A strategic marketing and financial analysis of Toys R Us

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ABSTRACT
The following is a strategic marketing and financial analysis concerning the highly dynamic operations of Toys R Us.

Microsoft account
May 6, 2016
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Toys “R” Us proves to have more than its popular misspelled name going for it. The company has had almost consistent success since it was founded around 1960. With a history of providing popular children’s toys, Toys “R” Us has also been able stand out amongst competition by providing the most up to date toys, a large variety of toys, and locations that attract customers from all over the world. Toys “R” Us has many groups within the company that work to keep it at its popular status amongst toys stores. Whether it is working with its partners or operational planning team, Toys “R” Us proves that building relationships is one of the major keys to running a successful business. Its unique hiring process provides stores with exceptionally great employees. Additionally, Toys “R” Us has a retail strategy that has been clearly thought out and implemented. Through many different aspects, this brand shows to be a great representation of how good retail strategies can make a company a success.

The store name “Children’s Bargain Town” does not have the same ring that Toys “R” Us does; however, this bland brand name is how the popular children’s toy store started off. Charles Lazarus, the man who established the company, started off with the idea of providing a store for parents’ to get all of their child’s wants and needs. This store received the well-known title of Toys “R” Us about 10 years after the “Children's Bargain Town” was founded in 1948, in Washington, D.C. In 1960, Lazarus added the well-known giraffe mascot, Geoffrey, to the store’s image. By 1978, the store had expanded to many different locations and was considered to be well established and a huge success amongst children’s stores.

In the beginning, Toys “R” Us claimed to follow a supermarket format. In 1996, there was $270 million dollars invested into the company for major renovations. There were 25 stores shut down, McDonald’s restaurants added to the stores, and a lot of remodeling to make the brand’s locations become part of the superstore craze that was going on at the time.

Today, there are many different types of Toys “R” Us stores globally. Some stores have adopted the supermarket model format, which allows the consumers to physically pick out the products at their convenience and pay for them at a register area. In 2006, Toys “R” Us adopted an integrated store
strategy which combined Toys”R”Us and Babies”R”Us under one roof. In order to provide the customers a one-stop shop, the company has converted approximately 25 percent of its wholly owned global store base to a side-by-side format that brings the company’s toy and juvenile product offerings together. The side-by-side format originated in Canada and is now present in 15 global markets. Since the execution of the new store strategy, Toys “R” Us has updated many existing locations with renovations to the interior and exterior. It has also allowed the company to relocate older stores to new markets where they will be in the center of retail activity in those select areas.

Toys “R” Us’ target market is children under the age of five and then from five to twelve years old with their wide selection of toys. Lazarus believed that success meant focusing on the everyday shopper, such as a parent searching for the perfect birthday gift or a child hoping to spend his or her weekly allowance. Not only is their target market aimed towards children, but also to the parents of these children, which are the ones who ultimately buy the products. Toys “R” Us provide all the necessities that parents need from clothing for their children, to toys, to furniture, etc.

With the increasing popularity in e-commerce, Toys “R” Us launched their online site in 1998, Toysrus.com, becoming the fastest growing sites in the toy and baby products shopping category. Today, it is one of the most frequently visited sites in the specialty toy and baby products retail category offering a wide assortment of toys for children of all ages. Their site also offers exclusives, helpful services, and everyday deals. Babiesrus.com also offers a wide selections of baby products and supplies, as well as a premier baby registry. Positioning the global franchise for the future, Toys “R” Us became a private company in 2005. An investment group of affiliates of Bain Capital Partners LLC, Kohlberg Kravis Roberts & Co. (KKR) and Vornado Realty Trust completed the acquisition of Toys “R” Us, Inc. for $6.6 billion. Since then, Toys “R” Us has further strengthened their position in the market in many ways. They are growing their line of exclusive brands, such as their line of baby essentials under Babies “R” Us which was easily identified by its distinctive purple and white Babies “R” Us logo in 2009. Their exclusive line offers parents
and gift-givers a wide range of infant and toddler care products. The Babies “R” Us brand now includes more than 1,600 affordable, high-quality products such as formula, diapers, wipes, etc. Toys “R” Us opened its first outlet store, Toys “R” Us Express, in 2009, with several pop-up stores nationwide in malls and other shopping centers. The company continues to increase its presence in malls and shopping centers during holiday season, making it easier for consumers to access it. Due to high popularity of the smaller format stores, in 2010 Toys “R” Us began opening permanent outlet locations all across the country. Lastly, Toys “R” Us, in efforts to create a seamless in-store and online shopping experience for their customers, now has enhanced omnichannel offerings that include Buy Online, Pickup in Store, Ship to Store, Ship from Store and Pay in Store, a robust e-commerce site, mobile shopping platform, social networking sites and a vast network of stores across the country. Toys “R” Us has made it easier than ever for its consumers to shop with them when they want, how they want, and whenever they want which is the ultimate advantage for the company. By dominating this industry (biggest competitor Kay Bee Toys folded in 2009, as discussed in the financial analysis section), they have perhaps created the biggest competitive advantage of all by being one the last remaining providers.

