ACE HARDWARE CORPORATION

Quarterly period ended March 29, 2008

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CONSOLIDATED BALANCE SHEETS

	March 29, 2008	December 29, 2007
	(In thousands, except share data)	
	(Unaudited)	(Audited)
Assets		
Cash and cash equivalents	$ 18,167	$ 84,385
Marketable securities	32,055	29,545
Receivables, net of allowance for doubtful accounts of $6,937 and $6,443, respectively	374,193	337,336
Inventories	501,444	472,305
Prepaid expenses and other current assets	45,663	43,685
Total current assets	971,522	967,256
Property and equipment, net	303,038	304,474
Notes receivable, net of allowance for doubtful accounts of $9,763 and $9,873, respectively	68,391	69,497
Other assets	54,280	55,112
Total assets	$1,397,231	$1,396,339
Liabilities and Member Retailers' Equity		
Current maturities of long-term debt	$ 2,195	$ 18,212
Short-term borrowings	151,292	130,707
Accounts payable	554,392	524,212
Patronage distributions payable in cash	19,691	17,505
Patronage refund certificates payable	19,752	18,776
Accrued expenses	116,774	142,134
Total current liabilities	864,096	851,546
Long-term debt	175,416	171,824
Patronage refund certificates payable	55,250	75,010
Other long-term liabilities	74,239	72,643
Total liabilities	1,169,001	1,171,023
Member Retailers' Equity:		
Class A voting common stock, $1,000 par value, 10,000 shares authorized, 3,131 and 3,106 issued and outstanding, respectively	3,131	3,106
Class B nonvoting common stock, $1,000 par value, $2,000 redemption value, 6,500 shares authorized, 6,499 issued, 1,344 and 1,356 outstanding, respectively	6,499	6,499
Class C nonvoting common stock, $100 par value, 4,000,000 shares authorized, 3,149,247 and 3,142,567 issued and outstanding, respectively	314,925	314,257
Class C nonvoting common stock, $100 par value, issuable to retailers for patronage distributions, 92,333 and 81,735, shares issuable, respectively	9,233	8,174
Additional stock subscribed, net	173	155
Contributed capital	13,485	13,485
Variance allocation	(72,316)	(80,560)
Accumulated deficit	(27,139)	(27,710)
Accumulated other comprehensive loss	(4,793)	(1,804)
Treasury stock, at cost, 5,155 and 5,143 Class B shares held, respectively	(14,968)	(10,286)
Total member retailers' equity	228,230	225,316
Total liabilities and member retailers' equity	$1,397,231	$1,396,339

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

	Quarterly Period Ended	
	March 29, 2008 (13 Weeks)	March 31, 2007 (13 Weeks)
	(Unaudited, in thousands)	(As Restated)
Revenues	$872,073	$939,856
Cost of sales	779,461	831,729
Gross profit	92,612	108,127
Distribution operations expenses	20,971	24,202
Selling, general and administrative expenses	31,163	26,342
Retail success and development expenses	24,626	39,505
Total operating expenses	76,760	90,049
Operating income	15,852	18,078
Interest expense	(7,196)	(7,045)
Interest income	1,684	1,617
Other income, net	1,241	1,191
Income tax (expense) benefit	(823)	266
Net income	$ 10,758	$ 14,107
Accrued patronage distributions	$ 10,187	$ 12,616

