CHILDRENS PLACE RETAIL STORES INC
Form 10-K
April 02, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

ý **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fifty-two weeks ended February 2, 2008

o **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 0-23071

THE CHILDREN'S PLACE RETAIL STORES, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**31-1241495** (I.R.S. employer identification number)
915 Secaucus Road **Secaucus, New Jersey** (Address of Principal Executive Offices)	**07094** (Zip Code)

(201) 558-2400
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act: **Common Stock, $0.10 par value**

Name of each exchange on which registered: **Nasdaq Global Select Market**

Securities registered pursuant to Section 12(g) of the Act: **None.**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No ý

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No ý

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 ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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 definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ý	Accelerated filer o	Non-accelerated filer o (Do not check if smaller reporting Company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No ý

The aggregate market value of common stock held by non-affiliates was $738,484,725 at the close of business on August 4, 2007 (the last business day of the registrant's fiscal 2007 second fiscal quarter) based on the closing price of the common stock as reported on the Nasdaq Global Select Market. For purposes of this disclosure, shares of common stock held by persons who hold more than 10% of the outstanding shares of common stock and shares held by executive officers and directors of the registrant have been excluded because such persons may be deemed affiliates. This determination of executive officer or affiliate status is not necessarily a conclusive determination for other purposes.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date: Common Stock, par value $0.10 per share, outstanding at March 28, 2008: 29,186,397.

Documents Incorporated by Reference: Portions of The Children's Place Retail Stores, Inc. 2008 Definitive Proxy Statement for its Annual Meeting of Stockholders to be held on June 27, 2008 are incorporated by reference into Part III.

THE CHILDREN'S PLACE RETAIL STORES, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE FIFTY-TWO WEEKS ENDED FEBRUARY 2, 2008
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PART I

ITEM 1. BUSINESS

The Business section and other parts of this Annual Report on Form 10-K may contain certain forward-looking statements regarding future circumstances. Forward-looking statements provide current expectations of future events based on certain assumptions and include any statement that does not directly relate to any historical or current fact. Forward-looking statements can also be identified by words such as "anticipates," "believes," "estimates," "expects," "intends," "plans," "predicts," and similar terms. These forward-looking statements are based upon the Company's current expectations and assumptions and are subject to various risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements including, but not limited to, those discussed in the subsection entitled "Risk Factors" under Part I, Item 1A of this Annual Report on Form 10-K. Actual results, events, and performance may differ significantly from the results discussed in the forward-looking statements. Readers of this Annual Report on Form 10-K are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to release publicly any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. The inclusion of any statement in this Annual Report on Form 10-K does not constitute an admission by the Company or any other person that the events or circumstances described in such statement are material.

The following discussion should be read in conjunction with the Company's audited financial statements and notes thereto included elsewhere in this Annual Report on Form 10-K.

Recent Developments

Since November 2004, we have operated the Disney Store retail chain in North America (the "DSNA Business") through two wholly-owned subsidiaries. (For clarification, the "DSNA Business" refers to the historical business we acquired from certain affiliates of The Walt Disney Company ("Disney") as of November 21, 2004, whereas the "Disney Store business" refers to the Disney Store business we have operated since the acquisition.) The Company's subsidiaries that operated the Disney Store business are referred to herein interchangeably and collectively as "Hoop."

As a result of the acquisition, these subsidiaries acquired 313 Disney Stores, consisting of all existing Disney Stores in the United States and Canada, other than "flagship" stores and stores located at Disney theme parks and other Disney properties, along with certain other assets used in the Disney Store business. In addition, the lease obligations for all 313 stores and other legal obligations became obligations of the Company's subsidiaries. Subsequently, the Company's subsidiaries acquired two Disney Store flagship stores, one in Chicago, Illinois and the other in San Francisco, California as well as certain Disney Store outlet stores.

Concurrent with the acquisition of the DSNA Business, the Company entered into a License and Conduct of Business Agreement with Disney (the "License Agreement") and a Guaranty and Commitment (the "Guaranty and Commitment Agreement"). Under the License Agreement, Hoop has the right to use certain Disney intellectual property, subject to Disney approval, in the Disney Store business in exchange for ongoing royalty payments. Pursuant to the terms of the License Agreement, Hoop operates retail stores in North America using the "Disney Store" name and sells merchandise featuring Disney-branded characters.

