

**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 4, 2018**

**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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer	<input type="checkbox"/>	Accelerated Filer	<input type="checkbox"/>
Non-Accelerated Filer	<input checked="" type="checkbox"/> (Do not check if a smaller reporting company)	Smaller Reporting Company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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.

<b>Common Stock</b>	<b>Outstanding at August 24, 2018</b>
Common Stock, \$.01 par value per share	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.

**J.CREW GROUP, INC.**  
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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 4, 2018	February 3, 2018
ASSETS		(As adjusted)
Current assets:		
Cash and cash equivalents	\$ 34,742	\$ 107,066
Merchandise inventories, net	412,862	292,489
Prepaid expenses and other current assets	107,855	92,348
Refundable income taxes	6,761	1,622
Total current assets	562,220	493,525
Property and equipment, net	256,313	289,441
Intangible assets, net	305,025	308,702
Goodwill	107,900	107,900
Other assets	7,222	6,374
Total assets	\$ 1,238,680	\$ 1,205,942
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>		
Current liabilities:		
Accounts payable	\$ 297,505	\$ 232,480
Other current liabilities	161,228	177,206
Due to Parent	39,771	38,210
Borrowings under the ABL Facility	25,300	—
Interest payable	22,632	21,914
Current portion of long-term debt	29,039	15,670
Total current liabilities	575,475	485,480
Long-term debt, net	1,680,371	1,697,812
Lease-related deferred credits, net	109,166	117,688
Deferred income taxes, net	35,584	27,752
Other liabilities	27,841	30,168
Total liabilities	2,428,437	2,358,900
Stockholders' deficit:		
Common stock \$0.01 par value; 1,000 shares authorized, issued and outstanding	—	—
Additional paid-in capital	733,191	733,071
Accumulated other comprehensive income (loss)	497	(2,603)
Accumulated deficit	(1,923,445)	(1,883,426)
Total stockholders' deficit	(1,189,757)	(1,152,958)
Total liabilities and stockholders' deficit	\$ 1,238,680	\$ 1,205,942

See notes to unaudited condensed consolidated financial statements.

J.CREW GROUP, INC.

Condensed Consolidated Statements of Operations and Comprehensive Loss  
(unaudited)  
(in thousands)

	For the Thirteen Weeks Ended August 4, 2018	For the Thirteen Weeks Ended July 29, 2017  (As adjusted)
Revenues:		
Net sales	\$ 550,541	\$ 544,903
Other	37,032	25,760
Total revenues	<u>587,573</u>	<u>570,663</u>
Cost of goods sold, including buying and occupancy costs	<u>361,572</u>	<u>352,880</u>
Gross profit	226,001	217,783
Selling, general and administrative expenses	192,659	209,111
Impairment losses	—	3,898
Income from operations	<u>33,342</u>	<u>4,774</u>
Interest expense, net	<u>34,400</u>	<u>22,818</u>
Loss before income taxes	(1,058)	(18,044)
Provision for income taxes	5,036	434
Net loss	<u>\$ (6,094)</u>	<u>\$ (18,478)</u>
Other comprehensive income (loss):		
Reclassification of losses on cash flow hedges, net of tax, to earnings	365	1,682
Unrealized loss on cash flow hedges, net of tax	(201)	(497)
Foreign currency translation adjustments	(147)	777
Comprehensive loss	<u>\$ (6,077)</u>	<u>\$ (16,516)</u>

See notes to unaudited condensed consolidated financial statements.

J.CREW GROUP, INC.

Condensed Consolidated Statements of Operations and Comprehensive Loss  
(unaudited)  
(in thousands)

	For the Twenty-six Weeks Ended August 4, 2018	For the Twenty-six Weeks Ended July 29, 2017
Revenues:		(As adjusted)
Net sales	\$ 1,058,247	\$ 1,049,759
Other	69,776	46,671
Total revenues	<u>1,128,023</u>	<u>1,096,430</u>
Cost of goods sold, including buying and occupancy costs	<u>695,214</u>	<u>688,048</u>
Gross profit	432,809	408,382
Selling, general and administrative expenses	393,495	419,594
Impairment losses	<u>6,866</u>	<u>135,055</u>
Income (loss) from operations	32,448	(146,267)
Interest expense, net of interest income	<u>67,382</u>	<u>43,254</u>
Loss before income taxes	(34,934)	(189,521)
Provision (benefit) for income taxes	<u>5,085</u>	<u>(50,050)</u>
Net loss	<u>\$ (40,019)</u>	<u>\$ (139,471)</u>
Other comprehensive income (loss):		
Reclassification of losses on cash flow hedges, net of tax, to earnings	1,361	3,546
Unrealized gain (loss) on cash flow hedges, net of tax	2,217	(501)
Foreign currency translation adjustments	<u>(478)</u>	<u>1,187</u>
Comprehensive loss	<u>\$ (36,919)</u>	<u>\$ (135,239)</u>

See notes to unaudited condensed consolidated financial statements.

J.CREW GROUP, INC.

Condensed Consolidated Statements of Changes in Stockholders' Deficit  
(unaudited)

(in thousands, except shares)

	Common stock		Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive income (loss)	Total stockholders' deficit
	Shares	Amount				
<b>Balance at January 28, 2017 (as adjusted)</b>	<u>1,000</u>	<u>\$ —</u>	<u>\$ 980,368</u>	<u>\$ (1,760,227)</u>	<u>\$ (11,536)</u>	<u>\$ (791,395)</u>
Net loss	—	—	—	(123,199)	—	(123,199)
Share-based compensation	—	—	2,299	—	—	2,299
Non-cash contribution to Parent in connection with Exchange Offer	—	—	(249,596)	—	—	(249,596)
Reclassification of realized losses on cash flow hedges, net of tax, to earnings	—	—	—	—	6,537	6,537
Unrealized gain on cash flow hedges	—	—	—	—	693	693
Foreign currency translation adjustments	—	—	—	—	1,703	1,703
<b>Balance at February 3, 2018 (as adjusted)</b>	<u>1,000</u>	<u>\$ —</u>	<u>\$ 733,071</u>	<u>\$ (1,883,426)</u>	<u>\$ (2,603)</u>	<u>\$ (1,152,958)</u>
Net loss	—	—	—	(40,019)	—	(40,019)
Share-based compensation	—	—	120	—	—	120
Reclassification of realized losses on cash flow hedges, net of tax, to earnings	—	—	—	—	1,361	1,361
Unrealized gain on cash flow hedges	—	—	—	—	2,217	2,217
Foreign currency translation adjustments	—	—	—	—	(478)	(478)
<b>Balance at August 4, 2018</b>	<u>1,000</u>	<u>\$ —</u>	<u>\$ 733,191</u>	<u>\$ (1,923,445)</u>	<u>\$ 497</u>	<u>\$ (1,189,757)</u>

See notes to unaudited condensed consolidated financial statements.

J.CREW GROUP, INC.

Condensed Consolidated Statements of Cash Flows  
(unaudited)  
(in thousands)

	For the Twenty-six Weeks Ended August 4, 2018	For the Twenty-six Weeks Ended July 29, 2017
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		(As adjusted)
Net loss	\$ (40,019)	\$ (139,471)
Adjustments to reconcile to cash flows from operating activities:		
Depreciation of property and equipment	45,253	49,739
Impairment losses	6,866	135,055
Deferred income taxes	5,508	(52,136)
Amortization of intangible assets	3,603	4,558
Amortization of deferred financing costs and debt discount	3,579	2,554
Reclassification of hedging losses to earnings	1,854	5,814
Foreign currency transaction (gains) losses	229	(627)
Share-based compensation	120	373
Changes in operating assets and liabilities:		
Merchandise inventories, net	(120,761)	15,067
Prepaid expenses and other current assets	(15,715)	6,973
Other assets	(1,214)	(543)
Accounts payable and other liabilities	41,847	(39,220)
Federal and state income taxes	(1,169)	2,216
Net cash used in operating activities	<u>(70,019)</u>	<u>(9,648)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Capital expenditures	<u>(19,106)</u>	<u>(20,173)</u>
Net cash used in investing activities	<u>(19,106)</u>	<u>(20,173)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net borrowings under the ABL Facility	25,300	—
Quarterly principal repayments of Term Loan Facility	(7,835)	(7,835)
Proceeds from New Notes, net of discount	—	94,090
Proceeds from New Term Loan Borrowings, net of discount	—	29,400
Repayments pursuant to the Term Loan amendment	—	(150,456)
Cost paid in connection with refinancings of debt	—	(5,740)
Net cash provided by (used in) financing activities	<u>17,465</u>	<u>(40,541)</u>
Effect of changes in foreign exchange rates on cash and cash equivalents	<u>(664)</u>	<u>562</u>
Decrease in cash and cash equivalents	<u>(72,324)</u>	<u>(69,800)</u>
Beginning balance	107,066	132,226
Ending balance	<u>\$ 34,742</u>	<u>\$ 62,426</u>
<b>Supplemental cash flow information:</b>		
Income taxes paid	<u>\$ 793</u>	<u>\$ 825</u>
Interest paid	<u>\$ 63,053</u>	<u>\$ 41,467</u>
Non-cash contribution to Parent in connection with Exchange Offer	<u>\$ —</u>	<u>\$ 249,596</u>

See notes to unaudited condensed consolidated financial statements.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the thirteen and twenty-six weeks ended August 4, 2018 and July 29, 2017

(Dollars in thousands, unless otherwise indicated)

**1. Basis of Presentation**

J.Crew Group, Inc. and its wholly owned subsidiaries (the “Company” or “Group”) were 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, 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 3, 2018.

The Company’s fiscal year ends on the Saturday closest to January 31. All references to “fiscal 2018” represent the 52-week fiscal year that will end on February 2, 2019 and to “fiscal 2017” represent the 53-week fiscal year that ended February 3, 2018.

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 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. Revenue Recognition**

*Overview.* The Company generates revenue from three sources: (i) customers who shop in its brick-and-mortar stores, (ii) customers who shop on its websites, and (iii) wholesale customers who buy and resell its merchandise. The Company recognizes revenue at (i) the point-of-sale in brick-and-mortar stores, (ii) an estimated date of receipt by a customer in the e-commerce business, and (iii) the time ownership is transferred in the wholesale business.

*New Pronouncement.* At the beginning of fiscal 2018, the Company adopted a pronouncement that clarified the principles of revenue recognition and standardized a comprehensive model for recognizing revenue arising from contracts with customers. Adoption of the new standard impacted the financial statements of the Company as follows:

- Change in the timing of recognition of breakage income associated with its loyalty program;
- Change in the timing of recognition of expenses related to direct-response advertising costs;
- Change in the presentation of the allowance for sales returns to recognize the reserve on a gross basis in the condensed consolidated financial statements, including recording a current asset related to its right to recover products for its sales returns, with an offsetting increase to its liability for returns; and
- Change in the presentation of income from its private label credit card from a reduction of SG&A to other revenues.



