

# FINAL TRANSCRIPT

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## **RCII - Q1 2007 Rent-A-Center Earnings Conference Call**

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## CORPORATE PARTICIPANTS

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**Mitch Fadel**

*Rent-A-Center - President, COO*

**Robert Davis**

*Rent-A-Center - SVP-Fin. CFO*

**Mark Speese**

*Rent-A-Center - Chairman, CEO*

## CONFERENCE CALL PARTICIPANTS

**Arvind Bhatia**

*Sterne Agee - Analyst*

**Jeff Schollaert**

*Wachovia Securities - Analyst*

**John Baugh**

*Stifel Nicolaus - Analyst*

**Unidentified Participant**

*- Analyst*

**Justin Boisseau**

*Gates Capital Management - Analyst*

**Carla Casella**

*JPMorgan - Analyst*

**Robert Straus**

*Merriman Curhan Ford - Analyst*

## PRESENTATION

**Operator**

Good morning and thank you for holding, welcome to Rent-A-Center's first quarter 2007 earnings release conference call. (OPERATOR INSTRUCTIONS) As a reminder, this conference is being recorded Tuesday, May 1, 2007. Your speakers today are Mr. Mark Speese, Chairman and Chief Executive Officer of Rent-A-Center; Mr. Mitch Fadel, President and Chief Operating Officer; Mr. Robert Davis, Chief Financial Officer; and Mr. David Carpenter, Vice President of Investor Relations.

I would now like to turn the conference over to Mr. Carpenter. Please go ahead, sir.

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**David Carpenter** - *Rent-A-Center - VP, IR*

Thank you. Good morning, everyone, and thank you for joining us. You should have received a copy of the earnings release distributed after the market close yesterday that outlines our operational and financial results that were made in the first quarter of 2007. If for some reason you did not receive a copy of the release, you can download it from our website at investor.rentacenter.com. In addition, certain financial and statistical information that will be discussed during the conference call will also be provided on the same website. Also in accordance with SEC rules concerning non-GAAP financial measures, the reconciliation of EBITDA is provided in our earnings press release under the statement of earnings highlights.

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Finally, I must remind you that some of the statements made in this call, such as forecast growth in revenues, earnings, operating margins, cash flow, and profitability and other business or trend information are forward-looking statements. These matters are of course subject to many factors that could cause actual results to differ materially from our expectations reflected in the forward-looking statements. These factors are described in our most recent annual report on Form 10-K for the year ended December 31, 2006 as filed with the SEC. Rent-A-Center undertakes no obligation to publicly update or revise any forward-looking statements. In addition, I would ask for your patience during the call because we are communicating from two locations. Our headquarters in Plano, Texas and also New York City. Mark and Robert are attending the Lehman Brother's retail conference at the St. Regis hotel in New York City. By the way, they will be presenting at 1:45 p.m. Eastern standard time and you can access the audio information -- audio of the presentation from a link on our investor relations website at investor.rentacenter.com. Now I'd now like to turn the call over to Mitch. Mitch?

**Mitch Fadel** - Rent-A-Center - President, COO

Thanks, Dave. Good morning, everyone, and thanks for joining us on our first quarter earnings call. The quarter turned out to be a very good one for us operationally as we achieved 2.9% same store sales, which was primarily driven by having more units on rent and more customers on rent. Certainly an indication that demand for our product and services is good. We believe that demand is being driven by a number of factors, including the impact of advertising changes that we made over the last couple of years. The inclusion of home packages into our lineup, the new flat panel electronics technology, our competitive price match program, just to name a few.

On the collections front, we remain very consistent with past performance, our delinquency numbers and our chargeoff numbers remain consistent with historical and expected ranges. Our inventory levels also remain consistent with our expectations, this inventory held for rent was at 21.4% within the expected range of 20 to 24. It didn't end up as low as last year's first quarter, but again, as we talked about in the last call, that was expected due to the Rent-Way acquisition and the additional inventory acquired in that transaction. So within our range, not quite as low as first quarter last year, but right where we expected it to be.

