

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended August 3, 2013

Or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission  
File Number  
333-175075

Registrant, State of Incorporation  
Address and Telephone Number

I.R.S. Employer  
Identification No.  
22-2894486

J.CREW GROUP, INC.

(Incorporated in Delaware)

770 Broadway  
New York, New York 10003  
Telephone: (212) 209-2500

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.\* Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock  
Common Stock, \$.01 par value per share

Outstanding at September 6, 2013  
1,000 shares

\* The Registrant has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934, but is not required to file such reports under such sections.

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## PART I – FINANCIAL INFORMATION

## ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## J.CREW GROUP, INC.

Condensed Consolidated Balance Sheets  
(unaudited)  
(in thousands, except share data)

	August 3, 2013	February 2, 2013
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 98,836	\$ 68,399
Merchandise inventories	321,194	265,628
Prepaid expenses and other current assets	73,234	65,791
Prepaid income taxes	5,455	11,620
Total current assets	<u>498,719</u>	<u>411,438</u>
Property and equipment, net	348,142	324,111
Favorable lease commitments, net	30,646	35,104
Deferred financing costs, net	46,881	51,851
Intangible assets, net	970,825	975,517
Goodwill	1,686,915	1,686,915
Other assets	3,318	1,778
Total assets	<u>\$ 3,585,446</u>	<u>\$ 3,486,714</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 214,304	\$ 141,119
Other current liabilities	124,519	153,743
Interest payable	18,353	18,812
Current portion of long-term debt	12,000	12,000
Total current liabilities	<u>369,176</u>	<u>325,674</u>
Long-term debt	1,561,000	1,567,000
Unfavorable lease commitments and deferred credits, net	82,425	71,146
Deferred income taxes, net	395,190	392,984
Other liabilities	35,074	38,419
Total liabilities	<u>2,442,865</u>	<u>2,395,223</u>
Stockholders' equity:		
Common stock \$0.01 par value; 1,000 shares authorized, issued and outstanding	—	—
Additional paid-in capital	1,005,575	1,003,184
Accumulated other comprehensive loss	(18,269)	(20,189)
Retained earnings	155,275	108,496
Total stockholders' equity	<u>1,142,581</u>	<u>1,091,491</u>
Total liabilities and stockholders' equity	<u>\$ 3,585,446</u>	<u>\$ 3,486,714</u>

See notes to unaudited condensed consolidated financial statements.

**J.CREW GROUP, INC.****Condensed Consolidated Statements of Operations and Comprehensive Income  
(unaudited)  
(in thousands)**

	Thirteen Weeks Ended <u>August 3, 2013</u>	Thirteen Weeks Ended <u>July 28, 2012</u>
Revenues:		
Net sales	\$ 550,946	\$ 517,985
Other	8,156	7,503
Total revenues	<u>559,102</u>	<u>525,488</u>
Cost of goods sold, including buying and occupancy costs	<u>329,110</u>	<u>288,751</u>
Gross profit	229,992	236,737
Selling, general and administrative expenses	<u>174,226</u>	<u>174,669</u>
Income from operations	55,766	62,068
Interest expense, net of interest income	<u>26,239</u>	<u>25,359</u>
Income before income taxes	29,527	36,709
Provision for income taxes	<u>12,069</u>	<u>14,702</u>
Net income	<u>\$ 17,458</u>	<u>\$ 22,007</u>
Other comprehensive income (loss):		
Reclassification of realized losses on cash flow hedges, net of tax, to earnings	2,132	—
Unrealized gain (loss) on cash flow hedges, net of tax	528	(1,259)
Foreign currency translation adjustments	<u>(731)</u>	<u>—</u>
Comprehensive income	<u>\$ 19,387</u>	<u>\$ 20,748</u>

See notes to unaudited condensed consolidated financial statements.

**J.CREW GROUP, INC.****Condensed Consolidated Statements of Operations and Comprehensive Income  
(unaudited)  
(in thousands)**

	Twenty-six Weeks Ended August 3, 2013	Twenty-six Weeks Ended July 28, 2012
Revenues:		
Net sales	\$ 1,107,300	\$ 1,015,430
Other	15,913	13,580
Total revenues	1,123,213	1,029,010
Cost of goods sold, including buying and occupancy costs	641,206	552,485
Gross profit	482,007	476,525
Selling, general and administrative expenses	352,622	338,787
Income from operations	129,385	137,738
Interest expense, net of interest income	51,920	50,771
Income before income taxes	77,465	86,967
Provision for income taxes	30,686	34,263
Net income	\$ 46,779	\$ 52,704
Other comprehensive income (loss):		
Reclassification of realized losses on cash flow hedges, net of tax, to earnings	3,135	—
Unrealized loss on cash flow hedges, net of tax	(238)	(1,256)
Foreign currency translation adjustments	(977)	—
Comprehensive income	\$ 48,699	\$ 51,448

See notes to unaudited condensed consolidated financial statements.

**J.CREW GROUP, INC.****Condensed Consolidated Statements of Changes in Stockholders' Equity**  
**(unaudited)**  
**(in thousands, except shares)**

	<u>Common Stock</u>		<u>Additional paid-in capital</u>	<u>Retained earnings</u>	<u>Accumulated other comprehensive loss</u>	<u>Total stockholders' equity</u>
	<u>Shares</u>	<u>Amount</u>				
<b>Balance at January 28, 2012</b>	<u>1,000</u>	<u>\$ —</u>	<u>\$ 1,183,606</u>	<u>\$ 12,409</u>	<u>\$ (18,963)</u>	<u>\$ 1,177,052</u>
Net income	—	—	—	96,087	—	96,087
Share-based compensation	—	—	5,284	—	—	5,284
Contribution from Parent, net	—	—	11,744	—	—	11,744
Dividend	—	—	(197,450)	—	—	(197,450)
Net loss on cash flow hedges, net of tax	—	—	—	—	(1,226)	(1,226)
<b>Balance at February 2, 2013</b>	<u>1,000</u>	<u>\$ —</u>	<u>\$ 1,003,184</u>	<u>\$ 108,496</u>	<u>\$ (20,189)</u>	<u>\$ 1,091,491</u>
Net income	—	—	—	46,779	—	46,779
Share-based compensation	—	—	2,845	—	—	2,845
Contribution to Parent	—	—	(454)	—	—	(454)
Reclassification of realized losses on cash flow hedges, net of tax, to earnings	—	—	—	—	3,135	3,135
Unrealized gain (loss) on cash flow hedges, net of tax	—	—	—	—	(238)	(238)
Foreign currency translation adjustments	—	—	—	—	(977)	(977)
<b>Balance at August 3, 2013</b>	<u>1,000</u>	<u>\$ —</u>	<u>\$ 1,005,575</u>	<u>\$ 155,275</u>	<u>\$ (18,269)</u>	<u>\$ 1,142,581</u>

See notes to unaudited condensed consolidated financial statements.