*Impact of Adoption.* The adoption was applied retrospectively to each prior period presented, with the cumulative effect of all fiscal years prior to those periods presented recorded to retained earnings. The cumulative effect recorded as of January 31, 2016 was \$5.0 million. The impact of adoption on the condensed consolidated statement of operations for the previous two fiscal years is as follows:

	For the Year Ended					
	February 3, 2018			January 28, 2017		
	As reported	Adjustments	As adjusted	As reported	Adjustments	As adjusted
Revenues:						
Net sales	\$ 2,270,190	\$ (2,380)	\$ 2,267,810	\$ 2,359,622	\$ 388	\$ 2,360,010
Other	99,928	5,957	105,885	65,840	5,745	71,585
Total revenues	2,370,118	3,577	2,373,695	2,425,462	6,133	2,431,595
Cost of goods sold, including buying and occupancy costs	1,477,943	(1,879)	1,476,064	1,550,185	120	1,550,305
Gross profit	892,175	5,456	897,631	875,277	6,013	881,290
Selling, general and administrative expenses	870,950	1,731	872,681	818,546	5,744	824,290
Impairment losses	141,187	—	141,187	7,752	—	7,752
Income (loss) from operations	(119,962)	3,725	(116,237)	48,979	269	49,248
Interest expense, net	110,513	—	110,513	79,359	—	79,359
Loss on refinancings	—	—	—	435	—	435
Loss before income taxes	(230,475)	3,725	(226,750)	(30,815)	269	(30,546)
Benefit for income taxes	(105,516)	1,965	(103,551)	(7,301)	486	(6,815)
Net loss	\$ (124,959)	\$ 1,760	\$ (123,199)	\$ (23,514)	\$ (217)	\$ (23,731)

The impact of the adoption on the condensed consolidated statement of operations for the second quarter and the first half of fiscal 2017 is as follows:

	For the Thirteen Weeks Ended July 29, 2017			For the Twenty-six Weeks Ended July 29, 2017		
	As reported	Adjustments	As adjusted	As reported	Adjustments	As adjusted
Revenues:						
Net sales	\$ 536,180	\$ 8,723	\$ 544,903	\$ 1,049,359	\$ 400	\$ 1,049,759
Other	24,726	1,034	25,760	43,513	3,158	46,671
Total revenues	560,906	9,757	570,663	1,092,872	3,558	1,096,430
Cost of goods sold, including buying and occupancy costs	344,274	8,606	352,880	688,004	44	688,048
Gross profit	216,632	1,151	217,783	404,868	3,514	408,382
Selling, general and administrative expenses	210,136	(1,025)	209,111	420,558	(964)	419,594
Impairment losses	3,898	—	3,898	135,055	—	135,055
Income (loss) from operations	2,598	2,176	4,774	(150,745)	4,478	(146,267)
Interest expense, net	22,818	—	22,818	43,254	—	43,254
Loss before income taxes	(20,220)	2,176	(18,044)	(193,999)	4,478	(189,521)
Provision (benefit) for income taxes	434	—	434	(50,050)	—	(50,050)
Net loss	\$ (20,654)	\$ 2,176	\$ (18,478)	\$ (143,949)	\$ 4,478	\$ (139,471)

The impact of the adoption on the condensed consolidated balance sheets as of February 3, 2018 and July 29, 2017 is as follows:

	As of					
	February 3, 2018			July 29, 2017		
	As reported	Adjustments	As adjusted	As reported	Adjustments	As adjusted
<b>ASSETS</b>						
Current assets:						
Cash and cash equivalents	\$ 107,066	\$ —	\$ 107,066	\$ 62,426	\$ —	\$ 62,426
Merchandise inventories, net	292,489	—	292,489	299,796	—	299,796
Prepaid expenses and other current assets	83,228	9,120	92,348	51,261	6,037	57,298
Refundable income taxes	5,807	(4,185)	1,622	8,139	(3,644)	4,495
Total current assets	<u>488,590</u>	<u>4,935</u>	<u>493,525</u>	<u>421,622</u>	<u>2,393</u>	<u>424,015</u>
Property and equipment, net	289,441	—	289,441	330,006	—	330,006
Intangible assets, net	308,702	—	308,702	313,161	—	313,161
Goodwill	107,900	—	107,900	107,900	—	107,900
Other assets	6,374	—	6,374	7,321	—	7,321
Total assets	<u>\$ 1,201,007</u>	<u>\$ 4,935</u>	<u>\$ 1,205,942</u>	<u>\$ 1,180,010</u>	<u>\$ 2,393</u>	<u>\$ 1,182,403</u>
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>						
Current liabilities:						
Accounts payable	\$ 232,480	\$ —	\$ 232,480	\$ 188,297	\$ —	\$ 188,297
Other current liabilities	167,113	10,093	177,206	150,321	6,256	156,577
Due to Parent	38,210	—	38,210	20,959	—	20,959
Interest payable	21,914	—	21,914	6,769	—	6,769
Current portion of long-term debt	15,670	—	15,670	19,588	—	19,588
Total current liabilities	<u>475,387</u>	<u>10,093</u>	<u>485,480</u>	<u>385,934</u>	<u>6,256</u>	<u>392,190</u>
Long-term debt, net	1,697,812	—	1,697,812	1,701,887	—	1,701,887
Lease-related deferred credits, net	117,688	—	117,688	129,228	—	129,228
Deferred income taxes, net	29,486	(1,734)	27,752	98,011	(3,158)	94,853
Other liabilities	30,168	—	30,168	40,101	—	40,101
Total liabilities	<u>2,350,541</u>	<u>8,359</u>	<u>2,358,900</u>	<u>2,355,161</u>	<u>3,098</u>	<u>2,358,259</u>
Total stockholders' deficit	<u>(1,149,534)</u>	<u>(3,424)</u>	<u>(1,152,958)</u>	<u>(1,175,151)</u>	<u>(705)</u>	<u>(1,175,856)</u>
Total liabilities and stockholders' deficit	<u>\$ 1,201,007</u>	<u>\$ 4,935</u>	<u>\$ 1,205,942</u>	<u>\$ 1,180,010</u>	<u>\$ 2,393</u>	<u>\$ 1,182,403</u>

#### Disaggregation of Revenue

A summary of disaggregated revenue is as follows:

	For the Thirteen Weeks Ended		For the Twenty-six Weeks Ended	
	August 4, 2018	July 29, 2017 (As adjusted)	August 4, 2018	July 29, 2017 (As adjusted)
J.Crew	\$ 428,891	\$ 450,726	\$ 820,756	\$ 872,202
Madewell	121,650	94,177	237,491	177,557
Other(a)	37,032	25,760	69,776	46,671
Total revenues	<u>\$ 587,573</u>	<u>\$ 570,663</u>	<u>\$ 1,128,023</u>	<u>\$ 1,096,430</u>

(a) Consists primarily of revenues from wholesale customers and shipping and handling fees.

*Accounts Receivable from our Wholesale Customers*

A summary of accounts receivable, included in prepaid expenses and other current assets, with respect to our wholesale customers is as follows:

	<u>August 4, 2018</u>	<u>February 3, 2018</u>
Accounts receivable	\$ 34,975	\$ 23,503
Less allowance for doubtful accounts	(295)	(312)
Accounts receivable, net	<u>\$ 34,680</u>	<u>\$ 23,191</u>

*Contract Liabilities*

The Company recognizes a contract liability when it has received consideration from a customer and has a future performance obligation to transfer merchandise to the customer. The Company's contract liabilities include (i) unredeemed gift cards and (ii) unredeemed loyalty program rewards.

With respect to unredeemed gift cards, the Company is obligated to transfer merchandise in the future when a holder uses a gift card to make a purchase. The contract liability for gift cards is increased when customers purchase cards, and decreased when (i) a customer redeems the card or (ii) the Company estimates the gift card will go unredeemed (referred to as "breakage"). All of our gift cards do not have an expiration date, and are classified as a current liability.

With respect to unearned loyalty program rewards, the Company is obligated to transfer merchandise to the customer upon accumulating points to certain thresholds. The contract liability for unearned loyalty program rewards is increased as certain customers make qualifying purchases, and decreased when (i) a customer achieves a threshold and a rewards card is issued or merchandise is transferred or (ii) the expiration of accumulated points that did not reach a threshold.

Rollforwards of the liabilities for gift cards and loyalty program awards are as follows:

	<u>Unredeemed Gift Cards</u>			
	<u>For the Thirteen Weeks Ended</u>		<u>For the Twenty-six Weeks Ended</u>	
	<u>August 4, 2018</u>	<u>July 29, 2017</u>	<u>August 4, 2018</u>	<u>July 29, 2017</u>
Balance at beginning of period	\$ 28,882	\$ 28,781	\$ 32,665	\$ 34,698
Issuance of cards	14,274	14,077	27,495	27,691
Redemption of cards	(14,382)	(15,593)	(30,345)	(33,686)
Recognition of estimated breakage	(867)	(1,107)	(1,788)	(2,307)
Other	24	(3)	(96)	(241)
Balance at end of period	<u>\$ 27,931</u>	<u>\$ 26,155</u>	<u>\$ 27,931</u>	<u>\$ 26,155</u>

	<u>Unredeemed Loyalty Program Rewards</u>			
	<u>For the Thirteen Weeks Ended</u>		<u>For the Twenty-six Weeks Ended</u>	
	<u>August 4, 2018</u>	<u>July 29, 2017</u>	<u>August 4, 2018</u>	<u>July 29, 2017</u>
Balance at beginning of period	\$ 3,914	\$ 7,415	\$ 8,422	\$ 8,420
Redemption of cards	(2,048)	(2,480)	(9,511)	(5,774)
Recognition of estimated breakage	(1,136)	(1,347)	(1,903)	(3,311)
Earning of loyalty program points	4,615	3,738	8,152	7,903
Other	31	55	216	143
Balance at end of period	<u>\$ 5,376</u>	<u>\$ 7,381</u>	<u>\$ 5,376</u>	<u>\$ 7,381</u>

### 3. Debt Exchange and Refinancing

#### Transaction Overview

On July 13, 2017, the Parent and certain of its subsidiaries completed the following interrelated liability management transactions:

- a private exchange offer (the “Exchange Offer”) pursuant to which \$565.7 million aggregate principal amount of the outstanding 7.75%/8.50% Senior PIK Toggle Notes due 2019 (the “PIK Notes”) issued by Chinos Intermediate Holdings A, Inc., a direct wholly-owned subsidiary of the Parent (the “PIK Notes Issuer”), were exchanged for aggregate consideration consisting of:
  - \$249,596,000 aggregate principal amount of 13% Senior Secured Notes due 2021 issued by J.Crew Brand, LLC and J.Crew Brand Corp. (the “Exchange Notes”), which are secured primarily by the U.S. intellectual property assets held by J.Crew Domestic Brand, LLC (“IPCo”);
  - 189,688 shares of Parent’s 7% non-convertible perpetual series A preferred stock, no par value per share, with an aggregate initial liquidation preference of \$189,688,000 (the “Series A Preferred Stock”); and
  - 15% of Parent’s common equity, or 17,362,719 shares of Parent’s class A common stock, \$0.00001 par value per share (the “Class A Common Stock”);
- the receipt of consents from the holders of a majority of the PIK Notes with respect to certain amendments to the indenture governing the PIK Notes;
- completion of an amendment to the Company’s Amended and Restated Credit Agreement, dated as of March 5, 2014 (the “Term Loan Facility”) to, among other things, facilitate the following related transactions:
  - the repayment of \$150.5 million principal amount of term loans then outstanding under the Term Loan Facility;
  - the transfer of the remaining undivided 27.96% ownership interest in the U.S. intellectual property rights of the J.Crew brand (the “Additional Transferred IP”) to IPCo, which, together with the undivided 72.04% ownership interest transferred in December 2016 (the “Initial Transferred IP”) represent 100% of the U.S. intellectual property rights of the J.Crew brand (the “Transferred IP”), and the execution of related license agreements;
  - the issuance of \$97.0 million aggregate principal amount of an additional series of 13% Senior Secured Notes due 2021 by J.Crew Brand, LLC and J.Crew Brand Corp. (the “New Money Notes” and, together with the Exchange Notes, the “Notes”), subject to the same terms and conditions as the Exchange Notes, for cash at a 3% discount, subject to the terms of the note purchase agreement, dated June 12, 2017, the proceeds of which were loaned on a subordinated basis to the Company and were applied, in part, to finance the repayment of the \$150.5 million principal amount of term loans referenced above; and
  - the raising of additional borrowings under the Term Loan Facility of \$30.0 million (at a 2% discount) provided by the Company’s Sponsors (the “New Term Loan Borrowings”), the net proceeds of which were also applied, in part, to finance the repayment of the \$150.5 million principal amount of term loans referenced above.

### 4. Management Services Agreement

Pursuant to a management services agreement entered into in connection with the Acquisition, and in exchange for ongoing consulting and management advisory services (the “Services”), the Sponsors received an aggregate annual monitoring fee prepaid quarterly equal to the greater of (i) 40 basis points of consolidated annual revenues or (ii) \$8 million (in either case, the “Advisory Fee”). The Sponsors also receive reimbursement for out-of-pocket expenses incurred in connection with services provided pursuant to the agreement.

On July 13, 2017, the management services agreement was amended and restated to require the Parent to provide the Services previously provided by the Sponsors. In addition to the amendment, the Parent and Sponsors entered into a new management services agreement, pursuant to which the Sponsors provide the Services to the Parent for an amount equal to the Advisory Fee less the accrued cash dividend in an amount equal to 5% of the liquidation preference on the outstanding Series A Preferred Stock of the Parent.

The Company recorded an expense of \$5.0 million and \$4.7 million in the first half of fiscal 2018 and fiscal 2017, respectively, for monitoring fees and out-of-pocket expenses, included in selling, general and administrative expenses in the statements of operations and comprehensive loss.

