TOO INC
Form 10-Q
September 14, 2001

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

FORM 10-Q

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

For the quarterly period ended August 4, 2001

OR

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

For the transition period from to

Commission file number 1-14987

TOO, INC.
(Exact name of registrant as specified in its charter)

Delaware	31-1333930
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3885 Morse Road, Columbus, OH	43219
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (614) 479-3500

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 (or such shorter time as the Company became effective).

Yes X 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 September 13, 2001
$.01 Par Value	31,041,877 Shares

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TOO, INC.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

TOO, INC.
CONSOLIDATED STATEMENTS OF INCOME
(unaudited, in thousands except per share amounts)

	Thirteen Weeks Ended	
	August 4, 2001	July 29, 2000
Net sales	$125,468	$108,315
Costs of goods sold, buying and occupancy costs	84,494	73,584

Gross income	40,974	34,731	
General, administrative and store operating expenses	35,720	31,133	
Operating income	5,254	3,598	
Interest expense, net	377	477	
Income before income taxes	4,877	3,121	
Provision for income taxes	2,000	1,200	
Net income	$ 2,877	$ 1,921	
Earnings per share:			
Basic	$ 0.09	$ 0.06	
Diluted	$ 0.09	$ 0.06	
Weighted average common shares:			
Basic	30,938	30,736	
Diluted	32,006	31,818	

The accompanying notes are an integral part of these consolidated financial statements.

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TOO, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands)

	August 4, 2001 (unaudited)	
ASSETS		
Current Assets:		
Cash and equivalents	$ 40,343	
Receivables	3,278	
Inventories	51,877	
Store supplies	9,254	
Deferred income taxes	2,978	
Other	825	
Total current assets	108,555	
Property and equipment, net	95,030	
Deferred income taxes	11,174	
Other assets	999	

TOTAL ASSETS	$ 215,758
LIABILITIES AND SHAREHOLDERS' EQUITY	
Current Liabilities:	
Current portion long-term debt	$ 10,000
Accounts payable	29,715
Accrued expenses	34,437
Income taxes payable	6,818
Total current liabilities	80,970
Long-term debt	40,000
Other long-term liabilities	4,683
Commitments and contingencies	
SHAREHOLDERS' EQUITY	
Preferred stock, 50 million shares authorized	-
Common stock, $.01 par value, 100 million shares authorized, 31.0 million and 30.8 million issued and outstanding, respectively	310
Paid in capital	30,108
Retained earnings	59,687
Total shareholders' equity	90,105
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 215,758

The accompanying notes are an integral part of these consolidated financial statements.

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TOO, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

	Twenty-Six Week
	August 4, 2001
Cash flows from operating activities:	
Net income	$ 6,692
Impact of other operating activities on cash flows:	
Depreciation and amortization	8,852
Changes in assets and liabilities:	
Inventories	(6,162)
Accounts payable and accrued expenses	2,937
Income taxes	(7,317)
Other assets	2
Other liabilities	802

Net cash provided by (used for) operating activities	5,806
Investing activities:	
Capital expenditures	(23,552)
Net cash used for investing activities	(23,552)
Financing activities:	
Stock options, restricted stock and other equity changes	3,301
Net cash provided by financing activities	3,301
Net decrease in cash and equivalents	(14,445)
Cash and equivalents, beginning of period	54,788
Cash and equivalents, end of period	$ 40,343

The accompanying notes are an integral part of these consolidated financial statements.

TOO, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

1. BASIS OF PRESENTATION

Too, Inc. (referred to herein as "the Company") is a specialty retailer that sells apparel, underwear, sleepwear, swimwear, lifestyle and personal care products for fashion-aware, trend-setting young girls ages seven to fourteen years. The consolidated financial statements include the accounts of Too, Inc. and its wholly owned subsidiaries and reflect the Company's assets, liabilities, results of operations and cash flows on a historical cost basis.

The accompanying unaudited interim consolidated financial statements as of August 4, 2001 and for the thirteen and twenty-six week periods ended August 4, 2001 and July 29, 2000, are presented to comply with the rules and regulations of the Securities and Exchange Commission. Accordingly, these consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's 2000 Annual Report on Form 10-K. In the opinion of management, the accompanying interim consolidated financial statements reflect all adjustments (which are of a normal, recurring nature) necessary to present fairly the financial position, results of operations and cash flows for the interim periods, but are not necessarily indicative of the results of operations for a full fiscal year.

