our Dollar Tree stores. At February 3, 2007, 121 of these stores were selling items priced at over $1.00.

We paid approximately $32.0 million for store-related and other assets and $22.1 million for inventory. The results of Deal$ store operations are included in our financial statements since the acquisition date and did not have a significant impact on our operating results through February 3, 2007. This acquisition is immaterial to our operations as a whole and therefore no proforma disclosure of financial information has been presented.

Results of Operations

The following table expresses items from our consolidated statements of operations, as a percentage of net sales:

	Year Ended February 3, 2007	Year Ended January 28, 2006	Year Ended January 29, 2005
Net sales	**100.0%**	100.0%	100.0%
Cost of sales	**65.8%**	65.5%	64.4%
Gross profit	**34.2%**	34.5%	35.6%
Selling, general and administrative expenses	**26.4%**	26.2%	26.2%
Operating income	**7.8%**	8.3%	9.4%
Interest income	**0.2%**	0.2%	0.1%
Interest expense	**(0.4%)**	(0.4%)	(0.3%)
Income before income taxes	**7.6%**	8.1%	9.2%
Provision for income taxes	**(2.8%)**	(3.0%)	(3.4%)
Net income	**4.8%**	5.1%	5.8%

FISCAL YEAR ENDED FEBRUARY 3, 2007 COMPARED TO FISCAL YEAR ENDED JANUARY 28, 2006

Net Sales. Net sales increased 16.9%, or $575.5 million, in 2006 compared to 2005, resulting from sales in our new and expanded stores, including 138 Deal$ stores acquired in March 2006 and the 53 weeks of sales in 2006 versus 52 weeks in 2005, which accounted for approximately $70 million of the increase. Our sales increase was also impacted by a 4.6% increase in comparable store net sales for the year. This increase is based on a 53-week comparison for both periods. Comparable store net sales are positively affected by our expanded and relocated stores, which we include in the calculation, and, to a lesser extent, are negatively affected when we open new stores or expand stores near existing ones.

The following table summarizes the components of the changes in our store count for fiscal years ended February 3, 2007 and January 28, 2006.

	February 3, 2007	January 28, 2006
New stores	**190**	197
Deal$ acquisition	**138**	—
Acquired leases	**21**	35
Expanded or relocated stores	**85**	93
Closed stores	**(44)**	(53)

Of the 3.3 million selling square foot increase in 2006, approximately 1.2 million resulted from the acquisition of the Deal$ stores and 0.4 million was added by expanding existing stores.

Gross Profit. Gross profit margin decreased to 34.2% in 2006 compared to 34.5% in 2005. The decrease was primarily due to a 35 basis point increase in merchandise cost, including inbound freight. This increase in merchandise cost was due to a slight shift in mix to more consumables, which have a lower margin, higher cost merchandise at our Deal$ stores and increased inbound domestic freight costs.

Selling, General and Administrative Expenses. Selling, general and administrative expenses, as a percentage of net sales, increased to 26.4% for 2006 as compared to 26.2% for 2005. The increase is primarily due to the following:

- Payroll and benefit related costs increased 35 basis points due to increased incentive compensation costs resulting from better overall company performance in the current year as compared to the prior year and increased stock compensation expense, partially offset by lower workers' compensation costs in the current year.

- Operating and corporate expenses decreased 10 basis points primarily as the result of payments received for early lease terminations in the current year.

Operating Income. Due to the reasons discussed above, operating income margin decreased to 7.8% in 2006 compared to 8.4% in 2005.

Income Taxes. Our effective tax rate was 36.6% in 2006 compared to 36.8% in 2005. The decreased tax rate for 2006 was due primarily to increased tax-exempt interest on certain of our investments in the current year.

FISCAL YEAR ENDED JANUARY 28, 2006 COMPARED TO FISCAL YEAR ENDED JANUARY 29, 2005

Net Sales. Net sales increased 8.6% in 2005 compared to 2004. We attribute this $267.9 million increase in net sales primarily to new stores in 2005 and 2004 (which are not included in our comparable store net sales calculation) partially offset by a slight decrease in comparable store net sales of 0.8% in 2005. Our comparable store net sales are positively affected by our expanded and relocated stores, which we include in the calculation, and, to a lesser extent, are negatively affected when we open new stores or expand stores near existing stores.

The following table summarizes the components of the changes in our store count for fiscal years ended January 28, 2006 and January 29, 2005.

	January 28, 2006	January 29, 2005
New stores	**197**	209
Acquired leases	**35**	42
Expanded or relocated stores	**93**	129
Closed stores	**(53)**	(29)

Of the 2.6 million selling square foot increase in 2005, approximately 0.5 million in selling square feet was added by expanding existing stores.

Gross Profit. Gross profit margin decreased to 34.5% in 2005 compared to 35.6% in 2004. The decrease is primarily due to the following:

- Merchandise cost, including inbound freight, increased approximately 55 basis points, due to a slight shift in mix to more consumables, which have a lower margin and increased inbound freight costs due to higher fuel costs.
- Occupancy costs increased approximately 45 basis points due primarily to deleveraging associated with the negative comparable store net sales for the year.

Selling, General and Administrative Expenses. Selling, general and administrative expenses, as a percentage of net sales, were 26.2% for 2005 and 2004. However, several components had increases or decreases as noted below:

- Operating and corporate expenses decreased approximately 25 basis points primarily due to decreased store supplies expense as a result of better pricing, decreased professional fees and the receipt of insurance proceeds resulting from a fire at one of our locations, partially offset by increased interchange fees resulting from the rollout of debit card acceptance in 2005.
- Payroll related costs decreased approximately 10 basis points due to a reduction in incentive compensation accruals that are based on lower than budgeted 2005 earnings and lower workers' compensation and health care claims in 2005.
- These decreases were partially offset by an approximate 25 basis point increase in store operating costs primarily due to higher utility costs due to higher rates and consumption in 2005.
- Depreciation expense for stores also increased 10 basis points primarily due to the deleveraging associated with negative comparable store net sales for 2005.

Operating Income. Due to the reasons discussed above, operating income margin decreased to 8.3% in 2005 compared to 9.4% for 2004.

Interest Income. Interest income increased $2.2 million in 2005 compared to 2004 because of higher investment balances in 2005 and increased interest rates.

Interest Expense. Interest expense increased $4.8 million in 2005 as compared to 2004. This increase is primarily due to increased rates on our revolver in 2005.

Income Taxes. Our effective tax rate was 36.8% in 2005 compared to 37.5% in 2004. The decreased tax rate for 2005 was due primarily to the resolution of tax uncertainties in 2005 and increased tax-exempt interest on certain of our investments.

Liquidity and Capital Resources

Our business requires capital to build and open new stores, expand our distribution network and operate existing stores. Our working capital requirements for existing stores are seasonal and usually reach their peak in September and October. Historically, we have satisfied our seasonal working capital requirements for existing stores and have funded our store opening and distribution network expansion programs from internally generated funds and borrowings under our credit facilities.

The following table compares cash-related information for the years ended February 3, 2007, January 28, 2006, and January 29, 2005:

(in millions)	**Year Ended February 3, 2007**	Year Ended January 28, 2006	Year Ended January 29, 2005
Net cash provided by (used in):			
Operating activities	**$412.8**	$365.1	$276.5
Investing activities	**(190.7)**	(235.5)	(315.4)
Financing activities	**(202.9)**	(170.3)	61.2

The $47.7 million increase in cash provided by operating activities in 2006 was primarily due to increased earnings before depreciation in the current year and better payables management in the current year, partially offset by approximately $20.0 million of rent payments for February 2007 made prior to the end of fiscal 2006.

The $44.8 million decrease in cash used in investing activities in 2006 compared to 2005 was the result of a $114.9 million increase in net proceeds from short-term investments which were used to help fund stock repurchases and the Deal$ acquisition in the current year. In the current year, we purchased an additional $9.3 million of investments in a restricted account to collateralize certain long-term insurance obligations. Additional uses of cash for investing activities consisted of $54.1 million for the Deal$ acquisition in the current year and an increase of $36.1 million in capital expenditures due primarily to new store growth and the installation of freezers and coolers to certain stores in the current year.

The $32.6 million increase in cash used in financing activities in 2006 compared to 2005 primarily resulted from $248.2 million in stock repurchases in the current year compared to $180.4 million in the prior year. This increase was partially offset by increased proceeds from stock option exercises in the current year resulting from our higher stock prices in 2006 as compared to 2005.

The $88.6 million increase in cash provided by operating activities in 2005 was primarily due to an approximate 12% decrease in inventory per store at January 28, 2006 compared to January 29, 2005. The inventory per store decrease is the result of an initiative to lower backroom inventory levels and increase inventory turns through a reduction in 2005 purchases. The aforementioned net cash provided by operating activities was partially offset by a decrease in deferred tax liabilities chiefly as a result of the elimination of bonus depreciation.

The $79.9 million decrease in cash used in investing activities in 2005 compared to 2004 was the result of a $34.2 million decrease in net purchases of investments resulting from more cash used to repurchase stock in 2005. The net purchases of investments in 2005 include $29.9 million of investments that are in a restricted account to collateralize certain long-term insurance obligations. These investments replaced higher cost stand-by letters of credit and surety bonds. Capital expenditures also decreased $42.5 million in 2005 after two distribution center projects and point-of-sale installations were completed in 2004.

The $231.5 million change in cash used in financing activities in 2005 compared to 2004 primarily resulted from $180.4 million in stock repurchases in 2005 compared to $48.6 million in 2004. Also in 2004, we entered into a five-year $450.0 million Revolving Credit Facility, under which we received net proceeds of $248.9 million. We used a portion of these proceeds to repay $142.6 million of variable rate debt for our distribution centers and invested the balance in short-term tax exempt municipal bonds.

At February 3, 2007, our long-term borrowings were $268.8 million and our capital lease commitments were $0.7 million. We also have $125.0 million and $50.0 million Letter of Credit Reimbursement and Security Agreements, under which approximately $84.8 million were committed to letters of credit issued for routine purchases of imported merchandise at February 3, 2007.

In March 2005, our Board of Directors authorized the repurchase of up to $300.0 million of our common stock through March 2008. During fiscal 2006, we repurchased 5,650,871 shares for approximately $148.2 million under the March 2005 authorization.

In November 2006, our Board of Directors authorized the repurchase of up to $500.0 million of our common stock. This amount was in addition to the $27.0 million remaining on the March 2005 authorization. In December 2006, we entered into two agreements with a third party to repurchase approximately $100.0 million of the Company's common shares under an Accelerated Share Repurchase Agreement (ASR).

The first $50.0 million was executed in an "uncollared" agreement. In this transaction, we initially received 1,656,178 shares based on the market price of our stock of $30.19 as of the trade date (December 8, 2006). A weighted average price was calculated using stock prices from December 16, 2006 – March 8, 2007. This represents the calculation period and based on the weighted average price during this period, a settlement took place in March 2007 resulting in additional funding of $3.3 million.