To appeal to the target market, big name retailers such as Toys “R” Us implement a variety of retail strategies. These tactics include but are not limited to logistics, optimal pricing, ideal location, and store design/layout.

Toys “R” Us carries very few different product categories. However, as their name suggests, they specialize in toys for children. Despite their lack of merchandise breadth, Toys “R” Us offers an extremely deep assortment of toys. Upon arrival to the website or a store location, Toys “R” Us displays their updated featured brands by gender. Their current featured boys’ toys are Hot Wheels, Minecraft, LEGO, Star Wars, Transformers, and Teenage Mutant Ninja Turtles. Their current featured girls’ toys are Disney Frozen, Barbie, Disney Princess, My Little Pony, Monster High, and Doc McStuffins. Aside from their
featured brands, Toys “R” Us offers a multitude of other toys for children such as action figures, arts &
crafts, bikes & scooters, building blocks, cooking, dolls, electronics, vehicles, and video games.

Although Toys “R” Us is known for being a product retailer, some of their stores contain attractions
that can be considered a service. For example, their flagship store in New York City’s Time Square is home
to a giant robotic T-Rex, a life-size Barbie dollhouse, and even an entire city built of LEGO's. According to
Zagat’s U.S. Family Travel Guide, Toys “R” Us in Times Square is one of the top family and tourist
destination spots in New York City. The draw of these attractions aid the retailing side of the company
tremendously.

Toys “R” Us has more than 570 stores in the United States. Internationally, they have 745 stores
including more than 250 licensed stores in 38 countries outside of the United States. Toys “R” Us has
always been strategic when picking store locations in order to optimize retailing. The company is aware
that they need to reach parents of children, especially during the holiday season. The most effective way
to achieve this goal is to place store locations in malls and shopping centers alongside other specialty
stores. This way, busy shoppers can conveniently access the stores they need to without having to face
the restrictions of traffic and lack of variety. Toys “R” Us also has an online store at the utmost
convenience for the shopper including delivery or in-store pickup options.

Big name retailers like Toys “R” Us do not always need promotional mixes to succeed since they can
just rest on their laurels. However, Toys “R” Us is never complacent and aims to grow as a company by
drawing in new customers. The retailer offers coupons and newspaper inserts containing many deals on
products to attract shoppers. Combined with their paper deals, Toys “R” Us also offers in-store
promotions and sales. Furthermore, the company website lists access to all of their former press releases
within the last 10 years.
Due to Toys “R” Us’ popularity and loyal consumers, they have very little competition in the toy industry. Thus, Toys “R” Us has some freedom when it comes to pricing their products and can usually markup accordingly. Their ability to offer in-store presentation greatly helps their retailing ability. On the other hand, massive online retailers like Amazon keep Toys “R” Us’ prices reasonable and modest. Competition is good for the market because it effectively eliminates monopolies and allows the consumers to be the ultimate decision makers.

Toys “R” Us works very carefully with their partners to make sure they are in sync throughout the supply chain. They have their own planning and allocation group that focuses on establishing a more logical flow of product and tying that flow back into supply-chain capacity. Toys “R” Us also has an operational planning team that is mostly supply-chain oriented. This team works across the organization to ensure that the needs of the consumers are met all the while making sure the strategies implemented accommodate for the logistics physical capacity to handle the product. Toys “R” Us orders products from manufacturers like Hasbro and Mattel and then directly sells them to consumers through their stores or website.

Toys “R” Us is comprised of 66,000 employees that all endured a very similar and standard hiring process. According to glassdoor.com, Toys “R” Us favors group interviews that involve team building exercises. If the interviewee can succeed in group work, then they are asked to come back for an individual interview. These one on one interviews allow the interviewers to see how the interviewee responds to certain questions and scenarios without the aid of a group. Clearly, Toys “R” Us believes in teamwork and its ability to grow the business through their sales associates.

