

**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 May 4, 2019**

**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)**

**225 Liberty Street  
New York, New York 10281  
Telephone: (212) 209-2500**

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Trading Symbol(s) | Name of each exchange on which registered |
|---------------------|-------------------|---|
| None                | N/A               | N/A                                       |

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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a 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"/> | 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.

| Common Stock                            | Outstanding at May 24, 2019 |
|---|-----------------------------|
| 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.**  
**TABLE OF CONTENTS – FORM 10-Q**

|  | <u>Page<br/>Number</u> |
|--|------------------------|
| <b><u>PART I. FINANCIAL INFORMATION</u></b>  |                        |
| Item 1. <a href="#"><u>Condensed Consolidated Financial Statements (unaudited):</u></a>  | 3                      |
| <a href="#"><u>Condensed Consolidated Balance Sheets at May 4, 2019 and February 2, 2019</u></a>   | 3                      |
| <a href="#"><u>Condensed Consolidated Statements of Operations and Comprehensive Loss for the thirteen weeks ended May 4, 2019 and May 5, 2018</u></a> | 4                      |
| <a href="#"><u>Condensed Consolidated Statements of Changes in Stockholders' Deficit for the thirteen weeks ended May 4, 2019 and May 5, 2018</u></a>  | 5                      |
| <a href="#"><u>Condensed Consolidated Statements of Cash Flows for the thirteen weeks ended May 4, 2019 and May 5, 2018</u></a>                        | 6                      |
| <a href="#"><u>Notes to Unaudited Condensed Consolidated Financial Statements</u></a>  | 7                      |
| Item 2. <a href="#"><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></a>                                   | 21                     |
| Item 3. <a href="#"><u>Quantitative and Qualitative Disclosure About Market Risk</u></a>   | 31                     |
| Item 4. <a href="#"><u>Controls and Procedures</u></a>   | 32                     |
| <b><u>PART II. OTHER INFORMATION</u></b>   |                        |
| Item 1. <a href="#"><u>Legal Proceedings</u></a>   | 33                     |
| Item 1A. <a href="#"><u>Risk Factors</u></a>   | 33                     |
| Item 6. <a href="#"><u>Exhibits</u></a>  | 34                     |

PART I – FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

J.CREW GROUP, INC.  
Condensed Consolidated Balance Sheets  
(unaudited)  
(in thousands, except share data)

|  | May 4,<br>2019 | February 2,<br>2019 |
|--|----------------|---------------------|
| <b>ASSETS</b>  |                |                     |
| Current assets:  |                |                     |
| Cash and cash equivalents  | \$ 30,236      | \$ 25,738           |
| Restricted cash  | 5,258          | 13,747              |
| Accounts receivable, net   | 56,444         | 40,342              |
| Merchandise inventories, net   | 418,009        | 390,470             |
| Prepaid expenses and other current assets                                      | 68,739         | 84,942              |
| Refundable income taxes  | 5,772          | 7,331               |
| Total current assets   | 584,458        | 562,570             |
| Property and equipment, net  | 239,478        | 243,620             |
| Right-of-use lease assets  | 513,037        | —                   |
| Intangible assets, net   | 300,117        | 301,397             |
| Goodwill   | 107,900        | 107,900             |
| Other assets   | 7,642          | 6,164               |
| Total assets   | \$ 1,752,632   | \$ 1,221,651        |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>                                   |                |                     |
| Current liabilities:   |                |                     |
| Accounts payable   | \$ 224,700     | \$ 259,705          |
| Borrowings under the ABL Facility  | 215,800        | 70,800              |
| Other current liabilities  | 203,903        | 244,864             |
| Current portion of right-of-use lease liabilities                              | 114,052        | —                   |
| Due to Parent  | 35,004         | 37,462              |
| Interest payable   | 8,848          | 23,866              |
| Current portion of long-term debt  | 32,070         | 32,070              |
| Total current liabilities  | 834,377        | 668,767             |
| Long-term debt, net  | 1,672,166      | 1,673,282           |
| Long-term right-of-use lease liabilities                                       | 487,765        | —                   |
| Lease-related deferred credits, net  | —              | 105,877             |
| Deferred income taxes, net   | 16,545         | 16,872              |
| Other liabilities  | 31,199         | 29,096              |
| Total liabilities  | 3,042,052      | 2,493,894           |
| Stockholders' deficit:   |                |                     |
| Common stock \$0.01 par value; 1,000 shares authorized, issued and outstanding | —              | —                   |
| Additional paid-in capital   | 733,233        | 733,229             |
| Accumulated other comprehensive loss   | (2,918)        | (1,967)             |
| Accumulated deficit  | (2,019,735)    | (2,003,505)         |
| Total stockholders' deficit  | (1,289,420)    | (1,272,243)         |
| Total liabilities and stockholders' deficit                                    | \$ 1,752,632   | \$ 1,221,651        |

See notes to unaudited condensed consolidated financial statements.

**J.CREW GROUP, INC.**

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

|   | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 4, 2019</b> | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 5, 2018</b> |
|---|---|---|
| Revenues:   |   |   |
| Net sales   | \$ 508,976  | \$ 507,706  |
| Other   | 69,530  | 32,744  |
| Total revenues  | <u>578,506</u>  | <u>540,450</u>  |
| Cost of goods sold, including buying and occupancy costs                        | <u>364,729</u>  | <u>333,642</u>  |
| Gross profit  | 213,777   | 206,808   |
| Selling, general and administrative expenses                                    | 189,750   | 200,836   |
| Impairment losses   | <u>1,918</u>  | <u>6,866</u>  |
| Income (loss) from operations   | 22,109  | (894)   |
| Interest expense, net   | <u>36,918</u>   | <u>32,982</u>   |
| Loss before income taxes  | (14,809)  | (33,876)  |
| Provision for income taxes  | <u>1,421</u>  | <u>49</u>   |
| Net loss  | <u>\$ (16,230)</u>  | <u>\$ (33,925)</u>  |
| Other comprehensive income (loss):  |   |   |
| Reclassification of losses (gains) on cash flow hedges, net of tax, to earnings | (333)   | 996   |
| Unrealized gain (loss) on cash flow hedges, net of tax                          | (666)   | 2,418   |
| Foreign currency translation adjustments  | <u>48</u>   | <u>(331)</u>  |
| Comprehensive loss  | <u>\$ (17,181)</u>  | <u>\$ (30,842)</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<br>paid-in<br>capital | Accumulated<br>deficit | Accumulated<br>other<br>comprehensive<br>loss | Total<br>stockholders'<br>deficit |
|---|--------------|-------------|----------------------------------|------------------------|---|-----------------------------------|
|   | Shares       | Amount      |                                  |                        |   |                                   |
| <b>Balance at February 3, 2018</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  | —            | —           | —                                | (33,925)               | —   | (33,925)                          |
| Share-based compensation  | —            | —           | 46                               | —                      | —   | 46                                |
| Reclassification of realized losses on cash flow<br>hedges, net of tax, to earnings | —            | —           | —                                | —                      | 996   | 996                               |
| Unrealized gain on cash flow hedges   | —            | —           | —                                | —                      | 2,418   | 2,418                             |
| Foreign currency translation adjustments  | —            | —           | —                                | —                      | (331)   | (331)                             |
| <b>Balance at May 5, 2018</b>   | <u>1,000</u> | <u>\$ —</u> | <u>\$ 733,117</u>                | <u>\$(1,917,351)</u>   | <u>\$ 480</u>                                 | <u>\$(1,183,754)</u>              |
| <b>Balance at February 2, 2019</b>  | <u>1,000</u> | <u>\$ —</u> | <u>\$ 733,229</u>                | <u>\$(2,003,505)</u>   | <u>\$ (1,967)</u>                             | <u>\$(1,272,243)</u>              |
| Net loss  | —            | —           | —                                | (16,230)               | —   | (16,230)                          |
| Share-based compensation  | —            | —           | 4                                | —                      | —   | 4                                 |
| Reclassification of realized gains on cash flow<br>hedges, net of tax, to earnings  | —            | —           | —                                | —                      | (333)   | (333)                             |
| Unrealized loss on cash flow hedges   | —            | —           | —                                | —                      | (666)   | (666)                             |
| Foreign currency translation adjustments  | —            | —           | —                                | —                      | 48  | 48                                |
| <b>Balance at May 4, 2019</b>   | <u>1,000</u> | <u>\$ —</u> | <u>\$ 733,233</u>                | <u>\$(2,019,735)</u>   | <u>\$ (2,918)</u>                             | <u>\$(1,289,420)</u>              |

See notes to unaudited condensed consolidated financial statements.