The remaining $50.0 million relates to a "collared" agreement in which we initially received 1,500,703 shares representing the minimum number of shares under the agreement. The maximum number of shares that can be repurchased under the agreement is 1,693,101. The number of shares was determined based on the weighted average market price of our common stock during the same calculation period as defined in the "uncollared" agreement. The weighted average market price as of February 3, 2007 as defined in the "collared" agreement was $30.80. Therefore, as of February 3, 2007, we would receive an additional 122,742 shares under the "collared" agreement. Based on the applicable accounting literature, these additional shares were not included in the weighted average diluted earnings per share calculation because their effect would be antidilutive. The weighted average stock price of our common stock as defined in the "collared" agreement as of March 8, 2007 (termination date) was $31.97. We received an additional 63,325 shares on March 8, 2007 under this agreement.

On March 29, 2007, we entered into an agreement with a third party to repurchase approximately $150.0 million of our common shares under another ASR. The entire $150.0 million was executed under a "collared" agreement. Within two weeks of the March 29, 2007 execution date, we will receive the minimum number of shares. Up to four months after the initial execution date, we will receive additional shares from the third party depending on the volume weighted average price of our common shares during that period, subject to the maximum share delivery provisions of the agreement.

Funding Requirements

Overview

We expect our cash needs for opening new stores and expanding existing stores in fiscal 2007 to total approximately $160.7 million, which includes capital expenditures, initial inventory and pre-opening costs. Our estimated capital expenditures for fiscal 2007 are between $170.0 and $190.0 million, including planned expenditures for our new and expanded stores, the addition of freezers and coolers to approximately 250 stores, an expansion of the Briar Creek Distribution Center and an expansion to our home office and data center in Chesapeake, Va. We believe that we can adequately fund our working capital requirements and planned capital expenditures for the next few years from net cash provided by operations and potential borrowings under our existing credit facilities.

The following tables summarize our material contractual obligations, including both on- and off-balance sheet arrangements, and our commitments, excluding interest on long-term borrowings (in millions):

Contractual Obligations	Total	2007	2008	2009	2010	2011	Thereafter
Lease Financing							
Operating lease obligations	$1,177.0	$284.2	$246.0	$207.2	$161.5	$110.6	$167.5
Capital lease obligations	0.8	0.4	0.3	0.1	—	—	—
Long-term Borrowings							
Revolving credit facility	250.0	—	—	250.0	—	—	—
Revenue bond financing	18.8	18.8	—	—	—	—	—
Total obligations	$1,446.6	$303.4	$246.3	$457.3	$161.5	$110.6	$167.5

Commitments	Total	Expiring in 2007	Expiring in 2008	Expiring in 2009	Expiring in 2010	Expiring in 2011	Thereafter
Letters of credit and surety bonds	$116.3	$115.6	$ 0.7	$ —	$—	$—	$—
Freight contracts	57.1	38.6	9.9	8.6	—	—	—
Technology assets	3.8	3.8	—	—	—	—	—
Total commitments	$177.2	$158.0	$10.6	$8.6	$—	$—	$—

Lease Financing

Operating Lease Obligations. Our operating lease obligations are primarily for payments under non-cancelable store leases. The commitment includes amounts for leases that were signed prior to February 3, 2007 for stores that were not yet open on February 3, 2007.

Capital Lease Obligations. Our capital lease obligations are primarily for payments for distribution center equipment and computer equipment at the store support center.

Long-Term Borrowings

Revolving Credit Facility. In March 2004, we entered into a five-year Revolving Credit Facility (the Facility). The Facility provides for a $450.0 million line of credit, including up to $50.0 million in available letters of credit. Interest is assessed under the line based on matrix pricing which currently approximates LIBOR, plus 0.475%. The Facility, among other things, requires the maintenance of certain specified financial ratios, restricts the payment of certain distributions and prohibits the incurrence of certain new indebtedness. We used availability under this Facility to repay the $142.6 million of variable-rate debt and to purchase short-term investments. As of February 3, 2007, we had $250.0 million outstanding on this Facility.

Revenue Bond Financing. In May 1998, we entered into an agreement with the Mississippi Business Finance Corporation under which it issued $19.0 million of variable-rate demand revenue bonds. We used the proceeds from the bonds to finance the acquisition, construction and installation of land, buildings, machinery and equipment for our distribution facility in Olive Branch, Mississippi. At February 3, 2007, the balance outstanding on the bonds was $18.8 million. These bonds are due to be fully repaid in June 2018. The bonds do not have a prepayment penalty as long as the interest rate remains variable. The bonds contain a demand provision and, therefore, outstanding amounts are classified as current liabilities. We pay interest monthly based on a variable-interest rate, which was 5.4% at February 3, 2007.

Commitments

Letters of Credit and Surety Bonds. In March 2001, we entered into a Letter of Credit Reimbursement and Security Agreement, which provides $125.0 million for letters of credit. In December 2004, we entered into an additional Letter of Credit Reimbursement and Security Agreement, which provides $50.0 million for letters of credit. Letters of credit are generally issued for the routine purchase of imported merchandise and we had approximately $84.8 million of purchases committed under these letters of credit at February 3, 2007. We also have approximately $31.5 million of letters of credit or surety bonds outstanding for our insurance programs and certain utility payment obligations at some of our stores.

Freight Contracts. We have contracted outbound freight services from various carriers with contracts expiring through April 2009. The total amount of these commitments is approximately $57.1 million.

Technology Assets. We have commitments totaling approximately $3.8 million to primarily purchase store technology assets for our stores during 2007.

Derivative Financial Instruments

We are party to one interest rate swap, which allows us to manage the risk associated with interest rate fluctuations on the demand revenue bonds. The swap is based on a notional amount of $18.8 million. Under the $18.8 million agreement, as amended, we pay interest to the bank that provided the swap at a fixed rate. In exchange, the financial institution pays us at a variable-interest rate, which is similar to the rate on the demand revenue bonds. The variable-interest rate on the interest rate swap is set monthly. No payments are made by either party under the swap for monthly periods with an established interest rate greater than a predetermined rate (the knock-out rate). The swap may be canceled by the bank or us and settled for the fair value of the swap as determined by market rates and expires in 2009.

Because of the knock-out provision in the $18.8 million swap, changes in the fair value of that swap are recorded in earnings. For more information on the interest rate swaps, see "Quantitative and Qualitative Disclosures About Market Risk – Interest Rate Risk."

Critical Accounting Policies

The preparation of financial statements requires the use of estimates. Certain of our estimates require a high level of judgment and have the potential to have a material effect on the financial statements if actual results vary significantly from those estimates. Following is a discussion of the estimates that we consider critical.

Inventory Valuation

As discussed in Note 1 to the Consolidated Financial Statements, inventories at the distribution centers are stated at the lower of cost or market with cost determined on a weighted-average basis. Cost is assigned to store inventories using the retail inventory method on a weighted-average basis. Under the retail inventory method, the valuation of inventories at cost and the resulting gross margins are computed by applying a calculated cost-to-retail ratio to the retail value of inventories. The retail inventory method is an averaging method that has been widely used in the retail industry and results in valuing inventories at lower of cost or market when markdowns are taken as a reduction of the retail value of inventories on a timely basis.

Inventory valuation methods require certain significant management estimates and judgments, including estimates of future merchandise markdowns and shrink, which significantly affect the ending inventory valuation at cost as well as the resulting gross margins. The averaging required in applying the retail inventory method and the estimates of shrink and markdowns could, under certain circumstances, result in costs not being recorded in the proper period.

We estimate our markdown reserve based on the consideration of a variety of factors, including, but not limited to, quantities of slow moving or seasonal, carryover merchandise on hand, historical markdown statistics and future merchandising plans. The accuracy of our estimates can be affected by many factors, some of which are outside of our control, including changes in economic conditions and consumer buying trends. Historically, we have not experienced significant differences in our estimated reserve for markdowns compared with actual results.

Our accrual for shrink is based on the actual, historical shrink results of our most recent physical inventories adjusted, if necessary, for current economic conditions. These estimates are compared to actual results as physical inventory counts are taken and reconciled to the general ledger. Our physical inventory counts are generally taken between January and September of each year; therefore, the shrink accrual recorded at February 3, 2007 is based on estimated shrink for most of 2006, including the fourth quarter. We have not experienced significant fluctuations in historical shrink rates beyond 10 to 15 basis points in our Dollar Tree stores for the last two years. However, we have sometimes experienced higher than typical shrink in acquired stores in the year following an acquisition. We periodically adjust our shrink estimates to address these factors as they become apparent.

Our management believes that our application of the retail inventory method results in an inventory valuation that reasonably approximates cost and results in carrying inventory at the lower of cost or market each year on a consistent basis.

Accrued Expenses

On a monthly basis, we estimate certain expenses in an effort to record those expenses in the period incurred. Our most material estimates include domestic freight expenses, self-insurance programs, store-level operating expenses, such as property taxes and utilities, and certain other expenses. Our freight and store-level operating expenses are estimated based on current activity and historical trends and results. Our workers' compensation and general liability insurance accruals are recorded based on actuarial valuations which are adjusted annually based on a review performed by a third-party actuary. These actuarial valuations are estimates based on historical loss development factors. Certain other expenses are estimated and recorded in the periods that management becomes aware of them. The related accruals are adjusted as management's estimates change. Differences in management's estimates and assumptions could result in an accrual materially different from the calculated accrual. Our experience has been that some of our estimates are too high and others are too low. Historically, the net total of these differences has not had a material effect on our financial condition or results of operations.

Income Taxes

On a quarterly basis, we estimate our required income tax liability and assess the recoverability of our deferred tax assets. Our income taxes payable are estimated based on enacted tax rates, including estimated tax rates in states where our store base is growing applied to the income expected to be taxed currently. The current tax liability also includes a liability for resolution of tax uncertainties. Management assesses the recoverability of deferred tax assets based on the availability of carrybacks of future deductible amounts and management's projections for future taxable income. We cannot guarantee that we will generate taxable income in future years. Historically, we have not experienced significant differences in our estimates of our tax accrual. In 2006 and 2005, we recognized approximately $0.7 million and $1.5 million, respectively, of tax benefits related to the resolution of tax uncertainties in certain states.

Seasonality and Quarterly Fluctuations

We experience seasonal fluctuations in our net sales, comparable store net sales, operating income and net income and expect this trend to continue. Our results of operations may also fluctuate significantly as a result of a variety of factors, including:

- shifts in the timing of certain holidays, especially Easter;
- the timing of new store openings;
- the net sales contributed by new stores;
- changes in our merchandise mix; and
- competition.

Our highest sales periods are the Christmas and Easter seasons. Easter was observed on March 27, 2005, April 16, 2006 and will be observed on April 8, 2007. We generally realize a disproportionate amount of our net sales and of our operating and net income during the fourth quarter. In anticipation of increased sales activity during these months, we purchase substantial amounts of inventory and hire a significant number of temporary employees to supplement our continuing store staff. Our operating results, particularly operating and net income, could suffer if our net sales were below seasonal norms during the fourth quarter or during the Easter season for any reason, including merchandise delivery delays due to receiving or distribution problems or consumer sentiment. Fiscal 2006 consisted of 53 weeks, commensurate with the retail calendar. This extra week contributed approximately $70.0 million of sales in 2006. Fiscal 2007 will consist of 52 weeks.