## 5. Goodwill and Intangible Assets

A summary of the components of intangible assets is as follows:

	Favorable Lease Commitments	Madewell Trade Name	Key Money	J.Crew Trade Name
Balance at February 3, 2018	\$ 3,912	\$ 53,642	\$ 953	\$ 250,195
Amortization expense	(743)	(1,025)	(35)	—
Effect of changes in foreign exchange rates	—	—	(39)	—
Balance at May 5, 2018	\$ 3,169	\$ 52,617	\$ 879	\$ 250,195
Amortization expense	(743)	(1,025)	(33)	—
Effect of changes in foreign exchange rates	—	—	(34)	—
Balance at August 4, 2018	<u>\$ 2,426</u>	<u>\$ 51,592</u>	<u>\$ 812</u>	<u>\$ 250,195</u>
Total accumulated amortization or impairment losses at August 4, 2018	<u>\$ (58,584)</u>	<u>\$ (30,408)</u>	<u>\$ (4,005)</u>	<u>\$ (635,105)</u>

The impairment losses were the result of the write-down of the following assets:

	For the Thirteen Weeks Ended		For the Twenty-six Weeks Ended	
	August 4, 2018	July 29, 2017	August 4, 2018	July 29, 2017
Intangible asset related to the J.Crew trade name	\$ —	\$ —	\$ —	\$ 129,800
Long-lived assets (see note 9)	—	3,898	6,866	5,255
Impairment losses	<u>\$ —</u>	<u>\$ 3,898</u>	<u>\$ 6,866</u>	<u>\$ 135,055</u>

The carrying value of goodwill of \$107.9 million relates to the Madewell reporting unit. There is no remaining goodwill attributable to the J.Crew reporting unit, which has previously recorded accumulated impairment losses of \$1,579.0 million. The carrying value of the J.Crew and Madewell trade names is \$250.2 million and \$51.6 million, respectively, at August 4, 2018. If revenues or operating results decline below the Company's current expectations, additional impairment charges may be recorded in the future.

## 6. Share-Based Compensation

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

On March 4, 2011, the Parent adopted the Chinos Holdings, Inc. 2011 Equity Incentive Plan (the "2011 Plan"). On July 13, 2017, in connection with a debt exchange and refinancing, the Parent completed a recapitalization of its outstanding equity. The recapitalization resulted in, among other things, a reverse stock split of the shares of common stock underlying the share-based awards issued by the Company. The reverse stock split of 10,000-to-1 resulted in (i) a substantial decrease in number of authorized awards from 91,740,627 shares to 9,174 shares and (ii) a substantial increase in the exercise price of \$0.10 to \$1,000 per share.

The recapitalization included (i) the issuance of preferred stock of the Parent, including an authorization for equity awards to be granted up to 20,000 shares and (ii) the issuance of additional shares of common stock of the Parent, including an authorization for equity awards to be granted up to 13,003,295 shares. Additionally, on October 3, 2017, the Company authorized additional awards of 5,209,823 shares to be granted to its Chief Executive Officer in accordance with an employment agreement. The following disclosures are presented with respect to the newly authorized share-based awards only.

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

	For the Thirteen Weeks Ended		For the Twenty-six Weeks Ended	
	August 4, 2018	July 29, 2017	August 4, 2018	July 29, 2017
Share-based compensation	<u>\$ 74</u>	<u>\$ 164</u>	<u>\$ 120</u>	<u>\$ 373</u>

A summary of shares available for grant as stock options or other share-based awards, as adjusted for the reverse stock split, is as follows:

	<u>Common Stock Awards</u>	<u>Preferred Stock Awards</u>
Available for grant at February 3, 2018	13,018,649	20,000
Authorized	—	—
Granted	(8,749,186)	—
Forfeited and available for reissuance	348,208	—
Available for grant at August 4, 2018	<u>4,617,671</u>	<u>20,000</u>

## 7. Long-Term Debt and Credit Agreements

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

	<u>August 4, 2018</u>	<u>February 3, 2018</u>
Term Loan Facility	\$ 1,380,899	\$ 1,388,258
Notes	346,596	346,596
Less current portion of Term Loan	(29,039)	(15,670)
Less deferred financing costs	(12,584)	(14,879)
Less discount	(5,501)	(6,493)
Long-term debt, net	<u>\$ 1,680,371</u>	<u>\$ 1,697,812</u>
Borrowings under the ABL Facility	<u>\$ 25,300</u>	<u>\$ —</u>

### ABL Facility

The Company has an ABL Facility, which is governed by a credit agreement with Bank of America, N.A., as administrative agent and the other agents and lenders party thereto, that provides for a \$350 million senior secured asset-based revolving line of credit (which may be increased by up to \$100 million in certain circumstances), subject to a borrowing base limitation. The ABL Facility includes borrowing capacity in the form of letters of credit up to \$200 million, 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 the maturity date of November 17, 2021.

On August 4, 2018, standby letters of credit were \$58.1 million, outstanding borrowings were \$25.3 million, and excess availability, as defined, was \$215.0 million. The weighted average interest rate on the borrowings outstanding under the ABL Facility was 5.25% on August 4, 2018. Average short-term borrowings under the ABL Facility were \$35.5 million in the first half of fiscal 2018. There were no short-term borrowings under the ABL Facility in the first half of fiscal 2017.

### 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 \$20 million of documentary letters of credit on a no fee basis. On August 4, 2018, outstanding documentary letters of credit were \$19.9 million and availability under this facility was \$0.1 million.

### Term Loan Facility

*2017 Amendment.* On July 13, 2017, concurrently with the settlement of the Exchange Offer, the Company amended its Term Loan Facility to, among other things, (i) increase the interest rate applicable to the loans held by consenting lenders, which represented 88% of lenders, (the “Consenting Lenders”; and the loans held by the Consenting Lenders, the “Amended Loans”) by 22 basis points, (ii) increase the amount of amortization payable to Consenting Lenders, (iii) provide for the New Term Loan Borrowings of \$30.0 million, (iv) amend certain covenants and events of default and (v) direct Wilmington Savings Fund Society, FSB, as administrative agent under the Term Loan Facility, to dismiss, with prejudice, certain litigation regarding the Initial Transferred IP (and the related actions). Additionally, the Company repaid \$150.5 million of principal amount of term loans outstanding under the Term Loan Facility, which was financed with (i) the net proceeds from the New Money Notes of \$94.1 million, (ii) the net proceeds from the New Term Loan Borrowings of \$29.4 million and (iii) cash on hand of \$27.0 million.

**Interest Rate.** Initial borrowings under the Term Loan Facility bear interest at a rate per annum equal to an applicable margin (which, in the case of the Amended Loans, was increased by 22 basis points) plus, at Group's option, either (a) a LIBOR determined by reference to the costs of funds for U.S. dollar deposits for the relevant interest period 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, plus 1.00%. New Term Loan Borrowings bear interest at 9% per annum payable in cash plus 3% per annum payable in kind.

The weighted average interest rate on the borrowings outstanding under the Term Loan Facility was 5.61% on August 4, 2018. The applicable margin (i) in effect for base rate borrowings was, (x) in the case of term loans, other than the New Term Loan Borrowings and the Amended Loans, 2.00%, (y) in the case of the Amended Loans, 2.22% and (z) in the case of the New Term Loan Borrowings, 12.00% (of which 3.00% is payable in kind) and (ii) with respect to LIBOR borrowings was, (x) in the case of term loans, other than the New Term Loan Borrowings and the Amended Loans, 3.00% and the LIBOR Floor, (y) in the case of the Amended Loans, 3.22% and the LIBOR Floor and (z) in the case of the New Term Loan Borrowings, 12.00% (of which 3.00% is payable in kind), respectively, at August 4, 2018.

**Principal Repayments.** The Company is required to make principal repayments equal to 0.25% of the original principal amount of the Term Loan Facility (excluding the New Term Loan Borrowings), or \$3.9 million, on the last business day of January, April, July, and October. The Company is also required (i) to repay the term loan based on an annual calculation of excess cash flow, as defined in the agreement, (ii) in the second quarter of fiscal 2019, to make a principal repayment of \$11.9 million which is equal to 1.00% of the aggregate principal amount of Amended Loans outstanding on July 13, 2017 and (iii) beginning on July 31, 2019, on the last business day of January, April, July and October, to make additional principal repayments of \$1.5 million equal to 0.125% of the aggregate principal amount of Amended Loans outstanding on July 13, 2017. The maturity date of the Term Loan Facility is March 5, 2021.

#### Notes

**General.** On July 13, 2017, in connection with settlement of the Exchange Offer and the issuance of the Notes, J.Crew Brand, LLC and J.Crew Brand Corp. (together, the "Notes Co-Issuers") and the Guarantors (as defined below) entered into (i) an indenture with U.S. Bank National Association, as Trustee and collateral agent, governing the terms of the Exchange Notes (the "Exchange Notes Indenture") and (ii) an indenture with the Trustee and U.S. Bank, as collateral agent, governing the terms of the New Money Notes (the "New Money Notes Indenture"), which is in substantially the same form as the Exchange Notes Indenture.

**Interest Rate.** The Notes bear interest at a rate of 13% per annum, and interest is payable semi-annually on March 15 and September 15 of each year. The Notes mature on September 15, 2021.

**Notes Guarantee.** The Notes are guaranteed by J.Crew Brand Intermediate, LLC, IPCo and J.Crew International Brand, LLC, each of which is a Delaware limited liability company and a wholly-owned indirect subsidiary of the Company (collectively, the "Guarantors," and each, a "Guarantor"). The PIK Notes Issuer also unconditionally guarantees the payment obligations of the Notes Co-Issuers and the Guarantors.

**Exchange Notes Collateral.** The Exchange Notes and the guarantees thereof are general senior secured obligations of the Notes Co-Issuers and the Guarantors, secured on a first priority lien basis by the Initial Transferred IP and certain other assets of the Notes Co-Issuers and Guarantors, and on a second priority lien basis by the Additional Transferred IP, subject, in each case, to permitted liens under the Exchange Notes Indenture and that certain intercreditor agreement, entered into between the collateral agents on July 13, 2017.

**New Money Notes Collateral.** The New Money Notes and the guarantees thereof are general senior secured obligations of the Notes Co-Issuers and the Guarantors, secured on a first priority lien basis by the Additional Transferred IP and certain other assets, and on a second priority lien basis by the Initial Transferred IP, subject, in each case, to permitted liens under the New Money Notes Indenture and the intercreditor agreement.

**Redemption.** The Notes are redeemable at the option of the Notes Co-Issuers, in whole or in part, at any time, at a price equal to one hundred percent (100%) of the principal amount of the Notes to be redeemed, plus accrued and unpaid interest, if any, to, but not including, the redemption date, plus a "make whole" premium. The Notes are not subject to any mandatory redemption obligation, and there is no sinking fund provided for the Notes.

**Change in Control.** Upon the occurrence of a Change of Control (as defined in each of the indentures, as applicable), the Notes Co-Issuers will be required to offer to repay all of the Notes at 100% of the aggregate principal amount repaid plus accrued and unpaid interest, if any, to, but not including, the date of purchase.

*Covenants.* Each of the indentures contains covenants covering (i) the payment of principal and interest, (ii) maintenance of an office or agency for the payment of the Notes, (iii) reports to the applicable Trustee and holders of the Notes, (iv) stay, extension and usury laws, (v) payment of taxes, (vi) existence, (vii) maintenance of properties and (viii) maintenance of insurance. Each of the indentures relating to the Notes also includes covenants that (i) limit the ability to transfer the collateral and (ii) limit liens that may be imposed on the assets of the Guarantors, which covenants are, in each case, subject to certain exceptions set forth in each of the indentures.

### Interest expense

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

	<b>For the Thirteen Weeks Ended</b>		<b>For the Twenty-six Weeks Ended</b>	
	<u>August 4, 2018</u>	<u>July 29, 2017</u>	<u>August 4, 2018</u>	<u>July 29, 2017</u>
Term Loan Facility	\$ 19,501	\$ 15,939	\$ 37,884	\$ 31,446
Notes	11,264	2,128	22,529	2,128
Amortization of deferred financing costs and debt discount	1,790	1,325	3,579	2,554
Realized hedging losses	498	2,758	1,854	5,814
ABL Facility	538	—	875	—
Other interest, net of interest income	809	668	661	1,312
Interest expense, net	<u>\$ 34,400</u>	<u>\$ 22,818</u>	<u>\$ 67,382</u>	<u>\$ 43,254</u>

### **8. Derivative Financial Instruments**

In August 2014, the Company entered into interest rate swap agreements that limit exposure to interest rate increases on a portion of the Company's floating rate indebtedness. The interest rate swap agreements cover a notional amount of \$800 million from March 2016 to March 2019 and carry a fixed rate of 2.56% plus the applicable margin.

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 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 is 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). Liabilities for interest rate swaps, included in other liabilities, were \$0.4 million and \$4.3 million at August 4, 2018 and February 3, 2018, respectively.

