bebe stores, inc.
Form 10-Q
February 10, 2017

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 December 31, 2016
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File Number 0-24395

bebe stores, inc.
(Exact name of registrant as specified in its charter)

California	94-2450490
(State or Jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

400 Valley Drive
Brisbane, California 94005
(Address of principal executive offices)
Telephone: (415) 715-3900

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 x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined Rule12b-2 of the Exchange Act). Yes ¨ No x

Table of Contents

The number of shares of the registrant's common stock, par value $0.001 per share, outstanding as of January 31, 2017 was 8,066,805.

Table of Contents

bebe stores, inc.

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. Condensed Consolidated Financial Statements

bebe stores, inc.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)
(unaudited)

	As of December 31, 2016	As of July 2, 2016	As of January 2, 2016
Assets:			
Current assets:			
Cash and equivalents	$66,792	$55,525	$43,372
Available for sale securities	—	—	5,070
Receivables	8,411	8,502	6,055
Inventories, net	23,250	28,736	28,282
Prepaid and other	5,166	10,498	14,665
Total current assets	103,619	103,261	97,444
Available for sale securities	—	—	5,166
Property and equipment, net	62,585	72,623	83,306
Other assets	2,681	3,561	3,673
Total assets	$168,885	$179,445	$189,589
Liabilities and Shareholders’ Equity:			
Current liabilities:			
Accounts payable	$12,987	$11,263	$14,760
Accrued liabilities and other	24,027	21,510	25,407
Total current liabilities	37,014	32,773	40,167
Deferred rent and other lease incentives	15,977	17,983	20,741
Uncertain tax positions	86	85	83
Total liabilities	53,077	50,841	60,991
Commitments and contingencies			
Shareholders’ equity:			
Preferred stock-authorized 1,000,000 shares at $0.001 par value per share; no shares issued and outstanding	—	—	—
Common stock-authorized 14,000,000 shares at $0.001 par value per share; issued and outstanding 8,067,174; 8,005,116 and 8,002,444 shares	8	8	8
Additional paid-in capital	147,966	147,585	147,001
Accumulated other comprehensive income (loss)	561	728	(3,577)
Retained earnings (accumulated deficit)	(32,727)	(19,717)	(14,834)
Total shareholders’ equity	115,808	128,604	128,598
Total liabilities and shareholders’ equity	$168,885	$179,445	$189,589

See accompanying notes to condensed consolidated financial statements.

3

Table of Contents

bebe stores, inc.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(In thousands, except per share data)
(unaudited)

	Three Months Ended		Six Months Ended	
	December 31, 2016	January 2, 2016	December 31, 2016	January 2, 2016
Net sales	$101,931	$122,447	$189,169	$218,730
Cost of sales, including production and occupancy	66,903	80,767	126,647	149,188
Gross margin	35,028	41,680	62,522	69,542
Selling, general and administrative expenses	41,399	47,116	77,119	92,006
Operating loss	(6,371)	(5,436)	(14,597)	(22,464)
Interest and other income (loss), net	121	8	136	(79)
Loss from operations, before income taxes	(6,250)	(5,428)	(14,461)	(22,543)
Income tax provision (benefit)	10	30	27	57
Earnings in equity method investment	$1,029	$—	$1,479	$—
Net loss	$(5,231)	$(5,458)	$(13,009)	$(22,600)
Net Loss per share amounts:				
Basic	$(0.65)	$(0.68)	$(1.62)	$(2.83)
Diluted	$(0.65)	$(0.68)	$(1.62)	$(2.83)
Basic weighted average shares outstanding	8,040	7,989	8,023	7,981
Diluted weighted average shares outstanding	8,040	7,989	8,023	7,981
Other comprehensive income (loss)				
Unrealized loss on available for sale securities	$—	$(124)	$—	$(75)
Foreign currency translation adjustments	(101)	(678)	(168)	(1,726)
Other comprehensive income (loss)	(101)	(802)	(168)	(1,801)
Comprehensive loss	$(5,332)	$(6,260)	$(13,177)	$(24,401)

See accompanying notes to condensed consolidated financial statements.