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Quarterly Period Ended	
	March 29, 2008 (13 Weeks)	March 31, 2007 (13 Weeks)
	(Unaudited, in thousands)	(As Restated)
Operating activities		
Net income	$ 10,758	$ 14,107
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	7,122	6,981
Amortization of deferred gain on sale leaseback	(319)	(319)
Provision for doubtful accounts	390	1,331
Loss (gain) on disposal of assets, net	107	(1,216)
Deferred income tax expense (benefit)	691	(266)
Changes in operating assets and liabilities:		
Receivables	(32,028)	(70,940)
Inventories	(29,139)	(2,085)
Other current assets	(2,668)	(4,188)
Other long-term assets	832	2,500
Accounts payable and accrued expenses	38,232	47,975
Other long-term liabilities	(477)	827
Net cash used in operating activities	(6,499)	(5,293)
Investing activities		
Purchases of marketable securities	(7,756)	(2,555)
Proceeds from sale of marketable securities	4,648	3,512
Purchases of property and equipment	(5,801)	(8,654)
Proceeds from sale of assets	8	4,082
Increase in notes receivable, net	(2,683)	(7,856)
Net cash used in investing activities	(11,584)	(11,471)
Financing activities		
Proceeds from short-term borrowings, net	20,585	60,100
Principal payments on long-term debt	(12,425)	(11,614)
Change in cash overdraft	(33,411)	(7,236)
Payments of patronage refund certificates and patronage financing deductions	(18,913)	(18,335)
Proceeds from sale of stock	711	1,003
Repurchases of stock	(4,682)	(4,769)
Net cash (used in) provided by financing activities	(48,135)	19,149
Increase (decrease) in cash and cash equivalents	(66,218)	2,385
Cash and cash equivalents at beginning of period	84,385	15,813
Cash and cash equivalents at end of period	$ 18,167	$ 18,198
Supplemental disclosure of cash flow information:		
Interest paid (net of amount capitalized)	$ 8,665	$ 9,215
Income taxes paid	$ 115	$ 61

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements
(Unaudited, in thousands)

(1) Summary of Significant Accounting Policies

The Company and Its Business

Ace Hardware Corporation ("the Company") is a wholesaler of hardware and other related products, and is a manufacturer and wholesaler of paint products. The Company also provides its retail members value-added services such as advertising, marketing, merchandising and store location and design services. Ace's goods and services are sold predominately within the United States, primarily to retailers that operate hardware stores and with whom the Company has a retail membership agreement. As a retailer-owned cooperative, the Company distributes substantially all of its patronage sourced income in the form of patronage distributions to member retailers based on their volume of merchandise purchases. See Note 3 for further discussion regarding patronage distributions.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The Company's quarterly periods end on the thirteen-weeks ended Saturday, March 29, 2008 and March 31, 2007.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries. All significant intercompany transactions have been eliminated. The equity method of accounting is used for 50% or less owned affiliates over which the Company has the ability to exercise significant influence. Due to the timing of receipt of available financial information, the results of the Company's New Age Insurance Limited ("NAIL") subsidiary are consolidated on a one-month lag.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current financial statement presentation, with no net effect on consolidated balance sheets, statements of income or statements of cash flows.

Restatement

On September 5, 2007, the Company issued a press release announcing that it had discovered a material error in its historical financial statements related to its inventory accounting. The accounting error stemmed from a significant dollar difference between the Company's general ledger inventory balances and that of its perpetual inventory records. As a result, the Company has restated its previously issued consolidated balance sheets, statements of income, statements of cash flows and related notes for the quarterly period ended March 31, 2007. For additional details on the restatement, see the Company's Restated 2006 Annual Report.

(2) Divestitures

Prior to mid-2005, the Company had engaged in a strategy to extend the Ace brand into certain markets through purchasing and opening new Company-owned Ace locations. These activities are included in the other segment. The Company-owned stores contributed operating losses of $83 and $236 and net sales of $0 and $3,523 for the quarterly periods ended March 29, 2008 and March 31, 2007, respectively.

As of March 30, 2007, the Company had completed the sale of its remaining Company-owned stores at a sales price of $4,087.

(3) Patronage Distributions and Refund Certificates Payable

The Company operates as a cooperative organization and has paid or may pay patronage distributions to member retailers on the portion of patronage based income derived from business done with such retailers. Patronage distributions are allocated in proportion to the volume of purchases by member retailers during the period.

In December 2007, the Company's Board of Directors approved an Equity Restoration Plan to restore its equity position due to the loss of equity incurred from the inventory accounting error which the Company announced in an external press release on September 5, 2007. Under the plan, the Company established a variance allocation account in the amount of $148,556 which allocates the overstatement of the Company's net income stemming from the inventory accounting error to the Company's retailer members, based on the retailer members' proportionate share of warehouse distribution pool purchases for the fiscal years 2002 through 2006.