### **9. 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 long-term debt was estimated to be \$1,589 million and \$1,388 million at August 4, 2018 and February 3, 2018, respectively, based on quoted market prices of the debt (level 1 inputs).



The Company's interest rate swap agreements are measured in the financial statements at fair value on a recurring basis. See note 8 for more information regarding the fair value of this financial liability.

The carrying amounts reported in the condensed 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***

Certain non-financial assets, including goodwill, the intangible asset for the J.Crew trade name, and certain long-lived assets, have been written down and measured in the financial statements at fair value. The Company does not have any other non-financial assets or liabilities as of August 4, 2018 or February 3, 2018 that are measured on a recurring basis in the financial statements at fair value.

The Company assesses the recoverability of goodwill and intangibles whenever there are indicators of impairment, or at least annually in the fourth quarter. If the recorded carrying value of an intangible asset exceeds its fair value, the Company records a charge to write-down the intangible asset to its fair value. Impairment charges of goodwill are based on fair value measurements derived using a combination of an income approach, specifically the discounted cash flow, a market approach, and a transaction approach. Impairment charges of intangible assets are based on fair value measurements derived using an income approach, specifically the relief from royalty method, which is a revenue and royalty rate approach. The valuation methodologies incorporate unobservable inputs reflecting significant estimates and assumptions made by management (level 3 inputs). For more information related to goodwill and intangible asset impairment charges, see note 5.

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 (for example, leasehold improvements) or at the corporate level (for example, software). 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 Thirteen Weeks Ended		For the Twenty-six Weeks Ended	
	August 4, 2018	July 29, 2017	August 4, 2018	July 29, 2017
Carrying value of long-term assets written down to fair value	\$ —	\$ 3,898	\$ 6,866	\$ 5,255
Impairment charge	\$ —	\$ 3,898	\$ 6,866	\$ 5,255

## **10. Income Taxes**

On December 22, 2017, H.R.1, or the Tax Cuts and Jobs Act ("Tax Reform") was signed into law. Among its many provisions, Tax Reform substantially reduced the Company's ability to deduct all of its interest expense in fiscal 2018. The inability to deduct all of its interest expense will generate a significant carry forward of unutilized interest deductions. The Company is not forecasting future taxable income sufficient to utilize the carry forward. Therefore, the Company has recognized a valuation allowance with respect to the deferred tax asset related to the carry forward of unutilized interest deductions.

In the first half of fiscal 2018, the Company recorded a provision for income taxes of \$5.1 million, which reflects a charge for the valuation allowance with respect to the deferred tax asset related to the carry forward of unutilized interest deductions. Other items impacting the provision for income taxes include the recognition of international valuation allowances, lower rates in foreign jurisdictions and reserves for uncertain tax positions. These items primarily drove the difference between the federal statutory rate of 21% and the effective rate of 15%.

In the first half of fiscal 2017, the Company recognized a deferred tax benefit of \$52.1 million, primarily a result of the reversal of deferred taxes related to the intangible asset for the J.Crew trade name, which was written down by \$129.8 million in the first quarter. The Company did not recognize any additional deferred tax benefit on other operating losses due to an increase in the valuation allowance. The impact of not recognizing tax benefit on the Company's other operating losses was the primary driver of the difference between the statutory rate of 35% to the effective rate of 26%.

The Company regularly assesses the need for a valuation allowance related to its deferred tax assets. In making that assessment, the Company considers both positive and negative evidence related to the likelihood of realization of the deferred tax assets to determine, based on a weighing process of available evidence, whether it is more-likely-than-not that its deferred tax assets will not be realized. As of August 4, 2018, the Company maintains valuation allowances against its deferred tax assets related to (i) the carry forward of unutilized interest deductions, (ii) carry forwards of net operating losses of its international subsidiaries and (iii) temporary differences deductible in certain states that did not adopt Tax Reform, and therefore interest expense currently remains fully deductible in those jurisdictions.

The federal tax returns for the periods ended January 2013 through January 2016 are currently under 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 2013 to 2016. The results of these audits and appeals are not expected to have a significant effect on the results of operations or financial position.

While the Company expects the amount of unrecognized tax benefits to change in the next 12 months, the change is not expected to have a significant effect on the results of operations or financial position. However, the outcome of tax matters is uncertain and unforeseen results can occur.

## 11. Legal Proceedings

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 effect on the Company's financial position, results of operations or cash flows. As of August 4, 2018, the Company has recorded a reserve for certain legal contingencies in connection with ongoing claims and litigation. The reserve is not material to its results of operations. In addition, there are certain other claims and legal proceedings pending against the Company for which accruals have not been established.

***Eaton Vance Management, et al. v. Wilmington Savings Fund Society, FSB, as Administrative Agent and Collateral Agent, et al., Index No. 654397/2017, (Sup. Ct. N.Y. C'ty.).***

On June 22, 2017, Eaton Vance Management and certain affiliated funds as well as Highland Capital Management and certain affiliated funds (collectively, the "Highland/EV Plaintiffs"), filed a complaint in the New York State Supreme Court, Commercial Division, against the Company and WSFS, seeking, among other things, declarations that the July 13, 2017 Amendment to the Term Loan Facility was ineffective absent unanimous consent of all lenders under the facility, that certain of the Company's actions with respect to certain of its intellectual property assets were taken in violation of the terms of the Term Loan Facility, and that those actions also constituted fraudulent conveyances.

On August 7, 2017, WSFS and the Company filed separate motions to dismiss certain of the Highland/EV Plaintiffs' claims for failure to state a claim and lack of standing, among other reasons. On September 7, 2017, the Highland/EV Plaintiffs filed an amended complaint in the New York State Supreme Court, Commercial Division, against the Company and WSFS. The amended complaint continued to assert claims for breach of the terms of the Term Loan Facility, and for fraudulent conveyance and added an additional claim for fraudulent inducement against the Company.

In response to the amended complaint, WSFS and the Company withdrew their prior motions to dismiss and, on October 20, 2017, filed renewed motions seeking dismissal in whole or part. Among other things, the Company sought dismissal of the amended complaint for failure to state a claim, lack of standing, and because its fraud claims are duplicative of the Highland/EV Plaintiffs' claims under the documents governing the Term Loan Facility. The Highland/EV Plaintiffs filed an omnibus brief on December 1, 2017 opposing the motions to dismiss. The Company and WSFS each filed reply briefs on December 22, 2017 reiterating that the majority of the Highland/EV Plaintiffs' claims should be dismissed as a matter of law.

Oral argument on the motions to dismiss occurred on March 8, 2018. On April 25, 2018, the judge issued a Memorandum Decision and Order, which granted the Company's partial motion to dismiss in its entirety and dismissed as a matter of law the majority of the Highland/EV Plaintiffs' claims with prejudice. The Highland/EV Plaintiffs' sole remaining claim is for breach of contract based on the theory that the July 13, 2017 Amendment to the Term Loan Facility required unanimous consent of all lenders under the facility. Discovery in the action is ongoing. The Company believes that the Highland/EV Plaintiffs' claim is wholly without merit, and intends to vigorously oppose the claim.

## 12. Workforce Reductions

The Company executed various strategic changes including the eliminations of: (i) approximately 150 full-time and 100 open positions, primarily from its corporate headquarters, and (ii) approximately 600 full-time store positions, in the first quarter of fiscal 2017 and fiscal 2018, respectively.

A rollforward of the reserve for severance and related costs is as follows:

	<b>For the Thirteen Weeks Ended August 4, 2018</b>	<b>For the Twenty-six Weeks Ended August 4, 2018</b>
Balance at beginning of period	\$ 2,131	\$ 3,543
Provisions charged to expense	5	3,293
Reversals	(856)	(856)
Payments	(753)	(5,453)
Balance at end of period	<u>\$ 527</u>	<u>\$ 527</u>

The Company expects the unpaid severance at August 4, 2018 to be paid through the fourth quarter of fiscal 2018.

## 13. Corporate Headquarters Relocation

On May 10, 2018, the Company entered into a lease amendment and surrender agreement (the "Surrender Agreement") with Vornado Office Management, LLC ("Vornado"). The terms of the Surrender Agreement provide for, among other things, the early termination and surrender of the space currently occupied by the Company as its corporate headquarters at 770 Broadway in New York City. In exchange for the surrender, Vornado agreed to pay the Company a termination payment of \$35 million. The Company plans to be fully vacated from its current corporate headquarters by June 30, 2019, and expects to collect the termination payment in installments through such date. The Company will recognize the benefit of \$35 million, as a reduction of selling, general and administrative expense, over the period starting May 10, 2018 until June 30, 2019.

Additionally, concurrent with the entry into the Surrender Agreement, the Company entered into a sublease of new corporate office space at 225 Liberty Street in New York City. The sublease provides for, among other things, a 16-year occupancy of 325,000 square feet of office space in lower Manhattan with aggregate base rent of \$272 million, net of free rent. The Company will begin relocating to the new corporate office space in August 2018 and the Company expects to reinvest a significant portion of the termination payment of \$35 million into the new corporate office space. As a result of the move, the Company expects pre-tax rent savings of approximately \$4 million in fiscal 2018.

## 14. Related Party Transactions

### *Intellectual property license agreements*

In October 2016, the Company formed wholly-owned indirect subsidiaries, including IPCo and J.Crew Brand, LLC (collectively, "J.Crew BrandCo"). In December 2016, J.Crew International, Inc. ("JCI") transferred an undivided 72.04% ownership interest in the U.S. intellectual property rights of the J.Crew brand to IPCo, and entered into a related intellectual property license agreement with IPCo. In July 2017, JCI transferred the remaining undivided 27.96% ownership interest in the U.S. intellectual property rights of the J.Crew brand to IPCo, which, together with the initial intellectual property contributed in December 2016, represent 100% of the U.S. intellectual property rights of the J.Crew brand, entered into a license agreement amending and restating the December 2016 license agreement with IPCo and entered into an additional intellectual property license agreement with IPCo (collectively, the "IP License Agreements").

Under the IP License Agreements, J.Crew Operating Corp. ("OpCo"), a direct wholly-owned subsidiary of the Company, pays a fixed license fee of \$59 million per annum to IPCo, which owns the U.S. intellectual property rights of the J.Crew brand. The license fees are payable on March 1 and September 1 of each fiscal year. These royalty payments have no impact on the Company's condensed consolidated results of operations and are not subject to the covenants under the Company's credit facilities or the PIK Notes.

The proceeds from the license fees to IPCo are used by J.Crew BrandCo to meet debt service requirements on the Notes. Any license fees in excess of the debt service requirements are loaned back to OpCo on a subordinated basis. As of August 4, 2018, J.Crew BrandCo had total assets of \$396.1 million, consisting of intangible assets of \$250.2 million, receivable due from OpCo of \$121.0 million, license fee receivable of \$24.6 million and cash and cash equivalents of \$0.3 million, and total liabilities of \$357.1 million related to the Notes. IPCo earned royalty revenue of \$14.8 million and \$29.5 million in the second quarter and first half of fiscal 2018, respectively. The Notes are guaranteed by the intangible assets of J.Crew BrandCo.

#### ***Chinos Intermediate Holdings A, Inc. Senior PIK Toggle Note***

On November 4, 2013, the PIK Notes Issuer, which is an indirect parent holding company of Group, issued \$500 million of PIK Notes. The PIK Notes were: (i) senior unsecured obligations of the PIK Notes Issuer, (ii) structurally subordinated to all of the liabilities of the PIK Notes Issuers' subsidiaries, and (iii) not guaranteed by any of the PIK Notes Issuers' subsidiaries, and therefore are not recorded in the Company's financial statements. As part of the refinancing in July 2017, \$565.7 million in aggregate principal amount of the PIK Notes were exchanged for \$249.6 million of Exchange Notes and shares of preferred and common stock of the Parent. As of August 4, 2018, there were \$0.9 million in aggregate principal amount of PIK Notes outstanding. For more information on the Exchange Offer, see note 3.

The PIK Notes were not guaranteed by any of the PIK Notes Issuer's subsidiaries, and therefore were not recorded in the Company's financial statements. The Exchange Notes, however, are guaranteed by the Company's subsidiaries, and therefore are recorded in its financial statements. In connection with recognizing the Exchange Notes, the Company recorded a non-cash contribution to its Parent as a reduction of additional paid-in capital. For more information on the long-term debt of the Company, see note 7.

#### ***Due to Sponsors***

As part of the debt refinancing, the Sponsors purchased \$30.0 million principal amount of new term loans under the Term Loan Facility. For more information on the New Term Loan Borrowings, see note 7.