Speaking of Rent-Way, as we've said in the past, the Rent-Way acquisition that was closed last November has gone well as the integration has essentially been completed. And we continue to be pleased with the improving performance of those stores. And we're on track to achieving the accretion that we previously announced from that acquisition. The co-workers of Rent-Way have blended well with the Rent-A-Center folks. And it's now a matter of continuing to execute our business model to enhance the revenue and profitability of those acquired stores.

In summary, our core business is performing well. The Rent-Way integration is complete and going well. Our 20,000 co-workers have done a tremendous job in executing our plan and allowing us to report such a positive quarter. And for that, I want to thank each and every one of those co-workers on a job very well done. With that I'll turn it over to Robert for a financial

**Robert Davis** - Rent-A-Center - SVP-Fin. CFO

Thank you, Mitch. I'm going to spend just a few quick moments here updating you on a few of our financial highlights that we achieved during the quarter and then I'll turn the call over to Mark.

As always, I'd like to reiterate that much of the information that I present today whether it's historical results, or forecasted results, I'm going to present on a recurring and comparable basis, which in this case will exclude the Perez matter discussed in the press release issued after market close last evening. So really just focusing on operating results.

As outlined in the press release, total revenues during the first quarter did increase 24.4% with net earnings and diluted earnings per share increasing 17.4% and 15.8% respectively to \$47.3 million in net earnings and \$0.66 in diluted earnings per share. Our EBITDA increased 31.8% from the prior year to \$118.4 million. The margin increased 90 basis points to 15.7%. This translated

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into the generation of over \$86 million in operating cash flow during the first quarter. And as a result, we were able to reduce our outstanding indebtedness since year-end by over \$77 million. This combination of increased EBITDA and the reduction in our debt balance has allowed us to report a consolidated leverage ratio below 3 times to 2.82 times.

We do continue to expect over \$200 million in operating cash flow and roughly \$140 million in free cash flow for the entire year of 2007 before the potential funding of the Perez matter. Our quarter ending cash balance was just over \$80 million and our debt to book cap at quarter end equated to 55%, a 300 basis point reduction since year end. At the quarter end, our debt levels were approximately \$916 million in senior term debt and \$300 million in the 7.5% subordinated notes. However, there's over \$300 million in capacity within our revolver and line of credit. It was undrawn at the end of the quarter.

In terms of guidance, going forward, we do anticipate for the second quarter total revenues to range between 719 and \$734 million on same store sales of between a positive 0.5% and 2% with diluted earnings per share ranging between \$0.57 and \$0.63. For the full fiscal year ending 12/31, we expect total revenues between 2.915 and \$2.955 billion. And same store sales between a positive 1 and a positive 2%. Additionally we're projecting 2007 EBITDA of approximately \$430 million and a margin around 14.5%. Diluted earnings per share are estimated to be in the range of \$2.24 and \$2.32.

Now although we're not changing our annual EPS forecast at this point in time I would like to mention that we currently believe the consensus estimates that the analysts have out there of \$0.48 for the third quarter of this year, which as always is traditionally our seasonally slowest to us looked to be about \$0.03 to \$0.05 too high. You may recall last quarter we discussed the fact that the third quarter of fiscal 2006 included an extra Saturday, which masked the seasonality we typically experience in the summer. Since there won't be an extra Saturday in the third quarter of this year, we do expect to see that seasonal dip in revenue and earnings. Again, we're not changing our annual guidance, however, based on our current expectations, I would encourage the spreads and consensus EPS estimates over the course of the next three quarters to be adjusted according to the guidance provided. This current guidance excludes any potential benefits associated with potential future stock repurchases or acquisitions completed after the date of this press release. With that update, I'm going to turn the call over to Mark now.

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**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Robert, thank you very much. Mitch also. Good morning, everyone. I certainly appreciate your time and interest in joining us this morning. First, let me add how pleased I am with the overall operating performance. As you heard from Mitch, the core business continues to perform well. And as he also discussed, the integration of Rent-Way has gone quite smoothly also. I'm very proud of the hard work and cooperation of all of our coworkers in making this a smooth integration. As Mitch mentioned we are on track to realize the results that we previously discussed concerning those stores and believe that the core stores are well-positioned also. So a very good start to the year for us.