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

|   | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 4, 2019</b> | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 5, 2018</b> |
|---|---|---|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |   |   |
| Net loss  | \$ (16,230)   | \$ (33,925)   |
| Adjustments to reconcile to cash flows from operating activities:                         |   |   |
| Depreciation of property and equipment  | 20,282  | 21,505  |
| Impairment losses   | 1,918   | 6,866   |
| Amortization of deferred financing costs and debt discount                                | 1,796   | 1,790   |
| Amortization of intangible assets   | 1,285   | 1,803   |
| Foreign currency transaction losses   | 20  | 30  |
| Share-based compensation  | 4   | 46  |
| Deferred income taxes   | (327)   | (991)   |
| Reclassification of hedging losses (gains) to earnings                                    | (333)   | 1,355   |
| Changes in operating assets and liabilities:  |   |   |
| Accounts receivable, net  | (16,102)  | (9,164)   |
| Merchandise inventories, net  | (27,584)  | (53,005)  |
| Prepaid expenses and other current assets   | 16,157  | 7,686   |
| Other assets  | (1,620)   | (1,668)   |
| Accounts payable and other  | (109,887)   | (43,913)  |
| Federal and state income taxes  | 2,624   | 563   |
| Net cash used in operating activities   | (127,997)   | (101,022)   |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |   |   |
| Capital expenditures  | (17,997)  | (7,179)   |
| Net cash used in investing activities   | (17,997)  | (7,179)   |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>  |   |   |
| Net borrowings under the ABL Facility   | 145,000   | 41,561  |
| Proceeds from Notes   | 1,003   | —   |
| Quarterly principal repayments of Term Loan Facility                                      | (3,917)   | (3,918)   |
| Net cash provided by financing activities   | 142,086   | 37,643  |
| Effect of changes in foreign exchange rates on cash, cash equivalents and restricted cash | (83)  | (470)   |
| Decrease in cash, cash equivalents and restricted cash                                    | (3,991)   | (71,028)  |
| Beginning balance   | 39,485  | 107,066   |
| Ending balance  | \$ 35,494   | \$ 36,038   |
| <b>Supplemental cash flow information:</b>  |   |   |
| Income taxes paid   | \$ 7  | \$ 9  |
| Interest paid   | \$ 50,301   | \$ 42,131   |

See notes to unaudited condensed consolidated financial statements.

**J.CREW GROUP, INC.**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**For the thirteen weeks ended May 4, 2019 and May 5, 2018**

**(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 2, 2019.

The Company’s fiscal year ends on the Saturday closest to January 31. All references to “fiscal 2019” represent the 52-week fiscal year that will end on February 1, 2020 and to “fiscal 2018” represent the 52-week fiscal year that ended February 2, 2019.

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) the date of receipt by a customer in the e-commerce business and (iii) the time ownership is transferred in the wholesale business.

### Disaggregation of Revenue

A summary of disaggregated revenue is as follows:

|                            | For the<br>Thirteen<br>Weeks Ended |                   |
|----------------------------|------------------------------------|-------------------|
|                            | May 4, 2019                        | May 5, 2018       |
| J.Crew                     | \$ 376,082                         | \$ 391,864        |
| Madewell                   | 132,894                            | 115,842           |
| Other revenues:            |                                    |                   |
| Wholesale                  | 59,301                             | 23,247            |
| Shipping and handling fees | 7,618                              | 7,321             |
| Other                      | 2,611                              | 2,176             |
| Total revenues             | <u>\$ 578,506</u>                  | <u>\$ 540,450</u> |

### Accounts Receivable

A summary of accounts receivable with respect to the Company's wholesale customers is as follows:

|                                      | May 4, 2019        | February 2,<br>2019         |
|--------------------------------------|--------------------|-----------------------------|
|                                      | <u>May 4, 2019</u> | <u>February 2,<br/>2019</u> |
| Accounts receivable                  | \$ 56,550          | \$ 40,439                   |
| Less allowance for doubtful accounts | (106)              | (97)                        |
| Accounts receivable, net             | <u>\$ 56,444</u>   | <u>\$ 40,342</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 the Company's 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:

|                                   | Unredeemed Gift Cards              |                  |
|-----------------------------------|------------------------------------|------------------|
|                                   | For the<br>Thirteen<br>Weeks Ended |                  |
|                                   | May 4, 2019                        | May 5, 2018      |
| Balance at beginning of period    | \$ 36,167                          | \$ 32,665        |
| Issuance of cards                 | 12,231                             | 13,220           |
| Redemption of cards               | (14,701)                           | (15,963)         |
| Recognition of estimated breakage | (810)                              | (921)            |
| Other                             | 75                                 | (119)            |
| Balance at end of period          | <u>\$ 32,962</u>                   | <u>\$ 28,882</u> |



|                                   | <b>Unredeemed Loyalty Program<br/>Rewards</b> |                    |
|-----------------------------------|---|--------------------|
|                                   | <b>For the<br/>Thirteen<br/>Weeks Ended</b>   |                    |
|                                   | <b>May 4, 2019</b>                            | <b>May 5, 2018</b> |
| Balance at beginning of period    | \$ 13,830                                     | \$ 8,422           |
| Earning of loyalty program points | 9,272   | 3,537              |
| Redemption of cards               | (5,433)                                       | (7,463)            |
| Recognition of estimated breakage | (2,269)                                       | (766)              |
| Other                             | (8)   | 184                |
| Balance at end of period          | <u>\$ 15,392</u>                              | <u>\$ 3,914</u>    |

### 3. Leases

#### *Overview*

The Company is party to various long-term operating lease agreements in connection with the leasing of its brick-and-mortar stores and its corporate offices. These operating leases expire on varying dates through 2034, with a portion of these leases containing options to renew for periods of up to 5 years. Generally, these leases contain standard provisions concerning the payment of rent, events of default and the rights and obligations of each party. Rent due under the leases is typically comprised of annual base rent plus a contingent rent payment based on the store's sales in excess of a specified threshold. Some of the leases also contain early termination options, which can be exercised by the Company or the landlord under certain conditions. The leases ordinarily require the Company to pay real estate taxes, insurance, certain utilities and common area costs.

#### *Accounting for Leases*

Historically, these operating leases were accounted for by expensing rent payments on a straight-line basis after consideration of rent holidays, step rent provisions and escalation clauses. Differences between rental expense, which was recognized from the date of possession, and actual rental payments were recorded as deferred rent and included in deferred credits. No liabilities were recognized on the balance sheet for long-term obligations pursuant to these lease agreements.

During the first quarter of fiscal 2019, however, the Company adopted pronouncements that were issued with respect to the accounting for leases. The pronouncements require lessees to recognize right-of-use lease assets ("ROU assets") and right-of-use lease liabilities ("ROU liabilities") for leases with terms of more than one year. The ROU liabilities are measured as the present value of the lease obligations. The ROU assets reflect the amount of the ROU liabilities less lease-related deferred credits. The Company used the effective date method whereby initial application occurred on the date of adoption with comparative periods unchanged.

Upon adoption of the new standard, the Company recorded a significant gross-up to the balance sheet, including ROU assets of \$533.5 million and ROU liabilities of \$624.6 million. The Company utilized the package of practical expedients permitted by the transition guidance, which allowed for a carryforward of its identification of leases, historical lease classification and initial direct costs for existing leases. The Company elected to use hindsight in determining lease term.

The new pronouncement requires a company to discount its ROU liabilities using implicit rates of return in the underlying leases. To the extent these rates of return cannot be readily determined, a company is permitted to use its incremental borrowing rate, which is required to be a collateralized rate for a period of time that corresponds to the remaining lease term.