#### ***Due to Parent***

Certain transactions, primarily related to income taxes, between Group and its Parent give rise to intercompany receivables and payables. A summary of the components of Due to Parent is as follows:

	<u>August 4, 2018</u>	<u>February 3, 2018</u>
Income taxes payable to Parent	\$ (49,888)	\$ (49,888)
Monitoring fees payable	(3,007)	(1,446)
Payment of certain transaction costs on behalf of Parent	13,124	13,124
Due to Parent	<u>\$ (39,771)</u>	<u>\$ (38,210)</u>

## **15. Recent Accounting Pronouncements**

In February 2016, a pronouncement was issued that requires lessees to recognize assets and liabilities in the amount of the present value of future lease payments for leases with terms of more than 12 months. The pronouncement is effective for fiscal years beginning after December 15, 2018. The Company is currently evaluating the impact of the new pronouncement on its condensed consolidated financial statements. However, the adoption is expected to have a material impact on its balance sheet. As an indicator of magnitude, as of February 3, 2018, the Company has committed to future minimum lease payments through 2028 of approximately \$900 million, on an undiscounted basis. However, minimum lease payments are expected to change during the period prior to the date of adoption due to a number of factors including the opening, closing, renewing, and renegotiating of store and corporate leases.

In January 2017, a pronouncement was issued that simplifies the measurement of goodwill impairment by no longer requiring an entity to perform a hypothetical purchase price allocation. Instead, impairment will be measured using the difference between the carrying amount and the fair value of the reporting unit. The pronouncement is effective for annual and interim periods in fiscal years beginning after December 15, 2019. The Company does not expect there to be a significant impact on its condensed consolidated financial statements.

In August 2017, a pronouncement was issued that simplifies the application of hedge accounting guidance and more closely aligns risk management activities and financial reporting. The pronouncement is effective for annual and interim periods in fiscal years beginning after December 15, 2018. The Company is currently evaluating the impact of the new pronouncement on its condensed consolidated financial statements.

In February 2018, a pronouncement was issued that will permit entities to reclassify tax effects stranded in accumulated other comprehensive income or loss, as a result of tax reform, to retained earnings. The pronouncement is effective for annual and interim periods in fiscal years beginning after December 15, 2018. The Company is currently evaluating the impact of the new pronouncement on its 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, our substantial lease obligations, our ability to anticipate and timely respond to changes in trends and consumer preferences, the strength of the global economy, competitive market conditions, our ability to attract and retain key personnel, our ability to successfully develop, launch and grow our newer concepts and execute on strategic initiatives, product offerings, sales channels and businesses, our ability to implement our growth strategy, material disruption to our information systems, our ability to implement our real estate strategy, changes in demographic patterns, adverse or unseasonable weather or other 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 3, 2018 filed with the Securities and Exchange Commission (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 3, 2018 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 subsidiaries.

### Executive Overview

J.Crew is an internationally recognized multi-brand apparel and accessories retailer that differentiates itself through high standards of quality, style, design and fabrics. We are a vertically-integrated, omni-channel specialty retailer that operates stores and websites both domestically and internationally. We design our products, including those under the J.Crew® and Madewell® brands and sub-brands, to offer complete assortments of women's, men's and children's apparel and accessories.

We sell our J.Crew and Madewell merchandise primarily through our retail and factory stores, our websites and select partners. As of August 4, 2018, we operated 229 J.Crew retail stores, 175 J.Crew factory stores (including 42 J.Crew Mercantile® stores), and 122 Madewell stores throughout the United States, Canada, the United Kingdom and Hong Kong; compared to 272 J.Crew retail stores, 182 J.Crew factory stores (including 42 J.Crew Mercantile stores), and 119 Madewell stores as of July 29, 2017. During fiscal 2018, we expect to open 10 Madewell stores and one J.Crew retail store and close approximately 30 stores.

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

<i>(Dollars in millions)</i>	<b>For the Thirteen Weeks Ended August 4, 2018</b>	<b>For the Thirteen Weeks Ended July 29, 2017</b>
		<i>(As adjusted)</i>
J.Crew	\$ 428.9	\$ 450.7
Madewell	121.7	94.2
Other(a)	37.0	25.8
Total revenues	<u>\$ 587.6</u>	<u>\$ 570.7</u>

(a) Consists primarily of revenues from wholesale customers and shipping and handling fees.

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

- Revenues increased 3.0% to \$587.6 million, with comparable company sales up 5.4%.
- J.Crew revenues decreased 4.8% to \$428.9 million, with J.Crew comparable sales up 0.5%.
- Madewell revenues increased 29.2% to \$121.7 million, with Madewell comparable sales up 27.8%.
- Gross margin increased to 38.5% from 38.2% last year.
- We opened one J.Crew retail store and one Madewell store. We closed one J.Crew retail store.

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

<i>(Dollars in millions)</i>	<b>For the Twenty-six Weeks Ended August 4, 2018</b>	<b>For the Twenty-six Weeks Ended July 29, 2017</b>
		<i>(As adjusted)</i>
J.Crew	\$ 820.7	\$ 872.2
Madewell	237.5	177.5
Other(a)	69.8	46.7
Total revenues	<u>\$ 1,128.0</u>	<u>\$ 1,096.4</u>

(a) Consists primarily of revenues from wholesale customers and shipping and handling fees.

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

- Revenues increased 2.9% to \$1,128.0 million, with comparable company sales up 3.0%.
- J.Crew revenues decreased 5.9% to \$820.7 million, with J.Crew comparable sales down 2.5%.
- Madewell revenues increased 33.8% to \$237.5 million, with Madewell comparable sales up 29.3%.
- Gross margin increased to 38.4% from 37.2% last year.
- We opened one J.Crew retail store and one Madewell store. We closed seven J.Crew retail stores and one J.Crew factory store.

### ***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 12 months, (ii) e-commerce net sales, and (iii) shipping and handling fees. Due to the 53<sup>rd</sup> week in fiscal 2017, when calculating comparable company sales for fiscal 2018, we have realigned the weeks of last year to be consistent with the current year retail calendar.

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 3, 2018 filed with the SEC.

### ***Results of Operations – Second Quarter of Fiscal 2018 compared to Second Quarter of Fiscal 2017***

<i>(Dollars in millions)</i>	<b>For the Thirteen Weeks Ended August 4, 2018</b>		<b>For the Thirteen Weeks Ended July 29, 2017</b>		<b>Variance Increase/(Decrease)</b>	
	<b>Amount</b>	<b>Percent of Revenues</b>	<b>Amount (As adjusted)</b>	<b>Percent of Revenues</b>	<b>Dollars</b>	<b>Percentage</b>
Revenues	\$ 587.6	100.0%	\$ 570.7	100.0%	\$ 16.9	3.0%
Gross profit	226.0	38.5	217.8	38.2	8.2	3.8
Selling, general and administrative expenses	192.7	32.8	209.1	36.6	(16.4)	(7.9)
Impairment losses	—	—	3.9	0.7	(3.9)	(100.0)
Income from operations	33.3	5.7	4.8	0.8	28.5	NM
Interest expense, net	34.4	5.9	22.8	4.0	11.6	50.8
Provision for income taxes	5.0	0.9	0.4	0.1	4.6	NM
Net loss	\$ (6.1)	(1.0)%	\$ (18.5)	(3.2)%	\$ 12.4	67.0%

### ***Revenues***

Total revenues increased \$16.9 million, or 3.0%, to \$587.6 million in the second quarter of fiscal 2018 from \$570.7 million in the second quarter last year, driven primarily by an increase in sales of women's apparel, specifically pants, dresses and knits. Comparable company sales increased 5.4% following a decrease of 4.8% in the second quarter last year.

J.Crew sales decreased \$21.8 million, or 4.8%, to \$428.9 million in the second quarter of fiscal 2018 from \$450.7 million in the second quarter last year. J.Crew comparable sales increased 0.5% following a decrease of 7.6% in the second quarter last year.

Madewell sales increased \$27.5 million, or 29.2%, to \$121.7 million in the second quarter of fiscal 2018 from \$94.2 million in the second quarter last year. Madewell comparable sales increased 27.8% following an increase of 12.2% in the second quarter last year.



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 4, 2018</u>	<u>For the Thirteen Weeks Ended July 29, 2017</u>
Apparel:		
Women's	58%	56%
Men's	22	24
Children's	6	6
Accessories	14	14
	<u>100%</u>	<u>100%</u>

Other revenues increased \$11.2 million to \$37.0 million in the second quarter of fiscal 2018 from \$25.8 million in the second quarter last year, primarily a result of revenue from wholesale customers.

### **Gross Profit**

Gross profit increased \$8.2 million to \$226.0 million in the second quarter of fiscal 2018 from \$217.8 million in the second quarter last year. This increase resulted from the following factors:

<u>(Dollars in millions)</u>	<u>Increase/ (decrease)</u>
	<u>(As adjusted)</u>
Increase in revenues	\$ 8.8
Increase in merchandise margin	2.0
Increase in buying and occupancy costs	(2.6)
Increase in gross profit	<u>\$ 8.2</u>

Gross margin increased to 38.5% in the second quarter of fiscal 2018 from 38.2% in the second quarter last year. The increase in gross margin was driven by a 30 basis point expansion in merchandise margin due to favorable product costs.

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

Selling, general and administrative expenses decreased \$16.4 million to \$192.7 million in the second quarter of fiscal 2018 from \$209.1 million in the second quarter last year. This decrease resulted from the following:

<u>(Dollars in millions)</u>	<u>Increase/ (decrease)</u>
	<u>(As adjusted)</u>
Decrease in transaction costs	\$ (14.7)
Decrease in transformation costs	(10.3)
Corporate occupancy actions	(9.3)
Increase in share-based and incentive compensation	1.9
Increase in operating and corporate expenses	6.0
Increase in marketing costs	10.0
Total decrease in selling, general and administrative expenses	<u>\$ (16.4)</u>

As a percentage of revenues, selling, general and administrative expenses decreased to 32.8% in the second quarter of fiscal 2018 from 36.6% in the second quarter last year.

### **Interest Expense, Net**

Interest expense, net of interest income, increased \$11.6 million to \$34.4 million in the second quarter of fiscal 2018 from \$22.8 million in the second quarter last year. A summary of interest expense is as follows:

<i>(Dollars in millions)</i>	<b>For the Thirteen Weeks Ended August 4, 2018</b>	<b>For the Thirteen Weeks Ended July 29, 2017</b>
Term Loan Facility	\$ 19.5	\$ 15.9
Notes(1)	11.3	2.1
Amortization of deferred financing costs and debt discount	1.8	1.3
ABL Facility	0.5	—
Realized hedging losses	0.5	2.8
Other, net of interest income	0.8	0.7
Interest expense, net	<u>\$ 34.4</u>	<u>\$ 22.8</u>

(1) We completed a debt exchange and refinancing in the second quarter of fiscal 2017. See “—Liquidity and Capital Resources” for more information.

### **Provision for Income Taxes**

On December 22, 2017, H.R.1, or the Tax Cuts and Jobs Act (“Tax Reform”) was signed into law. Among its many provisions, Tax Reform substantially reduced our ability to deduct all of our interest expense in fiscal 2018. The inability to deduct all of our interest expense will generate a significant carry forward of unutilized interest deductions. We are not forecasting future taxable income sufficient to utilize the carry forward. Therefore, we have recognized a valuation allowance with respect to the deferred tax asset related to the carry forward of unutilized interest deductions.

In the second quarter of fiscal 2018, we recorded a provision for income taxes of \$5.0 million, which reflects a charge for the valuation allowance with respect to the deferred tax asset related to the carry forward of unutilized interest deductions. Other items impacting the provision for income taxes include the recognition of international valuation allowances, lower rates in certain foreign jurisdictions, and reserves for uncertain tax positions.

The effective tax rate for the second quarter of 2017 was 2%. Items driving differences between the U.S. federal statutory rate of 35% and the effective rate include (i) the recognition of certain domestic and foreign valuation allowances, (ii) lower rates in certain foreign jurisdictions and (iii) reserves for uncertain tax positions.

### **Net Loss**

Net loss decreased \$12.4 million to \$6.1 million in the second quarter of fiscal 2018 from \$18.5 million in the second quarter last year. This decrease was due to: (i) a decrease in selling, general and administrative expenses of \$16.4 million, (ii) an increase in gross profit of \$8.2 million, (iii) lower impairment losses of \$3.9 million, offset by (iv) an increase in interest expense of \$11.6 million and (v) an increase in the provision for income taxes of \$4.6 million.