**J.CREW GROUP, INC.****Condensed Consolidated Statements of Cash Flows  
(unaudited)  
(in thousands)**

	Twenty-six Weeks Ended August 3, 2013	Twenty-six Weeks Ended July 28, 2012
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 46,779	\$ 52,704
Adjustments to reconcile to cash flows from operating activities:		
Depreciation of property and equipment	38,561	33,967
Share-based compensation	2,845	2,141
Amortization of favorable lease commitments	4,458	6,835
Amortization of intangible assets	4,692	4,902
Amortization of deferred financing costs	4,970	4,801
Realized hedging losses	5,140	—
Changes in operating assets and liabilities:		
Merchandise inventories	(55,869)	(40,152)
Prepaid expenses and other current assets	(7,490)	(9,245)
Other assets	(1,540)	199
Accounts payable and other liabilities	51,423	21,992
Federal and state income taxes	6,318	(4,708)
Net cash provided by operating activities	<u>100,287</u>	<u>73,436</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Capital expenditures	(63,029)	(75,590)
Net cash used in investing activities	<u>(63,029)</u>	<u>(75,590)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Repayment of debt	(6,000)	(6,000)
Contribution to Parent	(454)	(232)
Net cash used in financing activities	<u>(6,454)</u>	<u>(6,232)</u>
Effect of changes in foreign exchange rates on cash and cash equivalents	(367)	—
Increase (decrease) in cash and cash equivalents	30,437	(8,386)
Beginning balance	68,399	221,852
Ending balance	<u>\$ 98,836</u>	<u>\$ 213,466</u>
<b>Supplemental cash flow information:</b>		
Income taxes paid	<u>\$ 27,423</u>	<u>\$ 39,369</u>
Interest paid	<u>\$ 44,319</u>	<u>\$ 50,396</u>

See notes to unaudited condensed consolidated financial statements.

**J.CREW GROUP, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****For the thirteen and twenty-six weeks ended August 3, 2013 and July 28, 2012****(Dollars in thousands, unless otherwise indicated)****1. Basis of Presentation**

J.Crew Group, Inc. and its wholly owned subsidiaries (the “Company” or “Group”) was acquired (the “Acquisition”) on March 7, 2011 through a merger with a subsidiary of Chinos Holdings, Inc. (the “Parent”). The Parent was formed by investment funds affiliated with TPG Capital, L.P. (“TPG”) and Leonard Green & Partners, L.P. (“LGP” and together with TPG, the “Sponsors”). Subsequent to the Acquisition, Group became an indirect, wholly owned subsidiary of Parent, which is owned by affiliates of the Sponsors, co-investors and members of management. Prior to March 7, 2011, the Company operated as a public company with its common stock traded on the New York Stock Exchange.

The accompanying unaudited condensed consolidated financial statements were prepared in accordance with generally accepted accounting principles (“GAAP”) for interim financial information. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. Therefore, these financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K for the fiscal year ended February 2, 2013.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, necessary to present fairly in all material respects the Company’s financial position, results of operations and cash flows for the applicable interim periods. Certain prior year amounts have been reclassified to conform to current period presentation. The results of operations for these periods are not necessarily comparable to, or indicative of, results of any other interim period or for the fiscal year as a whole.

Management is required to make estimates and assumptions about future events in preparing financial statements in conformity with generally accepted accounting principles. These estimates and assumptions affect the amounts of assets, liabilities, revenues and expenses and the disclosure of loss contingencies at the date of the unaudited condensed consolidated financial statements. While management believes that past estimates and assumptions have been materially accurate, current estimates are subject to change if different assumptions as to the outcome of future events are made. Management evaluates estimates and judgments on an ongoing basis and predicates those estimates and judgments on historical experience and on reasonable factors. Since future events and their effects cannot be determined with absolute certainty, actual results may differ from the estimates used in preparing the accompanying unaudited condensed consolidated financial statements.

**2. Management Services Agreement**

Pursuant to a management services agreement entered into in connection with the Acquisition, and in exchange for on-going consulting and management advisory services, the Sponsors receive an aggregate annual monitoring fee prepaid quarterly equal to the greater of (i) 40 basis points of consolidated annual revenues or (ii) \$8 million. The Sponsors also receive reimbursement for out-of-pocket expenses incurred in connection with services provided pursuant to the agreement. The Company recorded an expense of \$4.9 million in the first half of fiscal 2013 for monitoring fees and out-of-pocket expenses, included in selling, general and administrative expenses in the statements of operations and comprehensive income.

**3. Goodwill and Intangible Assets**

The significant components of our intangible assets and goodwill are as follows:

	Loyalty Program and <u>Customer Lists</u>	Favorable Lease <u>Commitments</u>	Madewell <u>Brand Name</u>	J.Crew <u>Brand Name</u>	<u>Goodwill</u>
Balance at February 2, 2013	\$ 16,075	\$ 35,104	\$ 74,142	\$ 885,300	\$ 1,686,915
Amortization expense	(1,342)	(2,356)	(1,025)	—	—
Balance at May 4, 2013	\$ 14,733	\$ 32,748	\$ 73,117	\$ 885,300	\$ 1,686,915
Amortization expense	(1,300)	(2,102)	(1,025)	—	—
Balance at August 3, 2013	\$ 13,433	\$ 30,646	\$ 72,092	\$ 885,300	\$ 1,686,915
Total accumulated amortization at August 3, 2013	\$ (13,577)	\$ (30,364)	\$ (9,908)		

#### 4. Share-Based Compensation

##### *Chinos Holdings, Inc. 2011 Equity Incentive Plan*

During the first half of fiscal 2013, the Parent issued 9,416,000 options to certain members of management, including (i) 4,683,000 options with an exercise price of \$1.10 that become exercisable over a period of up to seven years and (ii) 4,733,000 options with an exercise price of \$1.10 that only become exercisable when certain owners of the Parent receive a specified level of cash proceeds, as defined in the equity incentive plan, from the sale of their initial investment. The options have terms of up to ten years. The weighted average grant-date fair value of the time-based awards granted in the first half was \$0.49 per share. Expense associated with the options exercisable when certain owners of the Parent receive a specified level of cash proceeds will not be recognized until that event occurs.

A summary of share-based compensation recorded in the statements of operations and comprehensive income is as follows:

	For the Twenty-six Weeks Ended August 3, 2013	For the Twenty-six Weeks Ended July 28, 2012
Share-based compensation	\$ 2,845	\$ 2,141

A summary of shares available for grant as stock options or other share-based awards is as follows:

	Shares
Available for grant at February 2, 2013	24,790,408
Granted	(9,452,750)
Forfeited and available for reissuance	1,400,900
Available for grant at August 3, 2013	16,738,558

#### 5. Long-Term Debt and Credit Agreements

A summary of the components of the Company's long-term debt is as follows:

	August 3, 2013	February 2, 2013
Term Loan	\$ 1,173,000	\$ 1,179,000
Notes	400,000	400,000
Less: current portion of Term Loan	(12,000)	(12,000)
Long-term debt	\$ 1,561,000	\$ 1,567,000
Borrowings under ABL Facility	\$ —	\$ —

In connection with the Acquisition, we entered into debt financing comprised of (i) \$1,450 million of senior secured credit facilities (the "Senior Credit Facilities") consisting of (a) a \$250 million, 5-year asset-based revolving credit facility (the "ABL Facility") and (b) a \$1,200 million, 7-year term loan credit facility due 2018 (the "Term Loan Facility"), and (ii) \$400 million of 8.125% senior notes due 2019 (the "Notes").