With regards to the financial services business, as I mentioned during our last call, we were going to slow down the growth in January and February due to the acquisition of Rent-Way as well as the seasonally weaker demand during that time and take that time to strengthen our bench and fine tune some of our processes. I believe that proved to be fruitful for us. As we've gained more experience, developed additional training, and personnel and fine tuned the process, we're beginning to see the impact of that. We did open 29 locations in the quarter and have opened an additional 27 thus far this quarter and the results of those stores have been favorable. Having said that, I do want to remind you we expect the financial services piece to be a drag on our earnings this year as we continue the ramp-up. As a whole remain very optimistic about that business and believe that we'll achieve our goal of adding additional -- 200 or so stores this fiscal year.

Let me spend a few minutes, if I may, and talk about the perspective settlement of the Perez litigation in New Jersey. As we announced yesterday, the Company has reached an agreement in principle to settle the class claims in the Perez case. You may recall upon the original filing of this case four years ago, the trial court in that matter dismissed the case and the appellate court in New Jersey affirmed that decision. Unfortunately, the New Jersey Supreme Court disagreed. As you may also recall, New

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Jersey is one of the few states in which there is not existing own legislation. Of course, once we received the Supreme Court ruling, we changed our business practices in New Jersey in a way which we believe is in compliance with New Jersey law.

We did ask the United States Supreme Court to review the New Jersey Supreme Court's decision. In January of this year, that request was denied. And so the case was sent back to the trial court for additional proceedings. The Company made the decision to enter into this prospective settlement after consideration of the relative strengths and weaknesses of the plaintiff's claims and our defenses. As well as the range of potential risk and foreseeable outcomes as well as the time and resources required to fully litigate this matter.

Now, the significant terms of the prospective settlement are set forth in the press release while that settlement is subject to the parties entering into definitive documentation with the plaintiffs as well as obtaining court approval, we believe that this settlement is fair and in the best interest of the Company and its stockholders. We believe that this prospective settlement resolving the Perez claims in total should allow the Company to move forward without this cloud of uncertainty. Again, we believe it is the right thing to do. We're pleased to have the matter at this stage and are looking forward to bringing it to final resolution. Having said that, again let me reiterate how pleased I am with the overall business, the integration of Rent-Way, and our current position as we enter the second quarter. As always, we appreciate your support, and we're happy to open the call up now for questions.

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## QUESTIONS AND ANSWERS

### Operator

(OPERATOR INSTRUCTIONS) And our first question comes from the line of Arvind Bhatia of Sterne Agee.

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**Arvind Bhatia** - *Sterne Agee - Analyst*

Morning, guys.

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**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Morning, Arvind.

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**Arvind Bhatia** - *Sterne Agee - Analyst*

First question is on the margin side looking at the salaries and expenses, other expense line. Looks like you guys took that up a little bit. I'm wondering if that's based on added expenses because of Rent-Way or is there something else going on there?

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**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

No, Arvind, that has a little bit to do with the ramp-up in the financial services -- if you'll notice also our revenue guidance is down a little bit on the total revenue side, although rental and fee revenue is actually increased in the guidance. And so that total revenue that's come down from the year from the original guidance we gave last quarter, that's what's causing the margin difference on the guidance for salaries and other.

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**Mitch Fadel** - Rent-A-Center - President, COO

Again, though, Robert -- Arvind, this is Mitch. Again, the rental and fee is actually up from prior guidance, but the overall is down a little bit on the slow down -- excuse me the ramp-up of financial services, but also the -- we're seeing less sales. So that's taking the less sales in stores, that's for those early payouts.

**Arvind Bhatia** - Sterne Agee - Analyst

Right.

**Mitch Fadel** - Rent-A-Center - President, COO

Which they're not high margin as you know, so it's not affecting the EPS. But it affects the overall revenue number, which affects that percentage a little bit. Not affecting the bottom line, but affecting some of those percentages because there's less dollars even though they're not high margin dollars on those EPOs. But rental and fee, the actual forecast is up in rental and fee. The core part of the business.

**Arvind Bhatia** - Sterne Agee - Analyst

Got it. And then given the seasonality that you just mentioned on the third quarter and then your same store sales guidance of 1 to 2% for the year, you obviously did better than that in the first quarter, better than certainly we were looking for. Help us with some trends that you expect on the same store sales front in the second and third quarters. Perhaps how the seasonality would play out in that line.