A summary of the components of lease expense included in statement of operations is as follows:

|                      | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 4, 2019</b> |
|----------------------|---|
| Operating lease cost | \$ 39,410   |
| Variable lease cost  | 28,745  |
| Total lease cost     | <u>\$ 68,155</u>  |

As of May 4, 2019, the weighted-average remaining lease term was 7.7 years and the weighted-average discount rate was 8.93%. The Company paid \$39.0 million in the first quarter of fiscal 2019 for amounts included in the measurement of the ROU liabilities.

A reconciliation of undiscounted cash flows to the ROU liabilities is as follows:

| Fiscal year                        | Amount             |
|------------------------------------|--------------------|
| Remainder of 2019                  | \$ 98,801          |
| 2020                               | 138,057            |
| 2021                               | 125,758            |
| 2022                               | 112,467            |
| 2023                               | 84,260             |
| Thereafter                         | 325,514            |
| Total lease payments               | \$ 884,857         |
| Less: interest                     | (283,040)          |
| Present value of ROU liabilities   | \$ 601,817         |
|                                    | <b>May 4, 2019</b> |
| Current portion of ROU liabilities | \$ 114,052         |
| Long-term ROU liabilities          | 487,765            |
| Total ROU liabilities              | \$ 601,817         |

A summary of aggregate minimum rent at February 2, 2019 is as follows:

| Fiscal year | Amount     |
|-------------|------------|
| 2019        | \$ 146,282 |
| 2020        | 132,209    |
| 2021        | 121,330    |
| 2022        | 107,245    |
| 2023        | 78,925     |
| Thereafter  | 313,800    |
| Total       | \$ 899,791 |

#### 4. Debt Exchange and Refinancing

##### *Transaction Overview*

In the second quarter of fiscal 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”) (which aggregate liquidation preference was \$196,108,732 as of May 4, 2019); 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”);
- certain amendments to the indenture governing the PIK Notes;
- 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.

## 5. Management Services Agreement

Pursuant to a management services agreement (as amended and restated, the “Management Services Agreement”) entered into by the Parent, the Sponsors and the Company in connection with the Acquisition, and amended in the second quarter of fiscal 2017 in connection with the debt exchange and refinancing, the Parent provides the Company with certain ongoing consulting and management advisory services (the “Services”) and the Parent receives an aggregate annual monitoring fee prepaid quarterly in an amount equal to the greater of (i) 40 basis points of consolidated annual revenues or (ii) \$8 million (in either case, the “Advisory Fee”). The Parent also receives reimbursement for out-of-pocket expenses incurred in connection with services provided pursuant to the Management Services Agreement.

In addition to the amendment to the Management Services Agreement, in the second quarter of fiscal 2017 the Parent and Sponsors entered into a new management services agreement (the “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 New Management Services Agreement also provides for reimbursement for out-of-pocket expenses incurred by the Sponsors or their designees.

The Company recorded an expense of \$2.5 million in the first quarter of both fiscal 2019 and fiscal 2018 for monitoring fees and out-of-pocket expenses, included in selling, general and administrative expenses in the statements of operations and comprehensive loss.

## 6. Goodwill and Intangible Assets

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

|  | Favorable<br>Lease<br>Commitments | Madewell<br>Trade Name | Key Money         | J.Crew<br>Trade Name | Total               |
|--|-----------------------------------|------------------------|-------------------|----------------------|---------------------|
| Balance at February 2, 2019  | \$ 908                            | \$ 49,542              | \$ 752            | \$ 250,195           | \$ 301,397          |
| Amortization expense   | (227)                             | (1,025)                | (33)              | —                    | (1,285)             |
| Effect of changes in foreign exchange rates                        | —                                 | —                      | 5                 | —                    | 5                   |
| Balance at May 4, 2019   | <u>\$ 681</u>                     | <u>\$ 48,517</u>       | <u>\$ 724</u>     | <u>\$ 250,195</u>    | <u>\$ 300,117</u>   |
| Total accumulated amortization or impairment losses at May 4, 2019 | <u>\$ (60,329)</u>                | <u>\$ (33,483)</u>     | <u>\$ (4,093)</u> | <u>\$ (635,105)</u>  | <u>\$ (733,010)</u> |

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

|   | For the<br>Thirteen<br>Weeks Ended |                 |
|---|------------------------------------|-----------------|
|   | May 4, 2019                        | May 5, 2018     |
| Intangible asset related to the J.Crew trade name | \$ —                               | \$ —            |
| Long-lived assets (see note 10)                   | 1,918                              | 6,866           |
| Impairment losses                                 | <u>\$ 1,918</u>                    | <u>\$ 6,866</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. The carrying value of the J.Crew and Madewell trade names is \$250.2 million and \$48.5 million, respectively, at May 4, 2019. If revenues or operating results decline below the Company's current expectations, additional impairment charges may be recorded in the future.

## 7. Share-Based Compensation

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

The Parent adopted the Chinos Holdings, Inc. 2011 Equity Incentive Plan (the "2011 Plan") in connection with the Acquisition. In the second quarter of fiscal 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 then-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<br>Thirteen<br>Weeks Ended |             |
|--------------------------|------------------------------------|-------------|
|                          | May 4, 2019                        | May 5, 2018 |
| Share-based compensation | \$ 4                               | \$ 46       |

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 2, 2019 | 5,344,394                  | 20,000                        |
| Authorized                              | —                          | —                             |
| Granted                                 | (168,050)                  | —                             |
| Forfeited and available for reissuance  | 1,588,796                  | —                             |
| Available for grant at May 4, 2019      | <u>6,765,140</u>           | <u>20,000</u>                 |

## 8. Long-Term Debt and Credit Agreements

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

|                                   | <u>May 4, 2019</u>  | <u>February 2, 2019</u> |
|-----------------------------------|---------------------|-------------------------|
| Term Loan Facility                | \$ 1,369,792        | \$ 1,373,554            |
| Notes                             | 347,599             | 346,596                 |
| Less: current portion             | (32,070)            | (32,070)                |
| Less: deferred financing costs    | (9,141)             | (10,288)                |
| Less: discount                    | (4,014)             | (4,510)                 |
| Long-term debt, net               | <u>\$ 1,672,166</u> | <u>\$ 1,673,282</u>     |
| Borrowings under the ABL Facility | <u>\$ 215,800</u>   | <u>\$ 70,800</u>        |

### ABL Facility

The Company has an ABL Facility, which is governed by an asset-based credit agreement with Bank of America, N.A., as administrative agent, and the other agents and lenders party thereto, that, following the Sixth Amendment described below, provides for a \$375 million senior secured asset-based revolving line of credit (which may be increased by up to \$75 million in certain circumstances), subject to a borrowing base limitation. The Company cannot borrow in excess of \$375 million under the ABL Facility without the consent of holders of at least a majority of the loans outstanding under the Term Loan Facility. 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 September 19, 2018, the Company entered into a Sixth Amendment to Credit Agreement (Incremental Amendment) (the “Sixth Amendment”), which amended the ABL Facility to increase the revolving credit commitment from \$350 million to \$375 million, with the additional \$25 million provided by MUFG Union Bank, N.A., which joined the ABL Facility as an additional lender.

On May 4, 2019, standby letters of credit were \$64.5 million, outstanding borrowings were \$215.8 million, and excess availability, as defined, was \$94.7 million. The weighted average interest rate on the borrowings outstanding under the ABL Facility was 4.62% on May 4, 2019. Average short-term borrowings under the ABL Facility were \$196.4 million and \$30.5 million in the first quarter of fiscal 2019 and fiscal 2018, respectively.

### 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 May 4, 2019, outstanding documentary letters of credit were \$1.6 million and availability under this facility was \$18.4 million.

### Term Loan Facility

*2017 Amendment.* In the second quarter of fiscal 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 5.93% on May 4, 2019. 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 May 4, 2019.