##### Term Loan

On December 18, 2012, the Term Loan Facility was amended to, among other things, (i) permit a one-time dividend to Chinos Intermediate Holdings B, Inc. (and by Chinos Intermediate Holdings B, Inc. to any of its direct or indirect parents) in an amount up to \$200 million and (ii) modify certain exceptions to the restrictive covenants in the credit agreement governing the Term Loan Facility that restrict the ability of Chinos Intermediate Holdings B, Inc., Group and its subsidiaries to pay dividends on, or redeem or repurchase capital stock, prepay certain indebtedness and make investments.

On February 4, 2013, the Company further amended the Term Loan Facility to, among other things, replace the \$1,179 million in term loans outstanding immediately prior to the amendment with a new class of term loans, and reduce the applicable margin and LIBOR floor with respect to the new class of term loans. Borrowings under the Term Loan Facility bear interest at a rate per annum equal to an applicable margin plus, at Group's option, either (a) LIBOR determined by reference to the costs of funds for U.S. dollar deposits for an interest period of one month adjusted for certain additional costs (subject to a floor) or (b) a base rate determined by reference to the highest of (1) the prime rate of Bank of America, N.A., (2) the federal funds effective rate plus 0.50% and (3) a LIBOR determined by reference to the costs of funds for U.S. dollar deposits for an interest period of one month adjusted for certain additional costs, plus 1.00%. Following the amendment, the applicable margin with respect to base rate borrowings is 2.00% and the LIBOR floor and applicable margin with respect to LIBOR borrowings are 1.00% and 3.00%, respectively. In addition, the Term Loan Facility provides for an incremental 0.25% step-down in applicable margin at any time on and after May 6, 2013 when Group's corporate family rating, as publicly announced by Moody's, is B1 or better.

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The Company is required to make principal repayments equal to 0.25% of the original \$1,200 million principal amount of the term loan, or \$3 million, on the last business day of January, April, July, and October. The Company is also required to repay the term loan based on annual excess cash flow as defined in the agreement, under certain circumstances. Borrowings under the Term Loan mature on March 7, 2018.

The interest rate on the \$1,173 million in outstanding borrowings pursuant to the Term Loan Facility was 4.00% on August 3, 2013.

Credit Facilities

Average short-term borrowings under the ABL Facility were \$4.9 million in the first half of fiscal 2013. Outstanding standby letters of credit were \$5.7 million and excess availability, as defined, was \$244.3 million at August 3, 2013. Additionally, the Company has an unsecured demand letter of credit facility with HSBC which provides for the issuance of up to \$35 million of documentary letters of credit on a no fee basis. Outstanding letters of credit under this facility were \$16.5 million and availability was \$18.5 million at August 3, 2013.

Interest expense

A summary of the significant components of interest expense is as follows:

	For the Twenty-six Weeks Ended August 3, 2013	For the Twenty-six Weeks Ended July 28, 2012
Term Loan	\$ 25,076	\$ 28,581
Notes	16,250	16,250
Realized hedging losses	5,140	—
Amortization of deferred financing costs	4,970	4,801
Other, net of interest income	484	1,139
Interest expense, net	<u>\$ 51,920</u>	<u>\$ 50,771</u>

**6. Derivative Financial Instruments**

***Interest Rate Swaps***

In April 2011, the Company entered into floating-to-fixed interest rate swap agreements for an aggregate notional amount of \$600 million. These instruments limit exposure to interest rate increases related to a portion of the Company's floating rate indebtedness through the expiration of the agreements in March 2016. As a result of the agreements, the Company's effective fixed interest rate on the notional amount of floating rate indebtedness is 3.56% plus the applicable margin.

During the first half of fiscal 2013, the Company realized hedging losses of \$5.1 million pursuant to the interest rate swap agreements. Such losses were included in interest expense, net in the statement of operations and comprehensive income.

The Company expects to reclassify unrealized losses of approximately \$8 million, net of tax, previously recorded in accumulated other comprehensive loss, thereby increasing interest expense by \$13 million in the next 12 months.

***Fair Value***

As of the effective date, the Company designated the interest rate swap agreements as cash flow hedges. As cash flow hedges, unrealized gains are recognized as assets while unrealized losses are recognized as liabilities. The interest rate swap agreements are highly correlated to the changes in interest rates to which the Company is exposed. Unrealized gains and losses on these instruments are designated as effective or ineffective. The effective portion of such gains or losses is recorded as a component of accumulated other comprehensive income or loss, while the ineffective portion of such gains or losses will be recorded as a component of interest expense. Future realized gains and losses in connection with each required interest payment will be reclassified from accumulated other comprehensive income or loss to interest expense.

The fair values of the interest rate swap agreements are estimated using industry standard valuation models using market-based observable inputs, including interest rate curves (level 2 inputs). The fair value of the interest rate swaps, recorded in other liabilities, was \$29,769 and \$33,266 at August 3, 2013 and February 2, 2013, respectively.

## 7. Fair Value Measurements

The Company uses a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Observable inputs, other than quoted prices included in Level 1, such as quoted prices for markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

### *Financial assets and liabilities*

The fair value of the Company's debt is estimated to be \$1,604 million and \$1,617 million at August 3, 2013 and February 2, 2013 based on quoted market prices of the debt (level 1 inputs).

In April 2011, the Company entered into interest rate swap agreements in order to hedge the variability of cash flows related to a portion of the Company's floating rate indebtedness, which are measured in the financial statements at fair value on a recurring basis. See note 6 for more information regarding the fair value of this financial liability.

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts payable and other current liabilities approximate fair value because of their short-term nature.

### *Non-financial assets and liabilities*

Except for certain leasehold improvements, the Company does not have any non-financial assets or liabilities as of August 3, 2013 or February 2, 2013 that are measured in the financial statements at fair value.

The Company performs impairment tests of certain long-lived assets whenever there are indicators of impairment. These tests typically contemplate assets at a store level (e.g. leasehold improvements). The Company recognizes an impairment loss when the carrying value of a long-lived asset is not recoverable in light of the undiscounted future cash flows and measures an impairment loss as the difference between the carrying amount and fair value of the asset based on discounted future cash flows. The Company has determined that the future cash flow approach (level 3 inputs) provides the most relevant and reliable means by which to determine fair value in this circumstance.

A summary of the impact of the impairment of certain long-lived assets on financial condition and results of operations is as follows:

	For the Twenty-six Weeks Ended August 3, 2013	For the Twenty-six Weeks Ended July 28, 2012
Carrying value of long-term assets written down to fair value	\$ 673	\$ 160
Impairment charge	\$ 673	\$ 160

## 8. Income Taxes

The Parent files a consolidated federal income tax return, which includes Group and all of its wholly owned subsidiaries. Each subsidiary files separate, or combined where required, state or local tax returns in required jurisdictions.

During the second quarter of fiscal 2013, the Internal Revenue Service concluded its examination of tax returns for periods ended January 2010 through March 7, 2011. No adjustments were made to the tax returns as a result of the examination. Tax returns for the period ended January 2012 are subject to examination. Various state and local jurisdiction tax authorities are in the process of examining income tax returns or hearing appeals for certain tax years ranging from 2008 to 2011. The results of these audits and appeals are not expected to have a significant effect on the results of operations or financial position.