The consolidated financial statements as of August 4, 2001, and for the thirteen and twenty-six weeks ended August 4, 2001 and July 29, 2000

included herein have been reviewed by the independent public accounting firm of PricewaterhouseCoopers LLP and the report of such firm follows the notes to consolidated financial statements. PricewaterhouseCoopers LLP is not subject to the liability provisions of Section 11 of the Securities Act of 1933 for its report on the consolidated financial statements because that report is not a "report" within the meaning of Sections 7 and 11 of that Act.

2. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if stock options or restricted stock were converted to common stock using the treasury stock method.

The following table shows the amounts used in the computation of basic and diluted earnings per share (in thousands):

	Thirteen Weeks Ended		Twe
	August 4, 2001	July 29, 2000	August 4 2001
Net income	$ 2,877	$ 1,921	$ 6
Weighted average common shares - basic	30,938	30,736	30
Dilutive effect of stock options and restricted stock	1,068	1,082	
Weighted average common shares - diluted	32,006	31,818	31

Due to the options' price exceeding the average market price of the common shares for the reporting periods, certain options were excluded from the calculation of net income per diluted share. In Fiscal 2001, options to purchase 185,000 and 215,000 common shares, were not included in the computation of net income per diluted share for the thirteen and twenty-six week periods ended August 4, 2001, respectively. In Fiscal 2000, options to purchase 124,000 common shares, were not included in the computation of net income per diluted share for both the thirteen and twenty-six week periods ended July 29, 2000.

3. INVENTORIES

The fiscal year of the Company is comprised of two principal selling seasons: Spring (the first and second quarters) and Fall (the third and fourth quarters). Inventories are principally valued at the lower of average cost or market, on a first-in, first-out basis utilizing the retail method. Inventory valuation at the end of the first and third quarters reflects adjustments for inventory markdowns and shrinkage estimates for the total selling season.

4. PROPERTY AND EQUIPMENT, NET

Property and equipment, at cost, consisted of (in thousands):

	August 4, 2001	February 3, 2001
Land	$ 7,691	$ 7,69
Furniture, fixtures and equipment	97,816	93,88
Leasehold improvements	41,644	42,52
Construction-in-progress	21,487	3,64
Total	168,638	147,74
Less: accumulated depreciation and amortization	(73,608)	(66,55
Property and equipment, net	$ 95,030	$ $ 81,18

5. RELATIONSHIP WITH THE LIMITED

In connection with the Spin-off, the Company entered into a service agreement with Limited Logistics Services (formerly known as Limited Distribution Services), a wholly owned subsidiary of The Limited, to provide distribution services to us covering flow of merchandise from factory to our stores for up to three years after the August 23, 1999 Spin-off. Most of the merchandise and related materials for the Company's stores are shipped to a distribution center owned by The Limited in Columbus, Ohio, where the merchandise is received, inspected, allocated and packed for shipment to stores. Under the service agreement, The Limited distributes merchandise and related materials using common and contract carriers to the Company's stores. Inbound freight is charged to Too based upon actual receipts and related charges, while outbound freight is charged based on a percentage of cartons shipped.

Our main office is owned by Distribution Land Corp., a wholly owned subsidiary of the Limited, and leased to us with a lease term expiring in August 2002.

Our largest apparel supplier has been Mast Industries, Inc., a wholly owned subsidiary of The Limited. Mast Industries supplied approximately 30% of the apparel that we purchased in 2000. We believe that all transactions that we have entered into with Mast Industries have been on terms that would have been obtained on an arm's length basis since we treat them as if they were a third party. We were not, and will not be, obligated to continue to source products through Mast Industries.

Amounts payable to The Limited, including merchandise payables to Mast Industries, approximated $12.5 million at August 4, 2001.

6. CREDIT FACILITY

During August 1999, the Company entered into a five-year $100 million credit agreement (the "Credit Facility") with a syndicate of banks. The Credit Facility is collateralized by virtually all assets of the Company

and is comprised of a $50 million five-year term loan and a $50 million revolving loan commitment. The entire amount of the term portion was drawn in order to fund a $50 million dividend to The Limited and $14 million was drawn under the revolving loan commitment principally to repay a portion of working capital advances made by the Limited prior to the Spin-off.