*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.* In the second quarter of fiscal 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:

|  | For the<br>Thirteen<br>Weeks Ended |                  |
|--|------------------------------------|------------------|
|  | May 4, 2019                        | May 5, 2018      |
| Term Loan Facility   | \$ 21,130                          | \$ 18,383        |
| Notes  | 11,250                             | 11,264           |
| ABL Facility   | 2,361                              | 355              |
| Amortization of deferred financing costs and debt discount | 1,796                              | 1,790            |
| Realized hedging losses (gains)                            | (333)                              | 1,355            |
| Other interest, net of interest income                     | 714                                | (165)            |
| Interest expense, net                                      | <u>\$ 36,918</u>                   | <u>\$ 32,982</u> |

## 9. Derivative Financial Instruments

### *October 2018 Interest Rate Swap*

In October 2018, the Company entered into a floating-to-fixed interest rate swap agreement effective in March 2019 for a notional amount of \$750 million. This instrument limits exposure to interest rate increases on a portion of the Company's floating rate indebtedness through the expiration of the agreement in March 2020. Under the terms of this agreement, the Company's effective fixed interest rate on the notional amount of indebtedness is 3.03% plus the applicable margin.

### *August 2014 Interest Rate Swaps*

In August 2014, the Company entered into interest rate swap agreements that limited exposure to interest rate increases on a portion of the Company's floating rate indebtedness. The interest rate swap agreements covered an aggregate notional amount of \$800 million from March 2016 to March 2019 and carried 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 loss, while the ineffective portion of such gains or losses is recorded as a component of interest expense. Realized gains and losses in connection with each required interest payment are reclassified from accumulated other comprehensive 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). A summary of the recorded assets (liabilities) included in the condensed consolidated balance sheet is as follows:

|   | May 4, 2019       | February 2, 2019  |
|---|-------------------|-------------------|
| Interest rate swaps (included in other assets)      | \$ —              | \$ 480            |
| Interest rate swaps (included in other liabilities) | <u>\$ (3,973)</u> | <u>\$ (3,663)</u> |

## 10. 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 \$1,559 million and \$1,401 million at May 4, 2019 and February 2, 2019, 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 9 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 May 4, 2019 or February 2, 2019 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 6.

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:

|   | <b>For the<br/>Thirteen<br/>Weeks Ended</b> |                    |
|---|---|--------------------|
|   | <b>May 4, 2019</b>                          | <b>May 5, 2018</b> |
| Carrying value of long-term assets written down to fair value | <u>\$ 1,918</u>                             | <u>\$ 6,866</u>    |
| Impairment charge   | <u>\$ 1,918</u>                             | <u>\$ 6,866</u>    |

## **11. Income Taxes**

The Parent files a consolidated federal income tax return and state combined income tax returns, which include Group and all of its wholly owned subsidiaries. The income tax provision is calculated as if Group were a stand-alone taxpayer.

In the first quarter of fiscal 2019, the Company recorded a provision for income taxes of \$1.4 million on a pre-tax loss of \$14.8 million. The provision for income taxes reflects a charge for current federal and state tax liabilities and a discrete item of \$0.3 million related to state tax law changes. The Company's effective tax rate of (9.6)% differs from the U.S. federal statutory rate of 21% primarily related to current year pre-tax losses for which limited tax benefit was provided as the Company could not conclude that all of its deferred tax assets were realizable on a more-likely-than not basis. Other items impacting the provision for income taxes include the U.S. taxation of foreign earnings under the Global Intangible Low Tax Income ("GILTI") regime, the recognition of valuation allowances with respect to the carryforward of unutilized interest deductions, the recognition of international valuation allowances and lower rates in foreign tax jurisdictions.



In the first quarter of fiscal 2018, the Company recorded a provision for income taxes of \$49, which reflects a charge for the valuation allowance with respect to the deferred tax asset related to the carryforward of unutilized interest deductions. Other items impacting the provision for income taxes include the recognition of international valuation allowances, lower rates in foreign tax jurisdictions, and reserves for uncertain tax positions.

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 May 4, 2019, the Company maintained a full valuation allowance against its deferred tax assets.

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 for certain tax years ranging from 2014 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.

## 12. 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 May 4, 2019, 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 "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 Plaintiffs' claims for failure to state a claim and lack of standing, among other reasons. On September 7, 2017, 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 Plaintiffs' claims under the documents governing the Term Loan Facility. 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 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 Plaintiffs' claims with prejudice. 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.

On October 25, 2018, Highland Capital Management and certain affiliated funds were dismissed from the action with prejudice.

On November 21, 2018, the remaining Plaintiffs filed a limited appeal of the judge’s April 25, 2018 Memorandum Decision and Order with the First Department of the New York Appellate Division in an attempt to resuscitate their fraudulent conveyance claim. The Company filed an opposition brief on February 14, 2019, arguing that the trial court properly dismissed the fraudulent conveyance claim. On March 8, 2019, the remaining Plaintiffs filed a reply brief in support of their appeal. Oral argument on the appeal occurred on April 2, 2019. On April 25, 2019, the First Department unanimously affirmed the trial court’s decision to dismiss the fraudulent conveyance claim with prejudice.

Discovery in the action is ongoing. The Company believes that the remaining claim is wholly without merit, and intends to vigorously oppose the claim.

### 13. Workforce Reductions

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

|                                | For the<br>Thirteen<br>Weeks Ended |                 |
|--------------------------------|------------------------------------|-----------------|
|                                | May 4, 2019                        | May 5, 2018     |
| Balance at beginning of period | \$ 7,965                           | \$ 3,543        |
| Provisions charged to expense  | 2,543                              | 3,288           |
| Reversals                      | (107)                              | —               |
| Payments                       | (4,116)                            | (4,700)         |
| Balance at end of period       | <u>\$ 6,285</u>                    | <u>\$ 2,131</u> |

The Company expects the unpaid severance at May 4, 2019 to be paid through the third quarter of fiscal 2020.

### 14. Corporate Headquarters Relocation

In the second quarter of fiscal 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 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 former corporate headquarters by June 30, 2019, and expects to collect the termination payment in installments through such date. The Company records 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 \$277 million, net of free rent. The Company began 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.

### 15. Related Party Transactions

#### *Intellectual property license agreements*

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 IPCo and J.Crew Brand, LLC, wholly-owned subsidiaries of the Company (collectively, “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 May 4, 2019, J.Crew BrandCo had total assets of \$396.2 million, consisting of intangible assets of \$250.2 million, receivable due from OpCo of \$136.0 million, license fee receivable of \$9.8 million and cash and cash equivalents of \$0.2 million, and total liabilities of \$348.4 million related to the Notes. For the thirteen weeks ended May 4, 2019, IPCo earned royalty revenue of \$14.8 million. The Notes are guaranteed by the intangible assets of J.Crew BrandCo.

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

In the fourth quarter of fiscal 2013, the PIK Notes Issuer, which is an indirect parent holding company of Group, issued \$500 million of PIK Notes. As part of the debt exchange and 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 February 2, 2019, there were \$1.0 million in aggregate principal amount of PIK Notes outstanding, and in the first quarter of fiscal 2019 the Parent redeemed all remaining outstanding 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.

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 8.

*Due to Sponsors*

As part of the debt exchange and refinancing, the Sponsors purchased \$30.0 million principal amount of new term loans under the Term Loan Facility. As of May 4, 2019, the principal amount outstanding was \$31.6 million. For more information on the New Term Loan Borrowings, see note 8.

*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>May 4, 2019</u> | <u>February 2, 2019</u> |
|--|--------------------|-------------------------|
| Income taxes payable to Parent                   | \$ (48,648)        | \$ (48,648)             |
| Monitoring fees payable                          | (483)              | (1,938)                 |
| Transaction-related payments on behalf of Parent | 14,127             | 13,124                  |
| Due to Parent                                    | <u>\$ (35,004)</u> | <u>\$ (37,462)</u>      |

**16. Recent Accounting Pronouncements**

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 2018, a pronouncement was issued that modifies the disclosure requirements on fair value measurements. The pronouncement is effective for annual and interim periods in fiscal years beginning after December 15, 2019. 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, compromises to our data security, our ability to maintain the value of our brands and protect our trademarks, our ability to implement our real estate strategy, changes in demographic patterns, adverse or unseasonable weather or other interruptions in our foreign sourcing, customer call, order fulfillment or distribution operations, increases in the demand for or prices of raw materials used to manufacture our products, trade restrictions or disruptions and other factors which are set forth in the section entitled “Risk Factors” and elsewhere in our Annual Report on Form 10-K for the fiscal year ended February 2, 2019 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 2, 2019 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 generate approximately half of our net sales through our e-commerce business. We design our products, including those under the J.Crew® and Madewell® brands, to offer complete assortments of women's, men's and children's apparel and accessories.