In October 2007, the Company's Board and management embarked on a review of strategic alternatives, assessing a wide variety of options to improve our business and competitive position, including, but not limited to, opportunities for organizational and operational improvement, a possible recapitalization, or other transactions. After a thorough review of the operation of the Disney Store business, its potential for earnings growth, its capital needs and its ability to fund such needs from its own resources, the Company announced on March 20, 2008 that it has decided to exit the Disney Store business. Reflecting its decision to exit the Disney Store business, the Company recognized a pre-tax asset impairment charge of $80.3 million in the fourth quarter of fiscal 2007. For more information please see "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

Unrelated to the Company's decision to exit the Disney Store business, Hoop recently received notices of several material breaches under the License Agreement. Hoop believes it has cured some of the asserted breaches and intends to cure or to assert defenses to the other asserted breaches.

On March 26, 2008, Hoop Holdings, LLC, Hoop Retail Stores, LLC and Hoop Canada Holdings, Inc. each filed a voluntarily petition for relief under Chapter 11 of the United States Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware (the "US Bankruptcy Court") (Case Nos. 08-10544, 08-10545, and 08-10546, respectively), and Hoop Canada, Inc. filed for protection pursuant to the *Companies' Creditors Arrangement Act* (the "CCAA") in the Ontario Superior Court of Justice (Commercial List) ("Canadian Bankruptcy Court") on March 27, 2008. The Hoop entities currently manage, and will continue to manage, their properties and operate their businesses as "debtors-in-possession" under the jurisdiction of the US Bankruptcy Court or Canadian Bankruptcy Court, as applicable, and in accordance with the applicable provisions of the Bankruptcy Code or the CCAA, as applicable.

As a result of the filing of the bankruptcy cases (the "Filings"), Hoop's obligations under various agreements may be accelerated. Further, the Company has provided notice that it is discontinuing the Guaranty and Commitment Agreement and, on March 28, 2008, Disney sent the Company notice that it disputes the validity of the discontinuance. Valid discontinuance will constitute an event of default under the Guaranty and Commitment Agreement. The Filings also constituted an event of default under the Guaranty and Commitment Agreement. Under the Guaranty and Commitment Agreement, the Company has agreed to guarantee Hoop's royalty payments and other obligations to TDS Franchising LLC, an affiliate of Disney ("TDSF"), subject to a maximum guaranty liability of $25 million, plus expenses. Additionally, the Company made an initial investment of $50 million to Hoop and agreed to invest, under certain conditions, up to an additional $50 million to ensure Hoop's ability to pay its obligations under its license agreement with TDSF and to fund Hoop's operating losses. On March 18, 2008, the Company made a capital contribution to Hoop of approximately $8.3 million in cash.

As a result of the Filings, outstanding indebtedness, in the amount of approximately $9.3 million, under the Amended Hoop Loan Agreement (as defined and further described in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Credit Facilities Amended Hoop Loan Agreement") will be frozen and capped as of the March 26, 2008. In order to fund the bankruptcy proceedings and all projected working capital needs and subject to US Bankruptcy Court approval, Hoop entered into a Debtor-In-Possession Loan and Security Agreement, dated March 26, 2008, as described in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Credit Facilities Amended Hoop Loan Agreement."

In addition, the bankruptcy proceedings may give rise to other material obligations of the Company and exit costs as discussed in this Annual Report on Form 10-K.

In connection with the Filings, Hoop intends to pursue the transfer of a substantial portion of the Disney Store business and assets to Disney (the "Private Sale"), subject to court approval. In connection with the proposed Private Sale, the Hoop entities filed motions for orders that grant authority to sell their assets to Disney pursuant to section 363 of the Bankruptcy Code (and a similar provision under the CCAA) and that request the courts to set a hearing date for the proposed Private Sale.

The proposed Private Sale would be subject to the satisfaction of certain conditions, including approval of the US Bankruptcy Court and Canadian Bankruptcy Court, and would be targeted for completion by April 30, 2008. The Company continues to expect the pre-tax cash costs to exit the Disney Store business to be within the previously stated range of $50 million to $100 million, payable over a period of time, including estimated severance and other employee costs for the Company's employees servicing Hoop, professional fees and other costs the Company may incur during the Hoop bankruptcy cases, as well as claims that might be asserted against the Company in the bankruptcy proceedings.

In the event of a transfer of all or a portion of the Disney Store business to Disney during the ongoing bankruptcy proceedings and subject to the satisfaction of other conditions, the Company would be released from liabilities and claims that have been or might be asserted by Disney, including those described above.

Overview

In this Annual Report, the words the "Company", "we", "us", "our" and similar terms collectively refer to The Children's Place Retail Stores, Inc. and subsidiaries. As described in "Recent Developments" and "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Recent Developments," the Company has determined to exit the Disney Store business. In an effort to facilitate an understanding of our financial condition and results of operation for the fiscal year ended February 2, 2008 ("fiscal 2007"), as well as the Company's fiscal 2007 audited financial statements and notes thereto, included in this Annual Report on Form 10-K, we have included a discussion of the Disney Store business, as such business was a part of our Company during fiscal 2007. For the fiscal year ended January 31, 2009 ("fiscal 2008"), the Disney Store business will be classified as "Discontinued Operations."

