Jones Apparel Group, Inc. Conference Call
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Q4 2001 Summary

Jones Apparel Group, Inc. (NYSE: JNY) announced earnings per share of $0.25 for its fourth quarter ended December 31, 2001, as compared to $0.52 for the fourth quarter of 2000. Revenues for the quarter were $887 million, as compared to $962 million for the fourth quarter of 2000.

Financial Highlights

- Revenues approximated $4.1 billion in both fiscal 2001 and 2000.
- Earnings per share for the full year 2001 totaled $2.31, as compared to $2.49 for the full year 2000 (excluding purchase accounting adjustments of $.08 and $.01, respectively, to write up inventories of acquirees to fair market value, and $.41 for a non-recurring charge taken in the third quarter of 2001 to reflect the write-down of goods to net realizable value and incremental customer allowance provisions by the Company resulting from the economic climate in the aftermath of the events of September 11, 2001).
- Inventories totaled $573 million at year-end 2001, or $510 million, excluding McNaughton Apparel Group and the special reserve noted above, which were not reflected in year-end 2000 balances. This compares to a year-end 2000 inventory balance of $557 million, representing an 8.4% reduction.
- Strong cash flow during the fourth quarter enabled Jones to repay all short-term borrowings, which totaled $478 million at the end of the third quarter. Funded debt, net of $77 million in cash and short-term investments, totaled $908 million at year-end, representing 32.3% of book capitalization.
- Net cash provided by operating activities for the year 2001 totaled $562 million.

Condensed Operating Results

Jones Apparel Group, Inc.
Amounts in millions except per share data

	Fiscal Quarter Ended			Year Ended		
	12/31/2001	12/31/2000	% Change	12/31/2001	12/31/2000	% Change
Total Revenues	$887	$962	-7.8%	$4,073	$4,143	-1.7%
Operating Income	71	130	-45.4%	480	605	-20.7%
Net Interest Expense	16	24	-33.3%	80	102	-21.6%
EBT	55	106	-48.1%	400	503	-20.5%
Income Taxes	24	43	-44.2%	164	201	-18.4%
Net Income	31	63	-50.8%	236	302	-21.9%
EPS	$0.25	$0.52	-51.9%	$1.82	$2.48	-26.6%

Jones' Chairman, Sidney Kimmel, commented, "As anticipated, the retail environment was very challenging during the fourth quarter of 2001, with an unprecedented level of promotional activity. We believed that this was inevitable, given the economic climate following the terrorist events of September 11, 2001. Accordingly, we supported our wholesale customers' initiatives to clear our products through the retail channel as quickly and efficiently as possible. As a result, we believe that retail stocks of our merchandise are in balance with retailer stock plans and that we are transitioning well to current season product."

Outlook for 2002

Jones management remains cautious in its planning process for 2002. They believe that the retail landscape will continue to remain challenging given the many uncertain economic indicators. However, they believe that they are positioned operationally and financially, to capitalize on any sign of a turnaround. As a result, they are maintaining previous guidance of $2.50 per share for 2002. Earnings per share for 2001, adjusted for comparability for the adoption of SFAS No. 142 (Accounting for Goodwill and Certain Other Intangibles) effective January 1, 2002, were $2.71 per share (excluding the purchase accounting adjustment and the non-recurring charge mentioned above). Jones management estimates that revenues for 2002 will remain even with 2001 at approximately $4.1 billion.

Comments on Call and Analyst Concerns

Overall the conference call was very positive in the wake of a very difficult retailing environment. Jones has certainly suffered from the current recession as full year 2001 EPS fell over 26% from last year; however, this is on revenues declining only 2% for the same period. Clearly, profitability has been damaged due to the major promotions and mark-downs initiated to clear inventories. Jones indicates that this trend may continue into Q2'02 as consumer spending is not expected to fully recover and spring lines have already been shipped and will likely require continued promotions and mark-downs to move inventory. I am very confident that Jones is taking the necessary steps to work through this period with as little damage to the core businesses while maintaining very strong financials. With that in mind, Jones remains cautious about Q1 & Q2 EPS although it should be significantly higher than Q4'01. As the economy strengthens in the back half of 02, Jones is confident and conservative in maintaining their previous guidance of EPS $2.50 for 2002.

The major strength with Jones Apparel is its diverse portfolio of leading brands and product lines. They cater to all major segments, including the moderate and high-end apparel as well as footware and accessories. They are strategically focused to capture market share in the moderate segment, which is believed to be the area with most growth potential, through their acquisition of McNaughton Apparel Group and through a new distribution relationship with Sears.

Analysts Concerns

Analysts were primarily concerned with understanding the magnitude of the continued promotions and mark-downs and the effect on profitability. Management acknowledged that up to 10% of sales could be through the off price channels during 1H'02, but that was factored into the $2.50 EPS guidance. Also, margins were a major topic among analysts. Again, with the off price strategy to reduce inventories, gross margins are expected to remain below standard (from 2000) until the economy heats back up and promotions can be greatly reduced. However, Jones does not foresee any material price increases or decreases during the year. Overall, Jones expects operating margins to average around 10% for 2002.

Valuation Considerations

Valuation Ratios	
Price/Book (mrq*)	2.38
Price/Earnings (ttm)	19.37
Price/Sales (ttm)	1.14

As we can see, JNY is relatively attractively priced at its current levels although it has appreciated approximately 12% since the earnings announcement. In addition, JNY's PEG has increased from below 1 to around 1.25. I believe that the current run-up will subside and the stock should fall back a couple points until further earnings news supports such appreciation. However, with a conservative 12 month price target by 8 brokers of $38-40, the stock still appears to have significant upside potential especially relative to the market, should it manage to achieve only mid to high single digit returns for the year. In addition, Jones forecasted EPS growth over the next 3-5 years of 14-15% leads its piers and the S&P 500. I think the market's reaction to Jones' was a bit unjustified, but it is not surprising to see this considering the lack of positive guidance (in general) coming from the street. I recommend holding Jones as the downside risk appears to be minimal and the upside has a strong possibility of playing out in the later half of 2002.