We sell our J.Crew and Madewell merchandise through our retail and factory stores, our websites and select partners. As of May 4, 2019, we operated 196 J.Crew retail stores, 173 J.Crew factory stores (including 41 J.Crew Mercantile® stores) and 131 Madewell stores throughout the United States, Canada, the United Kingdom and Hong Kong; compared to 229 J.Crew retail stores, 175 J.Crew factory stores (including 42 J.Crew Mercantile stores) and 121 Madewell stores as of May 5, 2018. During fiscal 2019, we expect to open 10 Madewell stores and one J.Crew retail store and close approximately 20 stores.

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

| <i>(Dollars in millions)</i> | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 4, 2019</b> | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 5, 2018</b> |
|------------------------------|---|---|
| J.Crew                       | \$ 376.1  | \$ 391.9  |
| Madewell                     | 132.9   | 115.8   |
| Other(1)                     | 69.5  | 32.8  |
| Total revenues               | <u>\$ 578.5</u>   | <u>\$ 540.5</u>   |

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

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

- Revenues increased 7.0% to \$578.5 million, with comparable company sales up 1.3%.
- J.Crew revenues decreased 4.0% to \$376.1 million, with J.Crew comparable sales down 1.2%.
- Madewell revenues increased 14.7% to \$132.9 million, with Madewell comparable sales up 9.5%.
- Gross margin decreased to 37.0% from 38.3% last year.
- We opened two Madewell stores. 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 fiscal 2017 to be consistent with the fiscal 2018 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 2, 2019 filed with the SEC.

**Results of Operations – First Quarter of Fiscal 2019 compared to First Quarter of Fiscal 2018**

| <i>(Dollars in millions)</i>                 | For the<br>Thirteen<br>Weeks Ended<br>May 4, 2019 |                        | For the<br>Thirteen<br>Weeks Ended<br>May 5, 2018 |                        | Variance<br>Increase/(Decrease) |            |
|--|---|------------------------|---|------------------------|---------------------------------|------------|
|  | Amount  | Percent of<br>Revenues | Amount  | Percent of<br>Revenues | Dollars                         | Percentage |
| Revenues                                     | \$ 578.5  | 100.0%                 | \$ 540.5  | 100.0%                 | \$ 38.0                         | 7.0%       |
| Gross profit                                 | 213.8   | 37.0                   | 206.8   | 38.3                   | 7.0                             | 3.4        |
| Selling, general and administrative expenses | 189.8   | 32.8                   | 200.8   | 37.2                   | (11.0)                          | (5.5)      |
| Impairment losses                            | 1.9   | 0.3                    | 6.9   | 1.3                    | (5.0)                           | (72.1)     |
| Income (loss) from operations                | 22.1  | 3.8                    | (0.9)   | (0.2)                  | 23.0                            | NM         |
| Interest expense, net                        | 36.9  | 6.4                    | 33.0  | 6.1                    | 3.9                             | 11.9       |
| Provision for income taxes                   | 1.4   | 0.2                    | —   | —                      | 1.4                             | NM         |
| Net loss                                     | \$ (16.2)   | (2.8)%                 | \$ (33.9)   | (6.3)%                 | \$ 17.7                         | 52.2%      |

**Revenues**

Total revenues increased \$38.0 million, or 7.0%, to \$578.5 million in the first quarter of fiscal 2019 from \$540.5 million in the first quarter last year, driven primarily by an increase in revenue from wholesale customers. Comparable company sales increased 1.3% following an increase of 0.6% in the first quarter last year.

J.Crew sales decreased \$15.8 million, or 4.0%, to \$376.1 million in the first quarter of fiscal 2019 from \$391.9 million in the first quarter last year. J.Crew comparable sales decreased 1.2% following a decrease of 5.6% in the first quarter last year.

Madewell sales increased \$17.1 million, or 14.7%, to \$132.9 million in the first quarter of fiscal 2019 from \$115.8 million in the first quarter last year. Madewell comparable sales increased 9.5% following an increase of 30.9% in the first quarter last year.

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

|             | For the<br>Thirteen<br>Weeks Ended<br>May 4, 2019 | For the<br>Thirteen<br>Weeks Ended<br>May 5, 2018 |
|-------------|---|---|
| Apparel:    |   |   |
| Women's     | 60%   | 60%   |
| Men's       | 18  | 19  |
| Children's  | 6   | 7   |
| Accessories | 16  | 14  |
|             | <u>100%</u>                                       | <u>100%</u>                                       |

Other revenues increased \$36.7 million to \$69.5 million in the first quarter of fiscal 2019 from \$32.8 million in the first quarter last year, primarily a result of revenue from wholesale customers.

**Gross Profit**

Gross profit increased \$7.0 million to \$213.8 million in the first quarter of fiscal 2019 from \$206.8 million in the first quarter last year. This increase resulted from the following factors:

| <i>(Dollars in millions)</i>           | Increase/<br>(decrease) |
|--|-------------------------|
| Increase in revenues                   | \$ 20.2                 |
| Decrease in margin                     | (16.9)                  |
| Decrease in buying and occupancy costs | 3.7                     |
| Increase in gross profit               | \$ 7.0                  |

Gross margin decreased to 37.0% in the first quarter of fiscal 2019 from 38.3% in the first quarter last year. The decrease in gross margin was driven by: (i) a 290 basis point deterioration in margin primarily due to the dilutive effect of the planned inventory liquidation and increased penetration of our wholesale business, offset by (ii) a 160 basis point decrease in buying and occupancy costs as a percentage of revenues.

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

Selling, general and administrative expenses decreased \$11.0 million to \$189.8 million in the first quarter of fiscal 2019 from \$200.8 million in the first quarter last year. This decrease resulted from the following:

| <i>(Dollars in millions)</i>                                   | <b>Increase/<br/>(decrease)</b> |
|--|---------------------------------|
| Corporate occupancy actions                                    | \$ (5.4)                        |
| Decrease in operating and corporate expenses                   | (4.0)                           |
| Decrease in marketing costs                                    | (2.4)                           |
| Decrease in transformation costs                               | (2.1)                           |
| Increase in transaction costs                                  | 2.9                             |
| Total decrease in selling, general and administrative expenses | <u>\$ (11.0)</u>                |

As a percentage of revenues, selling, general and administrative expenses decreased to 32.8% in the first quarter of fiscal 2019 from 37.2% in the first quarter last year.

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

Interest expense, net of interest income, increased \$3.9 million to \$36.9 million in the first quarter of fiscal 2019 from \$33.0 million in the first quarter last year. A summary of interest expense is as follows:

| <i>(Dollars in millions)</i>                               | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 4, 2019</b> | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 5, 2018</b> |
|--|---|---|
| Term Loan Facility   | \$ 21.1   | \$ 18.4   |
| Notes  | 11.3  | 11.3  |
| ABL Facility   | 2.4   | 0.3   |
| Amortization of deferred financing costs and debt discount | 1.8   | 1.8   |
| Realized hedging losses (gains)                            | (0.3)   | 1.4   |
| Other, net of interest income                              | 0.6   | (0.2)   |
| Interest expense, net                                      | <u>\$ 36.9</u>  | <u>\$ 33.0</u>  |

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

In the first quarter of fiscal 2019, we recorded a provision for income taxes of \$1.4 million on a pre-tax loss of \$14.8 million. The provision for income taxes reflects a charge for current federal and state tax liabilities and a discrete item of \$0.3 million related to state tax law changes. Our effective tax rate of (9.6)% differs from the U.S. federal statutory rate of 21% primarily related to current year pre-tax losses for which limited tax benefit was provided as we could not conclude that all of its deferred tax assets were realizable on a more-likely-than not basis. Other items impacting the provision for income taxes include the U.S. taxation of foreign earnings under the Global Intangible Low Tax Income (“GILTI”) regime, the recognition of valuation allowances with respect to the carryforward of unutilized interest deductions, the recognition of international valuation allowances and lower rates in foreign tax jurisdictions.