Our unaudited results of operations for the eight most recent quarters are shown in a table in Footnote 13 of the Consolidated Financial Statements.

Inflation and Other Economic Factors

Our ability to provide quality merchandise at a fixed price and on a profitable basis may be subject to economic factors and influences that we cannot control. Consumer spending could decline because of economic pressures, including rising fuel prices. Reductions in consumer confidence and spending could have an adverse effect on our sales. National or international events, including war or terrorism, could lead to disruptions in economies in the United States or in foreign countries where we purchase some of our merchandise. These and other factors could increase our merchandise costs and other costs that are critical to our operations, such as shipping and wage rates.

Shipping Costs. Currently, trans-Pacific shipping rates are negotiated with individual freight lines and are subject to fluctuation based on supply and demand for containers and current fuel costs. As a result, our trans-Pacific shipping costs in fiscal 2007 may increase compared with fiscal 2006 when we renegotiate our import shipping rates effective May 2007. We can give no assurances as to the amount of the increase, as we are in the early stages of our negotiations.

Minimum Wage. Although our average hourly wage rate is significantly higher than the federal minimum wage, an increase in the mandated minimum wage could increase our payroll costs. In early 2007, proposals increasing the federal minimum wage to $7.25 per hour over a three-year period have passed both houses of Congress. If the federal minimum wage were to increase over the next three years to $7.25 per hour, we believe that it would not have a material effect on our annual payroll expenses.

New Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 ("FIN 48"), *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes 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. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosures, and transition. FIN

48 is effective for fiscal years beginning after December 15, 2006. We do not expect that the adoption of FIN 48 will have a material impact on our consolidated financial position, results of operations or cash flows.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to various types of market risk in the normal course of our business, including the impact of interest rate changes and foreign currency rate fluctuations. We may enter into interest rate swaps to manage exposure to interest rate changes, and we may employ other risk management strategies, including the use of foreign currency forward contracts. We do not enter into derivative instruments for any purpose other than cash flow hedging purposes and we do not hold derivative instruments for trading purposes.

Interest Rate Risk

We use variable-rate debt to finance certain of our operations and capital improvements. These obligations expose us to variability in interest payments due to changes in interest rates. If interest rates increase, interest expense increases. Conversely, if interest rates decrease, interest expense also decreases. We believe it is beneficial to limit the variability of our interest payments.

To meet this objective, we entered into a derivative instrument in the form of an interest rate swap to manage fluctuations in cash flows resulting from changes in the variable-interest rates on the Demand Revenue Bonds. The interest rate swap reduces the interest rate exposure on this variable-rate obligation. Under the interest rate swap, we pay the bank at a fixed-rate and receive variable-interest at a rate approximating the variable-rate on the obligation, thereby creating the economic equivalent of a fixed-rate obligation. Under the swap, no payments are made by parties under the swap for monthly periods in which the variable-interest rate is greater than the predetermined knock-out rate.

The following table summarizes the financial terms of our interest rate swap agreement and the fair value of the interest rate swap at February 3, 2007:

Hedging Instrument	Receive Variable	Pay Fixed	Knock-out Rate	Expiration	Fair Value
$18.8 million interest rate swap	LIBOR	4.88%	7.75%	4/1/09	—

At February 3, 2007, the fair value of this interest rate swap is less than $0.1 million. Hypothetically, a 1% change in interest rates results in approximately a $0.2 million change in the amount paid or received under the terms of the interest rate swap agreement on an annual basis. Due to many factors, management is not able to predict the changes in fair value of our interest rate swap. The fair values are the estimated amounts we would pay or receive to terminate the agreement as of the reporting date. These fair values are obtained from an outside financial institution.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Dollar Tree Stores, Inc.:

We have audited the accompanying consolidated balance sheets of Dollar Tree Stores, Inc. and subsidiaries (the Company) as of February 3, 2007 and January 28, 2006, and the related consolidated statements of operations, shareholders' equity and comprehensive income, and cash flows for each of the fiscal years in the three-year period ended February 3, 2007. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of February 3, 2007 and January 28, 2006, and the results of their operations and their cash flows for each of the fiscal years in the three-year period ended February 3, 2007, in conformity with U.S. generally accepted accounting principles.

As discussed in note 1 to the consolidated financial statements, effective January 29, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment*.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of February 3, 2007, based on the criteria established in *Internal Control – Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated April 2, 2007, expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

KPMG LLP

Norfolk, Virginia
April 2, 2007

CONSOLIDATED STATEMENTS OF OPERATIONS

(in millions, except per share data)	**Year Ended February 3, 2007**	Year Ended January 28, 2006	Year Ended January 29, 2005
Net sales	**$3,969.4**	$3,393.9	$3,126.0
Cost of sales (Note 4)	**2,612.2**	2,221.5	2,013.5
Gross profit	**1,357.2**	1,172.4	1,112.5
Selling, general and administrative expenses (Notes 8 and 9)	**1,046.4**	888.5	819.0
Operating income	**310.8**	283.9	293.5
Interest income	**8.6**	6.8	3.9
Interest expense (Notes 5 and 6)	**(16.5)**	(15.5)	(9.2)
Income before income taxes	**302.9**	275.2	288.2
Provision for income taxes (Note 3)	**110.9**	101.3	107.9
Net income	**$ 192.0**	$ 173.9	$ 180.3
Basic net income per share (Note 7)	**$ 1.86**	$ 1.61	$ 1.59
Diluted net income per share (Note 7)	**$ 1.85**	$ 1.60	$ 1.58

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEETS

(in millions, except share data)	February 3, 2007	January 28, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 85.0	$ 65.8
Short-term investments	221.8	274.0
Merchandise inventories	605.0	576.6
Deferred tax assets (Note 3)	10.7	10.8
Prepaid expenses and other current assets	36.5	16.5
Total current assets	959.0	943.7
Property, plant and equipment, net (Note 2)	715.3	681.8
Intangibles, net (Notes 2 and 10)	146.6	129.3
Other assets, net (Notes 2, 8 and 11)	52.4	43.6
TOTAL ASSETS	$1,873.3	$1,798.4
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt (Note 5)	$ 18.8	$ 19.0
Accounts payable	189.2	135.6
Other current liabilities (Note 2)	132.0	99.2
Income taxes payable	43.3	41.7
Total current liabilities	383.3	295.5
Long-term debt, excluding current portion (Note 5)	250.0	250.0
Deferred tax liabilities (Note 3)	1.5	23.5
Other liabilities (Notes 6 and 8)	70.8	57.1
Total liabilities	705.6	626.1
Shareholders' equity (Notes 6, 7 and 9):		
Common stock, par value $0.01. 300,000,000 shares authorized, 99,663,580 and 106,552,054 shares issued and outstanding at February 3, 2007 and January 28, 2006, respectively	1.0	1.1
Additional paid-in capital	—	11.4
Accumulated other comprehensive income (loss)	0.1	0.1
Retained earnings	1,166.6	1,159.7
Total shareholders' equity	1,167.7	1,172.3
Commitments, contingencies and subsequent event (Notes 4 and 12)	—	—
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$1,873.3	$1,798.4

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME

Years Ended February 3, 2007, January 28, 2006 and January 29, 2005

(in millions)	Common Stock Shares	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Unearned Compensation	Retained Earnings	Shareholders' Equity
Balance at January 31, 2004	114.1	$1.1	$208.9	$(0.9)	$ (0.1)	$ 805.5	$1,014.5
Net income for the year ended January 29, 2005	—	—	—	—	—	180.3	180.3
Other comprehensive income (Note 7)	—	—	—	0.6	—	—	0.6
Total comprehensive income							180.9
Issuance of stock under Employee Stock Purchase Plan (Note 9)	0.1	—	3.3	—	—	—	3.3
Exercise of stock options, including income tax benefit of $2.1 (Note 9)	0.6	—	14.0	—	—	—	14.0
Repurchase and retirement of shares (Note 7)	(1.8)	—	(48.6)	—	—	—	(48.6)
Restricted stock amortization (Note 9)	—	—	0.1	—	—	—	0.1
Balance at January 29, 2005	113.0	1.1	177.7	(0.3)	(0.1)	985.8	1,164.2
Net income for the year ended January 28, 2006	—	—	—	—	—	173.9	173.9
Other comprehensive income (Note 7)	—	—	—	0.4	—	—	0.4
Total comprehensive income							174.3
Issuance of stock under Employee Stock Purchase Plan (Note 9)	0.1	—	3.0	—	—	—	3.0
Exercise of stock options, including income tax benefit of $1.2 (Note 9)	0.4	—	8.8	—	—	—	8.8
Repurchase and retirement of shares (Note 7)	(7.0)	—	(180.3)	—	—	—	(180.3)
Stock-based compensation (Notes 1 and 9)	—	—	2.2	—	0.1	—	2.3
Balance at January 28, 2006	106.5	1.1	11.4	0.1	—	1,159.7	1,172.3
Net income for the year ended February 3, 2007	—	—	—	—	—	192.0	192.0
Other comprehensive income (Note 7)	—	—	—	—	—	—	—
Total comprehensive income							192.0
Issuance of stock under Employee Stock Purchase Plan (Note 9)	0.1	—	2.8	—	—	—	2.8
Exercise of stock options, including income tax benefit of $5.6 (Note 9)	1.7	—	43.1	—	—	—	43.1
Repurchase and retirement of shares (Note 7)	(8.8)	(0.1)	(63.0)	—	—	(185.1)	(248.2)
Stock-based compensation, net (Notes 1 and 9)	0.1	—	5.7	—	—	—	5.7
Balance at February 3, 2007	**99.6**	**$1.0**	**$ —**	**$ 0.1**	**$ —**	**$1,166.6**	**$1,167.7**

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in millions)	**Year Ended February 3, 2007**	Year Ended January 28, 2006	Year Ended January 29, 2005
Cash flows from operating activities:			
Net income	**$ 192.0**	$ 173.9	$ 180.3
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**159.0**	140.7	129.3
Provision for deferred income taxes	**(21.9)**	(21.5)	15.6
Tax benefit of stock option exercises	**—**	1.2	2.1
Stock based compensation expense	**6.7**	2.4	—
Other non-cash adjustments to net income	**5.1**	5.6	3.9
Changes in assets and liabilities increasing (decreasing) cash and cash equivalents:			
Merchandise inventories	**(6.2)**	38.9	(89.8)
Other assets	**(19.8)**	(5.5)	0.5
Accounts payable	**53.7**	11.4	9.2
Income taxes payable	**1.6**	8.0	(3.4)
Other current liabilities	**31.8**	(6.4)	15.3
Other liabilities	**10.8**	16.4	13.5
Net cash provided by operating activities	**412.8**	365.1	276.5
Cash flows from investing activities:			
Capital expenditures	**(175.3)**	(139.2)	(181.8)
Purchase of short-term investments	**(1,044.4)**	(885.5)	(465.8)
Proceeds from sales of short-term investments	**1,096.6**	822.8	339.0
Purchase of Deal$ assets, net of cash acquired of $0.3	**(54.1)**	—	—
Acquisition of favorable lease rights	**(4.2)**	(3.7)	(6.8)
Purchase of restricted investments	**(9.3)**	(29.9)	—
Net cash used in investing activities	**(190.7)**	(235.5)	(315.4)
Cash flows from financing activities:			
Proceeds from long-term debt, net of facility fees of $1.1	**—**	—	248.9
Principal payments under long-term debt and capital lease obligations	**(0.6)**	(0.6)	(154.2)
Payments for share repurchases	**(248.2)**	(180.4)	(48.6)
Proceeds from stock issued pursuant to stock-based compensation plans	**40.3**	10.7	15.1
Tax benefit of stock options exercised	**5.6**	—	—
Net cash provided by (used in) financing activities	**(202.9)**	(170.3)	61.2
Net increase (decrease) in cash and cash equivalents	**19.2**	(40.7)	22.3
Cash and cash equivalents at beginning of year	**65.8**	106.5	84.2
Cash and cash equivalents at end of year	**$ 85.0**	$ 65.8	$ 106.5
Supplemental disclosure of cash flow information:			
Cash paid for:			
Interest, net of amount capitalized	**$ 14.9**	$ 11.8	$ 8.1
Income taxes	**$ 125.5**	$ 113.9	$ 93.4

Supplemental disclosure of non-cash investing and financing activities:

The Company purchased equipment under capital lease obligations amounting to $0.1 million, $0.4 million and $0.4 million in the years ended February 3, 2007, January 28, 2006, and January 29, 2005, respectively.

