



Deal Overview

Consortium: Bain Capital Partners LLC, Kohlberg Kravis Roberts & Co., L.P. and Vornado Realty Trust

In 2005, a consortium was formed to buy out Toys “R” Us at **\$26.75 per share**. This implied an offer value of **\$6.6B** and an **8.9x** EBITDA multiple, representing a premium of **8%** before the announcement and **39%** to the unaffected TOYS share price on Aug. 11, 2004. The last closing share price before the announcement was \$24.77 on 03/16/2005.

Sell Side Advisory

The Deal was announced on Thursday **03/17/2005**. With Credit Suisse and Duff & Phelps acting as the Sell side Advisor

Buy Side Advisory

Bank of America, Deutsche Bank, Citigroup



Deutsche Bank





History

1948

Founded by **Charles Lazarus** in Washington, D.C., Toys “R” Us was first marketed as a children’s furniture store in 1948. By 1957, the company was commonly known as **Toys “R” Us**.

1966

From 1966 onward, Toys “R” Us solidified its place as an American household staple by enlisting beloved athletes and celebrities in its marketing efforts to bring toys to life for kids. To expand nationally, the company was sold to Interstate Sales. Nine years later, Interstate Sales filed for **bankruptcy**, and Lazarus bought the company **back**.

1983

After repurchasing the company, Toys “R” Us expanded into retail clothing, creating the notable spin-off Kids “R” Us, and from that success, later created **Babies “R” Us**.

1990’s

By the early 1990s, Toys “R” Us began experiencing **heavy competition** from discount retailers such as Wal-Mart and Target. By 1998, Wal-Mart had **surpassed** Toys “R” Us as the top toy retailer in the nation. To deal with shrinking market share, **all** 146 Kids “R” Us stores had closed by 2003.

2005

→

In 2004, the company announced a **strategic evaluation** of all its assets to determine how to proceed, given pressure from shareholders and recent underperformance. This led to the hiring of Credit Suisse First Boston to evaluate its assets and began to entertain bids from potential buyers for divestitures. However, through the competitive process, it was determined that selling Toys “R” Us as a **whole** would be the best approach to maintain the **most value**.



Deal Rationale – The Dream Team

As opportunistic investors, the consortium saw a stagnant but cash-flow-generating business, with Toys “R” Us netting approximately **\$600–700 million** in unadjusted EBITDA annually. To regain market share, they sought to acquire more companies in the space and capitalize on the fact that the Babies “R” Us segment was growing **YoY**. Eventually, that thesis would come to fruition with the closure of several Toys “R” Us stores that were transformed into Babies “R” Us stores. Even if the thesis fell through, they still had copious amounts of valuable real estate (hence the importance of Vornado Realty Trust in the consortium). The consortium was not the only one to recognize this, as Toys “R” Us received offers for the company’s real estate assets from companies like Lowe’s and Home Depot. Through the LBO analysis, if all went according to plan, the consortium could have expected anywhere between **21 – 35% IRR,*** even if there was multiple contraction.

*“We became interested in Toys “R” Us principally because it has lots and lots of terrific real estate, in the U.S. and abroad”
– Seth Roth(CEO of Vornado Trust in 05’)*

Bain Capital Turnaround Specialists

In 2002, Bain Capital led a consortium for the buyout of Burger King at \$1.5 billion, Sealy Corporation for a majority stake at \$833 million, Domino’s Pizza for \$1.1 billion, and more.

KKR Financial Engineering Experts

Experienced in large LBOs with creative financing prowess. Famous \$25B takeover of RJR Nabisco, buyout of Safeway Stores.

Vornado Seasoned Real Estate Investors

they came in with decades of experience and notable deals such as Charles E. Smith Commercial Realty for \$1.5B and gaining control over sites like 731 Lexington Ave (modern-day Bloomberg HQ).

*These are based off continuing assumptions, minimal MD&A to forecast 3FS. 21% IRR @ exit EBITDA of 7.0x and 35% IRR @ exit EBITDA of 9.0x



What Went Wrong?

Extreme Competition

Toys “R” Us was a uniquely positioned company with almost no directly comparable companies. While its competitors, such as Wal-Mart and Target, operated as diversified platforms, Toys “R” Us focused only on toys and baby apparel. With their volume of sales, discounters began to **price them out**.

Rapidly evolving consumer preferences

While the company had an online presence with Toysrus.com, the vast majority of its revenue came from **brick-and-mortar stores**. The shift to e-commerce happened too **slowly**, while consumer preferences changed **rapidly**. While Bain had the turnaround experience, how does one conduct a turnaround in a flat market experiencing consolidation amid a large structural **regime change**?

The Dangers of Debt

By the time the changes in the industry were understood, the damage was largely **done**. With the debt levels they carried, required interest payments rose to nearly **\$400M** per year, leaving barely any leeway for survival and certainly none to invest multi laterally and aggressively to keep up with competitors.* This was an integral focus in attempting to turn the tide. Their debt levels **exacerbated** their issues and ultimately stunted the possibility of any **outsized growth** needed to compete.