The differences between the U.S. statutory income tax rate of 35% and the effective tax rates for the twenty-six weeks ended August 3, 2013 and July 28, 2012 of 39.6% and 39.4%, respectively, are primarily driven by state and local income taxes, net of federal benefit.

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While the Company expects the amount of unrecognized tax benefits to change in the next twelve months, the change is not expected to have a significant effect on the estimated effective annual tax rate, the results of operations or financial position. However, the outcome of tax matters is uncertain and unforeseen results can occur.

## **9. Legal Proceedings**

On June 20, 2013, a purported class action complaint was filed in the United States District Court for the District of Massachusetts by an individual claiming that the Company collected her ZIP code unlawfully in connection with a retail purchase she made at a Massachusetts store. That action, captioned *Miller v. J.Crew Group, Inc.*, 13-cv-11487 (the “Miller Action”), purports to be brought on behalf of a class of customers whose ZIP codes were collected and recorded at Company stores in Massachusetts in connection with credit card purchases, and claims that the Company used the collected ZIP code data to obtain customers’ addresses for purposes of mailing them unwanted advertising material. The Miller Action seeks money damages pursuant to a claim under Chapter 93A of the General Laws of Massachusetts and a claim for unjust enrichment. The Company believes the complaint is without merit and intends to defend against the Plaintiff’s claims. However, it is reasonably possible that the Company may incur a loss in connection with the Miller Action. The amount of such loss, if any, cannot be estimated as of the date these financial statements are issued.

The Company is also subject to various legal proceedings and claims arising in the ordinary course of business. Management does not expect that the results of any of these legal proceedings, either individually or in the aggregate, would have a material impact on the Company’s financial position, results of operations or cash flows.

## **10. Recent Accounting Pronouncements**

In December 2011, a pronouncement was issued that amended the guidance related to the disclosure of recognized financial instruments and derivative instruments that are either offset on the balance sheet or subject to an enforceable master netting arrangement or similar agreement. The amended provisions are effective for fiscal years beginning on or after January 1, 2013, and are required to be applied retrospectively for all prior periods presented. As this pronouncement relates to disclosure only, the adoption of this amendment did not have a significant impact on the Company’s condensed consolidated financial statements.

In February 2013, a pronouncement was issued that clarified the guidance relating to the reporting of reclassifications out of accumulated other comprehensive income depending on the significance of the reclassifications and whether they are required by U.S. GAAP. The pronouncement is effective for reporting periods beginning after December 15, 2012. The Company adopted this pronouncement on February 3, 2013. The adoption of this guidance required changes in presentation only and therefore did not have a significant impact on the Company’s condensed consolidated financial statements.

***Forward-Looking Statements***

This report contains “forward-looking statements,” which include information concerning our plans, objectives, goals, strategies, future events, future revenues or performance, capital expenditures, financing needs and other information that is not historical information. When used in this report, the words “estimate,” “expect,” “anticipate,” “project,” “plan,” “intend,” “believe” and variations of such words or similar expressions are intended to identify forward-looking statements. All forward-looking statements, including, without limitation, our examination of operating trends, are based upon our current expectations and various assumptions. We believe there is a reasonable basis for our expectations and beliefs, but there can be no assurance that we will realize our expectations or that our beliefs will prove correct.

There are a number of risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements contained in this report. Important factors that could cause our actual results to differ include, but are not limited to, our substantial indebtedness and lease obligations, the strength of the global economy, declines in consumer spending or changes in seasonal consumer spending patterns, competitive market conditions, our ability to anticipate and timely respond to changes in trends and consumer preferences, our ability to successfully develop, launch and grow our newer concepts and execute on strategic initiatives, products offerings, sales channels and businesses, material disruption to our information systems, our ability to implement our real estate strategy, our ability to attract and retain key personnel, interruptions in our foreign sourcing operations, and other factors which are set forth in the section entitled “Risk Factors” and elsewhere in our Annual Report on Form 10-K for the fiscal year ended February 2, 2013 filed with the SEC. There may be other factors of which we are currently unaware or deem immaterial that may cause our actual results to differ materially from the forward-looking statements.

All forward-looking statements attributable to us or persons acting on our behalf apply only as of the date they are made and are expressly qualified in their entirety by the cautionary statements included in this report. Except as may be required by law, we undertake no obligation to publicly update or revise any forward-looking statement to reflect events or circumstances occurring after the date they were made or to reflect the occurrence of unanticipated events.

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

This document should be read in conjunction with the Management's Discussion and Analysis section of our Annual Report on Form 10-K for the fiscal year ended February 2, 2013 filed with the SEC. When used herein, the terms "J.Crew," "Group," "Company," "we," "us" and "our" refer to J.Crew Group, Inc., including its wholly-owned consolidated subsidiaries.

**Executive Overview**

J.Crew is a nationally recognized apparel and accessories retailer that differentiates itself through high standards of quality, style, design and fabrics with consistent fits and authentic details. We are an integrated multi-channel, multi-brand specialty retailer that operates stores and websites to consistently communicate with our customers. We design, market and sell our products, including those under the J.Crew®, crewcuts® and Madewell® brands, offering complete assortments of women's, men's and children's apparel and accessories. We believe our customer base consists primarily of affluent, college-educated, professional and fashion-conscious women and men.

We conduct our business through two primary sales channels: (1) *Stores*, which consists of our retail, factory and Madewell stores, and (2) *Direct*, which consists of our websites and catalogs. As of August 3, 2013, we operated 309 retail stores (including eight crewcuts and 56 Madewell stores), 112 factory stores (including three crewcuts factory stores), and two clearance stores, throughout the United States and Canada; compared to 279 retail stores (including eight crewcuts and 39 Madewell stores), 97 factory stores (including four crewcuts factory stores), and three clearance stores as of July 28, 2012.

A summary of revenues for the second quarter is as follows:

<u>(Dollars in millions)</u>	For the	For the
	Thirteen	Thirteen
	Weeks Ended	Weeks Ended
	August 3, 2013	July 28, 2012
Stores	\$ 399.1	\$ 384.0
Direct	151.8	134.0
Net sales	550.9	518.0
Other, primarily shipping and handling fees	8.2	7.5
Total revenues	\$ 559.1	\$ 525.5

A summary of highlights for the second quarter is as follows:

- Revenues increased 6.4% to \$559.1 million.
- Comparable company sales decreased 0.6%.
- Direct net sales increased 13.4% to \$151.8 million.
- Income from operations decreased \$6.3 million to \$55.8 million.
- We opened three J.Crew retail stores, five J.Crew factory stores, and four Madewell stores.

A summary of revenues for the first half is as follows:

<u>(Dollars in millions)</u>	For the	For the
	Twenty-six	Twenty-six
	Weeks Ended	Weeks Ended
	August 3, 2013	July 28, 2012
Stores	\$ 779.3	\$ 738.0
Direct	328.0	277.4
Net sales	1,107.3	1,015.4
Other, primarily shipping and handling fees	15.9	13.6
Total revenues	\$ 1,123.2	\$ 1,029.0

A summary of highlights for the first half is as follows:

- Revenues increased 9.2% to \$1,123.2 million.