**Robert Davis** - Rent-A-Center - SVP-Fin. CFO

Well, I think, Arvind, obviously the first quarter 2.9% the guidance we gave for the second 0.5 to 2.0 given the third quarter this year we've got the comp against the extra Saturday last third quarter. So we would expect the comp in the third quarter this year to be probably negative to flat a little bit. And then coming back in the fourth quarter to allow us to report that 1 to 2% comp for the year.

**Arvind Bhatia** - Sterne Agee - Analyst

Got it. In your comments, Robert, you mentioned your guidance excludes any stock buybacks. Can you -- I know you've been -- historically you guys have obviously been aggressive buyers of your own stock. Just kind of help us on your thinking currently paying down debt versus stock repurchases?

**Robert Davis** - Rent-A-Center - SVP-Fin. CFO

Yes, I mean obviously with the acquisition of Rent-Way at the end of the year, we added \$600 million of debt. Thought that was the best way to finance that transaction. And given the investment in that business as well as the ramp-up of financial services, have not been deploying our capital to repurchase shares as aggressively as we had been in the past. We've still got about \$40 million roughly in authorization from our Board approval, which that can be changed fairly easily. The bank and bond indenture documents I think it's well over \$100 million in authorization. And so there's really not a limitation on us other than making sure we're deploying our capital in the right way. And coming off the acquisition in the fourth quarter, we had a leverage ratio of around 3 times, there's some benefit to us from a debt perspective to get that below 3 times from a spread perspective on the term A, which is about \$200 million. And our comfort zone historically 2.0 to 2.5 times leverage, that's kind of where we would

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like to see ourselves get back to. We're not uncomfortable with where we are today, but just feel like in the near term we want to try to delever a little bit and then evaluate on a go forward basis whether stock repurchases make sense.

**Arvind Bhatia** - *Sterne Agee - Analyst*

Great. That's all I had, good quarter, thanks.

**Mitch Fadel** - *Rent-A-Center - President, COO*

One more thing. Just to reiterate what Robert was saying about the comp. You see the 2.9 the good first quarter and the guidance for the second quarter, that third quarter being flat in that area, flat is again, because we're comping over a quarter last year, they had an extra Saturday, not that we would expect any slow down in the business. That's not an indication we would expect demand to be any slower than normal in the summer quarter. It's just comping over that Saturday. We'll make that number the lowest of the year. But still obviously we would expect the year to be in that 1 to 2% range. It's not that that we expect a slow down, it's just that calendar shift.

**Arvind Bhatia** - *Sterne Agee - Analyst*

Got it.

**Operator**

Our next question comes from Jeff Schollaert of Wachovia Securities.

**Jeff Schollaert** - *Wachovia Securities - Analyst*

Great. Thanks. A couple questions. I was hoping first you could quantify the EPS benefit in Q3 from last year of that extra Saturday?

**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

It's about -- it's about last year would have been about \$12 million in revenue or \$8 million in gross profit, which equates to if you tax effected--.

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

You also have some expense against that because of an extra business day. From a comp perspective, that Saturday is worth a couple percent anyways.

**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

Yes. Yes, 2 to 2.5--.

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

\$0.04 or \$0.05, probably.

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**Mitch Fadel** - Rent-A-Center - President, COO

Yes, Mark, it's 2 to 2.5% on the comp that extra Saturday. By the time that floats to the bottom line with 40 to 50% pull through, you're talking in that \$0.04 to \$0.05 range. And that's why as Robert was pointing out, that's probably why the estimate seemed \$0.03 to \$0.05 high to us in the third quarter.

**Jeff Schollaert** - Wachovia Securities - Analyst

Okay. Great. That's helpful. That's very helpful. And then also I was hoping you could quantify some of the delinquencies and charge-off numbers?

**Mitch Fadel** - Rent-A-Center - President, COO

Yes, as you probably know, Jeff, our goal is on a weekly basis to be at 5.9%, 5.99 or less on a weekly close. That's accounts that are one day or more past due, and we're right on top of that in the first quarter. And the charge-offs, our historical range, if you look at a K, I don't know, Dave since we've been filing it's been between 2.3 and 2.5% for skips and stolen. And on an annual basis and in the first quarter we're right in that range.