The Company was incorporated in June 1988 and is a leading specialty retailer of children's merchandise. We design, contract to manufacture and sell high-quality, value-priced merchandise under our proprietary "The Children's Place" and licensed "Disney Store" brand names. As of February 2, 2008 we owned and operated 904 The Children's Place stores and 335 Disney Stores across North America and operated Internet stores at www.childrensplace.com and www.disneystore.com.

In fiscal 2007 we were structured such that our administrative functions (e.g., finance, real estate, human resources, legal, information technology, logistics) were shared by both The Children's Place and the Disney Store brands. Functions such as design, merchandising, marketing and store operations were run independently of each other to maintain clearly defined and differentiated brands. Historically, each brand was overseen by a President who managed the day-to-day operations and who reported directly to our Chief Executive Officer ("CEO"). Because of the recent departure of the Company's President, who was responsible for leading the Children's Place brand operations, our interim CEO also is serving in the capacity of Company President. In anticipation of our exit from the Disney Store business in fiscal 2008, the Company has begun to reduce its shared services infrastructure. If a sale to Disney is completed through the Chapter 11 process, the Company is prepared to contract services to Disney during a transitional period.,

The Children's Place is a specialty retailer of apparel and accessories for children from newborn to ten years of age. The brand's merchandising objective is to offer a unique, colorful, coordinated and balanced lifestyle assortment of high quality, basic and fashion merchandise, at prices that represent substantial value to our customers.

Our goal is to be the leading specialty retailer in the children's space by executing on our "core purpose" of "making the very best accessible to all children."

During fiscal 2007, we opened 54 The Children's Place stores compared to 69 store openings in fiscal 2006. We also opened 15 Disney Stores in fiscal 2007 compared to 19 in fiscal 2006. We closed 16

The Children's Place stores and eight Disney Stores in fiscal 2007, compared to five The Children's Place store closures and eight Disney Store closures in fiscal 2006. Our store growth plan for fiscal 2008 includes opening approximately 30 The Children's Place stores.

Key Capabilities

We believe that the following capabilities have been and continue to be critical to our long-term success:

Merchandising Strategy. The Children's Place merchandising strategy is built on offering interchangeable outfits and accessories to create a coordinated look distinctive to the brand. We offer an updated, focused assortment of styles in a variety of colors and patterns, with the aim of consistently creating a fresh, youthful look at value prices that we believe distinguishes "The Children's Place" brand. We divide the year into quarterly merchandising seasons: spring, summer, back-to-school and holiday. Within each season, we typically deliver two merchandise lines. Each season is built around a color palette that includes an assortment of coordinated basic and fashion apparel with matching accessories.

High Quality/Value Pricing Strategy. We believe that our high quality, value price positioning is an important component of our long-term strategy. We offer high-quality clothing and accessories under "The Children's Place" brand name at prices below most of our direct mall-based competitors. We employ this value pricing strategy across our entire merchandise offering.

Brand Image. We strive to build our brand image and customer loyalty for "The Children's Place" by:

- Offering high-quality products at value prices;
- Providing colorful, coordinated and interchangeable outfits and accessories;
- Maintaining a uniform merchandise presentation;
- Emphasizing our image in our marketing visuals;
- Utilizing our customer database to target direct mailers to customers;
- Maintaining a marketing presence in targeted print publications; and
- Selling our merchandise exclusively in our The Children's Place stores and on our website.

Low-Cost Sourcing. We control the design, sourcing and presentation of our products. We believe that this control is essential in assuring the consistency and quality of our merchandise, as well as our ability to deliver value to our customers. We have established long-standing relationships with our vendors and suppliers. Through these relationships and our extensive knowledge of low cost sourcing, we are able to offer our customers high-quality products at value prices. Our offices in Hong Kong, Shanghai and New Delhi allow us to capitalize on new sourcing opportunities, increase our control over product quality and enable us to respond to changing merchandise trends effectively and efficiently.

Merchandising Process

To execute our merchandising strategies, we rely on the coordinated efforts of our design, merchandising, planning and sourcing teams. These teams, in conjunction with senior management, "hindsight" prior season results and review fashion trends, colors and design concepts that we will offer in upcoming seasons. Merchandising selects items for production from the assortment of merchandise designs that are created by the design team. Then, based upon detail design specifications and production quantities determined by merchandising and planning, the sourcing team arranges for the issuance of purchase orders and manufacture of the selected items.