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- Comparable company sales increased 2.4%.
- Direct net sales increased 18.2% to \$328.0 million.
- Income from operations decreased \$8.3 million to \$129.4 million.
- We opened six J.Crew retail stores, six J.Crew factory stores, and eight Madewell stores.

***How We Assess the Performance of Our Business***

In assessing the performance of our business, we consider a variety of performance and financial measures. A key measure used in our evaluation is comparable company sales, which includes (i) net sales from stores that have been open for at least twelve months, (ii) direct net sales, and (iii) shipping and handling fees.

A complete description of the measures we use to assess the performance of our business appears in the Management’s Discussion and Analysis section of our Annual Report on Form 10-K for the fiscal year ended February 2, 2013 filed with the SEC.

***Results of Operations – Second Quarter of Fiscal 2013 compared to Second Quarter of Fiscal 2012***

<u>(Dollars in millions)</u>	<u>Thirteen Weeks Ended August 3, 2013</u>		<u>Thirteen Weeks Ended July 28, 2012</u>		<u>Variance Increase /(Decrease)</u>	
	<u>Amount</u>	<u>Percent of Revenues</u>	<u>Amount</u>	<u>Percent of Revenues</u>	<u>Dollars</u>	<u>Percentage</u>
Revenues	\$ 559.1	100.0%	\$ 525.5	100.0%	\$ 33.6	6.4%
Gross profit	230.0	41.1	236.7	45.1	(6.7)	(2.8)
Selling, general and administrative expenses	174.2	31.2	174.7	33.2	(0.5)	(0.3)
Income from operations	55.8	10.0	62.1	11.8	(6.3)	(10.2)
Interest expense, net	26.2	4.7	25.4	4.8	0.8	3.5
Provision for income taxes	12.1	2.2	14.7	2.8	(2.6)	(17.9)
Net income	\$ 17.5	3.1%	\$ 22.0	4.2%	\$ (4.5)	(20.7)%

***Revenues***

Revenues increased \$33.6 million, or 6.4%, to \$559.1 million in the second quarter of fiscal 2013 from \$525.5 million in the second quarter last year, driven primarily by an increase in sales of men’s apparel, specifically woven shirts, shorts and pants. Comparable company sales decreased 0.6% in the second quarter of fiscal 2013. Comparable company sales increased 13.6% in the second quarter of fiscal 2012.

Stores sales increased \$15.1 million, or 3.9%, to \$399.1 million in the second quarter of fiscal 2013 from \$384.0 million in the second quarter last year. Stores sales increased 23.5% in the second quarter of fiscal 2012. Sales from stores that have been open for less than twelve months were \$56.1 million in the second quarter of fiscal 2013.

Direct sales increased \$17.8 million, or 13.4%, to \$151.8 million in the second quarter of fiscal 2013 from \$134.0 million in the second quarter last year. Direct sales increased \$18.0 million, or 15.5%, in the second quarter of fiscal 2012.

The approximate percentage of our sales by product category, based on our internal merchandising system, is as follows:

	<u>For the Thirteen Weeks Ended August 3, 2013</u>	<u>For the Thirteen Weeks Ended July 28, 2012</u>
Apparel:		
Women’s	5 6%	5 9%
Men’s	26	24
Children’s	6	5
Accessories	12	12
	<u>100%</u>	<u>100%</u>

Other revenues increased \$0.7 million to \$8.2 million in the second quarter of fiscal 2013 from \$7.5 million in the second quarter last year.

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[Table of Contents](#)**Gross Profit**

Gross profit decreased \$6.7 million to \$230.0 million in the second quarter of fiscal 2013 from \$236.7 million in the second quarter last year. This decrease resulted from the following factors:

<u>(Dollars in millions)</u>	<u>Increase/ (decrease)</u>
Increase in revenues	\$ 19.1
Decrease in merchandise margin	(16.0)
Increase in buying and occupancy costs	<u>(9.8)</u>
Decrease in gross profit	<u>\$ (6.7)</u>

Gross margin decreased to 41.1% in the second quarter of fiscal 2013 from 45.1% in the second quarter last year. The decrease in gross margin was driven by: (i) a 290 basis point deterioration in merchandise margin primarily due to increased markdowns and (ii) a 110 basis point increase in buying and occupancy costs as a percentage of revenues.

**Selling, General and Administrative Expenses**

Selling, general and administrative expenses decreased \$0.5 million to \$174.2 million in the second quarter of fiscal 2013 from \$174.7 million in the second quarter last year. This decrease primarily resulted from the following:

<u>(Dollars in millions)</u>	<u>Increase/ (decrease)</u>
Decrease in share-based and incentive compensation	<u>\$(11.9)</u>
Insurance proceeds	(3.0)
Increase in operating expenses, primarily Stores and payroll	5.4
Increase in advertising and catalog costs	3.1
Increase in depreciation	1.8
Other, net	4.1
Decrease in selling, general and administrative expenses	<u>\$ (0.5)</u>

As a percentage of revenues, selling, general and administrative expenses decreased to 31.2% in the second quarter of fiscal 2013 from 33.2% in the second quarter last year.

**Interest Expense, Net**

Interest expense, net of interest income, increased \$0.8 million to \$26.2 million in the second quarter of fiscal 2013 from \$25.4 million in the second quarter last year. A summary of interest expense is as follows:

<u>(Dollars in millions)</u>	<u>For the Thirteen Weeks Ended August 3, 2013</u>	<u>For the Thirteen Weeks Ended July 28, 2012</u>
Term Loan	\$ 11.9	\$ 14.3
Notes	8.1	8.1
Realized hedging losses	3.5	—
Amortization of deferred financing costs	2.5	2.4
Other, net of interest income	0.2	0.6
Interest expense, net	<u>\$ 26.2</u>	<u>\$ 25.4</u>

**Provision for Income Taxes**

The effective tax rates for the second quarter of fiscal 2013 and 2012 were approximately 40%. The differences between the statutory rate of 35% and the effective rates were driven primarily by state and local income taxes, net of federal benefit.

**Net Income**

Net income decreased \$4.5 million to \$17.5 million in the second quarter of fiscal 2013 from \$22.0 million in the second quarter last year. This decrease was due to: (i) a decrease in gross profit of \$6.7 million and (ii) an increase in interest expense of \$0.8 million, offset by (iii) a decrease in the provision for income taxes of \$2.6 million and (iv) a decrease in selling, general and administrative expenses of \$0.5 million.