See accompanying Notes to Consolidated Financial Statements.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

At February 3, 2007, Dollar Tree Stores, Inc. (DTS or the Company) owned and operated 3,219 discount variety retail stores. Approximately 3,100 of these stores sell substantially all items for $1.00 or less. The remaining stores were acquired as apart of the Deal$ acquisition and these stores sell many items for $1.00 or less but also sell items at prices greater than $1.00. The Company's stores operate under the names of Dollar Tree, Deal$, Dollar Bills and Dollar Express. Our stores average approximately 8,200 selling square feet.

The Company's headquarters and one of its distribution centers are located in Chesapeake, Virginia. The Company also operates distribution centers in Mississippi, Illinois, California, Pennsylvania, Georgia, Oklahoma, Utah and Washington. The Company's stores are located in all 48 contiguous states. The Company's merchandise includes food, health and beauty care, party goods, candy, toys, stationery, seasonal goods, gifts and other consumer items. Approximately 35% to 40% of the Company's merchandise is imported, primarily from China.

Principles of Consolidation

The consolidated financial statements include the financial statements of Dollar Tree Stores, Inc., and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Fiscal Year

The Company's fiscal year ends on the Saturday closest to January 31. Any reference herein to "2006" or "Fiscal 2006," "2005" or "Fiscal 2005," and "2004" or "Fiscal 2004" relates to as of or for the years ended February 3, 2007, January 28, 2006, and January 29, 2005, respectively. Fiscal year 2006 consisted of 53 weeks, while 2005 and 2004 both consisted of 52 weeks.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain 2005 and 2004 amounts have been reclassified for comparability with the current period presentation.

Cash and Cash Equivalents

Cash and cash equivalents at February 3, 2007 and January 28, 2006 includes $40.3 million and $31.4 million, respectively, of investments in money market securities and bank participation agreements which are valued at cost, which approximates market. The underlying assets of these short-term participation agreements are primarily commercial notes. For purposes of the consolidated statements of cash flows, the Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. The majority of payments due from financial institutions for the settlement of debit card and credit card transactions process within three business days, and therefore are classified as cash and cash equivalents.

Short-Term Investments

The Company's short-term investments consist primarily of government-sponsored municipal bonds and auction rate securities. These investments are classified as available for sale and are recorded at fair value, which approximates cost. The government-sponsored municipal bonds can be converted into cash depending on terms of the underlying agreement. The auction rate securities have stated interest rates, which typically reset to prevailing market rates every 35 days or less. The securities underlying both the government-sponsored municipal bonds and the auction rate securities have longer legal maturity dates.

Merchandise Inventories

Merchandise inventories at the distribution centers are stated at the lower of cost or market, determined on a weighted average cost basis. Cost is assigned to store inventories using the retail inventory method, determined on a weighted average cost basis.

Costs directly associated with warehousing and distribution are capitalized as merchandise inventories. Total warehousing and distribution costs capitalized into inventory amounted to $25.6 million and $25.3 million at February 3, 2007 and January 28, 2006, respectively.

Property, Plant and Equipment

Property, plant and equipment are stated at cost and depreciated using the straight-line method over the estimated useful lives of the respective assets as follows:

Buildings	40 years
Furniture, fixtures and equipment	3 to 15 years
Transportation vehicles	4 to 6 years

Leasehold improvements and assets held under capital leases are amortized over the estimated useful lives of the respective assets or the committed terms of the related leases, whichever is shorter. Amortization is included in "selling, general and administrative expenses" on the accompanying consolidated statements of operations.

In the fourth quarter of 2004, the Company revised its estimate of useful lives on certain store equipment and distribution center assets. This change increased net income by approximately $4.0 million in the first three quarters of 2005 as compared to 2004.

Costs incurred related to software developed for internal use are capitalized and amortized over three years. Costs capitalized include those incurred in the application development stage as defined in Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*.

Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of

The Company reviews its long-lived assets and certain identifiable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable, in accordance with Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. Recoverability of assets to be held and used is measured by comparing the carrying amount of an asset to future net undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the assets exceeds the fair value of the assets based on discounted cash flows or other readily available evidence of fair value, if any. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. In fiscal 2006, 2005 and 2004, the Company recorded charges of $0.5 million, $0.2 million and $0.5 million, respectively, to write down certain assets. These charges are recorded as a component of "selling, general and administrative expenses" in the accompanying consolidated statements of operations.

Intangible Assets

Goodwill and intangible assets with indefinite useful lives are not amortized, but rather tested for impairment at least annually. Intangible assets with finite useful lives are amortized over their respective estimated useful lives and reviewed for impairment in accordance with SFAS No. 144. The Company performs its annual assessment of impairment following the finalization of each November's financial statements.

Financial Instruments

The Company utilizes derivative financial instruments to reduce its exposure to market risks from changes in interest rates. By entering into receive-variable, pay-fixed interest rate swaps, the Company limits its exposure to changes in variable interest rates. The Company is exposed to credit-related losses in the event of non-performance by the counterparty to the interest rate swaps; however, the counterparties are major financial institutions, and the risk of loss due to non-performance is considered remote. Interest rate differentials paid or received on the swaps are recognized as adjustments to expense in the period earned or incurred. The Company formally documents all hedging relationships, if applicable, and assesses hedge effectiveness both at inception and on an ongoing basis.

Certain of the Company's interest rate swaps have not qualified for hedge accounting treatment pursuant to the provisions of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities (SFAS 133)*. These interest rate swaps are recorded at fair value in the accompanying

Consolidated Balance Sheets as a component of "other liabilities" (see Note 6). Changes in the fair values of these interest rate swaps are recorded as "interest expense" and "change in the fair value of non-hedging interest rate swaps" in the accompanying Consolidated Statements of Operations and the Consolidated Statements of Cash Flows, respectively.

Lease Accounting

The Company recognized a one-time non-cash, after-tax adjustment of $5.7 million, or $0.05 per diluted share, in the fourth quarter of 2004 to reflect the cumulative impact of a correction of its accounting practices related to leased properties. Of the aforementioned amount, approximately $1.2 million, or $0.01 per diluted share, related to fiscal 2004.

Consistent with industry practices, in prior periods, the Company had reported its straight line expenses for leases beginning on the earlier of the store opening date or the commencement date of the lease. This had the effect of excluding the pre-opening or build-out period of its stores (generally 60 days) from the calculation of the period over which it expenses rent. In addition, amounts received as tenant allowances were reflected in the balance sheet as a reduction to store leasehold improvement costs instead of being classified as deferred lease credits. The adjustment made to correct these practices does not affect historical or future net cash flows or the timing of payments under related leases. Rather, this change affected the classification of costs in the accompanying Consolidated Statement of Operations and Cash Flows by increasing depreciation and decreasing rent expense, which is included in cost of sales. In addition, fixed assets and deferred liabilities increased due to the net cumulative unamortized allowances and abatements.

Revenue Recognition

The Company recognizes sales revenue at the time a sale is made to its customer.

Taxes Collected

The Company reports taxes assessed by a governmental authority that are directly imposed on revenue-producing transactions (i.e., sales tax) on a net (excluded from revenues) basis.

Cost of Sales

The Company includes the cost of merchandise, warehousing and distribution costs, and certain occupancy costs in cost of sales.

Pre-Opening Costs

The Company expenses pre-opening costs for new, expanded and relocated stores, as incurred.

Advertising Costs

The Company expenses advertising costs as they are incurred. Advertising costs approximated $10.6 million, $11.8 million and $11.0 million for the years ended February 3, 2007, January 28, 2006, and January 29, 2005, respectively.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date of such change.

Stock-Based Compensation

Effective, January 29, 2006, the Company adopted Statement of Financial Accounting Standards, No. 123 (revised 2004), *Share-Based Payment*, (SFAS 123R). This statement is a revision of SFAS 123 and supersedes Accounting Principle Board Opinion No. 25, *Accounting for Stock Issued to Employees*, (APB Opinion 25). SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. The Company adopted SFAS 123R using the modified prospective method, which requires application of the standard to all awards granted, modified, repurchased or cancelled on or after January 29, 2006, and to all awards granted to employees that were unvested as of

January 29, 2006. In accordance with the modified prospective method of implementation, prior period financial statements have not been restated to reflect the impact of SFAS 123R. During 2006, the Company recognized $1.8 million of stock-based compensation expense as a result of the adoption of SFAS 123R. Total stock-based compensation expense for 2006 and 2005 was $6.7 million and $2.4 million, respectively. There was no stock-based compensation expense for 2004. Through January 28, 2006, the Company applied the intrinsic value recognition and measurement principles of APB Opinion 25 and related Interpretations in accounting for its stock-based employee compensation plans. Prior to the adoption of SFAS 123R, the Company reported all tax benefits resulting from the exercise of stock options as operating cash flows in the Consolidated Statements of Cash Flows. SFAS 123R requires cash flows resulting from the tax deductions in excess of the tax benefits of the related compensation cost recognized in the financial statements (excess tax benefits) to be classified as financing cash flows. Thus, the Company has classified the $5.6 million of excess tax benefits recognized in 2006 as financing cash flows. Excess tax benefits of $1.2 million and $2.1 million recognized in 2005 and 2004, respectively, prior to the adoption of SFAS 123R, are classified as operating cash flows.