Work on each of our seasonal lines begins approximately one year before the season. However, the Company maintains, and at times exercises, the ability to develop and deliver product on an expedited timeline. The merchandising process includes purchasing of samples and gathering market intelligence on fashion trends, which involves extensive European and domestic market research, studying media and fashion magazines, attending trade shows, engaging the services of fashion and color forecast organizations, and analyzing prior season performance. After the design teams present their ideas, the designers, with the direction of the merchandising team, translate those ideas into a merchandise assortment that reflects the theme of the season. These interpretations include variations in fabric and other materials, product color, decoration and age-appropriate silhouettes. Potential items are designed using computer aided design technology, which allows for a wide range of style and fashion options. Our sourcing teams and Asian offices coordinate the production of prototype samples which enable our merchandising teams to ensure that our merchandise will properly reflect our design concepts. We have also instituted a process that involves working with prototype samples in a simulated in-store environment.

The merchandise management teams create a detailed purchasing plan for the season covering each department, category and key item, based on historical, current and emerging category trends. The production process takes approximately five to six months from order confirmation to receipt of merchandise at our distribution facilities. Our planning teams monitor current and projected inventory levels on a weekly basis and analyze sales patterns to predict future demand for various items and categories. We regularly monitor sales and maintain some flexibility to adjust merchandise on order for future seasons or to accelerate delivery of merchandise. Our merchandise allocation teams are responsible for planning and allocating merchandise to each store based on sales levels, merchandise turns and other factors.

Sourcing and Procurement

We combine management's extensive apparel sourcing experience with a cost-based buying strategy to control merchandise costs, infuse quality features into our products and deliver value to our customers. We believe that our understanding of the economics of apparel manufacturing, including costs of materials and components enables us to identify cost-effective countries and manufacturers from which to source each item and obtain high quality at low product cost.

Four times a year, our U.S. sourcing team makes on-site visits to our independent agents and various manufacturers to negotiate product costs, finalize technical specifications for each product and confirm delivery of merchandise manufactured to our specifications. During fiscal 2007, approximately 300 independent manufacturers located primarily in Asia produced merchandise sold at The Children's Place and Disney Store to our specifications. To support our inventory needs and to control merchandise costs, we continue to pursue global sourcing opportunities and consider product quality and cost, reliability of the manufacturer, and service and product lead times, among other factors.

We have no exclusive or long-term contracts with our manufacturers and typically transact business on an item-by-item basis under purchase orders at freight on board cost in U.S. dollars. We are party to agency agreements with commissioned independent agents who oversee production, assist in sourcing and pre-production approval, provide quality inspection and ensure timely delivery of merchandise. During fiscal 2007, we purchased approximately 16% of our products through the support of a commissioned, independent agent in Taiwan, and approximately 13% of our products through an independent Hong Kong-based trading company. This trading company is responsible for procurement from wholly-owned facilities as well as contract manufacturers located throughout Asia. In addition, we believe our offices in Hong Kong, Shanghai and New Delhi enable us to obtain more favorable material and manufacturing costs and quickly identify and act on new sourcing and supplier opportunities. Our Asian offices also facilitate our prototype sample production and enable us to foster stronger relationships with our suppliers, manufacturers, agents and trading companies. During fiscal

2007, we purchased approximately 49% of our total merchandise without the aid of commissioned buying agents or trading companies. In addition, approximately 54% of our total goods were sourced from China. Specific to The Children's Place brand, in 2007, approximately 40% of our Children's Place merchandise was purchased without the aid of commissioned buying agents or trading companies, and approximately 47% was purchased from China. Using our purchase order, advanced shipping notification and tracking systems, our independent agents and our sourcing department actively monitor the status of each purchase order from order confirmation to merchandise receipt.

We augment our manufacturers' testing requirements with our own in-house quality assurance laboratory to test and evaluate fabric, trimming materials and pre-production samples against a comprehensive range of physical performance standards before production begins. The quality control personnel in our Asian offices, independent agents and trading company visit the various manufacturing facilities to monitor the quality control and production process. Our Asian offices enhance our quality control by enabling us to monitor component and manufacturing quality at close range and address related problems at an early stage. With this focus on pre-production quality, we are generally able to detect and correct quality-related problems before bulk production begins. We do not accept finished goods until each purchase order receives formal certification of compliance from our own quality assurance associates, agents or appointed third-party inspectors.

In addition to our quality control procedures, we administer a social compliance program designed to promote compliance with local legal regulations, as well as ethical and socially responsible business practices.