Toys “R” Us uses a common buying system to help them manage their stock. Thanks to this system they can keep track of inventory and become aware when it is time to restock certain products with exactly how many units. As previously stated, Toys “R” Us buys products directly from the toy
manufacturers like Hasbro and Mattel. After buying products from the manufacturers, they can restock their shelves so they can sell the products to the consumers.

In this section of the analysis, I reached out to regional financial investment firm Hilliard Lyons to assist with the collection of financial data for the past four years for both Toys-R-Us and competitive firms/industry leaders. This information supplemented statistics found from sec.gov. Much of the collected information and charts can be found in the appendices following this discussion. Toys “R” Us falls into the Consumer Discretionary sector of the financial world. The following information can be found in chart form the Appendix. The most recent fiscal year with full disclosure of performance (2014) concluded on January 31, 2015. I will begin the discussion by starting with the 2011 fiscal year and then chronologically move to 2014 by the end. The following information may be located in Appendix A.

In the 2011 fiscal year, net sales totaled $13.909 billion while cost of goods sold came to $8.939 billion. Given this, one can see the gross profit as $4.970 billion. In order to arrive at the gross margin percentage, simply take the gross profit and divide it by the company’s net sales for that fiscal year. By doing this, we see that Toys “R” Us achieved a gross margin of 35.73% in the 2011 fiscal year. In the expenses, often referred to as SGA (sales and general/administrative), Toys “R” Us incurred $4.029 billion dollars’ worth of expenses. All of this gave the company a net profit of $151 million. The number of stores in the beginning of the 2011 fiscal year was 1392 and they ended the fiscal year with 1502 stores. Taking the 1502 separate and distinct Toys “R” Us stores into consideration, they combined to account for 67 million square feet of retail space. At the beginning of the 2011 fiscal year, Toys “R” Us held $2.104 billion in inventory. Their ending inventory in that fiscal year was $2.232 billion, giving them an average inventory of $2.168 for the 2011 fiscal year. Lastly, total assets came out to be $8.842 billion that year.

For the 2012 fiscal year, net sales totaled $13.543 billion while cost of goods sold came to $8.592 billion. Given this, one can see the gross profit as $4.951 billion, a slight bump from 2011. Toys “R” Us
achieved a gross margin of 36.56% in the 2011 fiscal year. In the expenses, often referred to as SGA (sales and general/administrative), Toys “R” Us incurred $4.041 billion dollars’ worth of expenses. All of this gave the company a net profit of $39 million, a substantial decrease from the previous year. The number of stores in the beginning of the 2012 fiscal year was 1502 and they ended the fiscal year with 1540 stores. Taking the 1540 separate and distinct Toys “R” Us stores into consideration, they combined to account for 67 million square feet of retail space. At the beginning of the 2012 fiscal year, Toys “R” Us held $2.232 billion in inventory. Their ending inventory in that fiscal year was $2.229 billion, giving them an average inventory of $2230.5 for the 2012 fiscal year. Lastly, total assets came out to be $8.921 billion that year.

In the 2013 fiscal year, net sales totaled $12.543 billion while cost of goods sold came to $8.154 billion. Given this, one can see the gross profit as $4.389 billion, a slight fall from 2012. Toys “R” Us achieved a gross margin of 34.99% in the 2013 fiscal year. In the expenses, often referred to as SGA (sales and general/administrative), Toys “R” Us incurred $4.010 billion dollars’ worth of expenses. All of this gave the company a net profit of ($1.036) billion (that is, a net loss of $1.036 billion), a huge decrease from the previous year. The number of stores in the beginning of the 2013 fiscal year was 1540 and they ended the fiscal year with 1577 stores. Taking the 1577 separate and distinct Toys “R” Us stores into consideration, they combined to account for 68 million square feet of retail space. At the beginning of the 2013 fiscal year, Toys “R” Us held $2.229 billion in inventory. Their ending inventory in that fiscal year was $2.171 billion, giving them an average inventory of $2.200 for the 2013 fiscal year. Lastly, total assets came out to be $7.549 billion that year.

Finally, in the 2014 fiscal year, net sales totaled $12.361 billion while cost of goods sold came to $7.931 billion. Given this, one can see the gross profit as $4.430 billion, a slight raise from 2013. Toys “R” Us achieved a gross margin of 35.84% in the 2014 fiscal year. In the expenses, often referred to as SGA (sales and general/administrative), Toys “R” Us incurred $3.915 billion dollars’ worth of expenses. All of this gave the company a net profit of ($288) million (that is, a net loss of $288 million), a large decrease
from the previous year. The number of stores in the beginning of the 2014 fiscal year was 1577 and they ended the fiscal year with 1602 stores. Taking the 1602 separate and distinct Toys “R” Us stores into consideration, they combined to account for 68 million square feet of retail space. At the beginning of the 2014 fiscal year, Toys “R” Us held $2.171 billion in inventory. Their ending inventory in that fiscal year was $2.064 billion, giving them an average inventory of $2.117.5 for the 2014 fiscal year. Lastly, total assets came out to be $7.115 billion that year.