For fiscal years 2007 and 2008, the first 20% of patronage distributions are distributed in cash. The remaining balance of the patronage distribution will be applied to the retailer member's variance allocation account until the account is reduced to zero and any remaining patronage distribution will be distributed in the Company's Class C stock. Additionally, member retailers may choose to use any patronage certificates, shares of Class C stock issued as part of the patronage distribution in prior years or cash to pay all or a portion of their variance allocation account balance.

(4) Debt

Line of Credit

The Company has an established $250,000 secured committed revolving credit facility with a group of banks which includes $50,000 available for letters of credit. Effective in November 2007, the Company has obtained waivers from its lenders to waive certain defaults and events of default that may have occurred and may continue to exist under its borrowing agreements related to the inventory accounting error referenced in Note 3. During this waiver period, the credit facility's interest rate was increased to prime and the borrowing limit was temporarily decreased to $225,000 and $150,000 at March 29, 2008 and December 29, 2007, respectively, from $250,000. Subsequently, the borrowing limit will be reduced to $190,000 in April 2008 and $175,000 in May 2008. The waivers currently in place expire on May 30, 2008.

This credit facility is primarily used to fund short-term working capital needs, of which $56,187 and $1,172 was available at March 29, 2008 and December 29, 2007, respectively. Included in these balances were outstanding letters of credit of $17,521 and $18,121 at March 29, 2008 and December 29, 2007, respectively.

Borrowings under the revolving credit facility and the line of credit bear interest at a spread over LIBOR based upon quarterly debt to earnings before interest, taxes, depreciation and amortization ("EBITDA") ratios. The weighted average interest rate from the credit facility was 5.25% and 5.80% at March 29, 2008 and

December 29, 2007, respectively. At March 29, 2008 and December 29, 2007, the spread over LIBOR was 100 basis points, of which 12.5 basis points was fee related. This credit facility, which expires on April 29, 2010, requires the Company to comply with certain restrictive covenants including maintenance of fixed charge coverage and debt leverage ratios as defined by the facility. Additionally, the Company also pledged substantially all of its assets to secure the existing indebtedness.

Long-Term Debt

During the waiver period, all fixed and variable interest rates on long term debt were increased by 40 basis points. The weighted average interest rate on long-term debt was 6.91% and 6.50% as of March 29, 2008 and December 29, 2007, respectively.

The debt instruments require the Company to comply with various financial and non-financial covenants. The financial covenants require the Company to maintain certain fixed charge coverage and debt to EBITDA ratios. The Company, based on waiver agreements that it has received from its lenders, is in compliance with its financial covenants as of March 29, 2008 and December 29, 2007.

The Company completed its new senior debt facilities on May 15, 2008. See Note 9.

Long-term debt is comprised of the following:

	March 29, 2008	December 29, 2007
$30,000 due in semi-annual installments of $2,000 with interest payable quarterly at a fixed rate of 6.87% and a maturity date of June 22, 2008	$ 2,000	$ 2,000
$30,000 due in annual installments of $6,000 with interest payable quarterly at a fixed rate of 7.95% and a maturity date of March 25, 2009	6,000	12,000
$25,000 due in annual installments of $5,000 with interest payable quarterly at a fixed rate of 7.01% and a maturity date of February 9, 2010	10,000	15,000
$20,000 due in quarterly installments of $714 with interest payable quarterly at a fixed rate of 7.89% and a maturity date of June 15, 2011	9,286	10,000
$70,000 due in annual installments of $14,000 commencing April 30, 2009 with interest payable semi-annually at a fixed rate of 7.67% and a maturity date of April 30, 2013	70,000	70,000
$50,000 due at maturity with an early redemption option, with interest payable quarterly at a floating rate of LIBOR plus 1.05% and a maturity date of March 31, 2016	50,000	50,000
$25,000 due in annual installments of $5,000 commencing April 30, 2012 with interest payable semi-annually at a fixed rate of 6.00% and a maturity date of April 30, 2016	25,000	25,000
Installment notes with maturities through 2011 at a fixed rate of 6.00%	5,325	6,036
Total long-term debt	177,611	190,036
Less: maturities within one year	(2,195)	(18,212)
Long-term debt	$175,416	$171,824