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**Results of Operations – First Half of Fiscal 2013 compared to First Half of Fiscal 2012**

(Dollars in millions)	Twenty-six Weeks Ended August 3, 2013		Twenty-six Weeks Ended July 28, 2012		Variance Increase / (Decrease)	
	Amount	Percent of Revenues	Amount	Percent of Revenues	Dollars	Percentage
Revenues	\$1,123.2	100.0%	\$1,029.0	100.0%	\$94.2	9.2%
Gross profit	482.0	42.9	476.5	46.3	5.5	1.2
Selling, general and administrative expenses	352.6	31.4	338.8	32.9	13.8	4.1
Income from operations	129.4	11.5	137.7	13.4	(8.3)	(6.1)
Interest expense, net	51.9	4.6	50.8	4.9	1.1	2.3
Provision for income taxes	30.7	2.7	34.3	3.3	(3.6)	(10.4)
Net income	\$ 46.8	4.2%	\$ 52.7	5.1%	\$ (5.9)	(11.2)%

**Revenues**

Revenues increased \$94.2 million, or 9.2%, to \$1,123.2 million in the first half of fiscal 2013 from \$1,029.0 million in the first half last year, driven primarily by an increase in sales of (i) men's apparel, specifically woven shirts, pants, and suiting and (ii) women's apparel, specifically knits, shirts, and sweaters. Comparable company sales increased 2.4% in the first half of fiscal 2013. Comparable company sales increased 14.8% in the first half of fiscal 2012.

Stores sales increased \$41.3 million, or 5.6%, to \$779.3 million in the first half of fiscal 2013 from \$738.0 million in the first half last year. Stores sales increased 24.6% in the first half of fiscal 2012. Sales from stores that have been open for less than twelve months were \$105.0 million in the first half of fiscal 2013.

Direct sales increased \$50.6 million, or 18.2%, to \$328.0 million in the first half of fiscal 2013 from \$277.4 million in the first half last year. Direct sales increased \$41.1 million, or 17.4%, in the first half of fiscal 2012.

The approximate percentage of our sales by product category, based on our internal merchandising system, is as follows:

	For the Twenty-six Weeks Ended August 3, 2013	For the Twenty-six Weeks Ended July 28, 2012
Apparel:		
Women's	57%	60%
Men's	24	22
Children's	6	6
Accessories	13	12
	<u>100%</u>	<u>100%</u>

Other revenues increased \$2.3 million to \$15.9 million in the first half of fiscal 2013 from \$13.6 million in the first half last year.

**Gross Profit**

Gross profit increased \$5.5 million to \$482.0 million in the first half of fiscal 2013 from \$476.5 million in the first half last year. This increase resulted from the following factors:

(Dollars in millions)	Increase/ (decrease)
Increase in revenues	\$ 54.7
Decrease in merchandise margin	(31.4)
Increase in buying and occupancy costs	(17.8)
Increase in gross profit	<u>\$ 5.5</u>

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Gross margin decreased to 42.9% in the first half of fiscal 2013 from 46.3% in the first half last year. The decrease in gross margin was driven by: (i) a 280 basis point deterioration in merchandise margin primarily due to increased markdowns and (ii) a 60 basis point increase in buying and occupancy costs as a percentage of revenues.

### ***Selling, General and Administrative Expenses***

Selling, general and administrative expenses increased \$13.8 million to \$352.6 million in the first half of fiscal 2013 from \$338.8 million in the first half last year. This increase primarily resulted from the following:

<u>(Dollars in millions)</u>	<u>Increase/ (decrease)</u>
Increase in operating expenses, primarily Stores and payroll	\$ 14.4
Increase in advertising and catalog costs	6.9
Increase in depreciation	4.4
Decrease in share-based and incentive compensation	(16.6)
Insurance proceeds	(3.3)
Other, net	8.0
Increase in selling, general and administrative expenses	<u>\$ 13.8</u>

As a percentage of revenues, selling, general and administrative expenses decreased to 31.4% in the first half of fiscal 2013 from 32.9% in the first half last year.

### ***Interest Expense, Net***

Interest expense, net of interest income, increased \$1.1 million to \$51.9 million in the first half of fiscal 2013 from \$50.8 million in the first half last year. A summary of interest expense is as follows:

<u>(Dollars in millions)</u>	<u>For the Twenty-six Weeks Ended August 3, 2013</u>	<u>For the Twenty-six Weeks Ended July 28, 2012</u>
Term Loan	\$ 25.1	\$ 28.6
Notes	16.3	16.3
Realized hedging losses	5.1	—
Amortization of deferred financing costs	5.0	4.8
Other, net of interest income	0.4	1.1
Interest expense, net	<u>\$ 51.9</u>	<u>\$ 50.8</u>

### ***Provision for Income Taxes***

The effective tax rates for the first half of fiscal 2013 and 2012 were approximately 40%. The differences between the statutory rate of 35% and the effective rates were driven primarily by state and local income taxes, net of federal benefit.

### ***Net Income***

Net income decreased \$5.9 million to \$46.8 million in the first half of fiscal 2013 from \$52.7 million in the first half last year. This decrease was due to: (i) an increase in selling, general and administrative expenses of \$13.8 million and (ii) an increase in interest expense of \$1.1 million, offset by (iii) an increase in gross profit of \$5.5 million and (iv) a decrease in the provision for income taxes of \$3.6 million.

### ***Liquidity and Capital Resources***

Our primary sources of liquidity are our current balances of cash and cash equivalents, cash flows from operations and borrowings available under the ABL Facility. Our primary cash needs are capital expenditures in connection with opening new stores and remodeling our existing stores, investments in our distribution network, making information technology system enhancements, meeting debt service requirements and funding working capital requirements. The most significant components of our working capital are cash and cash equivalents, merchandise inventories, accounts payable and other current liabilities. See “—Outlook” below.

[Table of Contents](#)**Operating Activities**

<u>(Dollars in millions)</u>	<u>For the Twenty-six Weeks Ended August 3, 2013</u>	<u>For the Twenty-six Weeks Ended July 28, 2012</u>
Net income	\$ 46.8	\$ 52.7
Adjustments to reconcile to cash flows from operating activities:		
Depreciation of property and equipment	38.6	34.0
Share-based compensation	2.8	2.1
Amortization of favorable lease commitments	4.5	6.8
Amortization of intangible assets	4.7	4.9
Amortization of deferred financing costs	5.0	4.8
Realized hedging losses	5.1	—
Changes in operating assets and liabilities	(7.2)	(31.9)
Net cash provided by operating activities	<u>\$ 100.3</u>	<u>\$ 73.4</u>

Cash provided by operating activities of \$100.3 million in the first half of fiscal 2013 was driven by: (i) net income of \$46.8 million, (ii) non-cash expenses of \$60.7 million, offset by (iii) changes in operating assets and liabilities of \$7.2 million due to seasonal working capital fluctuations and working capital management.

Cash provided by operating activities of \$73.4 million in the first half of fiscal 2012 was driven by: (i) net income of \$52.7 million, (ii) non-cash expenses of \$52.6 million, offset by (iii) changes in operating assets and liabilities of \$31.9 million due to seasonal working capital fluctuations.

**Investing Activities**

	<u>For the Twenty-six Weeks Ended August 3, 2013</u>	<u>For the Twenty-six Weeks Ended July 28, 2012</u>
Capital expenditures:		
New stores	\$ 27.9	\$ 26.0
Information technology	21.4	20.5
Other(1)	13.7	29.1
Net cash used in investing activities	<u>\$ 63.0</u>	<u>\$ 75.6</u>

(1) Includes capital expenditures for warehouse and corporate office improvements, store renovations and general corporate purposes.

Capital expenditures are planned at approximately \$135 to \$145 million for fiscal year 2013, including \$55 to \$60 million for new stores, \$40 to \$45 million for information technology enhancements, \$15 to \$20 million for warehouse and corporate office improvements, and the remainder for store renovations and general corporate purposes.