Again, all of this information and several other metrics can be found in the appendices. Additionally, the trend information (% change from one year to another) may be found in the appendices. Some of the most notable trend statistics from year to year amongst the firm will be reviewed below. The sales trend, while still negative, has decreased over the last couple years from (7.4%) to (1.5%). Another good sign that Toys “R” Us is moving in the right direction is that their COGS has gone from (5.1%) to (2.7%). Gross margin percentage has gone from (11.4%) to now 0.9%. For a complete and thoroughly informative view of all trend information over the last four fiscal years, please refer to Appendix A. Here, additional trends such as SG&A Expense Ratio, Net Margin Percentage, Average Number of Stores, Average Inventory, Total Assets, Average Annual Assets, Sales per Square Foot, and even Adj. EBITDA have been calculated.

While the previous statistics provide a solid general look into Toys “R” Us, some financial ratios may bring more clarity to the picture. In 2011, sales per store totaled $9.61 million while sales per square foot was $207.60. The inventory turnover for the firm was 6.42 X (times over). The company’s ROA (Return on Assets) was 1.71%. The GMROI was 2.29%, while the expenses as a percentage of sales was 28.97%. The net profit margin for the fiscal year was 1.09% and the asset turnover was 1.57 X (times over). Lastly, the gross margin percentage was 35.73%.
In 2012, sales per store totaled $8.90 million while sales per square foot was $202.1. The inventory turnover for the firm was 6.07 X (times over). The company’s ROA (Return on Assets) was 0.44%. The GMROI was 2.22%, while the expenses as a percentage of sales was 29.84%. The net profit margin for the fiscal year was 0.29% and the asset turnover was 1.53 X (times over). Lastly, the gross margin percentage was 36.56%.

In 2013, sales per store totaled $7.90 million while sales per square foot was $184.46. The inventory turnover for the firm was 5.70 X (times over). The company’s ROA (Return on Assets) was -12.58%. The GMROI was 2.0%, while the expenses as a percentage of sales was 31.97%. The net profit margin for the fiscal year was -8.26% and the asset turnover was 1.52 X (times over). Lastly, the gross margin percentage was 34.99%.

Finally, 2014, sales per store totaled $7.78 million while sales per square foot was $181.78. The inventory turnover for the firm was 5.84 X (times over). The company’s ROA was -3.93%. The GMROI was 2.09 %, while the expenses as a percentage of sales was 31.67%. The net profit margin for the fiscal year was -2.33% and the asset turnover was 1.69 X (times over). Lastly, the gross margin percentage was 35.83%.

The change in same store sales most recently in 2014 was flat at 0.0%. This was following two consecutive negative years in same store sales. For the 2013 fiscal year, Toys “R” Us experienced a 4.4% decrease in same store sales. And prior to that, the company saw a 4.1% decrease in same store sales. The same store sales number was not available for 2011.

Up until 2005, Toys “R” Us was a publically traded stock under the ticker symbol TOY. In 2005, Toys “R” Us went through a $6.6 billion buyout by a group of firms known as KKR & Co. L.P. They operate and trade under the ticker symbol (KKR). Their 52 week low is $8.00 per share and their 52 week high is $25.04 per share. At the time this analysis was fully completed (November 27, 2015), KKR was trading for
$17.10 a share. Even though the buyout of Toys “R” Us occurred just over a decade ago, they are still with SEC filings due to debt securities that remain outstanding and publically traded. The most recent bond issued was 14 months ago back in October 2014. The 14 month high occurred in June of 2015 when the bond peaked at a price of 95.313. The 14 month low happened just this past November 2015 when it hit 85.313. Currently, the bond is priced at 85.875. So what does this all mean? Overall, the bond price is on the decline, as investors are selling more and buying less. Generally speaking, investors are feeling increasingly less positive about the Toys “R” Us bond. Please refer to Appendix B for more information.