(5) Derivative Financial Instrument

In an effort to mitigate the interest rate risk on floating rate debt, the Company entered into a LIBOR based interest rate swap agreement ("swap agreement") in May 2006. The swap agreement has a notional amount totaling $50,000 and effectively fixes the interest rate on the Company's $50,000 long-term floating rate debt which matures on March 31, 2016. This swap agreement is designated as a cash-flow hedge as defined under Financial Accounting Standards Board ("FASB") Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. Net gains and losses are reported as a component of interest expense. Changes in the fair value of a derivative that is designated as, and meets all the required criteria for, a cash flow hedge are recorded in accumulated other comprehensive loss.

The Company recorded an unrealized loss of $2,391 and $102 for the quarterly periods ended March 29, 2008 and March 31, 2007, respectively, for the swap agreement in accumulated other comprehensive loss. No amounts were recorded in operating income as there was no hedge ineffectiveness for these periods. The fair market value of the swap agreement is included in other long-term liabilities in the consolidated balance sheets as of March 29, 2008 and December 29, 2007. See Note 9 for information regarding the Company's termination of this swap agreement on April 28, 2008.

(6) Comprehensive Income

FASB Statement No. 130, "Reporting Comprehensive Income," establishes guidelines for the reporting and display of comprehensive income and its components in financial statements. Comprehensive income includes the following components:

	Quarterly Period Ended	
	March 29, 2008	March 31, 2007 (As Restated)
Net income	$10,758	$14,107
Unrealized (loss) gain on investments in marketable securities, net	(598)	19
Unrealized loss on derivative	(2,391)	(102)
Comprehensive income	$ 7,769	$14,024

(7) Income Taxes

Income tax (expense) benefit includes the following components:

	Quarterly Period Ended	
	March 29, 2008	March 31, 2007 (As Restated)
Current:		
State	$ (78)	$ —
Foreign	(54)	—
Total	(132)	—
Deferred:		
Federal	(612)	309
State	(79)	(43)
Total	(691)	266
Income tax (expense) benefit	$(823)	$266

A reconciliation of income tax (expense) benefit on income differs from the amount computed by applying the U.S. Federal income tax rate of 35% to income before income taxes because of the effect of the following items:

	Quarterly Period Ended	
	March 29, 2008	March 31, 2007 (As Restated)
Expected tax at U.S. Federal income tax rate	$(4,053)	$(4,844)
State income taxes, net of U.S. Federal income tax benefit	(104)	(29)
Patronage distribution deductions	3,565	4,416
Other, net	(231)	723
Income tax (expense) benefit	$ (823)	$ 266

(8) Segments

Under FASB Statement No. 131, "Disclosures about Segments of an Enterprise and Related Information," the Company determined that it has two reportable segments based on the way that our chief operating decision makers organize the Company's business activities for making operating decisions and assessing performance. The Company is principally engaged as a wholesaler of hardware and other related products, and is a manufacturer and wholesaler of paint products. The Company identifies segments based on management responsibility and the nature of the business activities of each component of the Company. Corporate expenses are included in the wholesale segment. The Company measures segment profit as operating profit including an allocation for interest expense and income taxes. Information regarding the identified segments and the related reconciliation to consolidated information is as follows:

	Quarterly Period Ended March 29, 2008				
	Wholesale	Paint Manufacturing	Other	Elimination of Intersegment Activities	Consolidated
Revenues from external customers	$ 864,413	$ 5,516	$ 2,144	$ —	$ 872,073
Intersegment sales	—	26,673	—	(26,673)	—
Interest expense	7,196	252	—	(252)	7,196
Depreciation and amortization	6,317	805	—	—	7,122
Segment profit (loss)	9,915	965	(122)	—	10,758
Identifiable segment assets	1,273,959	65,565	57,707	—	1,397,231
Expenditures for long-lived assets	5,333	468	—	—	5,801