**Financing Activities**

	<u>For the Twenty-six Weeks Ended August 3, 2013</u>	<u>For the Twenty-six Weeks Ended July 28, 2012</u>
Repayment of debt	\$ (6.0)	\$ (6.0)
Contribution to Parent	(0.5)	(0.2)
Net cash used in financing activities	<u>\$ (6.5)</u>	<u>\$ (6.2)</u>

Cash used in financing activities was \$6.5 million in the first half of fiscal 2013 resulting primarily from quarterly principal repayments of debt under the Term Loan Facility.

Cash used in financing activities was \$6.2 million in the first half of fiscal 2012 resulting from quarterly principal repayments of debt under the Term Loan Facility.

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*Financing Arrangements*

ABL Facility

In connection with the Acquisition, on March 7, 2011, we entered into the ABL Facility, governed by an asset-based credit agreement with Bank of America, N.A., as administrative agent and the other agents and lenders party thereto, that provides senior secured financing of \$250 million (which may be increased by up to \$75 million in certain circumstances), subject to a borrowing base limitation. On October 11, 2012, we entered into an amendment to the ABL Facility (the "First ABL Amendment"), with Bank of America, N.A., as administrative agent, and the other lenders party thereto. The borrowing base under the ABL Facility equals the sum of: 90% of the eligible credit card receivables; plus, 85% of eligible accounts; plus, 90% (or 92.5% for the period of August 1 through December 31 of any fiscal year) of the net recovery percentage of eligible inventory multiplied by the cost of eligible inventory; plus, 85% of the net recovery percentage of eligible letters of credit inventory, multiplied by the cost of eligible letter of credit inventory; plus, 85% of the net recovery percentage of eligible in-transit inventory, multiplied by the cost of eligible in-transit inventory; plus, 100% of qualified cash; minus, all availability and inventory reserves. The ABL Facility includes borrowing capacity in the form of letters of credit up to the entire amount of the facility, and up to \$25 million in U.S. dollars for loans on same-day notice, referred to as swingline loans, and is available in U.S. dollars, Canadian dollars and Euros. Any amounts outstanding under the ABL Facility are due and payable in full on October 11, 2017.

Loans drawn under the ABL Facility bear interest at a rate per annum equal to, at Group's option, any of the following, plus, in each case, an applicable margin: (a) in the case of loans in U.S. dollars, a base rate determined by reference to the highest of (1) the prime rate of Bank of America, N.A., (2) the federal funds effective rate plus 0.50% and (3) a LIBOR determined by reference to the costs of funds for U.S. dollar deposits for an interest period of one month adjusted for certain additional costs, plus 1.00%; (b) in the case of loans in U.S. dollars or in Euros, a LIBOR determined by reference to the costs of funds for deposits in the relevant currency for the interest period relevant to such loan adjusted for certain additional costs; (c) in the case of loans in Canadian dollars, the average offered rate for Canadian dollar bankers' acceptances having an identical term of the applicable loan; and (d) in the case of loans in Canadian dollars, a fluctuating rate determined by reference to the higher of (1) the average offered rate for 30 day Canadian dollar bankers' acceptances plus 0.50% and (2) the prime rate of Bank of America, N.A. for loans in Canadian dollars. The applicable margin for loans under the ABL Facility varies based on Group's average historical excess availability and ranges from 0.50% to 1.00% with respect to base rate loans and loans in Canadian dollars bearing interest at the rate described in the immediately preceding clause (d), and from 1.50% to 2.00% with respect to LIBOR loans and loans in Canadian dollars bearing interest at the rate described in the immediately preceding clause (c). In addition, Group is required to pay a commitment fees of 0.25% per annum, in respect of the unused commitments as well as customary letter of credit and agency fees.

Average short-term borrowings under the ABL Facility were \$4.9 million in the first half of fiscal 2013. On August 3, 2013, outstanding standby letters of credit were \$5.7 million, excess availability, as defined, was \$244.3 million, and there were no borrowings outstanding.

Demand Letter of Credit Facility

The Company has an unsecured demand letter of credit facility with HSBC which provides for the issuance of up to \$35 million of documentary letters of credit on a no fee basis. On August 3, 2013, outstanding documentary letters of credit were \$16.5 million and availability was \$18.5 million under this facility.

Term Loan

In connection with the Acquisition, on March 7, 2011, we entered into the Term Loan Facility, governed by a \$1,200 million term loan credit agreement with Bank of America, N.A., as administrative agent and the other agents and lenders party thereto.

On December 18, 2012, the Term Loan Facility was amended to, among other things, (i) permit a one-time dividend to Chinos Intermediate Holdings B, Inc. (and by Chinos Intermediate Holdings B, Inc. to any of its direct or indirect parents) in an amount up to \$200 million and (ii) modify certain exceptions to the restrictive covenants in the credit agreement governing the Term Loan Facility that restrict the ability of Chinos Intermediate Holdings B, Inc., Group and its subsidiaries to pay dividends on, or redeem or repurchase capital stock, prepay certain indebtedness and make investments.

On February 4, 2013, we further amended the Term Loan Facility to, among other things, replace the \$1,179 million in term loans outstanding immediately prior to the amendment with a new class of term loans, and reduce the applicable margin and LIBOR floor with respect to the new class of term loans. Borrowings under the Term Loan Facility bear interest at a rate per annum equal to an applicable margin plus, at Group's option, either (a) LIBOR determined by reference to the costs of funds for U.S. dollar deposits for an interest period of one month adjusted for certain additional costs (subject to a floor) or (b) a base rate determined by reference to the highest of (1) the prime rate of Bank of America, N.A., (2) the federal funds effective rate plus 0.50% and (3) a LIBOR determined by reference to the costs of funds for U.S. dollar deposits for an interest period of one month adjusted for certain additional costs, plus 1.00%. Following the amendment, the applicable margin with respect to base rate borrowings is 2.00% and the LIBOR

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floor and applicable margin with respect to LIBOR borrowings are 1.00% and 3.00%, respectively. In addition, the Term Loan Facility provides for an incremental 0.25% step-down in applicable margin at any time on and after May 6, 2013 when Group's corporate family rating, as publicly announced by Moody's, is B1 or better.

We are required to make principal repayments equal to 0.25% of the original \$1,200 million principal amount of the term loan, or \$3 million, on the last business day of January, April, July, and October. We are also required to repay the term loan based on annual excess cash flow as defined in the agreement, under certain circumstances. Borrowings under the Term Loan mature on March 7, 2018.

The interest rate on the \$1,173 million in outstanding LIBOR borrowings pursuant to the Term Loan Facility was 4.00% on August 3, 2013.