If the accounting provisions of SFAS 123 had been applied to 2005 and 2004, the Company's net income and net income per share would have been reduced to the pro forma amounts indicated in the following table:

(in millions, except per share data)	**Year Ended January 28, 2006**	Year Ended January 29, 2005
Net income as reported	**$173.9**	$180.3
Add: Total stock-based employee compensation expense included in net income, net of related tax effects	**1.5**	—
Deduct: Total stock-based employee compensation expense determined under fair value based method, net of related tax effects	**(18.2)**	(13.0)
	$157.2	$167.3
Net income per share:		
Basic, as reported	**$ 1.61**	$ 1.59
Basic, pro forma under FAS 123	**1.45**	1.48
Diluted, as reported	**$ 1.60**	$ 1.58
Diluted, pro forma under FAS 123	**1.44**	1.47

On December 15, 2005, the Compensation Committee of the Board of Directors of the Company approved the acceleration of the vesting date of all previously issued, outstanding and unvested options under all current stock option plans, including the 1995 Stock Incentive Plan, the 2003 Equity Incentive Plan and the 2004 Executive Officer Equity Incentive Plan (EOEP), effective as of December 15, 2005. At the effective date, almost all of these options had exercise prices higher than the actual stock price. The Company made the decision to accelerate vesting of these options to give employees increased performance incentives and to enhance current retention. This decision also eliminated non-cash compensation expense that would have been recorded in future periods following the Company's adoption of SFAS 123R on January 29, 2006. Compensation expense, as determined at the time of the accelerated vesting, has been reduced by $14.9 million, over a period of four years during which the options would have vested, as a result of the option acceleration program. This amount is net of compensation expense of $0.1 million recognized in fiscal 2005 for estimated forfeiture of certain (in the money) options.

The Company recognizes expense related to the fair value of restricted stock units (RSUs) over the requisite service period. The fair value of the RSUs is determined using the closing price of the Company's common stock on the date of grant.

On March 30, 2007, the Board of Directors granted approximately 0.3 million restricted stock units and options to purchase 0.4 million shares of the Company's common stock under the Company's Equity Incentive Plan and the EOEP.

Net Income Per Share

Basic net income per share has been computed by dividing net income by the weighted average number of shares outstanding. Diluted net income per share reflects the potential dilution that could occur assuming the inclusion of dilutive potential shares and has been computed by dividing net income by the weighted average number of shares and dilutive potential shares outstanding. Dilutive potential shares include all outstanding stock options and unvested restricted stock, excluding certain performance based restricted stock grants, after applying the treasury stock method.

NOTE 2 – BALANCE SHEET COMPONENTS

Intangibles, Net

Intangibles, net, as of February 3, 2007 and January 28, 2006 consist of the following:

(in millions)	**February 3, 2007**	January 28, 2006
Non-competition agreements	**$ 6.4**	$ 6.4
Accumulated amortization	**(5.1)**	(4.3)
Non-competition agreements, net	**1.3**	2.1
Favorable lease rights	**19.0**	12.6
Accumulated amortization	**(7.0)**	(4.1)
Favorable lease rights, net	**12.0**	8.5
Goodwill	**144.9**	130.3
Accumulated amortization	**(11.6)**	(11.6)
Goodwill, net	**133.3**	118.7
Total intangibles, net	**$146.6**	$129.3

Non-Competition Agreements

The Company has entered into non-competition agreements with certain former executives of certain acquired entities. These assets are being amortized over the legal term of the individual agreements, ranging from five to ten years.

Favorable Lease Rights

In 2006 and 2005, the Company acquired favorable lease rights for operating leases for retail locations from third parties, including the acquired favorable lease rights in its acquisition of 138 Deal$ stores (see Note 10). The Company's favorable lease rights are amortized on a straight-line basis to rent expense over the remaining initial lease terms, which expire at various dates through 2016. The weighted average life remaining on the favorable lease rights at February 3, 2007 is 54 months.

Amortization expense related to the non-competition agreements and favorable lease rights was $4.4 million, $3.3 million and $1.6 million for the years ended February 3, 2007, January 28, 2006 and January 29, 2005, respectively. Estimated annual amortization expense for the next five years follows: 2007 – $4.8 million; 2008 – $3.4 million; 2009 – $1.8 million, 2010 – $1.2 million, and 2011 – $0.7 million.

Goodwill

In accordance with SFAS No. 142, goodwill is no longer being amortized, but is tested annually for impairment. In addition, goodwill will be tested on an interim basis if an event or circumstance indicates that it is more likely than not that an impairment loss has been incurred. The Company performed its annual impairment testing in November 2006 and determined that no impairment loss existed.

Property, Plant and Equipment, Net

Property, plant and equipment, net, as of February 3, 2007 and January 28, 2006 consists of the following:

(in millions)	**February 3, 2007**	January 28, 2006
Land	**$ 29.4**	$ 29.4
Buildings	**154.7**	154.7
Improvements	**482.3**	418.1
Furniture, fixtures and equipment	**708.6**	608.4
Construction in progress	**38.3**	29.3
Total property, plant and equipment	**1,413.3**	1,239.9
Less: accumulated depreciation and amortization	**698.0**	558.1
Total property, plant and equipment, net	**$ 715.3**	$ 681.8

Other Assets, Net

Other assets, net includes $39.2 million of restricted investments. The Company purchased these restricted investments to collateralize long-term insurance obligations. These investments replaced higher cost stand

by letters of credit and surety bonds. These investments consist primarily of government-sponsored municipal bonds and auction rate securities, similar to our short-term investments. These investments are classified as available for sale and are recorded at fair value, which approximates cost.

Other Current Liabilities

Other current liabilities as of February 3, 2007 and January 28, 2006 consist of accrued expenses for the following:

(in millions)	**February 3, 2007**	January 28, 2006
Compensation and benefits	**$ 43.5**	$22.2
Taxes (other than income taxes)	**19.5**	15.8
Insurance	**26.8**	28.1
Other	**42.2**	33.1
Total other current liabilities	**$132.0**	$99.2

Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, other current assets, accounts payable and other current liabilities approximate fair value because of the short maturity of these instruments. The carrying values of other long-term financial assets and liabilities, excluding restricted investments, approximate fair value because they are recorded using discounted future cash flows or quoted market rates. Short-term investments and restricted investments are carried at fair value, which approximates cost, in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*.

The carrying value of the Company's long-term debt approximates its fair value because the debt's interest rates vary with market interest rates.

It is not practicable to estimate the fair value of the Company's outstanding commitments for letters of credit and surety bonds without unreasonable cost.

NOTE 3 – INCOME TAXES

Total income taxes were allocated as follows:

	Year Ended February 3, 2007	Year Ended January 28, 2006	Year Ended January 29, 2005
Income from continuing operations	**$110.9**	$101.3	$107.9
Accumulated other comprehensive income, marking derivative financial instruments to fair value	**—**	0.2	0.4
Stockholders' equity, tax benefit on exercise of stock options	**(5.6)**	(1.2)	(2.1)
	$105.3	$100.3	$106.2

The provision for income taxes consists of the following:

	Year Ended February 3, 2007	Year Ended January 28, 2006	Year Ended January 29, 2005
Federal – current	**$116.2**	$108.1	$75.8
State – current	**16.6**	14.7	16.5
Total current	**132.8**	122.8	92.3
Federal – deferred	**(19.1)**	(20.6)	15.9
State – deferred	**(2.8)**	(0.9)	(0.3)
Total deferred	**(21.9)**	(21.5)	15.6
Provision for income taxes	**$110.9**	$101.3	$107.9

A reconciliation of the statutory federal income tax rate and the effective rate follows:

	Year Ended February 3, 2007	Year Ended January 28, 2006	Year Ended January 29, 2005
Statutory tax rate	**35.0%**	35.0%	35.0%
Effect of:			
State and local income taxes, net of federal income tax benefit	**3.3**	3.4	3.6
Other, net	**(1.7)**	(1.6)	(1.1)
Effective tax rate	**36.6%**	36.8%	37.5%

The rate reduction in "other, net" in the above table consists primarily of benefits from the resolution of tax uncertainties, federal jobs credits and tax exempt interest in 2006, 2005 and 2004.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Deferred tax assets and liabilities are classified on the accompanying consolidated balance sheets based on the classification of the underlying asset or liability. Significant components of the Company's net deferred tax assets (liabilities) follows:

	February 3, 2007	January 28, 2006
Deferred tax assets:		
Accrued expenses	**$ 33.5**	$ 30.6
State tax net operating losses and credit carryforwards, net of federal tax benefit	**1.3**	—
Accrued compensation expense	**9.3**	1.0
Valuation allowance	**(1.3)**	—
Total deferred tax assets	**42.8**	31.6
Deferred tax liabilities:		
Intangible assets	**(9.2)**	(8.0)
Property and equipment	**(14.3)**	(34.9)
Prepaids	**(9.0)**	(1.2)
Other	**(1.1)**	(0.2)
Total deferred tax liabilities	**(33.6)**	(44.3)
Net deferred tax asset (liability)	**$ 9.2**	$(12.7)

A valuation allowance of $1.3 million, net of federal tax benefits, has been provided principally for certain state net operating losses and credit carryforwards. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred taxes will not be realized. Based upon the availability of carrybacks of future deductible amounts to the past two years' taxable income and management's projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not the remaining existing deductible temporary differences will reverse during periods in which carrybacks are available or in which the Company generates net taxable income.

During 2006, the Company concluded an examination with the Internal Revenue Service (IRS) for calendar year 1999 through fiscal year 2003. The results of the examination were immaterial to the financial statements. Fiscal year 2004 and forward are open for examination by the IRS. In addition, several years are open to state income tax audits. Management believes that adequate provisions have been made for any additional taxes and interest thereon that might arise as a result of future IRS and state examinations related to these open years.

NOTE 4 – COMMITMENTS AND CONTINGENCIES

Operating Lease Commitments

Future minimum lease payments under noncancelable stores and distribution center operating leases are as follows:

2007	$284.2
2008	246.0
2009	207.2
2010	161.5
2011	110.6
Thereafter	167.5
Total minimum lease payments	$1,177.0

The above future minimum lease payments include amounts for leases that were signed prior to February 3, 2007 for stores that were not open as of February 3, 2007.

Minimum rental payments for operating leases do not include contingent rentals that may be paid under certain store leases based on a percentage of sales in excess of stipulated amounts. Future minimum lease payments have not been reduced by expected future minimum sublease rentals of $2.3 million under operating leases.

Minimum and Contingent Rentals

Rental expense for store and distribution center operating leases (including payments to related parties) included in the accompanying Consolidated Statements of Operations are as follows:

	Year Ended February 3, 2007	Year Ended January 28, 2006	Year Ended January 29, 2005
Minimum rentals	**$261.8**	$225.8	$200.7
Contingent rentals	**0.9**	0.7	0.9

Non-Operating Facilities

The Company is responsible for payments under leases for certain closed stores. The Company was also responsible for payments under leases for two former distribution centers whose leases expired in June 2005 and September 2005. The Company accounts for abandoned lease facilities in accordance with SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. A facility is considered abandoned on the date that the Company ceases to use it. On this date, the Company records an expense for the present value of the total remaining costs for the abandoned facility reduced by any actual or probable sublease income. Due to the uncertainty regarding the ultimate recovery of the future lease and related payments, the Company recorded charges of $0.1 million, $0.3 million and $1.5 million in 2006, 2005 and 2004, respectively.