	Quarterly Period Ended March 31, 2007 (As Restated)				
	Wholesale	Paint Manufacturing	Other	Elimination of Intersegment Activities	Consolidated
Revenues from external customers	$ 929,699	$ 4,772	$ 5,385	$ —	$ 939,856
Intersegment sales	—	29,178	—	(29,178)	—
Interest expense	7,045	283	65	(348)	7,045
Depreciation and amortization	6,066	915	—	—	6,981
Segment profit (loss)	13,434	1,162	(489)	—	14,107
Identifiable segment assets	1,275,879	63,778	61,964	—	1,401,621
Expenditures for long-lived assets	7,117	1,442	95	—	8,654

Notes to Consolidated Financial Statements
(Unaudited, in thousands)

Revenues by geographic region and revenue type are as follows:

	Quarterly Period Ended	
	March 29, 2008	March 31, 2007 (As Restated)
Revenues by geographic region:		
United States	$827,329	$903,124
Foreign countries	44,744	36,732
Total	$872,073	$939,856
Revenue type:		
Merchandise sales	$800,857	$857,947
Retail services	71,216	81,909
Total	$872,073	$939,856

The Company has $92 of long-lived assets outside of the United States.

(9) Subsequent Events

On April 28, 2008, the Company terminated its $50,000 interest rate swap agreement and incurred a termination payment of $4,602, which will be recorded in interest expense in the Company's second quarter 2008 consolidated statements of income.

On May 15, 2008, the Company completed its new senior debt facilities. The new financing includes a $300,000 senior secured revolving credit facility with a group of banks maturing May 15, 2013 that includes $150,000 available for letters of credit. Borrowings under this facility will initially bear interest at a spread of 225 basis points over LIBOR. In addition, the Company issued $300,000 of senior secured notes maturing June 1, 2016 and bearing an interest coupon of 9.125%. Interest is payable semi-annually commencing on December 1, 2008. As a result of this new financing, the related current maturities of the long-term debt that has been refinanced were reclassified as long-term debt on the March 29, 2008 consolidated balance sheet.

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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our consolidated financial statements and the related notes appearing elsewhere in this quarterly report.

Executive Overview

For the quarter ended March 29, 2008, the Company reported net income of $10.8 million, a decrease of $3.3 million or 23.7%, as compared to the prior year. The Company's revenues decreased $67.8 million, or 7.2%, compared to the prior year. Merchandise sales to comparable domestic stores decreased $72.9 million, or 7.8%, in 2008 compared to the prior year. This decrease was partially offset by a $10.9 million increase in merchandise sales to net domestic stores opened in the 2007 and 2008 fiscal year periods and a $7.8 million increase in international sales. Gross profit decreased $15.5 million, or 14.3%, in 2008. Gross profit decreased $8.3 million due to a decline in the gross profit percentage and decreased $7.2 million as a result of a decline in merchandise sales. Operating expenses decreased $13.3 million, or 14.8%, in 2008 primarily due to lower incentive compensation and profit sharing expenses of $7.8 million, lower national advertising expenses of $6.7 million, a reduction in retail pilot store expenses of $2.7 million, lower expenses associated with the exit from Company-owned stores of $1.8 million and lower expenses associated with the discontinuation of the Vision 21 achievement award program of $1.6 million. These declines in operating expenses were partially offset by $5.6 million of expenses in 2008 related to the restatement, remediation and debt restructuring activities associated with the inventory accounting error announced in 2007.

Management utilizes a variety of key performance measures to evaluate the performance of the Company's business. These measures include revenues, store count, gross profit percentage, operating expenses and debt levels.

Results of Operations

Comparison of Quarter Ended March 29, 2008 to Quarter Ended March 31, 2007

Consolidated revenues for the quarter totaled $872.1 million, a decrease of $67.8 million or 7.2%, as compared to the prior year. A reconciliation of consolidated revenues follows (in thousands):

		% Change vs. 2007
2007 Revenues	$939,856	
Merchandise sales change based on new and cancelled domestic stores:		
Sales increase from 2008/2007 new stores	23,362	2.5%
Net decrease in sales from 2008/2007 store cancellations	(12,504)	(1.3)%
Decrease in merchandise sales to comparable domestic stores	(72,880)	(7.8)%
Increase in international merchandise sales	7,751	0.8%
Other revenue changes	(13,512)	(1.4)%
2008 Revenues	$872,073	(7.2)%

Merchandise sales to comparable domestic stores decreased $72.9 million, which reflects a decline in comparable store customer transactions.