Company Stores

The following section highlights various store information for both The Children's Place and Disney Store brands as of February 2, 2008.

Existing Stores. As of February 2, 2008, we operated a total of 1,239 stores: 904 The Children's Place stores and 335 Disney Stores in North America. Most of The Children's Place stores are clustered in and around major metropolitan areas in regional malls, with the exception of 150 strip center, 113 outlet and 48 street stores. All of the Disney Stores as of February 2, 2008 were in regional malls with the exception of 30 outlet stores, three strip stores and two street locations. The following table sets forth the number of stores in each state, Puerto Rico and Canadian province as of February 2, 2008:

State	The Children's Place	Disney Store	Total Number of Stores
Alabama	9	4	13
Arizona	15	7	22
Arkansas	5	1	6
California	82	51	133
Colorado	14	5	19
Connecticut	14	7	21
Delaware	4	3	7
Florida	47	26	73
Georgia	22	6	28
Hawaii	4	1	5
Idaho	1	1	2
Illinois	41	17	58
Indiana	18	7	25
Iowa	6	1	7
Kansas	5	2	7
Kentucky	8	3	11

Louisiana	13	3	16
Maine	4	1	5
Maryland	23	6	29
Massachusetts	25	7	32
Michigan	23	9	32
Minnesota	12	1	13
Mississippi	6	1	7
Missouri	15	8	23
Montana	1	0	1
Nebraska	3	1	4
New Hampshire	4	3	7
New Jersey	45	16	61
New Mexico	3	2	5
New York	76	21	97
Nevada	7	3	10
North Carolina	21	7	28
North Dakota	1	0	1
Ohio	30	10	40
Oklahoma	3	2	5
Oregon	9	3	12
Pennsylvania	48	21	69
Rhode Island	3	1	4
South Carolina	13	2	15
South Dakota	1	0	1
Tennessee	17	7	24
Texas	57	25	82
Utah	7	1	8
Vermont	1	0	1
Virginia	18	8	26
Washington	12	3	15
West Virginia	1	2	3
Wisconsin	13	3	16
Puerto Rico	14	0	14
Total United States and Puerto Rico	**824**	**319**	**1,143**

Province	**The Children's Place**	**Disney Store**	**Total Number of Stores**
Alberta	7	3	10
British Columbia	9	1	10
Manitoba	2	1	3
New Brunswick	3	1	4
Nova Scotia	2	1	3
Ontario	38	9	47
Quebec	17	0	17
Saskatchewan	2	0	2
Total Canada	**80**	**16**	**96**
Total Stores	**904**	**335**	**1,239**

Store Type.

The Children's Place. Our average Children's Place store is approximately 4,700 square feet. The majority of The Children's Place stores are in our "Apple-Maple" prototype.

During fiscal 2002, we introduced our "Technocolor" store prototype, which uses color to create boutique-like settings that better differentiate the various departments within the store. As of February 2, 2008, 328 stores were in this format, or approximately 36% of The Children's Place store base. In fiscal 2007, some of our new stores and remodels (except for outlets) were updated to our Technocolor store format, and averaged approximately 5,500 square feet in size to accommodate our new "store-within-a-store" shoe store, which the Company launched in July 2007. Our street and strip center locations represent approximately 22% of The Children's Place store base.

Our typical outlet stores are approximately 6,800 square feet and represent approximately 13% of The Children's Place store base. Our outlet stores are primarily located in outlet centers and are strategically placed within each market to liquidate clearance merchandise from nearby stores. Given the brand's value orientation, we also sell an assortment of full-priced merchandise in our outlet stores.

Disney Store. The average Disney Store is approximately 4,800 square feet. As of February 2, 2008, several Disney Store formats were in operation, as follows:

	% of Store Base
Pink and Green	33%
Piperail	28%
Mickey	20%
Millennium	6%
Castle	5%
Outlet*	8%
Total	100%

* *Note*: Disney Store outlets reflect various formats.

Store Operations

The Children's Place store operations are organized into ten regions. We employ two Zone Vice Presidents who oversee our operations and to whom regional managers report. A regional manager oversees each region and has several district managers reporting to them. Each district manager is responsible for approximately eight to ten stores. Our stores are staffed by a store management team and approximately 10 part-time sales associates, with additional part-time associates hired to support seasonal needs. Our store leadership teams spend a high percentage of their time on the store selling floors providing direction, motivation, and development to store personnel. To maximize selling productivity, our teams emphasize greeting, replenishment, presentation standards, procedures and controls. In order to motivate our store leadership, we offer a monthly incentive compensation plan that awards bonuses for achieving certain financial goals.