**Results of Operations – First Half of Fiscal 2018 compared to First Half of Fiscal 2017**

<i>(Dollars in millions)</i>	For the Twenty-six Weeks Ended August 4, 2018		For the Twenty-six Weeks Ended July 29, 2017		Variance Increase/(Decrease)	
	Amount	Percent of Revenues	Amount (As adjusted)	Percent of Revenues	Dollars	Percentage
	Revenues	\$ 1,128.0	100.0%	\$ 1,096.4	100.0%	\$ 31.6
Gross profit	432.8	38.4	408.4	37.2	24.4	6.0
Selling, general and administrative expenses	393.5	34.9	419.6	38.3	(26.1)	(6.2)
Impairment losses	6.9	0.6	135.1	12.3	(128.2)	(94.9)
Income (loss) from operations	32.4	2.9	(146.3)	(13.3)	178.7	NM
Interest expense, net	67.4	6.0	43.3	3.9	24.1	55.8
Provision (benefit) for income taxes	5.1	0.5	(50.1)	(4.6)	55.2	NM
Net loss	\$ (40.0)	(3.5)%	\$ (139.5)	(12.7)%	\$ 99.5	(71.3)%

**Revenues**

Total revenues increased \$31.6 million, or 2.9%, to \$1,128.0 million in the first half of fiscal 2018 from \$1,096.4 million in the first half last year driven primarily by an increase in sales of women's apparel, specifically pants, knits and lounge. Comparable company sales increased 3.0% following a decrease of 6.6% in the first half last year.

J.Crew sales decreased \$51.5 million, or 5.9%, to \$820.7 million in the first half of fiscal 2018 from \$872.2 million in the first half last year. J.Crew comparable sales decreased 2.5% following a decrease of 9.5% in the first half last year.

Madewell sales increased \$60.0 million, or 33.8%, to \$237.5 million in the first half of fiscal 2018 from \$177.5 million in the first half last year. Madewell comparable sales increased 29.3% following an increase of 11.7% in the first half last year.

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 4, 2018	For the Twenty-six Weeks Ended July 29, 2017
Apparel:		
Women's	59%	57%
Men's	21	22
Children's	6	7
Accessories	14	14
	<u>100%</u>	<u>100%</u>

Other revenues increased \$23.1 million to \$69.8 million in the first half of fiscal 2018 from \$46.7 million in the first half last year, primarily a result of revenue from wholesale customers.

**Gross Profit**

Gross profit increased \$24.4 million to \$432.8 million in the first half of fiscal 2018 from \$408.4 million in the first half last year. This increase resulted from the following factors:

<i>(Dollars in millions)</i>	Increase/ (decrease) (As adjusted)
Increase in revenues	\$ 16.4
Increase in merchandise margin	8.9
Increase in buying and occupancy costs	(0.9)
Increase in gross profit	<u>\$ 24.4</u>

Gross margin increased to 38.4% in the first half of fiscal 2018 from 37.2% in the first half last year. The increase in gross margin was driven by: (i) a 80 basis point expansion in merchandise margin due to favorable product costs and (ii) a 40 basis point decrease in buying and occupancy costs as a percentage of revenues.

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

Selling, general and administrative expenses decreased \$26.1 million to \$393.5 million in the first half of fiscal 2018 from \$419.6 million in the first half last year. This decrease resulted from the following:

<u>(Dollars in millions)</u>	<u>Increase/ (decrease)</u>
	<u>(As adjusted)</u>
Decrease in transaction costs	\$ (16.8)
Decrease in transformation costs	(13.5)
Corporate occupancy actions	(9.3)
Decrease in charges related to workforce reductions	(8.0)
Decrease in depreciation	(4.4)
Increase in share-based and incentive compensation	5.4
Increase in operating and corporate expenses	6.9
Increase in marketing costs	13.6
Total decrease in selling, general and administrative expenses	<u>\$ (26.1)</u>

As a percentage of revenues, selling, general and administrative expenses decreased to 34.9% in the first half of fiscal 2018 from 38.3% in the first half last year.

### ***Impairment Losses***

Impairment losses were \$6.9 million in the first half of fiscal 2018 compared to \$135.1 million in the first half last year. The impairment losses were the result of the write-down of the following assets:

<u>(Dollars in millions)</u>	<u>For the Twenty-six Weeks Ended August 4, 2018</u>	<u>For the Twenty-six Weeks Ended July 29, 2017</u>
Intangible asset related to the J.Crew trade name	\$ —	\$ 129.8
Long-lived assets	6.9	5.3
Impairment losses	<u>\$ 6.9</u>	<u>\$ 135.1</u>

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

Interest expense, net of interest income, increased \$24.1 million to \$67.4 million in the first half of fiscal 2018 from \$43.3 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 4, 2018</u>	<u>For the Twenty-six Weeks Ended July 29, 2017</u>
Term Loan Facility	\$ 37.9	\$ 31.4
Notes(1)	22.5	2.1
Amortization of deferred financing costs and debt discount	3.6	2.6
Realized hedging losses	1.9	5.8
ABL Facility	0.9	—
Other, net of interest income	0.6	1.4
Interest expense, net	<u>\$ 67.4</u>	<u>\$ 43.3</u>

(1) We completed a debt exchange and refinancing in the second quarter of fiscal 2017. See “—Liquidity and Capital Resources” for more information.

### Provision (Benefit) for Income Taxes

In the first half of fiscal 2018, we recorded a provision for income taxes of \$5.1 million, which reflects a charge for the valuation allowance with respect to the deferred tax asset related to the carry forward of unutilized interest deductions. Other items impacting the provision for income taxes include the recognition of international valuation allowances, lower rates in foreign jurisdictions, and reserves for uncertain tax positions. These items primarily drove the difference between the federal statutory rate of 21% and the effective rate of 15%.

In the first half of fiscal 2017, we recognized a deferred tax benefit of \$52.1 million primarily a result of the reversal of deferred taxes related to the intangible asset for the J.Crew trade name, which was written down by \$129.8 million in the first quarter. We did not recognize any additional deferred tax benefit on other operating losses due to an increase in the valuation allowance. The impact of not recognizing tax benefit on our other operating losses was the primary driver of the difference between the statutory rate of 35% and the effective rate of 26%.

### Net Loss

Net loss decreased \$99.5 million to \$40.0 million in the first half of fiscal 2018 from \$139.5 million in the first half last year. This decrease was due to: (i) lower impairment losses of \$128.2 million, (ii) a decrease in selling, general and administrative expenses of \$26.1 million, (iii) an increase in gross profit of \$24.4 million, offset by (iv) a decrease in the benefit for income taxes of \$55.2 million and (v) an increase in interest expense of \$24.1 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 (i) meeting debt service requirements, (ii) capital expenditures in connection with making information technology enhancements, opening new stores and improving our existing stores and making investments in our distribution network and (iii) funding working capital requirements. The most significant components of our working capital are cash and cash equivalents, merchandise inventories and accounts payable and other current liabilities. See “—Outlook” below.

### Operating Activities

<i>(Dollars in millions)</i>	For the Twenty-six Weeks Ended August 4, 2018	For the Twenty-six Weeks Ended July 29, 2017
Net loss	\$ (40.0)	\$ (139.5)
Adjustments to reconcile to cash flows from operating activities:		(As adjusted)
Depreciation of property and equipment	45.3	49.7
Impairment losses	6.9	135.1
Deferred income taxes	5.5	(52.1)
Amortization of intangible assets	3.6	4.6
Amortization of deferred financing costs and debt discount	3.6	2.6
Reclassification of hedging losses to earnings	1.9	5.8
Foreign currency transaction (gains) losses	0.2	(0.6)
Share-based compensation	0.1	0.4
Changes in operating assets and liabilities	(97.1)	(15.6)
Net cash used in operating activities	<u>\$ (70.0)</u>	<u>\$ (9.6)</u>

Cash used in operating activities of \$70.0 million in the first half of fiscal 2018 resulted from: (i) changes in operating assets and liabilities of \$97.1 million, primarily due to an increase in merchandise inventories as a result of an anticipated increase in revenues, and (ii) a net loss of \$40.0 million, partially offset by (iii) non-cash adjustments of \$67.1 million.

Cash used in operating activities of \$9.6 million in the first half of fiscal 2017 resulted from: (i) net loss of \$139.5 million and (ii) changes in operating assets and liabilities of \$15.6 million primarily due to seasonal working capital fluctuations, partially offset by (iii) non-cash adjustments of \$145.5 million.

## Investing Activities

<i>(Dollars in millions)</i>	<b>For the Twenty-six Weeks Ended August 4, 2018</b>	<b>For the Twenty-six Weeks Ended July 29, 2017</b>
Capital expenditures:		
Information technology	\$ (10.9)	\$ (8.9)
New stores and store improvements	(5.2)	(10.6)
Other(1)	(3.0)	(0.7)
Net cash used in investing activities	<u>\$ (19.1)</u>	<u>\$ (20.2)</u>

(1) Includes capital expenditures for warehouse improvements and general corporate purposes.

Capital expenditures are planned at approximately \$55 to 65 million for fiscal year 2018, including approximately \$35 million for information technology enhancements, approximately \$15 million for new stores and store improvements, and the remainder for warehouse improvements and general corporate purposes.

## Financing Activities

<i>(Dollars in millions)</i>	<b>For the Twenty-six Weeks Ended August 4, 2018</b>	<b>For the Twenty-six Weeks Ended July 29, 2017</b>
Net borrowings under the ABL Facility	\$ 25.3	\$ —
Quarterly principal repayments of Term Loan Facility	(7.8)	(7.8)
Proceeds from New Notes, net of discount	—	94.1
Proceeds from New Term Loan Borrowings, net of discount	—	29.4
Repayments pursuant to the Term Loan amendment	—	(150.5)
Cost paid in connection with refinancings of debt	—	(5.7)
Net cash provided by (used in) financing activities	<u>\$ 17.5</u>	<u>\$ (40.5)</u>

Cash provided by financing activities of \$17.5 million in the first half of fiscal 2018 resulted from (i) net borrowings under the ABL Facility, offset by (ii) quarterly principal repayments of the Term Loan Facility.

Cash used in financing activities of \$40.5 million in the first half of fiscal 2017 resulted primarily from (i) repayments pursuant to the Term Loan amendment, offset by (ii) the proceeds from New Money Notes and New Term Loan Borrowings.

### Debt Exchange and Refinancing

On July 13, 2017, the Parent and certain of its subsidiaries completed the following interrelated liability management transactions:

- a private exchange offer (the “Exchange Offer”) pursuant to which \$565.7 million aggregate principal amount of the outstanding 7.75%/8.50% Senior PIK Toggle Notes due 2019 (the “PIK Notes”) issued by Chinos Intermediate Holdings A, Inc., a direct wholly-owned subsidiary of the Parent (the “PIK Notes Issuer”), were exchanged for aggregate consideration consisting of:
  - \$249,596,000 aggregate principal amount of 13% Senior Secured Notes due 2021 issued by J.Crew Brand, LLC and J.Crew Brand Corp. (the “Exchange Notes”), which are secured primarily by the U.S. intellectual property assets held by J.Crew Domestic Brand, LLC (“IPCo”);
  - 189,688 shares of Parent’s 7% non-convertible perpetual series A preferred stock, no par value per share, with an aggregate initial liquidation preference of \$189,688,000; and
  - 15% of Parent’s common equity, or 17,362,719 shares of Parent’s class A common stock, \$0.00001 par value per share;
- the receipt of consents from the holders of a majority of the PIK Notes with respect to certain amendments to the indenture governing the PIK Notes;

- completion of an amendment to our Amended and Restated Credit Agreement, dated as of March 5, 2014 (the “Term Loan Facility”) to, among other things, facilitate the following related transactions:
  - the repayment of \$150.5 million principal amount of term loans then outstanding under the Term Loan Facility;
  - the transfer of the remaining undivided 27.96% ownership interest in the U.S. intellectual property rights of the J.Crew brand (the “Additional Transferred IP”) to IPCo, which, together with the undivided 72.04% ownership interest transferred in December 2016 (the “Initial Transferred IP”) represent 100% of the U.S. intellectual property rights of the J.Crew brand (the “Transferred IP”), and the execution of related license agreements;
  - the issuance of \$97.0 million aggregate principal amount of an additional series of 13% Senior Secured Notes due 2021 by J.Crew Brand, LLC and J.Crew Brand Corp. (the “New Money Notes” and, together with the Exchange Notes, the “Notes”), subject to the same terms and conditions as the Exchange Notes, for cash at a 3% discount, subject to the terms of the note purchase agreement, dated June 12, 2017, the proceeds of which were loaned on a subordinated basis to us and were applied, in part, to finance the repayment of the \$150.5 million principal amount of term loans referenced above; and
  - the raising of additional borrowings under the Term Loan Facility of \$30.0 million (at a 2% discount) provided by our Sponsors (the “New Term Loan Borrowings”), the net proceeds of which were also applied, in part, to finance the repayment of the \$150.5 million principal amount of term loans referenced above.