The number of Ace retailer outlets is summarized as follows:

Quarterly Period Ended	March 29, 2008	March 31, 2007
Retailer outlets at beginning of period	4,630	4,629
New retailer outlets	27	41
Retailer outlets cancellations	(41)	(36)
Retailer outlets at end of period	4,616	4,634

Management believes that new store count is a key metric in evaluating the health of Ace due to the incremental volume from these stores in future periods. Management is less concerned about total store count as the new stores being added to the network tend to significantly outpace the sales volume lost from cancelled stores. New stores for this quarterly comparison are defined as stores that were opened from January 2007 through March 2008. In 2008, the Company had an increase in sales due to new domestic stores of $23.4 million, which includes the addition of 24 new stores activated this quarter that generated revenues of $1.6 million. This increase was partially offset by a decrease in sales due to domestic store cancellations of $12.5 million, which includes retailer cancellations of 37 stores in 2008 which negatively impacted revenues by $3.5 million.

In 2008, the Company realized an increase in international sales of $7.8 million driven by an increase in sales to existing stores in the Middle East, sales to new stores in the Caribbean and sales growth in foreign-to-foreign wholesale operations located in Shanghai.

Warehouse and bulletin sales represented 71.5% of merchandise sales in 2008 compared to 72.8% in 2007, while direct ship sales were 28.5%, up from 27.2%.

Gross profit decreased $15.5 million and the gross profit percentage decreased 0.88% to 10.62% in 2008 from 11.50% in 2007. Gross profit decreased $8.3 million due to the gross profit percentage decline and $7.2 million due to the revenue decline of $67.8 million in 2008. The gross profit percentage decrease of 88 basis points in 2008 was largely attributable to $5.6 million in lower retailer reimbursement revenues on reduced national advertising expenses which are recorded in retail success and development expenses. Additionally, the gross profit percentage was also negatively impacted by $1.4 million from the exit of Company-owned stores, which was completed at the end of the first quarter of 2007.

Distribution operations expenses decreased $3.2 million and decreased as a percent of revenues to 2.40% in 2008 from 2.58% in 2007. The decrease is primarily due to lower incentive compensation and profit sharing accruals of $4.0 million, partially offset by lower distribution costs capitalized into inventory of $0.3 million in 2008.

Selling, general and administrative expenses increased $4.8 million and increased as a percent of revenues to 3.57% in 2008 from 2.80% in 2007. The increase is primarily due to $5.6 million of expenses in 2008 related to the restatement, remediation and debt restructuring activities associated with the inventory accounting error, along with inflationary driven increases in other general overhead costs in 2008. These increases were partially offset by lower incentive compensation and profit sharing accruals of $2.0 million in 2008, and a gain on the sale of a parcel of land in Aurora, Illinois of $1.2 million in 2007.

Retail success and development expenses decreased $14.9 million and decreased as a percent of revenues to 2.82% in 2008 from 4.20% in 2007. The decrease is primarily due to lower national advertising expenses of $6.7 million, a decrease in retail growth plan expenses of $2.7 million, a decrease in Company-owned store expenses of $1.8 million, a decrease in the Vision 21 achievement award of $1.6 million discontinued after 2007 and a decrease in incentive compensation and profit sharing accruals of $1.5 million.

Interest expense increased $0.2 million primarily due to increased interest rates reflective of the Company's current bank waiver.

Interest income increased $0.1 million primarily due to an increase in loans to retailers under the Company's Equity Match Financing ("EMF") program.

Income tax expense increased $1.1 million primarily due to higher non-patronage sourced net income, lower losses from Company-owned stores and the recognition of additional tax expense related to uncertain tax positions.