The $50 million revolving loan commitment is available to fund working capital requirements and for general corporate purposes. Interest on borrowings under the Credit Facility is based on matrix pricing applied to either the London Interbank Offered Rate or Prime, as defined in the agreement. Payments of principal under the term loan are due at various dates from July 2002 to August 2004. A commitment fee based on matrix pricing is charged on the unused portion of the revolving loan commitment. The commitment fee is up to 1/2 of 1% of the unused revolving credit commitment per annum. Under the terms of the Credit Facility, the Company is required to comply with certain covenants including financial ratios. The Credit Facility limits the Company from incurring certain additional indebtedness and restricts substantial asset sales, capital expenditures above approved limits and cash dividends. The Company is in compliance with all applicable terms of the Credit Facility. As of August 4, 2001, there were no amounts outstanding under the revolving portion of the Credit Facility.

Current maturities of long-term debt for each of the next three fiscal years are $17.5 million in 2002, $20.0 million in 2003, and $12.5 million in 2004.

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Interest expense, including the amortization of financing fees, amounted to $1,015,000 for the quarter ending August 4, 2001. Interest expense was partially offset by interest income of $638,000 for the quarter. Interest expense and interest income amounted to $1,245,000 and $768,000, respectively, for the quarter ending July 29, 2000. For the twenty-six periods ended August 4, 2001 and July 29, 2000, interest expense amounted to $2,067,000 and $2,479,000 and interest income amounted to $1,558,000 and $1,630,000, respectively.

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REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and
Shareholders of Too, Inc.:

We have reviewed the accompanying consolidated balance sheet of Too, Inc. and its subsidiaries (the "Company") as of August 4, 2001, and the related consolidated statements of income for each of the thirteen and twenty-six week periods ended August 4, 2001 and July 29, 2000 and the consolidated statements of cash flows for the twenty-six week periods ended August 4, 2001 and July 29, 2000. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole.

Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited in accordance with auditing standards generally accepted in the United States of America, the consolidated balance sheet as of February 3, 2001, and the related consolidated statements of income, shareholders' equity, and of cash flows for the year then ended (not presented herein), and in our report dated February 21, 2001 we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet information as of February 3, 2001 is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Columbus, Ohio
August 15, 2001

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Item 2. Management's Discussion and Analysis of Results of Operations and Financial Condition

Results of Operations

Net sales for the thirteen weeks ended August 4, 2001 were $125.5 million, an increase of 16% from $108.3 million for the comparable period of 2000. Gross income increased 18% to $41.0 million from $34.7 million in 2000 and operating income rose 47% to $5.3 million from $3.6 million in 2000. Net income increased 52% to $2.9 million from $1.9 million in 2000. Diluted earnings per share increased to $.09, a 50% increase, versus diluted earnings per share of $.06 in 2000.

Net sales for the twenty-six weeks ended August 4, 2001 were $262.1 million, an increase of 15% from $227.1 million for the comparable period of 2000. Gross income increased 16% to $85.9 million from $74.2 million in 2000 and operating income rose 27% to $11.7 million from $9.2 million in 2000. Net income increased 31% to $6.7 million from $5.1 million in 2000. Diluted earnings per share increased to $.21, a 31% increase, versus diluted earnings per share of $.16 in 2000.

FINANCIAL SUMMARY

The following summarized financial and statistical data compares the thirteen and twenty-six week periods ended August 4, 2001, to the comparable 2000 period:

	Thirteen Weeks Ended			Twe
	August 4, 2001	July 29, 2000	Percent Change	August 4, 2001
Net sales (millions)	$125.5	$108.3	16%	$262.

Comparable store sales performance/(1)/	0%	9%		-
Retail sales per average square foot/(2)/	$ 73	$ 71	3%	$ 15
Retail gross square feet at end of quarter (thousands)	1,725	1,529	13%	
Stores with "Girl Power" format	176	116		
Percentage of stores in "Girl Power" format	42%	31%		
Number of Stores:				
Beginning of period	413	359		40
Opened	9	14		1
Closed	-	-		(
End of period	422	373		42

/(1)/ A store is included in our comparable store sales calculation once it has completed 52 weeks of operation. Further, stores that are expanded more than 20% in square feet are treated as new stores for purposes of this calculation. Fiscal 2001 comparable store sales are reported on a calendar-shifted basis.

/(2)/ Retail sales per average square foot is the result of dividing net sales for the fiscal quarter by average gross square feet, which reflects the impact of opening and closing stores throughout the quarter.

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Net Sales

Net sales for the second quarter of 2001 increased 16% to $125.5 million from $108.3 million in 2000. Comparable store sales were flat at 0% for the second quarter 2001 compared to a 9% increase during second quarter 2000. Net sales benefited from a 13% increase in square footage growth over last year and a nearly $1 million increase in net sales coming through the catalog and web channels.