**Jeff Schollaert** - Wachovia Securities - Analyst

Okay. Great. And then how are the collections coming on the Rent-Way stores?

**Mitch Fadel** - Rent-A-Center - President, COO

They're just about in line with the Rent-A-Center stores. We've got them down. As you probably recall, Jeff, they were run higher than us, their business model was a little different. But they are just -- almost all of their metrics are just about right in line with a core Rent-A-Center store with the exception of volume that will come up over the next couple of years. And as I said earlier, we're pleased with the progress we've made so far. Their metrics are just about right on top of the Rent-A-Center metrics at this point.

**Jeff Schollaert** - Wachovia Securities - Analyst

Okay. Great. That sounds like it's a little bit sooner than you had initially expected.

**Mitch Fadel** - Rent-A-Center - President, COO

Well, it's gone well. It certainly has gone well. As I mentioned earlier, the coworkers have blended well with the Rent-A-Center coworkers. And in general, we've done quite a few acquisitions, this one has gone as well as any.

**Jeff Schollaert** - Wachovia Securities - Analyst

Thank you.

**Operator**

Our next question comes from John Baugh of Stifel Nicolaus.



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**John Baugh** - *Stifel Nicolaus - Analyst*

Thank you. Good quarter, guys. Couple three things. One, can you update us on the number of Rent-Way stores at this point that have been closed? And how many more roughly are to go?

**Mitch Fadel** - *Rent-A-Center - President, COO*

Yes, Dave, do you have that? I don't have it in front of me.

**David Carpenter** - *Rent-A-Center - VP, IR*

We have consolidated approximately 20% of the original 782 stores.

**Mitch Fadel** - *Rent-A-Center - President, COO*

And there may be a few more, but there's not many. There may just be a few more trickling in, John.

**John Baugh** - *Stifel Nicolaus - Analyst*

So you're largely done there. Just CapEx number for the year and the expectations for the sort of change in working capital will come out the inventory purchase versus written off and payables, all that?

**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

Yes, the CapEx number for the year we're estimating to be around 75 million. That's why when I was given the over \$200 million of operating cash, you back out \$75 million you're in that 130, \$140 million of free cash flow range. In terms of working capital investment, we're thinking around \$60 million. So starting out with EBITDA, if you want to kind of reconcile the \$430 million of EBITDA, you're going to have about \$85 million of interest expense, \$75 million in CapEx, \$60 million in working capital, inventory investment and so forth, \$65 million roughly in cash taxes to get you down about \$145 in free cash flow.

**John Baugh** - *Stifel Nicolaus - Analyst*

Great. That's very helpful. Thank you. And the \$109 million, I guess all in for the Perez case. That's cash that goes out somewhere in the remainder of calendar '07?

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Yes, John, this is Mark. Well, again, where we are right now it's a prospective settlement over the next 30 or 60 days get to a definitive documentation if you will. That will have to be taken to the court for approval, assuming, in fact all of that plays around the time frame that we would expect it to. I would anticipate that sometime in this fall that the -- that we would fund that settlement.

**John Baugh** - *Stifel Nicolaus - Analyst*

Okay. And is there any experience historically with how many people won't join the Class Action and therefore how much of that refund if you will you'll get of the 50% at least? Is there any--?

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**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Well, each one's a little different. And it's very difficult to estimate. I don't anticipate that they'll be frankly, a significant amount, but certainly we set the ceiling if you will, at the 109 and again, as was noted in the press release, there is a reversion 50/50. What that might equate to frankly, is hard to estimate at this point. I wouldn't, my expectation wouldn't be for a significant amount anyways. Be Pretty small I suspect.

**John Baugh** - *Stifel Nicolaus - Analyst*

And two last things, they may relate to Rent-Way, I don't know, but on the, as you touched on the inventory held for rent was higher than a year ago, but certainly well within your ranges. Discuss how the Rent-Way moved that number and then your thoughts sort of going forward on that number. And also on the cost of rentals, the fees, or the I guess the appreciation line. It looks to be running slightly below where I thought it would be whether that's Rent-Way related or something else.