Store Expansion Program

The Children's Place. During fiscal 2007, we opened 54 stores and closed 16, compared to opening 69 stores and closing five in fiscal 2006. We plan to open approximately 30 stores and remodel approximately 17 Children's Place stores in fiscal 2008.

Our new store return on investment (defined as the return on investment for stores in which the then current fiscal year was their first full year of operation) for The Children's Place chain for fiscal 2007, 2006 and fiscal 2005 approximated 47%, 87% and 81%, respectively. We define return on investment as store level operating cash flow for new stores divided by new store investment. Store

level operating cash flow for new stores is comprised of direct store contribution before the amortization of deferred rent and depreciation and amortization expense. We believe new store return on investment is a relevant measurement for assessing performance because it shows how quickly our investment in new stores becomes available for reinvestment. However, it is not a measure determined in accordance with generally accepted accounting principles in the United States ("U.S. GAAP") and should not be considered by investors as an alternative to operating income or net income as an indicator of our performance. The new store return on investment disclosed here is not necessarily comparable to new store return on investment disclosed by other companies because new store return on investment is not uniformly defined.

Average store level operating cash flow for stores in which fiscal 2007 was their first full year of operation approximated $281,200, a 31% decrease compared to fiscal 2006. Average new store investment for this group of stores approximated $595,500, a 28% increase from fiscal 2006. Average store investment includes store capital expenditures, initial inventory and pre-opening costs less lease incentives and an estimate for merchandise payables. This increase in average new store investment primarily reflects a higher capital investment in our store prototype. New stores in which fiscal 2007 was their first full year of operation had average net sales of approximately $1.5 million, comparable to fiscal 2006.

New 'Store-within-a-Store' Children's Place Shoe Store. In fiscal 2007, we launched a new 'store-within-a-store' shoe store during the back-to-school season. At the end of fiscal 2007, we operated 54 stores which feature our expanded shoe assortment, or approximately 6% of the chain. Our expanded shoe offering is also available for sale on our childrensplace.com website. While initially stores that carry the expanded shoe assortment were approximately 1,000 square feet larger than a typical store, we are considering a reduction in the amount of square footage dedicated solely to shoes in an effort to drive increased profitability.

Disney Store. In fiscal 2007 we opened 15 Disney Stores, closed eight, and remodeled seven, compared to opening 19, closing eight and remodeling 14 in fiscal 2006.

Our new store return on investment (defined as the return on investment for stores in which the then current fiscal year was their first full year of operation) for the Disney Stores in fiscal 2007 and fiscal 2006 approximated 23% and 62%, respectively. Average store level operating cash flow for new stores in which fiscal 2007 was their first full year of operation approximated $174,400, a 53% decrease compared to fiscal 2006. Average store investment for these stores approximated $762,300, a 27% increase from fiscal 2006, and included store capital expenditures, initial inventory and pre-opening costs less lease incentives and estimated merchandise payables. Fiscal 2007 new stores had average net sales of approximately $2.1 million, a 16% decrease compared to fiscal 2006.

Seasonality

Our business is also subject to seasonal influences, with heavier concentrations of sales during the back-to-school and holiday seasons. Our first quarter results are heavily dependent upon sales during the period leading up to the Easter holiday. Our third quarter results are heavily dependent upon back-to-school sales at The Children's Place. Our fourth quarter results are heavily dependent upon sales during the holiday season. In fiscal 2007, the Disney Store business was highly dependent upon Halloween sales in the third quarter and holiday sales in the fourth quarter, which is reflected in our fiscal 2007 results. For more information regarding the seasonality of our business, refer to Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Quarterly Results and Seasonality.

Internet Sales

Our The Children's Place Internet business represented approximately 3.6% of The Children's Place sales in fiscal 2007, compared to 2.9% of sales in fiscal 2006. This profitable business continues to grow at a rapid rate and we believe it is an integral part of our customer service and brand awareness strategies.

Beginning in July 2007, the Company's subsidiaries commenced Internet commerce operations through an alliance with a Disney affiliate in which certain Disney Store merchandise is sold on the disneyshopping.com website. For the use of the Disney Internet commerce website, the Company paid fees to a Disney affiliate based on a percentage of e-commerce sales, a portion of which is allocated to cost of sales and a portion to selling, general and administrative expenses, as reflected in our fiscal 2007 financial results. Given our decision to exit the Disney Store business, our fiscal 2008 results will only reflect a portion of sales and related expenses reflective of the Disney Store e-commerce operation.

Marketing

We strive to build brand recognition and equity by marketing our image, product and value message primarily through our store front windows, in-store marketing, direct mail, magazine advertising and "The Children's Place" private label credit card.