Table of Contents

bebe stores, inc.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(unaudited)

	Six Months Ended	
	December 31, 2016	January 2, 2016
Cash flows from operating activities:		
Net loss	$(13,009)	$(22,600)
Adjustments to reconcile net loss to cash used by operating activities:		
Stock compensation expense	602	1,421
Depreciation and amortization	8,527	10,302
Non-cash charge for asset impairment	2,673	3,493
Earnings in equity method investment	(1,479)	—
Cash receipt from equity method investment	1,850	—
Other	(259)	130
Changes in operating assets and liabilities:		
Receivables	91	1,058
Inventories	5,470	2,980
Prepaid expenses and other	5,796	(3,687)
Accounts payable	1,607	2,365
Deferred rent and other lease incentives	(1,542)	(3,082)
Accrued liabilities	2,755	(2,110)
Net cash provided (used) by operating activities	13,082	(9,730)
Cash flows from investing activities:		
Purchase of property and equipment and store construction deposits	(1,723)	(5,134)
Proceeds from sales of investment securities	—	11,411
Net cash provided (used) by investing activities	(1,723)	6,277
Cash flows from financing activities:		
Proceeds from issuance of common stock	2	8
Net cash provided (used) by financing activities	2	8
Net decrease in cash and equivalents	11,361	(3,445)
Effect of exchange rate changes on cash	(94)	(130)
Cash and equivalents:		
Beginning of period	55,525	46,947
End of period	$66,792	$43,372

See accompanying notes to condensed consolidated financial statements.

Table of Contents

bebe stores, inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
INTERIM FINANCIAL STATEMENTS
The accompanying condensed consolidated balance sheets of bebe stores, inc. (the "Company") as of December 31, 2016 and January 2, 2016, the condensed consolidated statements of operations and comprehensive loss for the three and six months ended December 31, 2016 and January 2, 2016 and the condensed consolidated statements of cash flows for the six months ended December 31, 2016 and January 2, 2016 have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X, without audit. Accordingly, they do not include all of the information required by accounting principles generally accepted in the United States of America for annual financial statements. Therefore, these condensed consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the fiscal year ended July 2, 2016.
In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary to present fairly the financial position at the balance sheet dates and the results of operations for the periods presented have been included. The condensed consolidated balance sheet at July 2, 2016, presented herein, was derived from the audited balance sheet included in the Company's Annual Report on Form 10-K for the fiscal year ended July 2, 2016.
The Company's business is affected by the pattern of seasonality common to most retail apparel businesses. The results for the periods presented are not necessarily indicative of future financial results.

The Company has incurred net losses and cash used in operating activities in fiscal 2016, 2015 and 2014. Cash and equivalents were $55.5 million as of July 2, 2016. During the six months ended December 31, 2016, net loss was $13.0 million however the Company generated net cash from operating activities totaling $13.1 million. As a result, cash and equivalents were $66.8 million as of December 31, 2016.

The Company used, $38.6 million, $25.0 million and $30.3 million net of cash in operating activities in the fiscal years 2016, 2015 and 2014 respectively. The Company's liquidity is dependent upon its ability to generate cash from operations along with usage of existing cash and cash equivalents. The strategic focus for the remainder of fiscal 2017 is to close unprofitable stores or negotiate rent reductions for stores with kickout rights or where the store lease is up for renewal. In addition, the Company continues to limit the size of the investment in inventory and capital expenditures. The Company is also expecting significant savings in selling, general and administrative expenses as compared with the prior year from the corporate restructuring activities which occurred in fiscal 2016 including headcount reductions. The Company believes its cash and equivalents, together with cash flows from operations, will be sufficient to meet its operating and capital requirements for at least the next twelve months. Future operating and capital requirements, however, will depend on numerous factors, including without limitation, investment costs for management information systems, potential investments and/or licensing arrangements, and future results of operations. The inability to generate positive cash flow from operations could have a material adverse effect on the Company's business and financial conditions.
FISCAL YEAR
The Company's fiscal year is a 52 or 53 week period, each period ending on the first Saturday on or after June 30. Fiscal years 2017 and 2016 both include 52 weeks.
The three month periods ended December 31, 2016 and January 2, 2016 each include 13 weeks. The six month periods ended December 31, 2016 and January 2, 2016 each included 26 weeks.
The Company's business is affected by the pattern of seasonality common to most retail apparel businesses. The results for the periods presented are not necessarily indicative of future financial results.
RECENT ACCOUNTING PRONOUNCEMENTS

Stock Compensation
In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-09, "Compensation - Stock Compensation (Topic 718)", which is part of the FASB's Simplification

Initiative. The updated guidance simplifies the accounting for share-based payment transactions. The amended guidance is effective for fiscal

Table of Contents

years, and interim periods within those years, beginning with fiscal 2018, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this standard on its consolidated financial statements.