Merchandise categories displaying solid sales increases were cut-and-sewn casual tops, active shorts and add-on, driven primarily by cami bras, footwear, and lifestyle products. Personal care and the ready-to-wear categories continued to struggle.

Gross Income

Gross income, expressed as a percentage of net sales, was 32.7% for the second quarter of 2001, an increase of 60 basis points from a gross income rate of 32.1% for the second quarter of 2000. This rate increase was due to higher merchandise margin. The increase in merchandise margin was due to higher initial mark-ups, and a lower markdown rate. These increases more than offset an increase in catalog costs, which are included in buying and occupancy costs.

For the year-to-date period, the gross income rate increased 10 basis points to

32.8% from 32.7% in 2000. Higher initial mark-ups more than offset an increase in the markdown rate and increased catalog costs.

General, Administrative and Store Operating Expenses

General, administrative and store operating expense, expressed as a percentage of net sales, decreased 20 basis points to 28.5% in the second quarter of 2001 from 28.7% for the same period in 2000. On a year-to-date basis general, administrative and store operating expense decreased by 30 basis points to 28.3% in 2001 from 28.6% in 2000. The decrease during the quarter and year-to-date periods was due to lower home office expenses and lower distribution center costs, expressed as a percentage of net sales, which were partially offset by slightly higher store operating and marketing expenses.

Operating Income

Operating income, expressed as a percentage of net sales, was 4.2 % in the second quarter of 2001 from 3.3% for the same period in 2000, resulting in a 90 basis point increase. Year-to-date operating income increased to 4.5% in 2001 compared to 4.1% in 2000. The increase in operating income, expressed as a percentage of net sales, for both the quarter and year-to-date periods was due to higher merchandise margins and lower home office and distribution center expenses, expressed as a percentage of net sales.

Net Interest Expense

Net interest expense amounted to $377,000 and $509,000 for the quarter and year-to-date periods ending August 4, 2001, respectively. Net interest expense in the comparable periods in 2000 amounted to $477,000 and $849,000, respectively. Interest expense, including the amortization of financing fees, amounted to $1,015,000 and $2,067,000 for the quarter and year-to-date periods ending August 4, 2001, respectively. Interest expense was partially offset by interest income of $638,000 and $1,558,000 for the quarter and year-to-date periods, respectively. Interest income was earned on money market instruments.

Income Taxes

Income tax expense, provided at an approximate rate of 40%, amounted to $2.0 million and $4.5 million for the quarter ending and year-to-date periods ending August 4, 2001, respectively, compared to $1.2 million and $3.3 million for the comparable

periods ending July 29, 2000. We anticipate that the annual effective tax rate will remain unchanged for the balance of fiscal 2001.

FINANCIAL CONDITION

Liquidity and Capital Resources

Cash provided from operating activities provides the resources to support operations, including projected growth, seasonal working capital requirements and capital expenditures.

Net cash provided by operating activities amounted to $5.8 million for the twenty-six weeks ending August 4, 2001 versus net cash used by operating activities of $11.8 million for the same period in 2000. The increase in net cash provided by operating activities versus the comparable period in 2000 was due to an increase in net income, a smaller increase in year-on-year inventories, including improved leveraging of accounts payable, and a year-on-

year reduction of accounts receivable.

Investing activities represented capital expenditures, which were primarily for new and remodeled stores, as well as progress payments on the construction of our new home office and distribution center.

Financing activities principally represented proceeds from employee stock option exercises and the issuance of restricted stock.

A summary of our working capital position and capitalization follows (thousands).

	August 4, 2001	February 3, 2001
Working capital	$ 27,585	$ 40,762
Capitalization:		
Long-term debt	40,000	50,000
Shareholders' equity	90,105	79,711
Total capitalization	$ 130,105	$ 129,711
Amounts authorized under revolving portion of credit facility	$ 50,000	$ 50,000

In August 1999, we entered into a five-year, $100 million collateralized Credit Facility. The Credit Facility consists of a $50 million five-year term loan and a $50 million, five-year annual revolving credit commitment. The Credit Facility's interest rates, which reflect matrix pricing, are based on the London Interbank Offered Rate or Prime plus a spread as defined in the agreement. The term loan is interest only until the end of the third year at which time the amortization of the outstanding principle balance will begin. The decrease in long-term debt is due to the classification of a $10 million payment due in July 2002 as a current liability. The Credit Facility contains customary representations and warranties as well as certain affirmative, negative and financial covenants.