Liquidity and Capital Resources

The Company expects that existing and internally generated funds, along with an established or refinanced line of credit and long-term financing, will continue to be sufficient in the foreseeable future to finance the Company's working capital requirements, debt service, patronage rebates, capital expenditures, share redemptions from retailer cancellations and growth initiatives.

Cash Flows

The Company had $18.2 million and $84.4 million of cash and cash equivalents, of which $15.5 million and $17.4 million related to the Company's insurance subsidiary, at March 29, 2008 and December 29, 2007, respectively. In addition, the Company had $56.2 million and $1.2 million available under its credit facility at March 29, 2008 and December 29, 2007, respectively.

For the quarter ended March 29, 2008 the decrease in cash and cash equivalents at March 29, 2008 as compared to March 31, 2007 was primarily due to the following:

• Net cash used in operating activities was $6.5 million and $5.3 million for 2008 and 2007, respectively. The modest increase in cash used in operations was due to a higher use of cash related to the change in inventories in 2008. Although inventory levels at the end of the first quarter of 2008 decreased by $22.5 million as compared to inventories the end of the first quarter of 2007, the higher use of cash in the first quarter 2008 to increase inventory levels was a result of a decrease in 2007 year-end inventory levels of $46.6 million compared to year-end 2006. Additionally, the increase in accounts payable and accrued expenses from year-end 2007 was slightly lower due mainly to reduced inventory purchases in the first quarter of 2008. Lastly, these changes in the use of cash were partially offset by a lower increase in receivables driven by the decline in revenues in 2008.

• Net cash used in investing activities was $11.6 million and $11.5 million for 2008 and 2007, respectively. Net cash used in 2008 increased primarily due to lower proceeds on the sales of assets and higher net purchases of marketable securities by the Company's insurance subsidiary. The increase in cash used was almost entirely offset by lower purchases of property and equipment and a lower increase in notes receivable in 2008.

• Net cash used in financing activities was $48.1 million and net cash provided by financing activities was $19.1 million for 2008 and 2007, respectively. The increase in net cash used was primarily due to lower proceeds from short-term borrowings and the decrease in the cash overdraft.

Application of Critical Accounting Policies and 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, liabilities, sales and expenses in the consolidated financial statements. On an ongoing basis, the Company evaluates its estimates and judgments based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates, and these estimates would vary under different assumptions or conditions. Management believes these estimates and assumptions are reasonable.

The Company annually reviews its financial reporting and disclosure practices and accounting policies to ensure that they provide accurate and comprehensive information relative to the current economic and business environment. For a description of Ace's significant accounting policies and estimates, see the Company's 2007 Annual Report.

Qualitative and Quantitative Disclosure About Market Risk

Market Risk and Interest Rate Risk. The Company is subject to market risks from changes in interest rates charged on its credit facility used to finance ongoing operations and on its floating-rate indebtedness. The impact

on earnings and the value of its long-term debt are subject to change as a result of movements in market rates and prices. As of March 29, 2008, the Company had $177.6 million of debt outstanding, excluding its revolving line of credit, at a weighted average interest rate of 6.91%, of which $2.2 million is due in the next 12 months. The Company also had $75.0 million in patronage rebate certificates outstanding.

The Company does not expect changes in interest rates to have a material effect on earnings or cash flows since 100% of its long-term debt has fixed rates or variable rates that are subject to swap agreements with major financial institutions to manage risk. As of March 29, 2008, a 100 basis point change in short term interest rates would impact pre-tax income by no more than $1.6 million per annum.

Inflation and Changes in Prices. The Company's business is not generally governed by contracts that establish prices substantially in advance of the receipt of goods or services. As vendors increase their prices for merchandise supplied to the Company, the Company generally increases the price to its retailers in an equal amount plus the normal handling charge on such amounts. In the past, these increases have provided adequate gross profit to offset the impact of inflation on operating expenses.

Non-GAAP Financial Measures

EBITDA and Adjusted EBITDA, as presented in this quarterly report, are supplemental measures of our performance that are not required by, or presented in accordance with, accounting principles generally accepted in the United States ("GAAP"). They are not measurements of our financial performance under GAAP and should not be considered as alternatives to net income or any other performance measures derived in accordance with GAAP or as alternatives to cash flows from operating activities as measures of our liquidity.