In the first quarter of fiscal 2018, we recorded a provision for income taxes of \$49, which reflects a charge for the valuation allowance with respect to the deferred tax asset related to the carryforward of unutilized interest deductions. Other items impacting the provision for income taxes include the recognition of international valuation allowances, lower rates in foreign tax jurisdictions, and reserves for uncertain tax positions.

### Net Loss

Net loss decreased \$17.7 million to \$16.2 million in the first quarter of fiscal 2019 from \$33.9 million in the first quarter last year. This decrease was due to: (i) an increase in gross profit of \$7.0 million, (ii) a decrease in selling, general and administrative expenses of \$11.0 million and (iii) a decrease in impairment losses of \$5.0 million, offset by (iv) an increase in interest expense of \$3.9 million and (v) an increase in the provision for income taxes of \$1.4 million.

### Liquidity and Capital Resources

Our primary sources of liquidity are our current balances of cash and cash equivalents 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 corporate headquarters and (iii) funding working capital requirements. The most significant components of our working capital are cash and cash equivalents, merchandise inventories, accounts payable and other current liabilities. See “—Outlook” below.

### Operating Activities

| <i>(Dollars in millions)</i>                                      | For the<br>Thirteen<br>Weeks Ended<br>May 4, 2019 | For the<br>Thirteen<br>Weeks Ended<br>May 5, 2018 |
|---|---|---|
| Net loss  | \$ (16.2)   | \$ (33.9)   |
| Adjustments to reconcile to cash flows from operating activities: |   |   |
| Depreciation of property and equipment                            | 20.3  | 21.5  |
| Impairment losses   | 1.9   | 6.9   |
| Amortization of deferred financing costs and debt discount        | 1.8   | 1.8   |
| Amortization of intangible assets                                 | 1.3   | 1.8   |
| Deferred income taxes   | (0.3)   | (1.0)   |
| Reclassification of hedging losses (gains) to earnings            | (0.3)   | 1.4   |
| Changes in operating assets and liabilities                       | (136.5)   | (99.5)  |
| Net cash used in operating activities                             | <u>\$ (128.0)</u>                                 | <u>\$ (101.0)</u>                                 |

Cash used in operating activities of \$128.0 million in the first quarter of fiscal 2019 resulted from: (i) changes in operating assets and liabilities of \$136.5 million, primarily due to seasonal working capital fluctuations, and (ii) a net loss of \$16.2 million, partially offset by (iii) non-cash adjustments of \$24.7 million.

Cash used in operating activities of \$101.0 million in the first quarter of fiscal 2018 resulted from: (i) changes in operating assets and liabilities of \$99.5 million, primarily due to an increase in merchandise inventories as a result of an anticipated increase in revenues, and (ii) a net loss of \$33.9 million, partially offset by (iii) non-cash adjustments of \$32.4 million.

### Investing Activities

| <i>(Dollars in millions)</i>          | For the<br>Thirteen<br>Weeks Ended<br>May 4, 2019 | For the<br>Thirteen<br>Weeks Ended<br>May 5, 2018 |
|---------------------------------------|---|---|
| Capital expenditures:                 |   |   |
| Corporate headquarters relocation     | \$ (9.7)  | \$ —  |
| New stores and store improvements     | (4.3)   | (1.2)   |
| Information technology                | (3.8)   | (5.4)   |
| Other(1)                              | (0.2)   | (0.6)   |
| Net cash used in investing activities | <u>\$ (18.0)</u>                                  | <u>\$ (7.2)</u>                                   |

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

Capital expenditures are planned at approximately \$60 to \$70 million for fiscal year 2019, including approximately \$25 million for our corporate headquarters relocation, approximately \$20 million for information technology enhancements, approximately \$20 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<br/>Thirteen<br/>Weeks Ended<br/>May 4, 2019</b> | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 5, 2018</b> |
|--|---|---|
| Net borrowings under the ABL Facility                | \$ 145.0  | \$ 41.5   |
| Proceeds from Notes                                  | 1.0   | —   |
| Quarterly principal repayments of Term Loan Facility | (3.9)   | (3.9)   |
| Net cash provided by financing activities            | <u>\$ 142.1</u>   | <u>\$ 37.6</u>  |

Cash provided by financing activities of \$142.1 million in the first quarter of fiscal 2019 resulted primarily from: (i) net borrowings under the ABL Facility, offset by (ii) quarterly principal repayments of the Term Loan Facility.

Cash provided by financing activities of \$37.6 million in the first quarter of fiscal 2018 resulted from: (i) net borrowings under the ABL Facility, offset by (ii) quarterly principal repayments of the Term Loan Facility.

### Debt Exchange and Refinancing

In the second quarter of fiscal 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 (which aggregate liquidation preference was \$196,108,732 as of May 4, 2019); 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;
- certain amendments to the indenture governing the PIK Notes;
- 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 an asset-based credit agreement with Bank of America, N.A., as administrative agent, and the other agents and lenders party thereto, that, following the Sixth Amendment described below, provides for a \$375 million senior secured asset-based revolving line of credit (which may be increased by up to \$75 million in certain circumstances), subject to a borrowing base limitation. We cannot borrow in excess of \$375 million under the ABL Facility without the consent of holders of at least a majority of the loans outstanding under our Term Loan Facility. 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 September 19, 2018, we entered into a Sixth Amendment to Credit Agreement (Incremental Amendment) (the “Sixth Amendment”), which amended the ABL Facility to increase the revolving credit commitment from \$350 million to \$375 million, with the additional \$25 million provided by MUFG Union Bank, N.A., which joined the ABL Facility as an additional lender.

On May 4, 2019, standby letters of credit were \$64.5 million, outstanding borrowings were \$215.8 million, and excess availability, as defined, was \$94.7 million. The weighted average interest rate on the borrowings outstanding under the ABL Facility was 4.62% on May 4, 2019. Average short-term borrowings under the ABL Facility were \$196.4 million and \$30.5 million in the first quarter of fiscal 2019 and fiscal 2018, respectively.

As of the date of this report, there were outstanding borrowings of approximately \$198 million under the ABL Facility with excess availability of approximately \$113 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 May 4, 2019, outstanding documentary letters of credit were \$1.6 million and availability under this facility was \$18.4 million.

### Term Loan Facility

*2017 Amendment.* In the second quarter of fiscal 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 5.93% on May 4, 2019. 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 May 4, 2019.

*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.* In the second quarter of fiscal 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

In the fourth quarter of fiscal 2013, the PIK Notes Issuer, an indirect parent holding company of Group, issued \$500 million of PIK Notes. As part of the debt exchange and 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 February 2, 2019, there were \$1.0 million in aggregate principal amount of PIK Notes outstanding, and in the first quarter of fiscal 2019 the Parent redeemed all remaining outstanding 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.