Leases

In February 2016 the FASB issued ASU 2016-02, "Leases". This standard requires lessees to put most leases on their balance sheets as a right-to-use asset and a lease liability, but to continue to recognize expenses in the statements of operations in a manner similar to current accounting. The Company will adopt this standard at the beginning of fiscal year 2020 and is currently assessing the impact to the consolidated financial statements, but due to the number of leases the Company has, adoption of the standard will result in an increase in long-term assets and liabilities.

Revenue Recognition

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers", or ASU 2014-09, which states that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve this, an entity will need to: identify the contract with a customer; identify the separate performance obligations in the contract; determine the transaction price; allocate the transaction price to the separate performance obligation in the contract; and recognize revenue when (or as) the entity satisfies each performance obligation. ASU No. 2014-09 will be effective beginning with fiscal year 2019. The Company is currently assessing its approach to the adoption of this standard and the impact on the results of operations and financial position.

Inventory

In July 2015, the FASB issued ASU No. 2015-11, "Simplifying the Measurement of Inventory". The new standard amends the guidelines for the measurement of inventory from lower of cost or market to the lower of cost and net realizable value (NRV). NRV is defined as the estimated selling prices in the ordinary course of business less reasonably predictable costs of completion, disposal and transportation. Under existing standards, inventory is measured at lower of cost or market, which requires the consideration of replacement cost, NRV and NRV less an amount that approximates a normal profit margin. This ASU eliminates the requirement to determine and consider replacement cost or NRV less an approximately normal profit margin for inventory measurement. The new standard is effective prospectively at the beginning of fiscal year 2018. The Company is currently evaluating the impact, if any, of adopting this new accounting guidance on its results of operations and financial position.

INVESTMENTS

As of December 31, 2016, the Company held no investments in auction rate securities nor any other marketable securities. As of January 2, 2016, the Company’s investment portfolio consisted of certificates of deposit and auction rate securities. The Company held short term available for sale securities totaling $5.1 million as of January 2, 2016, that consisted entirely of certificates of deposit at cost which approximates fair value. The Company also held long term available for sale securities at fair value totaling $5.2 million as of January 2, 2016, that consisted entirely of interest bearing auction rate securities (“ARS”).

The Company held interest bearing ARS consisting of federally insured student loan backed securities. As of January 2, 2016, the Company’s ARS portfolio totaled approximately $9.0 million and was classified as available for sale securities, net of a temporary impairment charge of $3.8 million. As of that date, the Company’s ARS portfolio consisted of approximately 22% A rated investments and 78% CCC rated investments. The Company's ARS were sold during the third quarter of fiscal 2016.

The valuation of the Company’s investment portfolio is subject to uncertainties that are difficult to predict. Factors that may impact its valuation include changes to credit ratings of the securities as well as to the underlying assets supporting those securities, rates of default of the underlying assets, underlying collateral value, discount rates and ongoing strength and quality of market credit and liquidity.

The following is a summary of the Company's available for sale securities:

Table of Contents

	As of January 2, 2016			
	Cost	Unrealized Losses Less Than 12 Months	Unrealized Losses 12 Months or Greater	Estimated Fair Value
	(In thousands)			
Short term certificates of deposit	$5,070	$ —	$ —	$ 5,070
Long term auction rate securities	$9,000	$ —	$ 3,834	$ 5,166

FAIR VALUE MEASUREMENTS

The FASB has established a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

As of December 31, 2016, the Company held financial instruments that are measured at fair value on a recurring basis. These included cash equivalents consisting of money market funds.

The Company determined the estimated fair value of its investment in ARS by reviewing trading activity for similar securities in secondary markets as well as by using a discounted cash flow model. The assumptions used in preparing the discounted cash flow model include estimates for liquidity (average of LIBOR +6.09%), interest rates (weighted average of 0.2%), timing (range from 9 – 13 years), credit ratings and amount of cash flows and expected holding periods of the ARS and recent trading activity in the secondary marketplace.

The following items are measured at fair value on a recurring basis as of December 31, 2016:

Description	December 31, 2016	Using Quoted Prices in Active&