**Outlook**

Our short-term and long-term liquidity needs arise primarily from (i) capital expenditures, (ii) debt service requirements, including quarterly principal payments and repayments based on annual excess cash flows as defined, and (iii) working capital needs. Management anticipates that capital expenditures in fiscal 2013 will be approximately \$135 to \$145 million, including \$55 to \$60 million for new stores, \$40 to \$45 million for information technology enhancements, \$15 to \$20 million for warehouse and corporate office improvements, and the remainder for store renovations and general corporate purposes. Management believes that our current balances of cash and cash equivalents, cash flow from operations and amounts available pursuant to the ABL Facility will be adequate to fund our debt service requirements, planned capital expenditures and working capital needs for the next twelve months. Our ability to make planned capital expenditures, to fund our debt service requirements and to remain in compliance with the financial covenants, and to fund our operations depends on our future operating performance, which in turn, may be impacted by prevailing economic conditions and other financial and business factors, some of which are beyond our control.

**Off Balance Sheet Arrangements**

We enter into documentary letters of credit to facilitate the international purchase of merchandise. We also enter into standby letters of credit to secure reimbursement obligations under certain insurance programs. As of August 3, 2013, we had the following obligations under letters of credit in future periods:

	Total	Within 1 Year	2-3 Years	4-5 Years	After 5 Years
	(amounts in millions)				
Letters of Credit					
Standby	\$ 5.7	\$ 5.7	\$ —	\$ —	\$ —
Documentary	16.5	16.5	—	—	—
	<u>\$ 22.2</u>	<u>\$ 22.2</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

**Cyclicality and Seasonality**

The industry in which we operate is cyclical, and consequently our revenues are affected by general economic conditions. Purchases of apparel and accessories are sensitive to a number of factors that influence the levels of consumer spending, including economic conditions and the level of disposable consumer income, consumer debt, interest rates and consumer confidence.

Our business is seasonal. As a result, our revenues fluctuate from quarter to quarter. We have four distinct selling seasons that align with our four fiscal quarters. Revenues are usually higher in our fourth fiscal quarter, particularly December, as customers make holiday purchases. Our working capital requirements also fluctuate throughout the year, increasing substantially in September and October in anticipation of holiday season inventory requirements.

**Critical Accounting Policies**

A summary of our critical accounting policies is included in the Management's Discussion and Analysis section of our Annual Report on Form 10-K for the fiscal year ended February 2, 2013 filed with the SEC.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

Borrowings under the Senior Credit Facilities are at variable rates of interest and expose us to interest rate risk. If interest rates increase, our debt service obligations on our variable rate indebtedness will increase even though the amount borrowed would remain the same, and our net income and cash flow, including cash available for servicing our indebtedness, will correspondingly decrease. If LIBOR increases above 1.00%, a 0.125% increase in the floating rate applicable to the \$1,173 million outstanding under the Term Loan Facility would result in a \$1.5 million increase in our annual interest expense. Assuming all revolving loans are drawn under the \$250 million ABL Facility, a 0.125% change in the floating rate would result in a \$0.3 million change in our annual interest expense. We have entered into interest rate swaps in order to hedge the volatility of cash flows related to a portion of the Company's floating rate indebtedness (see note 6 to the unaudited condensed consolidated financial statements). These hedges may not fully mitigate our interest rate risk, or may not be effective.

### **ITEM 4. CONTROLS AND PROCEDURES**

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

There were no changes in internal control over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II – OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

On June 20, 2013, a purported class action complaint was filed in the United States District Court for the District of Massachusetts by an individual claiming that the Company collected her ZIP code unlawfully in connection with a retail purchase she made at a Massachusetts store. That action, captioned Miller v. J.Crew Group, Inc., 13-cv-11487 (the “Miller Action”), purports to be brought on behalf of a class of customers whose ZIP codes were collected and recorded at Company stores in Massachusetts in connection with credit card purchases, and claims that the company used the collected ZIP code data to obtain customers’ addresses for purposes of mailing them unwanted advertising material. The Miller Action seeks money damages pursuant to a claim under Chapter 93A of the General Laws of Massachusetts and a claim for unjust enrichment. The Company believes the complaint is without merit and intends to defend against the Plaintiff’s claims. However, it is reasonably possible that the Company may incur a loss in connection with the Miller Action. The amount of such loss, if any, cannot be estimated at the date of this report.

Also, the Company is subject to various legal proceedings and claims arising in the ordinary course of business. Management does not expect that the results of any of these legal proceedings, either individually or in the aggregate, would have a material adverse effect on the Company’s financial position, results of operations or cash flows.

### ITEM 1A. RISK FACTORS

The Company’s Annual Report on Form 10-K for the fiscal year ended February 2, 2013 includes a detailed discussion of certain risks that could materially adversely affect our business, our operating results, or our financial condition. There have been no material changes to the risk factors previously disclosed.

### ITEM 6. EXHIBITS

#### *Articles of Incorporation and Bylaws*

<u>Exhibit No.</u>	<u>Document</u>
3.1	Amended and Restated Certificate of Incorporation of J.Crew Group, Inc., adopted March 7, 2011. Incorporated by reference to Exhibit 3.1 to the Form 8-K filed on March 10, 2011.
3.2	Amended and Restated By-laws of J.Crew Group, Inc., adopted March 7, 2011. Incorporated by reference to Exhibit 3.2 to the Form 8-K filed on March 10, 2011.

#### *Certifications*

<u>Exhibit No.</u>	<u>Document</u>
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**

#### *Interactive Data Files*

<u>Exhibit No.</u>	<u>Document</u>
101	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Condensed Consolidated Balance Sheets at August 3, 2013 and February 2, 2013, (ii) the Condensed Consolidated Statements of Operations and Comprehensive Income for the thirteen weeks ended August 3, 2013 and July 28, 2012, (iii) the Condensed Consolidated Statements of Operations and Comprehensive Income for the twenty-six weeks ended August 3, 2013 and July 28, 2012, (iv) the Condensed Consolidated Statements of Changes in Stockholders’ Equity for the twenty-six weeks ended August 3, 2013 and the fifty-three weeks ended February 2, 2013, (v) the Condensed Consolidated Statements of Cash Flows for the twenty-six weeks ended August 3, 2013 and July 28, 2012, and (vi) the Notes to Unaudited Condensed Consolidated Financial Statements.**

\* Filed herewith.

\*\* Furnished herewith.



**EXHIBIT INDEX**

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\* Filed herewith.

\*\* Furnished herewith.

**CERTIFICATION PURSUANT TO SECTION 302  
OF THE SARBANES-OXLEY ACT OF 2002**

I, Millard Drexler, certify that:

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

Date: September 11, 2013

/s/ MILLARD DREXLER

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Millard Drexler  
Chief Executive Officer

**CERTIFICATION PURSUANT TO SECTION 302  
OF THE SARBANES-OXLEY ACT OF 2002**

I, Stuart C. Haselden, certify that:

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

Date: September 11, 2013

/s/ STUART C. HASELDEN

Stuart C. Haselden  
Chief Financial Officer

**CERTIFICATION PURSUANT TO SECTION 906  
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the quarterly report of J.Crew Group, Inc. (the "Company") on Form 10-Q for the period ended August 3, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, Millard Drexler, Chief Executive Officer of the Company, and Stuart C. Haselden, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: September 11, 2013

\_\_\_\_\_  
/S/ MILLARD DREXLER

Millard Drexler  
Chief Executive Officer

\_\_\_\_\_  
/S/ STUART C. HASELDEN

Stuart C. Haselden  
Chief Financial Officer

The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350) and is not being filed as part of the Report or as a separate disclosure document.

*A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.*