**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

Okay, John, on the inventory held for rent. The way Rent-Way would affect that is a couple of ways, two ways, two main ways. One, the 160 or so consolidations. You've got two stores worth of inventory to work through. When you consolidate, and you know that we expect a loss of revenue when we consolidate. But you've still got to work through the inventory. You have got some extra inventory from that. And also in general, the inventory held for rent in a Rent-Way store was about the same dollar amount as a Rent-A-Center store. But as you know, the revenue was significantly less instead of about \$70,000 a month in revenue, they averaged about \$55,000 a month in rent. So the inventory on rent numbers lower because the stores aren't as big, but the inventory held for rent number is about the same as the Rent-A-Center stores. Until we get the inventory on rent up to the Rent-A-Center level, then it'll affect the percentage negatively, right. When you blend in stores that have a higher percentage because, again, not so much they have more inventory, but they have less on rent so it's a higher percentage. That and the consolidations are the two ways they affect that.

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

As well as the fact that we ordered a fair amount of our new products in December, as well as January February to start introducing them into their line-up.

**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

Correct.

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Even on top of what they already had. I don't know if anybody can quantify what that would have been otherwise, i.e. could that 21.4 have been 20% if it was the Rent-A-Center stand alone? I don't know that it--?

**Mitch Fadel** - *Rent-A-Center - President, COO*

Well, certainly when you have a range 20 to 24, and it comes in at 21.4, we're very comfortable with what it is.

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**John Baugh** - *Stifel Nicolaus - Analyst*

Yes, that's helpful color. That's very helpful, thank you. And then just lastly on that 21.6 to 22.0 guidance on the rental and fee cost. Is that influenced in any way by Rent-Way?

**Mitch Fadel** - *Rent-A-Center - President, COO*

No, I wouldn't say so, John. It's been -- or margins have been pretty strong. Last year we talked a lot about being less promotional. And when there's less -- when you're giving away less free time, the margins get a little better. So I think it's more that than anything to do with Rent-Way.

**John Baugh** - *Stifel Nicolaus - Analyst*

Great. Thank you, much.

**Operator**

Our next question comes from Susan Jansen of Lehman Brothers.

**Unidentified Participant** - *Analyst*

Yes, real quickly I wanted to ask a question about in terms of the financial services stores. The ones located within the rent to own stores, have you seen any additional comp from the financial services being located in those stores? Or are they operating on a comparable level?

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

All of the financial service stores that we're introducing are in fact going inside the existing four walls of a Rent-A-Center.

**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

I think it had a -- correct me if I'm wrong, Dave, I think it had a 0.3% impact on the quarter?

**David Carpenter** - *Rent-A-Center - VP, IR*

Yes, it had a slight impact.

**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

So the 2.9 would have been 2.6, 2.7 otherwise.

**Unidentified Participant** - *Analyst*

All right.

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**Robert Davis** - *Rent-A-Center - SVP-Fin. CFO*

The comp is being positively impacted by the financial services, which we knew all along.

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Certainly it's helping those stores that has it.

**Unidentified Participant** - *Analyst*

All right. Thank you very much, guys.

**Operator**

(OPERATOR INSTRUCTIONS) And our next question comes from Justin Boisseau of Gates Capital Management.

**Justin Boisseau** - *Gates Capital Management - Analyst*

Hi, thanks. I was wondering if you could talk a little bit about the legislative environment in New York State with the recent law they've introduced given the outcome from the Perez case is perhaps worse than originally expected?

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Well, again, I would remind everybody that New Jersey never had legislation. So certainly different. New York has like many, most of the other states does, in fact, have enabling legislation as we speak. And what you're referring to was a proposal of essentially changing the law that's already in place. That has happened in the past. And we take each one of those seriously. We don't think, frankly, that the likelihood of that happening is, I would view it as remote. We certainly again take it seriously. But the fact is we've got legislation that was introduced years ago in that state and again, most of these others supported on both sides of the isle and obviously in both houses, that has brought in fair and protective legislation to both the consumers and the businesses. And the likelihood of that being changed, even in light of New Jersey, and again, we're very cognizant of it, but I view it somewhat as a remote probability.

**Mitch Fadel** - *Rent-A-Center - President, COO*

As you mentioned, Mark, it has been proposed before New York.

**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Yes.

**Mitch Fadel** - *Rent-A-Center - President, COO*

Over the last few years, maybe the last 6 or 7 years. And it's never--.