Related Parties

The Company also leases properties for six of its stores from partnerships owned by related parties. The total rental payments related to these leases were $0.5 million for each of the years ended February 3, 2007, January 28, 2006, and January 29, 2005, respectively. Total future commitments under related party leases are $1.4 million.

Freight Services

The Company has contracted outbound freight services from various contract carriers with contracts expiring through January 2010. The total amount of these commitments is approximately $57.1 million, of which approximately $38.6 million is committed in 2007, $9.9 million is committed in 2008 and $8.6 million is committed in 2009.

Technology Assets

The Company has commitments totaling approximately $3.8 million to purchase store technology assets for its stores during 2007.

Letters of Credit

In March 2001, the Company entered into a Letter of Credit Reimbursement and Security Agreement. The agreement provides $125.0 million for letters of credit. In December 2004, the Company entered into an additional Letter of Credit Reimbursement and

Security Agreement, which provides $50.0 million for letters of credit. Letters of credit under both of these agreements are generally issued for the routine purchase of imported merchandise and approximately $84.8 million was committed to these letters of credit at February 3, 2007.

The Company also has approximately $29.4 million in stand-by letters of credit that serve as collateral for its high-deductible insurance programs and expire in fiscal 2007.

Surety Bonds

The Company has issued various surety bonds that primarily serve as collateral for utility payments at the Company's stores. The total amount of the commitment is approximately $2.1 million, which is committed through various dates through fiscal 2008.

Contingencies

In 2003, the Company was served with a lawsuit in a California state court by a former employee who alleged that employees did not properly receive sufficient meal breaks and paid rest periods, along with other alleged wage and hourly violations. The suit requested that the California state court certify the case as a class action. This suit was dismissed with prejudice in May 2005, and the dismissal was appealed. A California appeals court granted the appeal and the Company's petition for review to the California Supreme Court was denied. The case has been remanded to the trial court's where it will likely be consolidated with a companion suit which had been filed in the same court following the trial courts earlier dismissal. It is anticipated that the plaintiff will seek class certification which the Company will oppose.

In 2005, the Company was served with a lawsuit by former employees in Oregon who allege that they did not properly receive sufficient meal breaks and paid rest periods. They also allege other wage and hour violations. The plaintiffs requested the Court to certify classes for their various claims and the presiding judge recently did so with respect to two classes, one alleging that our Oregon employees, in violation of that state's labor laws, were not paid for rest breaks and the other that upon termination of employment, employees were not tendered their final pay in a timely manner. Other claims of the plaintiffs were dismissed by an earlier Order of the Court and are being appealed by the plaintiffs. Discovery will ensue on the certified class issues; no trial is anticipated before the end of 2007.

In 2006, the Company was served with a lawsuit by a former employee in a California state court alleging that she was paid for wages with a check drawn on a bank which did not have any branches in the state, an alleged violation of the state's labor code; that she was paid less for her work than other similar employees with the same job title based on her gender; and that we did not pay her final wages in a timely manner, also an alleged violation of the labor code. The plaintiff requested the court to certify the case as a class action. The Company has been successful in removing the case from state to the federal court level. The parties have reached a settlement and executed an Agreement which will be presented to the Court for its approval on April 24, 2007. The estimated settlement amount has been accrued in the accompanying consolidated financial statements as of February 3, 2007.

In 2006, the Company was served with a lawsuit filed in federal court in the state of Alabama by a former store manager. She claims that she should have been classified as a non-exempt employee under the Fair Labor Standards Act and, therefore, should have received overtime compensation and other benefits. She filed the case as a collective action on behalf of herself and all other employees (store managers) similarly situated. The Company's motion requesting that the case be transferred from Alabama to Virginia was denied. The plaintiff now seeks entry of an Order allowing nationwide notice be sent to all store managers employed by the Company now or within the past three years. The Company is contesting entry of such an Order.

The Company will vigorously defend itself in these lawsuits. The Company does not believe that any of these matters will, individually or in the aggregate, have a material adverse effect on its business or financial condition. The Company cannot give assurance, however, that one or more of these lawsuits will not have a material adverse effect on its results of operations for the period in which they are resolved.

NOTE 5 – LONG-TERM DEBT

Long-term debt at February 3, 2007 and January 28, 2006 consists of the following:

(in millions)	**February 3, 2007**	January 28, 2006
$450.0 million Unsecured Revolving Credit Facility, interest payable monthly at LIBOR, plus 0.475%, which was 5.8% at February 3, 2007, principal payable upon expiration of the facility in March 2009	**$250.0**	$250.0
Demand Revenue Bonds, interest payable monthly at a variable rate which was 5.4% at February 3, 2007, principal payable on demand, maturing June 2018	**18.8**	19.0
Total long-term debt	**268.8**	269.0
Less current portion	**18.8**	19.0
Long-term debt, excluding current portion	**$250.0**	$250.0

Maturities of long-term debt are as follows: 2007 – $18.8 million and 2009 – $250.0 million.

Unsecured Revolving Credit Facility

In March 2004, the Company entered into a five-year Unsecured Revolving Credit Facility (the Facility). The Facility provides for a $450.0 million revolving line of credit, including up to $50.0 million in available letters of credit, bearing interest at LIBOR, plus 0.475%. The Facility also bears an annual facilities fee, calculated as a percentage, as defined, of the amount available under the line of credit and an annual administrative fee payable quarterly. The Facility, among other things, requires the maintenance of certain specified financial ratios, restricts the payment of certain distributions and prohibits the incurrence of certain new indebtedness. The Company used availability under the Facility to repay $142.3 million of variable-rate debt and to purchase short-term, state and local government-sponsored municipal bonds. The Company's $150.0 million revolving credit facility (Old Facility) was terminated concurrent with entering into the Facility. The net debt issuance costs related to the Old Facility and the variable-rate debt totaling $0.7 million, were charged to interest expense in 2004.

Demand Revenue Bonds

On May 20, 1998, the Company entered into an unsecured Loan Agreement with the Mississippi Business Finance Corporation (MBFC) under which the MBFC issued Taxable Variable Rate Demand Revenue Bonds (the Bonds) in an aggregate principal amount of $19.0 million to finance the acquisition, construction, and installation of land, buildings, machinery and equipment for the Company's distribution facility in Olive Branch, Mississippi. The Bonds do not contain a prepayment penalty as long as the interest rate remains variable. The Bonds contain a demand provision and, therefore, are classified as current liabilities.

NOTE 6 – DERIVATIVE FINANCIAL INSTRUMENTS

Non-Hedging Derivatives

At February 3, 2007, the Company was party to a derivative instrument in the form of an interest rate swap that does not qualify for hedge accounting treatment pursuant to the provisions of SFAS No. 133 because it contains a knock-out provision. The swap creates the economic equivalent of a fixed rate obligation by converting the variable-interest rate to a fixed rate. Under this interest rate swap, the Company pays interest to a financial institution at a fixed rate, as defined in the agreement. In exchange, the financial institution pays the Company at a variable interest rate, which approximates the floating rate on the variable-rate obligation, excluding the credit spread. The interest rate on the swap is subject to adjustment monthly. No payments are made by either party for months in which the

variable-interest rate, as calculated under the swap agreement, is greater than the "knock-out rate." The following table summarizes the terms of the interest rate swap:

Derivative Instrument	Origination Date	Expiration Date	Pay Fixed Rate	Knock-out Rate
$18.8 million swap	4/1/99	4/1/09	4.88%	7.75%

This swap reduces the Company's exposure to the variable-interest rate related to the Demand Revenue Bonds (see Note 5).

Hedging Derivative

The Company was party to one derivative instrument in the form of an interest rate swap that qualified for hedge accounting treatment pursuant to the provisions of SFAS No. 133.

In 2001, the Company entered into a $25.0 million interest rate swap agreement (swap) to manage the risk associated with interest rate fluctuations on a portion of the Company's variable interest entity debt. In March 2004, the Company repaid all of the variable interest entity debt with borrowings from the Facility (see Note 5). The Company redesignated this swap to borrowings under the Facility. This redesignation does not affect the accounting treatment used for this interest rate swap. The swap created the economic equivalent of fixed-rate debt by converting the variable-interest rate to a fixed-rate. Under this agreement, the Company paid interest to a financial institution at a fixed-rate of 5.43%. In exchange, the financial institution paid the Company at a variable-interest rate, which approximated the floating rate on the debt, excluding the credit spread. The interest rate on the swap was subject to adjustment monthly consistent with the interest rate adjustment on the debt. The swap expired in March 2006.

NOTE 7 – SHAREHOLDERS' EQUITY

Preferred Stock

The Company is authorized to issue 10,000,000 shares of Preferred Stock, $0.01 par value per share. No preferred shares are issued and outstanding at February 3, 2007 and January 28, 2006.

Net Income Per Share

The following table sets forth the calculation of basic and diluted net income per share:

(in millions, except per share data)	**Year Ended February 3, 2007**	Year Ended January 28, 2006	Year Ended January 29, 2005
Basic net income per share:			
Net income	**$192.0**	$173.9	$180.3
Weighted average number of shares outstanding	**103.2**	108.3	113.3
Basic net income per share	**$ 1.86**	$ 1.61	$ 1.59
Diluted net income per share:			
Net income	**$192.0**	$173.9	$180.3
Weighted average number of shares outstanding	**103.2**	108.3	113.3
Dilutive effect of stock options and restricted stock (as determined by applying the treasury stock method)	**0.6**	0.4	0.7
Weighted average number of shares and dilutive potential shares outstanding	**103.8**	108.7	114.0
Diluted net income per share	**$ 1.85**	$ 1.60	$ 1.58

At February 3, 2007, January 28, 2006 and January 29, 2005, respectively, 1.5 million, 3.4 million and 1.5 million stock options are not included in the calculation of the weighted average number of shares and dilutive potential shares outstanding because their effect would be anti-dilutive.

Comprehensive Income

The Company's comprehensive income reflects the effect of recording derivative financial instruments pursuant to SFAS No. 133. The following table provides a reconciliation of net income to total comprehensive income:

(in millions)	**Year Ended February 3, 2007**	Year Ended January 28, 2006	Year Ended January 29, 2005
Net income	**$192.0**	$173.9	$180.3
Fair value adjustment-derivative cash flow hedging instrument	**—**	0.6	1.0
Income tax expense	**—**	0.2	0.4
Fair value adjustment, net of tax	**—**	0.4	0.6
Amortization of SFAS No. 133 cumulative effect	**—**	—	—
Income tax benefit	**—**	—	—
Amortization of SFAS No. 133 cumulative effect, net of tax	**—**	—	—
Total comprehensive income	**$192.0**	$174.3	$180.9

The cumulative effect recorded in "accumulated other comprehensive income (loss)" is being amortized over the remaining lives of the related interest rate swaps.

Share Repurchase Programs

In March 2005, the Company's Board of Directors authorized the repurchase of up to $300.0 million of the Company's common stock through March 2008. During fiscal 2006, the Company repurchased 5,650,871 shares for approximately $148.2 million under the March 2005 authorization.