We view The Children's Place private label credit card as an important marketing and communication tool. Pursuant to a merchant services agreement, private label credit cards are issued to our customers for use exclusively at The Children's Place stores, and credit is extended to such customers through a third-party financial institution on a non-recourse basis to us. Our private label credit card accounts for approximately 13% of The Children's Place net sales. We believe that our private label credit card promotes affinity and loyalty among those customers who use the card and facilitates communication with such customers through delivery of coupons and promotional materials.

Logistics

As of February 2, 2008 we supported both The Children's Place stores and Disney Stores with a leased 525,000 square foot distribution center in South Brunswick Township, New Jersey; a leased 250,000 square foot distribution center in Ontario, California; a leased 95,000 square foot distribution center in Ontario, Canada; and an owned 700,000 square foot distribution center in Ft. Payne, Alabama, which we opened in August 2007 to support projected growth at both brands. Our approximately 150,000 square foot leased fulfillment center in Secaucus, New Jersey is used to support our Children's Place Internet business. In addition, we operate other leased facilities on a seasonal basis to support warehousing needs. Going forward, given our decision to exit the Disney Store North America business, our logistics capacity will be used to support The Children's Place brand only.

Competition

The following discussion contemplates a competitive set for both The Children's Place and Disney Store North America brands as of February 2, 2008. Our fiscal 2007 results are reflective of this competitive universe.

The children's apparel, toy and media retail markets are highly competitive. We compete in substantially all of our markets with GapKids, babyGap and Old Navy (each of which is a division of The Gap, Inc.); The Gymboree Corporation; Too, Inc.; Babies "R" Us and Toys "R" Us (each of which is a division of Toys "R" Us, Inc.); J.C. Penney Company, Inc.; Sears (a division of Sears Holdings Corporation); Kohl's and other department stores as well as discount stores such as Wal-Mart Stores, Inc.; Target Corporation; and K-Mart (a division of Sears Holdings Corporation). In addition, given our expansion into the shoe category, we now compete with stores such as Stride Rite and

Payless, as well as smaller shoe retailers. We also compete with a wide variety of specialty stores, other national and regional retail chains, catalog companies and Internet retailers. The Disney Store business also competes with the Disney theme parks and with third parties selling Disney-branded merchandise under license. In addition, media items such as compact discs and DVDs can be purchased in virtually every retail channel. One or more of our competitors are present in substantially all of the areas in which we have stores.

Trademarks and Service Marks

"The Children's Place," "babyPLACE," "Place," "The Place," "TCP," "PLC" and certain other marks have been registered as trademarks and/or service marks with the United States Patent and Trademark Office. The registration of the trademarks and the service marks may be renewed to extend the original registration period indefinitely, provided the marks are still in use. We intend to continue to use and protect our trademarks and service marks and maintain their registrations. We have also registered our trademarks in Canada and other countries and are continuing to take steps to register our trademarks in certain other foreign countries. We believe our trademarks and service marks have received broad recognition and are of significant value to our business.

The trademarks and copyrights used by the Disney Store business are licensed by Hoop from Disney for use by the Disney Store so long as the License Agreement remains in effect. After completion of our exit from the Disney Store business, the License Agreement will terminate, and we will no longer be able to use such trademarks and copy rights.

Employees

As of February 2, 2008, we had approximately 23,800 employees, of whom approximately 1,900 are based at our corporate headquarters in New Jersey; our Disney Store office in Pasadena, California; our distribution centers; and international offices. We had approximately 4,250 full-time store employees and approximately 17,650 part-time store employees. None of our employees are covered by a collective bargaining agreement. We believe we have good relations with our employees. In addition, as of February 2, 2008, we employed approximately 9,700 seasonal part-time employees.

Primarily as a result of our decision to exit the Disney Store business, our employee headcount will decline in fiscal 2008. For reference, of the 23,800 employees as of February 2, 2008, 8,350 were Disney Store employees and 250 were corporate employees that worked out of the Pasadena office.

Internet Access to Reports

We are a public company and are subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Accordingly, we file periodic reports, proxy statements and other information with the Securities and Exchange Commission ("SEC"). Such reports, proxy statements and other information may be obtained by visiting the Public Reference Room of the SEC at 100 F Street, NE, Room 1580, Washington, D.C. 20549 or by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains a website (http://www.sec.gov) that contains reports, proxy and information statements and other information regarding us and other issuers that file electronically.

Our website address is http://www.childrensplace.com. We make available, without charge, through our website, copies of our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after such reports are filed with or furnished to the SEC. References in this document to our website are not and should not be considered part of this Annual Report on Form 10-K, and the information on our website is not incorporated by reference into this Annual Report on Form 10-K.