No amounts were borrowed against the $50 million revolving credit commitment during the twenty-six weeks ended August 4, 2001.

Capital Expenditures

Capital expenditures totaled $23.6 million for the twenty-six weeks ended August 4, 2001 compared to $17.1 million for the comparable period of 2000. 2001 capital expenditures were $9.0 million for new and remodeled stores, $11.4 million for the new distribution center and $3.2 million for the new home office and other items. We anticipate spending approximately $70 to $72 million in 2001 for capital expenditures including the construction of approximately 55 new stores, the remodel of 6 existing stores and 7 stores for our new concept, mishmash, along with $48 to $51 million for our new Home Office and Distribution Center facilities. Our store expansion and remodel program should add

approximately 220,000 to 236,000 gross square feet during 2001, representing a 13% to 14% increase over year-end 2000. The Company expects that capital expenditures will be funded principally by net cash provided by operating activities.

Recently Issued Accounting Pronouncements

EITF Issue No. 00-14, "Accounting for Certain Sales Incentives," will be effective in the first quarter of 2002 and addresses the accounting for, and classification of, various sales incentives. The Company has determined that adopting the provisions of this EITF Issue will not have a material impact on its consolidated financial statements.

Statement of Financial Accounting Standards ("SFAS") No. 143, Accounting for Asset Retirement Obligations will be effective in the first quarter of 2003. The standard requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the entity capitalizes a cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss upon settlement. Because costs associated with exiting leased properties at the end of the lease terms are minimal, the Company believes that when the statement is adopted, it will not have a significant effect on the Company's results of operations or its financial position.

Safe Harbor Statement Under The Private Securities Litigation Reform Act of 1995

The Company cautions that any forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995) contained in this Management's Discussion and Analysis or made by management of the Company involve risks and uncertainties and are subject to change based on various important factors, many of which may be beyond the Company's control. Forward-looking statements are indicated by words such as "anticipate," "estimate," "expect," "intend," "risk," "could," "may," "will," "pro forma," "likely," "possible," "potential," and similar words and phrases and the negative forms and variations of these words and phrases, and include statements in this Management's Discussion and Analysis relating to anticipated capital expenditures in 2001 for new stores and the remodeling or expansion of existing stores, and the related funding. The following factors, among others, in some cases have affected, and in the future could affect, the Company's financial performance and actual results and could cause future performance and financial results to differ materially from those expressed or implied in any forward-looking statements included in this Management's Discussion and Analysis or otherwise made by management: changes in consumer spending patterns, consumer preferences and overall economic conditions; the impact of competition and pricing; changes in weather patterns; currency and exchange risks; changes in existing or potential trade restrictions, duties, tariffs or quotas; changes in political or financial stability; changes in postal rates and charges and paper and printing costs; availability of suitable store locations at appropriate terms; ability to develop new merchandise; ability to hire and train associates; and/or other risk factors that may be described in the Risk Factors section of the Company's Form 10, filed August 18, 1999, as well as other filings with the Securities and Exchange Commission. Future economic and industry trends that could potentially impact revenue and profitability are difficult to predict. Therefore, there can be no assurance that the forward-looking statements included herein will prove to be accurate. In light of the significant uncertainties in the forward-looking statements included herein, the inclusion of such information should not be regarded a representation by the Company, or any other person, that the objectives of the Company will be

achieved. The forward-looking statements made herein are based on information presently available to the management of the Company. The Company assumes no obligation to publicly update or revise its forward-looking statements even if experience or future changes make it clear that any projected results expressed or implied therein will not be realized.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

Not applicable.

Item 4. Matters Submitted to a Vote of Security Holders

Not applicable.

Item 6. Exhibits

(a) Exhibits

15 Letter re: Unaudited Interim Financial Information to Securities and Exchange Commission re: Incorporation of Report of Independent Accountants.

(b) Reports on Form 8-K

On August 14, 2001, the Company filed a current report on Form 8-K that reported the Board's adoption of the Rights Agreement (also known as a stockholders rights plan) contained therein.

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TOO, INC.
(Registrant)

By /s/ Kent A. Kleeberger

Kent A. Kleeberger,
Executive Vice President - Chief Financial Officer,
Logistics and Systems
Secretary and Treasurer
(duly authorized officer and Principal Financial and Accounting Officer)

Date: September 14, 2001

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EXHIBIT INDEX

Exhibit No.	Document
15	Letter re: Unaudited Interim Financial Information to Securities and Exchange Commission re: Incorporation of Report of Independent Accountants.