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**Mark Speese** - *Rent-A-Center - Chairman, CEO*

Not gone anywhere.

**Mitch Fadel** - *Rent-A-Center - President, COO*

Nothing's been overturned in New York as in any other state in the country. No favorable rent to own laws have ever been overturned. As I said, New York has been this is the sixth or seventh year in a row that someone's proposed legislation that would hurt the business side of it and certainly the consumer side if it took an option away. It's never gone anywhere in the last 6 or 7 years we wouldn't expect that to happen this year just like it's never happened in any other state.

**Justin Boisseau** - *Gates Capital Management - Analyst*

And then, you mentioned that the revenue guidance for the year was coming down because of some softer merchandise sales than maybe you expect. What do you think is driving that?

**Mitch Fadel** - *Rent-A-Center - President, COO*

Well, Justin, the -- again it's not so much merchandise -- it's early purchase options from our customer that goes into our sales category. And it's actually a good thing for that to be lower because it's the lowest margin side of the business. But what's driving it is just the fact that bouncing off of a couple of years of negative comps, at least 6 or 7 quarters of negative comps until -- of course the last 5 have been positive. Our consumer tends to do the purchase option later in the agreement. And if two years ago we were renting less than we're renting to date or prior to that, let's say, if two years ago we were renting less than we were four years ago, then there's a tail to it and a couple years later you'd see less payouts. Businesses is softer or good, you'll see that payout number affect 18 to 20 months later.

**Justin Boisseau** - *Gates Capital Management - Analyst*

That's all I had, thanks.

**Mitch Fadel** - *Rent-A-Center - President, COO*

What was that?

**Justin Boisseau** - *Gates Capital Management - Analyst*

I said that's all I had, thanks.

**Mitch Fadel** - *Rent-A-Center - President, COO*

Okay, thanks, Justin.

**Operator**

Our next question comes from [Zubing Kapadia] of JPMorgan.

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**Carla Casella** - JPMorgan - Analyst

Hi, this is Carla Casella at JPMorgan with Zubing Kapadia. Are you -- you may have answered some of this, I just hopped on the call, but can you just talk about any notable trends in consumer lending business pluses or minuses? Are you seeing any weakness in the consumer that's affecting that business?

**Mitch Fadel** - Rent-A-Center - President, COO

I'll take that first and Mark or Robert might want to comment. But no, our demand's been good. The 2.9% comp has been strong for us in the first quarter. Rental and fee revenue was closer to the high end of the range than the low-end. So no, we're not seeing any weak demand. Our demand's been good. As I just mentioned five quarters in a row positive comp. And in fact, this was the first quarter of positive comp that was over the positive comp.

**Mark Speese** - Rent-A-Center - Chairman, CEO

That makes sense.

**Mitch Fadel** - Rent-A-Center - President, COO

Year-over-year, when you have four in a row, you're comping over negative numbers but the fifth one is the first time you comp over positive numbers. In all I'd say demand is good, Carla.

**Carla Casella** - JPMorgan - Analyst

And even post quarter, any comments, I know we're starting to see some more weakness in retail numbers after the first quarter.

**Mitch Fadel** - Rent-A-Center - President, COO

Well, you can see from our guidance it's staying the same for the year. And Robert talked earlier about spreads and so forth. But our guidance hasn't changed. That would be my comment on that.

**Carla Casella** - JPMorgan - Analyst

And then on the electronic side, Circuit City reported some weak numbers. Do you think this is any specific trend there? Are you seeing more people -- you think more people are renting versus buying or?

**Mark Speese** - Rent-A-Center - Chairman, CEO

Well, I think the -- certainly the deflation of price and I don't know all the ins and outs of circuit City's problems. but the deflation that I think has hurt some retailers from a retail standpoint is that that high end helps us because those TVs, the higher end electronics are now at a price point when we bring them at the rent to own where they're affordable for our consumer. And we can go up in sizes from 42-inch plasma, now we're looking at 50-inch plasma. Those kind of things. As that deflation might hurt a retailer, it actually brings it to the rent to own level where it's a good thing for us. You know product deflation, in the past we have talked about being a bad thing. When a product gets down below a certain price point, maybe 299 retail, then it's not a rental item because people can afford to go buy it and there's no need for it to be in the rental channel. Deflation is good when it's on the high end and it brings it down into our price points and at some point it will be a negative when it gets down below a certain amount. But right now, that's good deflation for us if that made sense.