### IP License Agreements

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 IPCo and J.Crew Brand, LLC, wholly-owned subsidiaries of the Company (collectively, "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 May 4, 2019, J.Crew BrandCo had total assets of \$396.2 million, consisting of intangible assets of \$250.2 million, receivable due from OpCo of \$136.0 million, license fee receivable of \$9.8 million and cash and cash equivalents of \$0.2 million, and total liabilities of \$348.4 million related to the Notes. For the thirteen weeks ended May 4, 2019, IPCo earned royalty revenue of \$14.8 million. 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 May 4, 2019.

|  | As of<br>May 4, 2019<br>(unaudited) |                                   |   |
|--|-------------------------------------|-----------------------------------|---|
|  | Consolidated<br>balance sheet       | Eliminations of<br>J.Crew BrandCo | Consolidated<br>balance sheet of<br>subsidiaries<br>excluding J.Crew<br>BrandCo |
| <b>ASSETS</b>  |                                     |                                   |   |
| Current assets:  |                                     |                                   |   |
| Cash and cash equivalents  | \$ 30,236                           | \$ (188)                          | \$ 30,048   |
| Restricted cash  | 5,258                               | —                                 | 5,258   |
| Accounts receivable, net   | 56,444                              | —                                 | 56,444  |
| Merchandise inventories, net   | 418,009                             | —                                 | 418,009   |
| Prepaid expenses and other current assets                                      | 68,739                              | —                                 | 68,739  |
| Refundable income taxes  | 5,772                               | —                                 | 5,772   |
| Total current assets   | <u>584,458</u>                      | <u>(188)</u>                      | <u>584,270</u>  |
| Property and equipment, net  | 239,478                             | —                                 | 239,478   |
| Right-of-use lease assets  | 513,037                             | —                                 | 513,037   |
| Intangible assets, net   | 300,117                             | (250,195)                         | 49,922  |
| Investment in subsidiary   | —                                   | 233,650                           | 233,650   |
| Goodwill   | 107,900                             | —                                 | 107,900   |
| Other assets   | 7,642                               | —                                 | 7,642   |
| Total assets   | <u>\$ 1,752,632</u>                 | <u>\$ (16,733)</u>                | <u>\$ 1,735,899</u>   |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>                                   |                                     |                                   |   |
| Current liabilities:   |                                     |                                   |   |
| Accounts payable   | \$ 224,700                          | \$ —                              | \$ 224,700  |
| Borrowings under the ABL Facility  | 215,800                             | —                                 | 215,800   |
| Other current liabilities  | 203,903                             | 9,833                             | 213,736   |
| Current portion of right-of-use lease liabilities                              | 114,052                             | —                                 | 114,052   |
| Due to Parent  | 35,004                              | —                                 | 35,004  |
| Interest payable   | 8,848                               | (5,632)                           | 3,216   |
| Current portion of long-term debt  | 32,070                              | —                                 | 32,070  |
| Total current liabilities  | <u>834,377</u>                      | <u>4,201</u>                      | <u>838,578</u>  |
| Long-term debt, net  | 1,672,166                           | (342,764)                         | 1,329,402   |
| Due to J.Crew BrandCo  | —                                   | 136,021                           | 136,021   |
| Long-term right-of-use lease liabilities                                       | 487,765                             | —                                 | 487,765   |
| Deferred income taxes, net   | 16,545                              | (16,545)                          | —   |
| Other liabilities  | 31,199                              | —                                 | 31,199  |
| Total liabilities  | <u>3,042,052</u>                    | <u>(219,087)</u>                  | <u>2,822,965</u>  |
| Stockholders' deficit:   |                                     |                                   |   |
| Common stock \$0.01 par value; 1,000 shares authorized, issued and outstanding | —                                   | —                                 | —   |
| Additional paid-in capital   | 733,233                             | 249,596                           | 982,829   |
| Accumulated other comprehensive loss   | (2,918)                             | —                                 | (2,918)   |
| Accumulated deficit  | (2,019,735)                         | (47,242)                          | (2,066,977)   |
| Total stockholders' deficit  | <u>(1,289,420)</u>                  | <u>202,354</u>                    | <u>(1,087,066)</u>  |
| Total liabilities and stockholders' deficit                                    | <u>\$ 1,752,632</u>                 | <u>\$ (16,733)</u>                | <u>\$ 1,735,899</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 weeks ended May 4, 2019.

|   | <b>For the<br/>Thirteen<br/>Weeks Ended<br/>May 4, 2019</b> |   |   |
|---|---|---|---|
|   | (unaudited)   |   |   |
| <b>Condensed Consolidated Statements of Operations and Comprehensive Loss</b> | <b>Consolidated</b>   | <b>Eliminations of<br/>J.Crew BrandCo</b> | <b>Consolidated<br/>subsidiaries<br/>excluding J.Crew<br/>BrandCo</b> |
| Revenues:   |   |   |   |
| Net sales   | \$ 508,976  | \$ —                                      | \$ 508,976  |
| Other   | 69,530  | —   | 69,530  |
| Total revenues  | <u>578,506</u>  | <u>—</u>                                  | <u>578,506</u>  |
| Cost of goods sold, including buying and occupancy costs                      | 364,729   | —   | 364,729   |
| Royalty expense   | —   | 14,750                                    | 14,750  |
| Gross profit  | 213,777   | (14,750)                                  | 199,027   |
| Selling, general and administrative expenses                                  | 189,750   | (61)                                      | 189,689   |
| Impairment losses   | 1,918   | —   | 1,918   |
| Income from operations  | 22,109  | (14,689)                                  | 7,420   |
| Interest expense, net of interest income                                      | 36,918  | (11,758)                                  | 25,160  |
| Loss before income taxes  | (14,809)  | (2,931)                                   | (17,740)  |
| Provision for income taxes  | 1,421   | —   | 1,421   |
| Net loss  | <u>\$ (16,230)</u>  | <u>\$ (2,931)</u>                         | <u>\$ (19,161)</u>  |
| Other comprehensive income (loss):  |   |   |   |
| Reclassification of gains on cash flow hedges, net of tax, to earnings        | (333)   | —   | (333)   |
| Unrealized loss on cash flow hedges, net of tax                               | (666)   | —   | (666)   |
| Foreign currency translation adjustments                                      | 48  | —   | 48  |
| Comprehensive loss  | <u>\$ (17,181)</u>  | <u>\$ (2,931)</u>                         | <u>\$ (20,112)</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 2019 will be approximately \$60 to \$70 million, including approximately \$25 million for our corporate headquarters relocation, approximately \$20 million for information technology enhancements, approximately \$20 million for new stores and store improvements, and the remainder for warehouse improvements and general corporate purposes. Management expects to pay interest of approximately \$145 million in fiscal 2019 to fund debt service obligations. During fiscal 2019, we expect to open 10 Madewell stores and one J.Crew retail store and close approximately 20 stores.

Management believes that our current balances of cash and cash equivalents, projected cash flows from operating, investing and financing activities 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. During the first quarter of fiscal 2019, we, in consultation with our legal and financial advisors, announced that we are actively exploring strategic alternatives to maximize the value of the Company, including a potential initial public offering of our Madewell business.

### **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 May 4, 2019, we had the following obligations under letters of credit in future periods:

| <b>Letters of Credit</b> | <b>Total</b>   | <b>Within 1 Year</b> | <b>2-3 Years</b>             | <b>4-5 Years</b> | <b>After 5 Years</b> |
|--------------------------|----------------|----------------------|------------------------------|------------------|----------------------|
|                          |                |                      | <i>(Dollars in millions)</i> |                  |                      |
| Standby                  | \$ 64.5        | \$ 64.4              | \$ 0.1                       | \$ —             | \$ —                 |
| Documentary              | 1.6            | 1.6                  | —                            | —                | —                    |
|                          | <u>\$ 66.1</u> | <u>\$ 66.0</u>       | <u>\$ 0.1</u>                | <u>\$ —</u>      | <u>\$ —</u>          |

### **Cyclical 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 in 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 2, 2019 filed with the SEC.

During the first quarter of fiscal 2019, we adopted pronouncements that were issued with respect to the accounting for leases. The pronouncements require lessees to recognize right-of-use lease assets ("ROU assets") and right-of-use lease liabilities ("ROU liabilities") for leases with terms of more than one year. The ROU liabilities are measured as the present value of the lease obligations. The ROU assets reflect the amount of the ROU liabilities less lease-related deferred credits. We used the effective date method whereby initial application occurred on the date of adoption with comparative periods unchanged. Additionally, we utilized the package of practical expedients permitted by the transition guidance, which allowed for a carryforward of our identification of leases, historical lease classification and initial direct costs for existing leases. See note 3 to our unaudited condensed consolidated financial statements included in this report for more information regarding our accounting for leases.

## **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. In October 2018, we entered into an interest rate swap agreement which covers a notional amount of \$750 million from March 2019 to March 2020. Under the terms of this agreement, our effective fixed interest rate on the notional amount of indebtedness is 3.03% plus the applicable margin.