We define "EBITDA" as earnings before interest, taxes, depreciation and amortization. We define "Adjusted EBITDA" as EBITDA adjusted to exclude certain items which we consider non-recurring and which we believe are not indicative of future performance. We caution investors that amounts presented in accordance with our definitions of EBITDA and Adjusted EBITDA may not be comparable to similar measures disclosed by other companies, because not all companies calculate EBITDA or Adjusted EBITDA in the same manner.

We present EBITDA because we consider it an important supplemental measure of our performance and believe it is frequently used in the evaluation of companies in our industry. In addition, the instruments governing our indebtedness use EBITDA (with additional adjustments) to measure our compliance with covenants such as interest coverage and debt incurrence. We present Adjusted EBITDA as a further supplemental measure of our performance. EBITDA and Adjusted EBITDA have several limitations that are discussed in the following EBITDA reconciliation table where we also include a quantitative reconciliation of EBITDA and Adjusted EBITDA to the most directly comparable GAAP financial performance measure, which is net income.

	Quarterly Period Ended	
	March 29, 2008	March 31, 2007
	(Unaudited, in thousands)	
EBITDA Reconciliation:		
Net income	$10,758	$14,107
Income tax expense (benefit)	823	(266)
Interest expense	7,196	7,045
Depreciation and amortization	7,122	6,981
EBITDA	$25,899	$27,867
Adjustments:		
Interest income(a)	(1,684)	(1,617)
Debt restructuring and restatement related expenses(b)	3,518	—
Remediation costs(c)	2,074	—
Severance(d)	1,407	—
Real estate gains(e)	—	(1,200)
Vision 21 achievement awards(f)	—	1,581
Reduction of employee incentives(g)	—	2,288
Other adjustments	—	241
Adjusted EBITDA	**$31,214**	**$29,160**

(a) Non-cash interest income received from patronage loans to member retailers plus cash interest earned by the Company's insurance subsidiary.

(b) Expenses related to the restatement of our 2004, 2005 and 2006 audited financial statements and related waivers, and similar fees paid to our lenders.

(c) Expenses related to the implementation of our inventory accounting error remediation plan.

(d) Expenses related to headcount reductions, primarily at our corporate headquarters.

(e) Gains recognized on the sale of real estate.

(f) Represents incentives provided to stores achieving Vision 21 brand standards. The financial incentive component of this program terminated at the end of 2007.

(g) Employee discretionary profit sharing expense accruals reversed later in the year.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The consolidated financial statements presented in this Quarterly Report have been prepared with integrity and objectivity and are the responsibility of the management of Ace Hardware Corporation. These consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles and properly reflect certain estimates and judgments based upon the best available information.

The Company maintains a system of internal accounting controls, which is supported by an internal audit program and is designed to provide reasonable assurance, at an appropriate cost, that the Company's assets are safeguarded and transactions are properly recorded. This system is continually reviewed and modified in response to changing business conditions and operations and as a result of recommendations by the internal and external auditors. In addition, the Company has distributed to employees its policies for conducting business affairs in a lawful and ethical manner.

The Audit Committee of the Board of Directors meets periodically with the independent auditors and with the Company's internal auditors, both privately and with management present, to review accounting, auditing, internal control and financial reporting matters. The Audit Committee retains the independent auditors and regularly reviews the internal accounting controls, the activities of the outside auditors and internal auditors and the financial condition of the Company. Both the Company's independent auditors and the internal auditors have free access to the Audit Committee.

May 29, 2008

/s/ Ray A. Griffith
Ray A. Griffith
President and
Chief Executive Officer

/s/ Arthur J. McGivern
Arthur J. McGivern
Senior Vice President
General Counsel and Secretary
(Principal Financial Officer through March 19, 2008)

/s/ Dorvin D. Lively
Dorvin D. Lively
Chief Financial Officer
(Principal Financial Officer effective March 20, 2008)

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