### *Financing Arrangements*

#### ABL Facility

We have an ABL Facility, which is governed by a credit agreement with Bank of America, N.A., as administrative agent and the other agents and lenders party thereto, that provides for a \$350 million senior secured asset-based revolving line of credit (which may be increased by up to \$100 million in certain circumstances), subject to a borrowing base limitation. 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 \$200 million, 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 the maturity date of November 17, 2021.

On August 4, 2018, standby letters of credit were \$58.1 million, outstanding borrowings were \$25.3 million, and excess availability, as defined, was \$215.0 million. The weighted average interest rate on the borrowings outstanding under the ABL Facility was 5.25% on August 4, 2018. Average short-term borrowings under the ABL Facility were \$35.5 million in the first half of fiscal 2018. There were no short term borrowings under the ABL Facility in the first half of fiscal 2017.

As of the date of this report, there were outstanding borrowings of approximately \$67 million under the ABL Facility with excess availability of approximately \$225 million.

#### Demand Letter of Credit Facility

We have an unsecured demand letter of credit facility with HSBC which provides for the issuance of up to \$20 million of documentary letters of credit on a no fee basis. On August 4, 2018, outstanding documentary letters of credit were \$19.9 million and availability under this facility was \$0.1 million.

#### Term Loan Facility

*2017 Amendment.* On July 13, 2017, concurrently with the settlement of the Exchange Offer, we amended our Term Loan Facility to, among other things, (i) increase the interest rate applicable to the loans held by consenting lenders, which represented 88% of lenders, (the “Consenting Lenders”; and the loans held by the Consenting Lenders, the “Amended Loans”) by 22 basis points, (ii) increase the amount of amortization payable to Consenting Lenders, (iii) provide for the New Term Loan Borrowings of \$30.0 million, (iv) amend certain covenants and events of default and (v) direct Wilmington Savings Fund Society, FSB, as administrative agent under the Term Loan Facility, to dismiss, with prejudice, certain litigation regarding the Initial Transferred IP (and the related actions). Additionally, we repaid \$150.5 million of principal amount of term loans outstanding under the Term Loan Facility, which was financed with (i) the net proceeds from the New Money Notes of \$94.1 million, (ii) the net proceeds from the New Term Loan Borrowings of \$29.4 million and (iii) cash on hand of \$27.0 million.

*Interest Rate.* Initial borrowings under the Term Loan Facility bear interest at a rate per annum equal to an applicable margin (which, in the case of the Amended Loans, was increased by 22 basis points) plus, at our option, either (a) a LIBOR determined by reference to the costs of funds for U.S. dollar deposits for the relevant interest period 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, plus 1.00%. New Term Loan Borrowings bear interest at 9% per annum payable in cash plus 3% per annum payable in kind.

The weighted average interest rate on the borrowings outstanding under the Term Loan Facility was 5.61% on August 4, 2018. The applicable margin (i) in effect for base rate borrowings was, (x) in the case of term loans, other than the New Term Loan Borrowings and the Amended Loans, 2.00%, (y) in the case of the Amended Loans, 2.22% and (z) in the case of the New Term Loan Borrowings, 12.00% (of which 3.00% is payable in kind) and (ii) with respect to LIBOR borrowings was, (x) in the case of term loans, other than the New Term Loan Borrowings and the Amended Loans, 3.00% and the LIBOR Floor, (y) in the case of the Amended Loans, 3.22% and the LIBOR Floor and (z) in the case of the New Term Loan Borrowings, 12.00% (of which 3.00% is payable in kind), respectively, at August 4, 2018.

*Principal Repayments.* We are required to make principal repayments equal to 0.25% of the original principal amount of the Term Loan Facility (excluding the New Term Loan Borrowings), or \$3.9 million, on the last business day of January, April, July, and October. We are also required (i) to repay the term loan based on an annual calculation of excess cash flow, as defined in the agreement, (ii) in the second quarter of fiscal 2019, to make a principal repayment of \$11.9 million which is equal to 1.00% of the aggregate principal amount of Amended Loans outstanding on July 13, 2017 and (iii) beginning on July 31, 2019, on the last business day of January, April, July and October, to make additional principal repayments of \$1.5 million equal to 0.125% of the aggregate principal amount of Amended Loans outstanding on July 13, 2017. The maturity date of the Term Loan Facility is March 5, 2021.

#### Notes

*General.* On July 13, 2017, in connection with settlement of the Exchange Offer and the issuance of the Notes, J.Crew Brand, LLC and J.Crew Brand Corp. (together, the “Notes Co-Issuers”) and the Guarantors (as defined below) entered into (i) an indenture with U.S. Bank National Association, as Trustee and collateral agent, governing the terms of the Exchange Notes (the “Exchange Notes Indenture”) and (ii) an indenture with the Trustee and U.S. Bank, as collateral agent, governing the terms of the New Money Notes (the “New Money Notes Indenture”), which is in substantially the same form as the Exchange Notes Indenture.

*Interest Rate.* The Notes bear interest at a rate of 13% per annum, and interest is payable semi-annually on March 15 and September 15 of each year. The Notes mature on September 15, 2021.

*Notes Guarantee.* The Notes are guaranteed by J.Crew Brand Intermediate, LLC, IPCo and J.Crew International Brand, LLC, each of which is a Delaware limited liability company and a wholly-owned indirect subsidiary of the Company (collectively, the “Guarantors,” and each, a “Guarantor”). The PIK Notes Issuer also unconditionally guarantees the payment obligations of the Notes Co-Issuers and the Guarantors.

*Exchange Notes Collateral.* The Exchange Notes and the guarantees thereof are general senior secured obligations of the Notes Co-Issuers and the Guarantors, secured on a first priority lien basis by the Initial Transferred IP and certain other assets of the Notes Co-Issuers and Guarantors, and on a second priority lien basis by the Additional Transferred IP, subject, in each case, to permitted liens under the Exchange Notes Indenture and that certain intercreditor agreement, entered into between the collateral agents on July 13, 2017.

*New Money Notes Collateral.* The New Money Notes and the guarantees thereof are general senior secured obligations of the Notes Co-Issuers and the Guarantors, secured on a first priority lien basis by the Additional Transferred IP and certain other assets, and on a second priority lien basis by the Initial Transferred IP, subject, in each case, to permitted liens under the New Money Notes Indenture and the intercreditor agreement.

*Redemption.* The Notes are redeemable at the option of the Notes Co-Issuers, in whole or in part, at any time, at a price equal to one hundred percent (100%) of the principal amount of the Notes to be redeemed, plus accrued and unpaid interest, if any, to, but not including, the redemption date, plus a “make whole” premium. The Notes are not subject to any mandatory redemption obligation, and there is no sinking fund provided for the Notes.

*Change in Control.* Upon the occurrence of a Change of Control (as defined in each of the indentures, as applicable), the Notes Co-Issuers will be required to offer to repay all of the Notes at 100% of the aggregate principal amount repaid plus accrued and unpaid interest, if any, to, but not including, the date of purchase.



*Covenants.* Each of the indentures contains covenants covering (i) the payment of principal and interest, (ii) maintenance of an office or agency for the payment of the Notes, (iii) reports to the applicable Trustee and holders of the Notes, (iv) stay, extension and usury laws, (v) payment of taxes, (vi) existence, (vii) maintenance of properties and (viii) maintenance of insurance. Each of the indentures relating to the Notes also includes covenants that (i) limit the ability to transfer the collateral and (ii) limit liens that may be imposed on the assets of the Guarantors, which covenants are, in each case, subject to certain exceptions set forth in each of the indentures.

#### PIK Notes

On November 4, 2013, PIK Notes Issuer, an indirect parent holding company of Group, issued \$500 million of PIK Notes. The PIK Notes were: (i) senior unsecured obligations of the PIK Notes Issuer, (ii) structurally subordinated to all of the liabilities of the PIK Notes Issuers' subsidiaries, and (iii) not guaranteed by any of the PIK Notes Issuers' subsidiaries, and therefore are not recorded in our financial statements. As part of the refinancing in July 2017, \$565.7 million in aggregate principal amount of the PIK Notes were exchanged for \$249.6 million of Exchange Notes and shares of preferred and common stock of the Parent.

As of August 4, 2018, there were \$0.9 million in aggregate principal amount of PIK Notes outstanding.

#### IP License Agreements

In October 2016, we formed wholly-owned indirect subsidiaries of the Company, including IPCo and J.Crew Brand, LLC (collectively, "J.Crew BrandCo"). In December 2016, J.Crew International, Inc. ("JCI") transferred an undivided 72.04% ownership interest in the U.S. intellectual property rights of the J.Crew brand to IPCo, and entered into a related intellectual property license agreement with IPCo. In July 2017, JCI transferred the remaining undivided 27.96% ownership interest in the U.S. intellectual property rights of the J.Crew brand to IPCo, which, together with the initial intellectual property contributed in December 2016, represent 100% of the U.S. intellectual property rights of the J.Crew brand, entered into a license agreement amending and restating the December 2016 license agreement with IPCo and entered into an additional intellectual property license agreement with IPCo (collectively, the "IP License Agreements").

Under the IP License Agreements, J.Crew Operating Corp. ("OpCo"), our direct wholly-owned subsidiary, pays a fixed license fee of \$59 million per annum to IPCo, which owns the U.S. intellectual property rights of the J.Crew brand. The license fees are payable on March 1 and September 1 of each fiscal year. The terms of the 2017 IP License Agreements are no less favorable than could be obtained in an arm's length transaction with an unaffiliated third party. These royalty payments have no impact on our condensed consolidated results of operations and are not subject to the covenants under our credit facilities or the PIK Notes.

The proceeds from the license fees to IPCo are used by J.Crew BrandCo to meet debt service requirements on the Notes. Any license fees in excess of the debt service requirements are loaned back to OpCo on a subordinated basis. As of August 4, 2018, J.Crew BrandCo had total assets of \$396.1 million, consisting of intangible assets of \$250.2 million, receivable due from OpCo of \$121.0 million, license fee receivable of \$24.6 million and cash and cash equivalents of \$0.3 million, and total liabilities of \$357.1 million related to the Notes. IPCo earned royalty revenue of \$14.8 million and \$29.5 million in the second quarter and first half of fiscal 2018, respectively. The Notes are guaranteed by the intangible assets of J.Crew BrandCo.

Below is consolidating balance sheet information reflecting the elimination of the accounts of J.Crew BrandCo from our condensed consolidated balance sheet as of August 4, 2018.

	As of August 4, 2018		
	(unaudited)		
	Consolidated balance sheet	Eliminations of J.Crew BrandCo	Consolidated balance sheet of subsidiaries excluding J.Crew BrandCo
<b>ASSETS</b>			
Current assets:			
Cash and cash equivalents	\$ 34,742	\$ (293)	\$ 34,449
Merchandise inventories, net	412,862	—	412,862
Prepaid expenses and other current assets	107,855	—	107,855
Refundable income taxes	6,761	—	6,761
Total current assets	<u>562,220</u>	<u>(293)</u>	<u>561,927</u>
Property and equipment, net	256,313	—	256,313
Intangible assets, net	305,025	(250,195)	54,830
Investment in subsidiary	—	183,581	183,581
Deferred income taxes, net	—	31,030	31,030
Goodwill	107,900	—	107,900
Other assets	7,222	—	7,222
Total assets	<u>\$ 1,238,680</u>	<u>\$ (35,877)</u>	<u>\$ 1,202,803</u>
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>			
Current liabilities:			
Accounts payable	\$ 297,505	\$ —	\$ 297,505
Other current liabilities	161,228	24,583	185,811
Due to Parent	39,771	—	39,771
Borrowings under the ABL Facility	25,300	—	25,300
Interest payable	22,632	(16,897)	5,735
Current portion of long-term debt	29,039	—	29,039
Total current liabilities	<u>575,475</u>	<u>7,686</u>	<u>583,161</u>
Long-term debt, net	1,680,371	(340,234)	1,340,137
Due to J.Crew BrandCo	—	121,018	121,018
Lease-related deferred credits, net	109,166	—	109,166
Deferred income taxes, net	35,584	(35,584)	—
Other liabilities	27,841	—	27,841
Total liabilities	<u>2,428,437</u>	<u>(247,114)</u>	<u>2,181,323</u>
Stockholders' deficit:			
Common stock \$0.01 par value; 1,000 shares authorized, issued and outstanding	—	—	—
Additional paid-in capital	733,191	249,596	982,787
Accumulated other comprehensive income	497	—	497
Accumulated deficit	(1,923,445)	(38,359)	(1,961,804)
Total stockholders' deficit	<u>(1,189,757)</u>	<u>211,237</u>	<u>(978,520)</u>
Total liabilities and stockholders' deficit	<u>\$ 1,238,680</u>	<u>\$ (35,877)</u>	<u>\$ 1,202,803</u>

Below is consolidating statement of operations and comprehensive loss information reflecting the elimination of the accounts of J.Crew BrandCo from our condensed consolidated statement of operations and comprehensive loss for the thirteen and twenty-six weeks ended August 4, 2018.