In November 2006, the Company's Board of Directors authorized the repurchase of up to $500.0 million of the Company's common stock. This amount was in addition to the $27.0 million remaining on the March 2005 authorization. In December 2006, the Company entered into two agreements with a third party to repurchase approximately $100.0 million of the Company's common shares under an Accelerated Share Repurchase Agreement (ASR).

The first $50.0 million was executed in an "uncollared" agreement. In this transaction the Company initially received 1,656,178 shares based on the market price of the Company's stock of $30.19 as of the trade date (December 8, 2006). A weighted average price is calculated using stock prices from December 16, 2006 – March 8, 2007. This represents the calculation period for the weighted average price. If the weighted average market price, as defined in the agreement, during the calculation period is greater than the $30.19 price per share, the Company will deliver to the third party cash or shares of Common Stock (at the Company's option) equal to the price difference. If the weighted average market price is less than $30.19 then the third party will deliver to Dollar Tree cash equal to the price difference. The weighted average market price of the Company's common stock through February 3, 2007 was $31.00. Therefore, if the transaction had settled on February 3, 2007, the Company would have had to return 43,207 shares to the third party which were included in the Company's weighted average dilutive potential common shares outstanding calculation. The weighted average stock price of the Company's common stock as defined in the "uncollared" agreement as of March 8, 2007 (termination date) was $32.17. The Company paid the third party an additional $3.3 million on March 8, 2007 for the 1,656,178 shares delivered under this agreement.

The remaining $50.0 million relates to a "collared" agreement in which the Company initially received 1,500,703 shares on December 8, 2006, representing the minimum number of shares under the agreement. The maximum number of shares that can be received under the agreement is 1,693,101. The number of shares is determined based on the weighted average market price of the Company's common

stock during the same calculation period as defined in the "uncollared" agreement. The weighted average market price through February 3, 2007 as defined in the "collared" agreement was $30.80. Therefore, if the transaction had settled on February 3, 2007, the Company would have received an additional 122,742 shares under the "collared" agreement. Based on the applicable accounting literature, these additional shares were not included in the weighted average diluted earnings per share calculation because their effect would be anti-dilutive. Based on the weighted average price as of February 3, 2007 of $30.80, there is approximately $3.8 million of the $50.0 million related to the "collared" agreement that is recorded as a reduction to stockholders' equity pending final settlement of the agreement. The weighted average stock price of the Company's common stock as defined in the "collared" agreement as of March 8, 2007 (termination date) was $31.97. The Company received an additional 63,525 shares on March 8, 2007 under this agreement.

NOTE 8 – EMPLOYEE BENEFIT PLANS

Profit Sharing and 401(k) Retirement Plan

The Company maintains a defined contribution profit sharing and 401(k) plan which is available to all employees over 21 years of age who have completed one year of service in which they have worked at least 1,000 hours. Eligible employees may make elective salary deferrals. The Company may make contributions at its discretion.

Contributions to and reimbursements by the Company of expenses of the plan included in the accompanying consolidated statements of operations were as follows:

Year Ended February 3, 2007	**$16.8 million**
Year Ended January 28, 2006	6.9 million
Year Ended January 29, 2005	8.5 million

Eligible employees hired prior to January 1, 2007 are immediately vested in the Company's profit sharing contributions. Eligible employees hired subsequent to January 1, 2007 vest in the Company's profit sharing contributions based on the following schedule:

- 25% after three years of service
- 50% after four years of service
- 100% after five years of service

All eligible employees are immediately vested in any Company match contributions under the 401(k) portion of the plan.

Deferred Compensation Plan

The Company has a deferred compensation plan which provides certain officers and executives the ability to defer a portion of their base compensation and bonuses and invest their deferred amounts. The plan is a nonqualified plan and the Company may make discretionary contributions. The deferred amounts and earnings thereon are payable to participants, or designated beneficiaries, at specified future dates, or upon retirement or death. Total cumulative participant deferrals were approximately $2.3 million and $2.0 million, respectively, at February 3, 2007 and January 28, 2006 and are included in "other liabilities" on the accompanying consolidated balance sheets. The related assets are included in "other assets, net" on the accompanying consolidated balance sheets. The Company made no discretionary contributions in the years ended February 3, 2007, January 28, 2006 and January 29, 2005.

NOTE 9 – STOCK-BASED COMPENSATION PLANS

At February 3, 2007, the Company has eight stock-based compensation plans. Each plan and the accounting method are described below.

Fixed Stock Option Compensation Plans

Under the Non-Qualified Stock Option Plan (SOP), the Company granted options to its employees for 1,047,264 shares of Common Stock in 1993 and 1,048,289 shares in 1994. Options granted under the SOP have an exercise price of $0.86 and are fully vested at the date of grant.

Under the 1995 Stock Incentive Plan (SIP), the Company granted options to its employees for the purchase of up to 12.6 million shares of Common Stock. The exercise price of each option equaled the market price of the Company's stock at the date of

grant, unless a higher price was established by the Board of Directors, and an option's maximum term is 10 years. Options granted under the SIP generally vested over a three-year period. This plan was terminated on July 1, 2003 and replaced with the Company's 2003 Equity Incentive Plan, discussed below.

The Step Ahead Investments, Inc. Long-Term Incentive Plan (SAI Plan) provided for the issuance of stock options, stock appreciation rights, phantom stock and restricted stock awards to officers and key employees. Effective with the merger with 98 Cent Clearance Center in December 1998 and in accordance with the terms of the SAI Plan, outstanding 98 Cent Clearance Center options were assumed by the Company and converted, based on 1.6818 Company options for each 98 Cent Clearance Center option, to options to purchase the Company's common stock. Options issued as a result of this conversion were fully vested as of the date of the merger.

Under the 1998 Special Stock Option Plan (Special Plan), options to purchase 247,500 shares were granted to five former officers of 98 Cent Clearance Center who were serving as employees or consultants of the Company following the merger. The options were granted as consideration for entering into non-competition agreements and a consulting agreement. The exercise price of each option equals the market price of the Company's stock at the date of grant, and the options' maximum term is 10 years. Options granted under the Special Plan vested over a five-year period. As of February 3, 2007, 240,000 of these options are still outstanding.

The 2003 Equity Incentive Plan (EIP) replaces the Company's SIP discussed above. Under the EIP, the Company may grant up to 6.0 million shares of its Common Stock, plus any shares available for future awards under the SIP, to the Company's employees, including executive officers and independent contractors. The EIP permits the Company to grant equity awards in the form of stock options, stock appreciation rights and restricted stock. The exercise price of each stock option granted equals the market price of the Company's stock at the date of grant. The options generally vest over a three-year period and have a maximum term of 10 years.

The 2004 Executive Officer Equity Plan (EOEP) is available only to the Chief Executive Officer and certain other executive officers. These officers no longer receive awards under the EIP. The EOEP allows the Company to grant the same type of equity awards as does the EIP. These awards generally vest over a three-year period, with a maximum term of 10 years.

Stock appreciation rights may be awarded alone or in tandem with stock options. When the stock appreciation rights are exercisable, the holder may surrender all or a portion of the unexercised stock appreciation right and receive in exchange an amount equal to the excess of the fair market value at the date of exercise over the fair market value at the date of the grant. No stock appreciation rights have been granted to date.

Any restricted stock or RSUs awarded are subject to certain general restrictions. The restricted stock shares or units may not be sold, transferred, pledged or disposed of until the restrictions on the shares or units have lapsed or have been removed under the provisions of the plan. In addition, if a holder of restricted shares or units ceases to be employed by the Company, any shares or units in which the restrictions have not lapsed will be forfeited.

The 2003 Non-Employee Director Stock Option Plan (NEDP) provides non-qualified stock options to non-employee members of the Company's Board of Directors. The stock options are functionally equivalent to such options issued under the EIP discussed above. The exercise price of each stock option granted equals the market price of the Company's stock at the date of grant. The options generally vest immediately.

The 2003 Director Deferred Compensation Plan permits any of the Company's directors who receive a retainer or other fees for Board or Board committee service to defer all or a portion of such fees until a future date, at which time they may be paid in cash or shares of the Company's common stock, or to receive all or a portion of such fees in non-statutory stock options. Deferred fees that are paid out in cash will earn interest at the 30-year Treasury Bond Rate. If a director elects to be paid in common stock, the number of shares will be determined by dividing the deferred fee amount by the current market price of a share of the Company's common stock. The number

of options issued to a director will equal the deferred fee amount divided by 33% of the price of a share of the Company's common stock. The exercise price will equal the fair market value of the Company's common stock at the date the option is issued. The options are fully vested when issued and have a term of 10 years.

Stock Options

In 2006, the Company granted a total of 342,216 stock options from the EIP, EOEP and the NEDP. For these options, the fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model and the fair value of these options of $3.4 million, net of expected forfeitures, is being recognized over the three-year vesting period of these options, or a shorter period based on the retirement eligibility of the grantee. All options granted to directors vest immediately and are expensed on the grant date. During 2006, the Company recognized $1.3 million of expense related to the 2006 option grants.

As of February 3, 2007, there was approximately $2.1 million of total unrecognized compensation expense related to these stock options which is expected to be recognized over a weighted average period of 26 months. The expected term of the awards granted was calculated using the "simplified method" in accordance with Staff Accounting Bulletin No. 107. Expected volatility is derived from an analysis of the historical and implied volatility of the Company's publicly traded stock. The risk free rate is based on the U.S. Treasury rates on the grant date with maturity dates approximating the expected life of the option on the grant date. For proforma disclosures required under FAS 123, the fair value of option awards in 2005 and 2004 was also calculated using the Black-Scholes option-pricing model. The weighted average assumptions used in the Black-Scholes option pricing model for grants in 2006, 2005 and 2004 are as follows:

	Fiscal 2006	Fiscal 2005	Fiscal 2004
Expected term in years	**6.0**	4.7	5.3
Expected volatility	**30.2%**	48.7%	59.8%
Annual dividend yield	**—**	—	—
Risk free interest rate	**4.8%**	3.7%	3.7%
Weighted average fair value of options granted during the period	**$10.93**	$11.27	$14.27
Options granted	**342,216**	320,220	1,682,572

The following tables summarize the Company's various option plans and information about options outstanding at February 3, 2007 and changes during the 53 weeks then ended.