Toys “R” Us presents a unique challenge when attempting to find a similar competitive firm. When thinking about the toy industry, companies such as Hasbro, Mattel, and Jakk’s Pacific come to mind. However, these companies are inadequate to draw comparisons due to one main reason. These three companies represent some of the largest toy manufacturers in the country, and across the entire world for that matter. Yet, they are just that – they are manufacturers. Toys “R” Us is a retailer who may have Hasbro, Mattel, and Jakk’s Pacific products in their assortment. In reality, there is no true, pure competitor to Toys “R” Us that does exactly what they do. Roughly five years ago, the last remaining competitor closed shop when national toy retailer Kay Bee Toys went under. Now, Walmart and Target are now the primary competition when it comes to retailing toys. However, it is nowhere near fair to compare Toys “R” Us’ number to either of those companies as they have many other groups of merchandise in their stores (apparel, food, electronics, etc). So the solution to examine competitive firms and industries came down to a two-step approach. Please reference Appendix C at this time. First, I grouped Target and Walmart together and reported their comparative numbers, as well as took an average of the two. Then, perhaps a better indicator of Toys “R” Us’ performance, I took other industry leaders and reported their data. Toys “R” Us is the industry leader in the Specialty Stores Industry within the Consumer Discretionary Sector. I compared them to other Industry leaders within the Consumer Discretionary Sector like Best Buy (Electronics), Bed Bath & Beyond (Home Furnishings), Kohl’s (Department), and several others. Again,
please refer to Appendix C to read the information (firm data and ratios have been calculated) in its entirety.

Upon completion of my research and analysis, I have come up with a few suggestions that I believe could potentially enhance or improve the performance of the retailer in the future. First, the SG&A Expense for Toys “R” Us is averaging $3.92 million per year over the past four fiscal years with a ratio of 31.7%. This is well above the group mean established by the other industry leaders of the Consumer Discretionary Sector. They report an average SG&A Expense of $3.54 million per year with a ratio of 21.7%. Toys “R” Us is clearly lagging behind as seen by their four year net profit margin of -2.4% versus the industry leader group average of 4.8%. Please reference Appendix C for this illustration. Since SG&A affects Net Profit which in turn affects the Net Profit Margin, Toys “R” Us must figure out a way to lower expenses. For instance, find ways to reduce and limit promotion costs. To be frank, this seems to be a dying industry with giants Walmart and Target dominating the toy retailing business by growing numbers each year. Also, Toys “R” Us could look to become an even more vertical and tall structured company to attempt to cut back on general and administrative costs, if the promotion cutbacks are simply undoable. Another suggestion that might enhance or improve the performance of Toys “R” Us would be to broaden their target market to an older age group, ages 14-18 years old. When you think of Toys “R” Us, you think of company that offers toys to younger kids, which it does already, but older children still use toys too, just in a different way. If Toys “R” Us could offer technology based toys to these children, they could be based around enhancing the learning of these children. These “toys” could include things such as headsets to improve their listening skills in the classroom or cameras where they could take pictures of the notes the teacher puts up on the board and then are able to take it home, upload the pictures to use to study. Most schools don’t allow the use of cell phones which would be their only means of taking pictures of notes. One major change the retailer could make is to offer more services and goods that relate to children but more so, appeal to the parents. This store could work on its lack of breadth by
offering services to parents. For example, a gift wrapping service at all stores so that parents don’t have to worry about taking the time to prepare gift. This would be especially important around the holidays. Making “convenience” the overall theme for parents would really benefit the company. Adults with children are wearing many different hats. Providing services for parents that get them in and out of the store with their purchase ready to be given would be a very appealing addition to Toys “R” Us’ image. The Toys “R” Us flagship store located in Times Square in New York City is a major draw for domestic families and international tourists alike. Unfortunately all of the other stores across the country follow the same cookie cutter appearance. Toy “R” Us could really thrive with some more “flagship” stores located in other major cities across the United States. With more super stores like the one in New York City, Toys “R” Us will indefinitely see a boost in name popularity. So it is with these suggestions that we would offer Toys “R” Us to improve in their future business.
J.J.B. Hilliards, W.L. Lyons, LLC company and database


http://www.toysrusinc.com/about-us/history/


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http://mhlnews.com/facilities-management/toys-r-us-embraces-just-time

http://www.toysrusinc.com/about-us/
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<th>% Change</th>
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<td>Toys R Us (dollars figures in millions, except sales per square foot)</td>
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Most Recent Bond Issue, October 2014
10 3/8\% coupon, due 8/15/2017

beginning price 91.438
hi-low, range to date 95.313 - 85.313
recent price, 11/25/15 85.875
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