	For the Thirteen Weeks Ended August 4, 2018		
	Consolidated	Eliminations of J.Crew BrandCo	Consolidated subsidiaries excluding J.Crew BrandCo
(unaudited)			
<b>Condensed Consolidated Statements of Operations and Comprehensive Loss</b>			
Revenues:			
Net sales	\$ 550,541	\$ —	\$ 550,541
Other	37,032	—	37,032
Total revenues	<u>587,573</u>	<u>—</u>	<u>587,573</u>
Cost of goods sold, including buying and occupancy costs	361,572	—	361,572
Royalty expense	—	14,750	14,750
Gross profit	<u>226,001</u>	<u>(14,750)</u>	<u>211,251</u>
Selling, general and administrative expenses	192,659	—	192,659
Income from operations	<u>33,342</u>	<u>(14,750)</u>	<u>18,592</u>
Interest expense, net of interest income	34,400	(11,773)	22,627
Loss before income taxes	<u>(1,058)</u>	<u>(2,977)</u>	<u>(4,035)</u>
Provision for income taxes	5,036	—	5,036
Net loss	<u>\$ (6,094)</u>	<u>\$ (2,977)</u>	<u>\$ (9,071)</u>
Other comprehensive income (loss):			
Reclassification of losses on cash flow hedges, net of tax, to earnings	365	—	365
Unrealized gain on cash flow hedges, net of tax	(201)	—	(201)
Foreign currency translation adjustments	(147)	—	(147)
Comprehensive loss	<u>\$ (6,077)</u>	<u>\$ (2,977)</u>	<u>\$ (9,054)</u>

	<b>For the Twenty-six Weeks Ended August 4, 2018</b>		
	(unaudited)		
<b>Condensed Consolidated Statements of Operations and Comprehensive Loss</b>	<u>Consolidated</u>	<u>Eliminations of J.Crew BrandCo</u>	<u>Consolidated subsidiaries excluding J.Crew BrandCo</u>
Revenues:			
Net sales	\$ 1,058,247	\$ —	\$ 1,058,247
Other	69,776	—	69,776
Total revenues	<u>1,128,023</u>	<u>—</u>	<u>1,128,023</u>
Cost of goods sold, including buying and occupancy costs	695,214	—	695,214
Royalty expense	—	29,500	29,500
Gross profit	<u>432,809</u>	<u>(29,500)</u>	<u>403,309</u>
Selling, general and administrative expenses	393,495	—	393,495
Impairment losses	6,866	—	6,866
Income from operations	<u>32,448</u>	<u>(29,500)</u>	<u>2,948</u>
Interest expense, net of interest income	67,382	(23,547)	43,835
Loss before income taxes	<u>(34,934)</u>	<u>(5,953)</u>	<u>(40,887)</u>
Provision for income taxes	5,085	—	5,085
Net loss	<u>\$ (40,019)</u>	<u>\$ (5,953)</u>	<u>\$ (45,972)</u>
Other comprehensive income (loss):			
Reclassification of losses on cash flow hedges, net of tax, to earnings	1,361	—	1,361
Unrealized loss on cash flow hedges, net of tax	2,217	—	2,217
Foreign currency translation adjustments	(478)	—	(478)
Comprehensive loss	<u>\$ (36,919)</u>	<u>\$ (5,953)</u>	<u>\$ (42,872)</u>

### **Outlook**

Our short-term and long-term liquidity needs arise primarily from (i) debt service requirements, including required (a) quarterly principal repayments and (b) repayments, if any, based on annual excess cash flows, if any, as defined, (ii) capital expenditures, and (iii) working capital. Management anticipates that capital expenditures in fiscal 2018 will be approximately \$55 to 65 million for fiscal year 2018, including approximately \$35 million for information technology enhancements, approximately \$15 million for new stores and store improvements, and the remainder for warehouse improvements and general corporate purposes. Management expects to pay interest of approximately \$130 million in fiscal 2018 to fund debt service obligations. During fiscal 2018, we expect to open 10 Madewell stores and one J.Crew retail store and close approximately 30 stores.

Management believes that our current balances of cash and cash equivalents, projected cash flow from operations and amounts available under the ABL Facility will be adequate to fund primary short-term and long-term liquidity needs. Our ability to satisfy these obligations and to remain in compliance with the financial covenants under our financing arrangements 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 a portion of our international purchase of merchandise. We also enter into standby letters of credit to secure reimbursement obligations under certain insurance and import programs and lease obligations. As of August 4, 2018, 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
Letters of Credit			(amounts in millions)		
Standby	\$ 58.1	\$ 30.9	\$ 27.2	\$ —	\$ —
Documentary	19.9	19.9	—	—	—
	<u>\$ 78.0</u>	<u>\$ 50.8</u>	<u>\$ 27.2</u>	<u>\$ —</u>	<u>\$ —</u>

### Cyclicality and Seasonality

Our industry is cyclical and 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, foreign currency exchange rates and consumer confidence.

Our business is seasonal, and 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 when 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 3, 2018 filed with the SEC.

During the first quarter of fiscal 2018, we adopted a pronouncement that clarified the principles of revenue recognition and standardized a comprehensive model for recognizing revenue arising from contracts with customers. The adoption impacted our critical accounting policies as follows:

- We now defer revenue and recognize a liability for rewards points issued in connection with our customer loyalty program for the rewards points expected to be redeemed for merchandise in the future, which resulted in a reduction of the liability recorded in connection with our loyalty program.
- We continue to make estimates of future sales returns related to current period sales but have changed the presentation of the allowance for sales returns to recognize the reserve on a gross basis in the condensed consolidated financial statements. On the condensed consolidated balance sheet, we now record an asset in other current assets for the inventory expected to be returned and a liability in other current liabilities for the sales expected to be refunded. On the statement of operations and comprehensive loss, we now present the change in the liability in total revenues and the change in the asset in cost of goods sold.

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

### Interest Rates

We are exposed to interest rate risk arising from changes in interest rates on the floating rate indebtedness under our Senior Credit Facilities. Borrowings pursuant to our Term Loan Facility bear interest at floating rates based on LIBOR, but in no event less than the floor rate of 1.00%, plus the applicable margin. Borrowings pursuant to our ABL Facility bear interest at floating rates based on LIBOR and the prime rate, plus the applicable margin. Accordingly, fluctuations in market interest rates may increase or decrease our interest expense which will, in turn, increase or decrease our net income or net loss and cash flow.

We manage a portion of our interest rate risk related to floating rate indebtedness by entering into interest rate swaps whereby we receive floating rate payments based on the greater of LIBOR and the floor rate and make payments based on a fixed rate. Our interest rate swap agreements cover a notional amount of \$800 million from March 2016 to March 2019. Under the terms of these agreements, our effective fixed interest rate on the notional amount of indebtedness is 2.56% plus the applicable margin.

As a result of the floor rate described above, we estimate that a 1% increase in LIBOR would increase our annual interest expense by \$6 million.

#### *Foreign Currency*

Foreign currency exposures arise from transactions denominated in a currency other than the entity's functional currency. Although our inventory is primarily purchased from foreign vendors, such purchases are denominated in U.S. dollars, and are therefore not subject to foreign currency exchange risk. However, we operate in foreign countries, which exposes the Company to market risk associated with exchange rate fluctuations. The Company is exposed to foreign currency exchange risk resulting from its foreign operating subsidiaries' U.S. dollar denominated transactions.

#### **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

We are 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 effect on our financial position, results of operations or cash flows. As of August 4, 2018, we have recorded a reserve for certain legal contingencies in connection with ongoing claims and litigation. The reserve is not material to our results of operations. In addition, there are certain other claims and legal proceedings pending against us for which accruals have not been established.

***Eaton Vance Management, et al. v. Wilmington Savings Fund Society, FSB, as Administrative Agent and Collateral Agent, et al., Index No. 654397/2017, (Sup. Ct. N.Y. C'ty.).***

On June 22, 2017, Eaton Vance Management and certain affiliated funds as well as Highland Capital Management and certain affiliated funds (collectively, the “Highland/EV Plaintiffs”), filed a complaint in the New York State Supreme Court, Commercial Division, against the Company and WSFS, seeking, among other things, declarations that the July 13, 2017 Amendment to the Term Loan Facility was ineffective absent unanimous consent of all lenders under the facility, that certain of our actions with respect to certain of its intellectual property assets were taken in violation of the terms of the Term Loan Facility, and that those actions also constituted fraudulent conveyances.

On August 7, 2017, WSFS and the Company filed separate motions to dismiss certain of the Highland/EV Plaintiffs’ claims for failure to state a claim and lack of standing, among other reasons. On September 7, 2017, the Highland/EV Plaintiffs filed an amended complaint in the New York State Supreme Court, Commercial Division, against the Company and WSFS. The amended complaint continued to assert claims for breach of the terms of the Term Loan Facility, and for fraudulent conveyance and added an additional claim for fraudulent inducement against the Company.

In response to the amended complaint, WSFS and the Company withdrew their prior motions to dismiss and, on October 20, 2017, filed renewed motions seeking dismissal in whole or part. Among other things, we sought dismissal of the amended complaint for failure to state a claim, lack of standing, and because its fraud claims are duplicative of the Highland/EV Plaintiffs’ claims under the documents governing the Term Loan Facility. The Highland/EV Plaintiffs filed an omnibus brief on December 1, 2017 opposing the motions to dismiss. The Company and WSFS each filed reply briefs on December 22, 2017 reiterating that the majority of the Highland/EV Plaintiffs’ claims should be dismissed as a matter of law.

Oral argument on the motions to dismiss occurred on March 8, 2018. On April 25, 2018, the judge issued a Memorandum Decision and Order, which granted our partial motion to dismiss in its entirety and dismissed as a matter of law the majority of the Highland/EV Plaintiffs’ claims with prejudice. The Highland/EV Plaintiffs’ sole remaining claim is for breach of contract based on the theory that the July 13, 2017 Amendment to the Term Loan Facility required unanimous consent of all lenders under the facility. Discovery in the action is ongoing. We believe that the Highland/EV Plaintiffs’ claim is wholly without merit, and intend to vigorously oppose the claim.

### ITEM 1A. RISK FACTORS

Our Annual Report on Form 10-K for the fiscal year ended February 3, 2018 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*

<b>Exhibit No.</b>	<b>Document</b>
3.1	<a href="#">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.</a>
3.2	<a href="#">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.</a>

**Certifications**

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

**Interactive Data Files**

<b>Exhibit No.</b>	<b>Document</b>
101	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Condensed Consolidated Balance Sheets at August 4, 2018 and February 3, 2018, (ii) the Condensed Consolidated Statements of Operations and Comprehensive Loss for the thirteen weeks ended August 4, 2018 and July 29, 2017, (iii) the Condensed Consolidated Statements of Operations and Comprehensive Loss for the twenty-six weeks ended August 4, 2018 and July 29, 2017, (iv) the Condensed Consolidated Statements of Changes in Stockholders' Deficit for the twenty-six weeks ended August 4, 2018 and the fifty-three weeks ended February 3, 2018, (v) the Condensed Consolidated Statements of Cash Flows for the twenty-six weeks ended August 4, 2018 and July 29, 2017, and (vi) the Notes to Unaudited Condensed Consolidated Financial Statements.*

\* Filed herewith.

\*\* Furnished herewith.





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

I, James Brett, 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: August 28, 2018

/s/ JAMES BRETT  
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**James Brett**  
Chief Executive Officer

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

I, Vincent Zanna, 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: August 28, 2018

/s/ VINCENT ZANNA

**Vincent Zanna**  
**Chief Financial Officer and Treasurer**

**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 4, 2018 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, James Brett, Chief Executive Officer of the Company, and Vincent Zanna, 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: August 28, 2018

/s/ JAMES BRETT

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**James Brett**  
**Chief Executive Officer**

/s/ VINCENT ZANNA

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**Vincent Zanna**  
**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.*