In August 2014, we entered into interest rate swap agreements that covered 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 was 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 approximately \$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 May 4, 2019, 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 “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 Plaintiffs’ claims for failure to state a claim and lack of standing, among other reasons. On September 7, 2017, 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 Plaintiffs’ claims under the documents governing the Term Loan Facility. 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 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 Plaintiffs’ claims with prejudice. 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.

On October 25, 2018, Highland Capital Management and certain affiliated funds were dismissed from the action with prejudice.

On November 21, 2018, the remaining Plaintiffs filed a limited appeal of the judge’s April 25, 2018 Memorandum Decision and Order with the First Department of the New York Appellate Division in an attempt to resuscitate their fraudulent conveyance claim. We filed an opposition brief on February 14, 2019, arguing that the trial court properly dismissed the fraudulent conveyance claim. On March 8, 2019, the remaining Plaintiffs filed a reply brief in support of their appeal. Oral argument on the appeal occurred on April 2, 2019. On April 25, 2019, the First Department unanimously affirmed the trial court’s decision to dismiss the fraudulent conveyance claim with prejudice.

Discovery in the action is ongoing. We believe that the remaining 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 2, 2019 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*

| Exhibit No. | Document  |
|-------------|---|
| 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>                      |

### *Material Contracts*

| Exhibit No. | Document  |
|-------------|---|
| 10.1        | <a href="#">J.Crew Group, Inc. 2019 Special Bonus Plan*</a> |

### *Certifications*

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

### *Interactive Data Files*

| Exhibit No. | Document  |
|-------------|---|
| 101         | Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Condensed Consolidated Balance Sheets at May 4, 2019 and February 2, 2019, (ii) the Condensed Consolidated Statements of Operations and Comprehensive Loss for the thirteen weeks ended May 4, 2019 and May 5, 2018, (iii) the Condensed Consolidated Statements of Changes in Stockholders' Deficit for the thirteen weeks ended May 4, 2019 and May 5, 2018, (iv) the Condensed Consolidated Statements of Cash Flows for the thirteen weeks ended May 4, 2019 and May 5, 2018, and (v) the Notes to Unaudited Condensed Consolidated Financial Statements.* |

\* Filed herewith.

\*\* Furnished herewith.



**J. CREW GROUP, INC.**  
**2019 SPECIAL BONUS PLAN**

**Section 1. Purpose**

The purpose of the Special Bonus Plan (the “Plan”) is to promote the interests of J. Crew Group, Inc. and its subsidiaries (the “Company”) by providing select associates of the Company with employment retention incentives.

**Section 2. Administration**

(a) The Plan shall be administered by the Compensation Committee (the “Committee”) of the Board of Directors of the Company.

(b) The Committee may, subject to the provisions of the Plan, establish, adopt or revise rules and regulations relating to the Plan or take such actions as it deems necessary or advisable for the proper administration of the Plan. The Committee shall have the authority to interpret the Plan in its absolute discretion. Each interpretation made or action taken by the Committee pursuant to the Plan shall be final and conclusive for all purposes and binding upon all Participants (as defined in Section 3) or former Participants and their successors in interest. The Committee may request advice or assistance or employ such persons (including, without limitation, legal counsel and accountants) as it deems necessary for the proper administration of the Plan.

(c) Neither the Committee nor any member of the Committee shall be liable for any act, omission, interpretation, construction or determination in connection with the Plan made in good faith, except for willful misconduct or as expressly provided by statute, and the members of the Committee shall be entitled to indemnification and reimbursement by the Company in respect of any claim, loss, damage or expense (including, without limitation, reasonable attorneys’ fees) arising or resulting therefrom to the fullest extent permitted by law.

**Section 3. Eligibility**

Awards may be granted only to associates of the Company who are selected for participation in the Plan by the Committee. A qualifying associate selected by the Committee to participate in the Plan shall be a “Participant” in the Plan. Participation in the Plan shall be in addition to participation, if any, in the Company’s Annual Incentive Plan.

**Section 4. Special Bonus and Payment**

(a) The maximum aggregate amount available for payment as Bonus Amounts hereunder shall be five million dollars (\$5 million).

(b) Each Participant shall be eligible to receive the grant of a special bonus equal to a percentage of such Participant’s base salary, as determined by the Committee in its sole discretion. Except as otherwise provided in the Award, such amount shall be earned in two equal installments on each of the last day of the Company’s fiscal year within which the Grant Date occurs, and the date that is the last day of the sixth month of the subsequent fiscal year following

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the Grant Date, provided that with respect to each installment, the Participant remains in continued employment with the Company from the Grant Date through the applicable date each installment is earned (each a "Vesting Date").

(c) Unless otherwise provided in the Award, payments of Bonus Amounts under this Plan shall be paid to the Participant as soon as reasonably practicable following the applicable Vesting Date, and in no event later than 30 days thereafter.

## Section 5. Definitions

As used herein, the following terms shall have the meanings set forth below:

- (a) "*Award*" means the grant of a special bonus pursuant to the terms of the Plan.
- (b) "*Bonus Amount*" means the amount payable in respect of an Award, in accordance with Section 4(b) herein.
- (c) "*Code*" means the U.S. Internal Revenue Code of 1986, as amended.
- (d) "*Grant Date*" shall have the meaning set forth in the Participant's Award.

## Section 6. Miscellaneous Provisions

(a) **No Rights to Awards or Continued Employment.** No associate of the Company shall have any claim or right to receive Awards under the Plan. Neither the Plan nor any action taken under the Plan shall be construed as giving any associate any right to be retained by the Company in any capacity.

(b) **No Limits on Other Awards and Plans.** Nothing contained in this Plan shall prohibit the Company from establishing other special awards or incentive compensation plans providing for the payment of incentive compensation to associates of the Company, including any Participants.

(c) **Withholding Taxes.** The Company shall deduct from all payments and distributions under the Plan any required federal, state or local governments tax withholdings.

(d) **Unfunded Status of Plan.** The Company shall not have any obligation to establish any separate fund or trust or other segregation of assets to provide for payments under the Plan. To the extent any person acquires any rights to receive payments hereunder from the Company, such rights shall be no greater than those of an unsecured creditor.

(e) **Effective Date; Amendment.** The Plan is effective as of April 11, 2019. The Committee may at any time and from time to time alter, amend, suspend or terminate the Plan in whole or in part.

(f) **Governing Law.** The Plan and the rights of all persons under the Plan shall be construed and administered in accordance with the laws of the State of New York without regard to its conflict of law principles.

(g) **Code Section 409A.** Each Award is intended not to be subject to Section 409A of the Code (“Section 409A”) by reason of being a short-term deferral and shall be interpreted accordingly. In the event any of the compensation or benefits provided to a Participant pursuant to this Plan would result in a violation of Section 409A (including any regulations promulgated thereunder), the Company will use its reasonable best efforts to amend the Plan in the least restrictive manner necessary in order, where applicable (i) to ensure that such compensation is not considered “nonqualified deferred compensation” for purposes of Section 409A, or (ii) to comply with the provisions of Section 409A, in each case, where possible, without any diminution in the value of the compensation or benefits to be paid or provided to the Participant pursuant to this Agreement; provided, however, that nothing in this Agreement shall require the Company to provide any gross-up or other tax reimbursement to a Participant in connection with any violation of Section 409A or otherwise.

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

I, Michael J. Nicholson, 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: May 29, 2019

/s/ Michael J. Nicholson

**Michael J. Nicholson**  
**Interim Chief Executive Officer**  
**(Principal 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: May 29, 2019

\_\_\_\_\_  
/s/ Vincent Zanna  
Vincent Zanna  
Chief Financial Officer and Treasurer  
(Principal Financial Officer)



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

In connection with the quarterly report of J.Crew Group, Inc. (the "Company") on Form 10-Q for the period ended May 4, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, Michael J. Nicholson, Interim 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: May 29, 2019

/s/ Michael J. Nicholson

**Michael J. Nicholson**  
**Interim Chief Executive Officer**  
**(Principal Executive Officer)**

/s/ Vincent Zanna

**Vincent Zanna**  
**Chief Financial Officer**  
**(Principal 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.*