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**Carla Casella** - JPMorgan - Analyst

That's great. Good color. And then lastly, have you said how many stores Rent-Way and Rent-A-Center stores will be consolidated this year, or next? Do you still have a lot of opportunity on the consolidation front?

**David Carpenter** - Rent-A-Center - VP, IR

We had discussed earlier that we have consolidated approximately 20% of the 782 stores. And right now, any other potential closures will just go into our regular operational review of all of our stores. So there's no particular initiative to close another large group of stores.

**Carla Casella** - JPMorgan - Analyst

Okay. Great. Thank you.

**David Carpenter** - Rent-A-Center - VP, IR

Thanks, Carla.

**Operator**

(OPERATOR INSTRUCTIONS) And our next question is from Robert Straus of Merriman Curhan Ford.

**Robert Straus** - Merriman Curhan Ford - Analyst

Just a couple of follow-up questions here. On the cost of rental and fee margin, you certainly beat the range that you originally gave. Was that primarily due to lower promotions? Or were there other factors involved in that line?

**Mitch Fadel** - Rent-A-Center - President, COO

I would say primarily due to being less promotional over a period of time over all of last year. Less free time drives higher margins.

**Robert Straus** - Merriman Curhan Ford - Analyst

And then on the cost of merchandise margins, that also pretty handily beat the range that you expected earlier. Could you give us some color in that area?

**Mitch Fadel** - Rent-A-Center - President, COO

Well, the first quarter's always lower than the year-to-date number because of income tax returns will drive a little lower margin. It'll be lower in the first quarter. It is every year. And then it'll be closer to our normal annual ranges in the second, third, and fourth quarter.

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**Robert Straus** - Merriman Curhan Ford - Analyst

On the financial services side, it sounds like you're slowing down that expansion a little bit. When you consider the stores that you added the Rent-A-Center stores that you added financial services to, how are the early stores performing for financial services compared to ones that you recently opened up?

**Mark Speese** - Rent-A-Center - Chairman, CEO

Robert, Mark Speese, yes, we did slow down a little bit. As we mentioned we were going to in January and February. Again, I still believe we'll be able to add those couple of hundred this year, 29 in March, almost 30 in April. In terms of performance, again, I would say that those that we've done of late, certainly these past 60 and even some of the ones that we did in the fourth quarter of last year are doing better than those early on. And I think it's fair to say as we get a little bit more experienced, as we fine tune some of the processes and whether that's the openings themselves, some of the training that goes into it, some of the advertising to support it. We get better and better. And I think we're starting to see the benefit of that. So I would say that yes, those that we've done here recently given where they are in their life cycle, relatively young, but compared to the others at that point in time, these are doing better.

**Robert Straus** - Merriman Curhan Ford - Analyst

Is all of your advertising for financial services tacked or linked to the rent to own booklets and pamphlets that you send out? Or is there also a different advertising campaign or separate advertising campaign going on?

**Mark Speese** - Rent-A-Center - Chairman, CEO

The latter. We do leverage the rent to own advertising, if you will for that store. The brochure that is supporting the rent to own business in that store will all have reference to or include some of the selling features on the cash advantage. But in addition, there is separate stand alone advertising that goes out for those stores, as well.

**Robert Straus** - Merriman Curhan Ford - Analyst

Okay. Well, congratulations on a really nice comp for the quarter and good luck going forward.

**Mark Speese** - Rent-A-Center - Chairman, CEO

Thank you.

**Mitch Fadel** - Rent-A-Center - President, COO

Thanks, Robert.

**Operator**

We have no further questions at this time. Mr. Speese, are there any closing remarks?



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**Mark Speese** - Rent-A-Center - Chairman, CEO

Well, again, I would like to say, first, we certainly appreciate your time and interest. We always appreciate your support. Very pleased with the current tone of business and the quarter that we just concluded. And we look forward to reporting back to you next quarter with our business results in. As always, we are available for follow-up. Feel free to call any of us if need be. Thank you very much.

**Operator**

This concludes today's Rent-A-Center first quarter earnings call. You may now disconnect.

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