We also make available our corporate governance materials, including our code of business conduct, on our website. If we make any substantive amendments to our code of business conduct or grant any waiver, including any implicit waiver, from a provision of the code to our CEO, Executive Vice President of Finance and Administration, Chief Financial Officer ("CFO") or Corporate Controller, we will disclose the nature of such amendment or waiver on that website or in a Current Report on Form 8-K.

ITEM 1A. RISK FACTORS

Investors in the Company should consider the following risk factors as well as the other information contained herein:

We depend on generating sufficient cash flow and having access to additional liquidity sources to fund our ongoing operations, the Disney Store business exit costs, capital expenditures, and debt repayment.

Our ability to fund our ongoing operations, anticipated exit costs associated with the wind-down of the Disney Store business, planned capital expenditures and debt repayment obligations will depend on our ability to generate cash flow and to access, if necessary, additional liquidity sources. Our cash flow is dependent on many factors, including:

- seasonal fluctuations in our net sales and net income, which typically are lowest in the second fiscal quarter;
- the timing of inventory purchases for upcoming seasons, which typically result in increased cash expenditures in the second fiscal quarter as we purchase merchandise for the back-to-school season;
- the amount and timing of cash expenditures associated with our exit from the Disney Store business, which could exceed the current estimated range of $50 million to $100 million and may be significant during our second fiscal quarter when sales are low and inventory costs are high;
- vendor and other supplier terms and related conditions, which may be less favorable to us in the future as a result of the Disney Store bankruptcy proceedings or as the Company becomes smaller upon its exit from the Disney Store business; and
- general business conditions, economic uncertainty or slowdown, including the recent significant slowdown in the overall economy.

Some of these factors are beyond our control. It is difficult to assess the impact that the general economic downturn will have on consumer spending and our financial results. However, we believe there is risk that the economic slowdown could result in reduced spending by our customers, which could reduce our revenues and our cash flows from operating activities from those that otherwise would have been generated. In addition, steps that we take to limit cash expenditures, such as delaying the purchase of inventory, may not be successful or could delay the arrival of merchandise for future selling seasons, which could reduce our net sales or profitability. If we are unable to generate sufficient cash flow, we may not be able to fund our ongoing operations, anticipated exit costs associated with the wind-down of the Disney Store business, planned capital expenditures and debt repayment obligations and may be required to access additional sources of liquidity.

Recent turmoil in the credit markets may make it difficult for us to obtain additional financing on commercially reasonable terms or at all. If we obtain additional financing, it may be on terms and with pricing significantly less favorable than our current financing arrangements. An inability to access, if necessary, additional sources of liquidity could materially adversely affect our ability to operate our business, our growth, our financial condition and our results of operations.

In fiscal 2007, we experienced deterioration in our profitability. If we are unable to anticipate and respond to merchandise trends, we may continue to suffer adverse business consequences.

We have experienced deterioration in our sales trends and profitability. Our continued success will depend in part on our ability to anticipate and respond to fashion trends and consumer preferences. Our design, manufacturing and distribution process generally takes up to one year, during which time fashion trends and consumer preferences may change. For the majority of fiscal 2007 our merchandise did not resonate with consumers and, as a result, our sales declined and inventory levels were too high. Failure to anticipate, identify or respond to future fashion trends may continue to adversely affect customer acceptance of our products or require substantial markdowns, which could continue to have a material adverse effect on our business.

Management and the Board have re-evaluated the Company's inventory strategy and have taken steps to reduce inventory levels and shortened inventory cycle periods, where possible. These steps may not be sufficient to prevent further markdowns and erosion of our profitability, particularly in the current difficult economic climate, and our results of operations could be materially and adversely affected.

Hoop may not be able to obtain confirmation of the plan of liquidation.

To complete the wind-down of the Disney Store business under the protection of the bankruptcy court, Hoop, like any debtor, must obtain approval of a plan of liquidation from its creditors and confirmation of the plan through the bankruptcy court. This process requires Hoop to solicit and obtain creditor acceptances of the proposed plan, meet certain statutory requirements with respect to the adequacy of disclosure concerning the proposed plan, and fulfill other statutory conditions relating to plan confirmation. Such a process is complex, involves numerous parties, and requires disclosure to and voting by creditors and confirmation by the bankruptcy court. It is possible that creditors would seek to file and confirm an alternative plan. Further, it is possible that a trustee could be appointed or the case converted to a liquidation under Chapter 7 of the Bankruptcy Code.

If Hoop does not reach an agreement with Disney, it is likely that the Disney Store business will be liquidated in the bankruptcy proceeding. In this case, Disney may seek to term