Stock Option Activity

	February 3, 2007			
	Shares	**Weighted Average Per Share Exercise Price**	Weighted Average Remaining Term	Aggregate Intrinsic Value *(in millions)*
Outstanding, beginning of period	**5,990,757**	**$ 24.71**		
Granted	**342,216**	**27.67**		
Exercised	**(1,725,593)**	**21.70**		
Forfeited	**(141,339)**	**29.23**		
Outstanding, end of period	**4,466,041**	**$25.96**	5.6	$25.8
Options vested and expected to vest at February 3, 2007	**4,431,978**	**$25.95**	5.6	$25.7
Options exercisable at end of period	**4,126,874**	**$25.83**	5.3	$24.4

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Options Outstanding at February 3, 2007	Weighted Avg. Remaining Contractual Life	Weighted Avg. Exercise Price	Options Exercisable at February 3, 2007	Weighted Avg. Exercise Price
$0.86	7,264	N/A	0.86	7,264	0.86
$2.95 to $10.98	7,174	0.1	9.93	7,174	9.93
$10.99 to $21.28	777,807	5.1	19.18	777,807	19.18
$21.29 to $29.79	2,511,244	5.8	25.26	2,172,077	24.90
$29.80 to $42.56	1,162,552	5.0	32.26	1,162,552	32.26
$0.86 to $42.56	4,466,041			4,126,874	

The intrinsic value of options exercised during 2006, 2005 and 2004 was approximately $13.1 million, $2.8 million and $5.7 million, respectively.

Restricted Stock

The Company granted 277,347 and 252,936 RSUs, net of forfeitures in 2006 and 2005, respectively, from the EIP and the EOEP to the Company's employees and officers. The fair value of all of these RSUs of $13.9 million is being expensed ratably over the three-year vesting periods, or a shorter period based on the retirement eligibility of the grantee. The fair value was determined using the Company's closing stock price on the date of grant. The Company recognized $4.5 million of expense related to the RSUs during 2006. As of February 3, 2007, there was approximately $7.8 million of total unrecognized compensation expense related to these RSUs which is expected to be recognized over a weighted average period of 24 months. In 2005, the Company recognized approximately $1.6 million of expense for the RSUs granted in 2005.

In 2005, the Company granted 40,000 RSUs from the EOEP to certain officers of the Company, contingent on the Company meeting certain performance targets in 2005 and future service of these officers through various points through July 2007. The Company met these performance targets in fiscal 2005; therefore, the fair value of these RSUs of $1.0 million is being expensed over the service period. The fair value of these RSUs was determined using the Company's closing stock price January 28, 2006 (the last day of fiscal 2005), when the performance targets were satisfied. The Company recognized $0.3 million of expense related to these RSUs in 2006. The remaining $0.1 million will be recognized over the vesting periods through July 2007. In 2005, the Company recognized $0.7 million of expense for these RSUs.

In 2006, the Company granted 6,000 RSUs from the EOEP and the EIP to certain officers of the Company, contingent on the Company meeting certain performance targets in 2006 and future service of the these officers through fiscal 2006. The Company met these performance targets in fiscal 2006; therefore, the Company recognized the fair value of these RSUs of $0.2 million during fiscal 2006. The fair value of these RSUs was determined using the Company's closing stock price on the grant date in accordance with SFAS 123R.

The following table summarizes the status of RSUs as of February 3, 2007, and changes during the 53 weeks then ended:

	Shares	Weighted Average Grant Date Fair Value
Nonvested at January 28, 2006	295,507	$25.00
Granted	292,697	27.69
Vested	(106,547)	25.08
Forfeited	(24,880)	26.63
Nonvested at February 3, 2007	456,777	$26.57

In connection with the vesting of RSUs in 2006, certain employees elected to receive shares net of minimum statutory tax withholding amounts which totaled $1.0 million.

Employee Stock Purchase Plan

Under the Dollar Tree Stores, Inc. Employee Stock Purchase Plan (ESPP), the Company is authorized to issue up to 1,040,780 shares of common stock to eligible employees. Under the terms of the ESPP, employees can choose to have up to 10% of their annual base earnings withheld to purchase the Company's common stock. The purchase price of the stock is 85% of the lower of the price at the beginning or the end of the quarterly offering period. Under the ESPP, the Company has sold 917,883 shares as of February 3, 2007.

The fair value of the employees' purchase rights is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Fiscal 2006	Fiscal 2005	Fiscal 2004
Expected term	**3 months**	3 months	3 months
Expected volatility	**13.1%**	12.0%	15.6%
Annual dividend yield	**—**	—	—
Risk free interest rate	**4.8%**	3.9%	2.1%

The weighted average per share fair value of those purchase rights granted in 2006, 2005 and 2004 was $4.59, $4.11 and $4.93, respectively.

NOTE 10 – ACQUISITION

On March 25, 2006, the Company completed its acquisition of 138 Deal$ stores. These stores are located primarily in the Midwest part of the United States and the Company has existing logistics capacity to service these stores. This acquisition also includes a few "combo" stores that offer an expanded assortment of merchandise including items that sell for more than $1. Substantially all Deal$ stores acquired will continue to operate under the Deal$ banner while providing the Company an opportunity to leverage its Dollar Tree infrastructure in the testing of new merchandise concepts, including higher price points, without disrupting the single-price point model in its Dollar Tree stores.

The Company paid approximately $32.0 million for store-related and other assets and $22.1 million for inventory. This amount includes approximately $0.6 million of direct costs associated with the acquisition. The results of Deal$ store operations are included in the Company's financial statements since the acquisition date and did not have a significant impact on the Company's operating results in 2006. This acquisition is immaterial to the Company's operations as a whole and therefore no proforma disclosure of financial information has been presented. The following table summarizes the allocation of the purchase price to the fair value of the assets acquired.

(in millions)	
Inventory	$22.1
Other current assets	0.1
Property and equipment	15.1
Goodwill	14.6
Other intangibles	2.2
	$54.1

The goodwill resulting from this acquisition will not be amortized but will be tested annually for impairment. Included in other intangibles is approximately $2.1 million related to net favorable lease rights for operating leases for retail locations. This amount is being amortized on a straight-line basis to rent expense over 35 months, the weighted average remaining initial lease term of the locations purchased.

NOTE 11 – INVESTMENT

In 2003, the Company paid $4.0 million to acquire a 10.5% fully diluted interest in Ollie's Holdings, Inc. (Ollie's), a multi-price point discount retailer located in the mid-Atlantic region. In addition, the SKM Equity Fund III, L.P. (SKM Equity) and SKM Investment Fund (SKM Investment) acquired a combined fully diluted interest in Ollie's of 53.1%. Two of the Company's directors, Thomas Saunders and John Megrue, are principal members of SKM Partners, L.L.C., which serves as the general partner

of SKM Equity. John Megrue is also a principal member of Apax Partners, L.P., which serves as the general partner for SKM Investment. The $4.0 million investment in Ollie's is accounted for under the cost method of accounting and is included in "other assets" in the accompanying consolidated balance sheets.

NOTE 12 – SUBSEQUENT EVENT

On March 29, 2007, the Company entered into an agreement with a third party to repurchase approximately $150.0 million of the Company's common shares under an Accelerated Share Repurchase Agreement. The entire $150.0 million was executed under a "collared" agreement. Within two weeks of the March 29, 2007 execution date, the Company will receive the minimum number of shares. Up to four months after the initial execution date, the Company will receive additional shares from the third party depending on the volume weighted average price of the Company's common shares during that period, subject to the maximum share delivery provisions of the agreement.

NOTE 13 – QUARTERLY FINANCIAL INFORMATION (Unaudited)

The following table sets forth certain items from the Company's unaudited Consolidated Statements of Operations for each quarter of fiscal year 2006 and 2005. The unaudited information has been prepared on the same basis as the audited consolidated financial statements appearing elsewhere in this report and includes all adjustments, consisting only of normal recurring adjustments, which management considers necessary for a fair presentation of the financial data shown. The operating results for any quarter are not necessarily indicative of results for a full year or for any future period.

	First Quarter(1)	Second Quarter	Third Quarter	Fourth Quarter(2)
Fiscal 2006:				
Net sales	**$856.5**	**$883.6**	**$910.4**	**$1,318.9**
Gross profit	**286.1**	**293.3**	**307.5**	**470.3**
Operating income	**53.5**	**48.2**	**53.5**	**155.6**
Net income	**32.9**	**29.0**	**32.5**	**97.6**
Diluted net income per share	**0.31**	**0.28**	**0.32**	**0.96**
Stores open at end of quarter	**3,119**	**3,156**	**3,192**	**3,219**
Comparable store net sales change	**4.0%**	**4.2%**	**4.0%**	**5.5%**
Fiscal 2005:				
Net sales	$749.1	$769.0	$796.8	$1,079.0
Gross profit	254.2	261.5	276.3	380.4
Operating income	48.2	46.8	52.3	136.6
Net income	29.0	27.3	31.1	86.5
Diluted net income per share	0.26	0.25	0.29	0.81
Stores open at end of quarter	2,791	2,856	2,899	2,914
Comparable store net sales change	(3.7%)	(1.5%)	(1.0%)	1.0%

(1) Easter was observed on April 16, 2006 and March 27, 2005.

(2) Fiscal 2006 contains 14 weeks ended February 3, 2007 while Fiscal 2005 contains 13 weeks ended January 28, 2006.

BOARD OF DIRECTORS

Macon F. Brock, Jr., *Chairman*
Mary Anne Citrino
H. Ray Compton
Richard G. Lesser
John F. Megrue
J. Douglas Perry, *Chairman Emeritus*
Bob Sasser
Thomas A. Saunders, III
Eileen R. Scott
Thomas E. Whiddon
Alan L. Wurtzel

OFFICERS

Bob Sasser,
President and Chief Executive Officer

Kent A. Kleeberger,
Chief Financial Officer

James E. Fothergill,
Chief People Officer

James A. Gorry, III,
General Counsel and Corporate Secretary

Raymond K. Hamilton,
Chief Information Officer

Gary M. Philbin,
Chief Operating Officer

Arvil L. Priode,
Senior Vice President, Merchandise Planning and Control

Robert H. Rudman,
Chief Merchandising Officer

Michael A. Saltzer,
Senior Vice President, New Business Development

Stephen W. White,
Chief Logistics Officer

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INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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Norfolk, VA 23510

STOCK LISTING

Dollar Tree's common stock has been traded on the NASDAQ Stock Market under the symbol "DLTR" since our initial public offering on March 6, 1995.

The following table gives the high and low sales prices of our common stock for the fiscal years 2006 and 2005.

STOCK PRICE

	HIGH	LOW
2006		
First Quarter	**$28.68**	**$24.34**
Second Quarter	**27.89**	**23.90**
Third Quarter	**32.00**	**25.62**
Fourth Quarter	**32.78**	**29.34**
2005		
First Quarter	$29.04	$23.95
Second Quarter	26.01	22.77
Third Quarter	25.65	20.56
Fourth Quarter	25.48	20.66

ANNUAL MEETING

You are cordially invited to attend our Annual Meeting of Shareholders, which will be held at 10:00 a.m. on Thursday, June 21, 2007, at the Princess Anne Country Club, 3800 Pacific Avenue, Virginia Beach, Virginia.

FISCAL 2007 EARNINGS RELEASE CALENDAR*

First quarter: May 30
Second quarter: August 29
Third quarter: November 28
Fourth quarter: February 27, 2008
** Dates are subject to change.*

INVESTORS' INQUIRIES

Requests for interim and annual reports, Forms 10-K, or more information should be directed to:

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500 Volvo Parkway
Chesapeake, VA 23320
(757) 321-5000

Or from our company web site:
www.DollarTree.com

THERE'S PLENTY OF RUNWAY AHEAD.

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