*They acquired Etoys.com, FAO Schwarz, and toys.com all within the **same** year however the competition from discount retailers ultimately outweighed the ROIs of these investments

Leveraged Buyout Model for Toys "R" Us

\$ mm except per share

Date announced 17-Mar-05

GENERAL INPUTS

Company name	Toys "R" Us
Ticker (if applicable)	TOY
Current share price (if applicable)	24.77
Latest closing share price date (f applicable)	3/17/2005
Circuit breaker:	OFF

SELECT FINANCIAL DATA / ASSUMPTIONS

EBITDA (LTM)	700.0
Gross Debt (input as a -)	(1,860)
Cash	2,203
Minimum cash desired	1,000
EV / LTM EBITDA multiple at exit	10.0x

USES OF FUNDS

Buyout of equity	6,600.0
Refinancing of oldco debt	1,860.0
Fees (transaction & financing)	189.9
Total Uses	8,649.9

SOURCES OF FUNDS

	EBITDA turns	\$ investment
Excess cash	1.72x	1,203.0
Revolver(Portion Drawn @ Close)	1.00x	700.0
European Working Cap Revolver	0.13x	89.6
Last Out Tranche	0.00x	0.0
CMBS Issuance	1.14x	800.8
Secured European Bridge Loan	1.43x	1,001.0
Senior Unsecured Bridge Loan	2.65x	1,855.0
Rolled Over Debt	2.71x	1,897.0
Mgmt rollover	0.00x	0.0
Sponsor equity(Bain,KKR,Vornado)	1.58x	1,103.5
Total Sources	12.36x	8,649.9

INCOME STATEMENT

Fiscal year	Historical				Forecasts				
	2003A	2004A	2005A	2006P	2007P	2008P	2009P	2010P	
Fiscal year end date	2/1/03	1/31/04	1/29/05	1/31/06	1/31/07	1/31/08	1/31/09	1/31/10	
Revenue	11,305.0	11,320.0	11,100.0	11,211.0	11,379.2	11,606.7	11,896.9	12,253.8	
Cost of sales (enter as -)	(7,799.0)	(7,646.0)	(7,506.0)	(7,573.1)	(7,632.3)	(7,766.7)	(7,932.8)	(8,135.2)	
Gross Profit	3,506.0	3,674.0	3,594.0	3,637.9	3,746.9	3,840.1	3,964.1	4,118.6	
Selling, general & administrative (enter	(2,724.0)	(3,089.0)	(2,936.0)	(2,852.6)	(2,946.6)	(2,951.6)	(2,984.9)	(3,059.9)	
Depreciation & Amortization	(339.0)	(368.0)	(354.0)	(309.1)	(288.2)	(263.8)	(240.9)	(217.4)	
Operating profit (EBIT)	443.0	217.0	304.0	476.2	512.2	624.8	738.3	841.3	
Interest income & Other Non operating	9.0	18.0	19.0	9.0	8.7	8.3	8.4	8.7	
Interest expense (enter as -)	(119.0)	(142.0)	(130.0)	(372.1)	(372.6)	(393.9)	(393.1)	(384.5)	
Pretax profit	333.0	93.0	193.0	113.1	148.3	239.2	353.6	465.6	
Taxes (enter expense as -) (enter Bene	(120.0)	(30.0)	59.0	(38.6)	(50.6)	(81.7)	(120.7)	(159.0)	
Net income	213.0	63.0	252.0	74.5	97.6	157.5	232.8	306.6	

INITIAL VALUATION

Select a valuation approach:

	Approach 2	Approach 1	Approach 2
	Explicit offer/share	Explicit EBITDA	Explicit offer/share
LTM EBITDA	700.0	700.0	700.0
EV / LTM EBITDA	8.9x	10.0x	8.9x
Enterprise value	6,257.0	7,000.0	6,257.0
Less: Gross Debt (latest filing)	(1,860.0)	(1,860.0)	(1,860.0)
Plus: Cash (latest filing)	2,203.0	2,203.0	2,203.0
Offer value	6,600.0	7,343.0	6,600.0
Diluted shares outstanding	246.7	246.7	246.7
Offer value / per share	26.75	29.76	26.75
% Premium / discount	8%	20%	8%

FEES

	% fees	Fee	Term	Fee amort / year
Financing fees				
Revolver(Portion [1.5%	10.5	5 yrs	2.1
European Working	2.0%	1.8	5 yrs	0.4
Last Out Tranche	1.5%	0.0	5 yrs	0.0
CMBS Issuance	1.5%	12.0	5 yrs	2.4
Secured Europear	1.5%	15.0	5 yrs	3.0
Senior Unsecured	1.0%	18.6	5 yrs	3.7
Financing fees		57.9		11.6
Trans. fees				
	% of offer value	Fee		
	2.0%	132.0		

<u>EBITDA reconciliation</u>								
EBIT (GAAP)	443.0	217.0	304.0	476.2	512.2	624.8	738.3	841.3
Depreciation and amortization	339.0	368.0	354.0	309.1	288.2	263.8	240.9	217.4
Stock based compensation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Restructuring and other nonrecurring	0.0	63.0	4.0	4.0	4.0	4.0	4.0	4.0
EBITDA	782.0	648.0	662.0	789.3	804.3	892.5	983.2	1,062.7

Growth rates & margins

Revenue growth		0.13%	-1.94%	1.0%	1.5%	2.0%	2.5%	3.0%	Step 0.5%
Gross profit as % of sales	31.0%	32.5%	32.4%	32.4%	32.9%	33.1%	33.3%	33.6%	0.5%
SG&A margin	24.1%	27.3%	26.5%	25.4%	25.9%	25.4%	25.1%	25.0%	(0.5%)
Tax rate	36.0%	32.3%	(30.6%)	34.1%	34.1%	34.1%	34.1%	34.1%	0.0%

WORKING CAPITAL

	Historical			Forecasts				
Fiscal year	2004A	2005A	2006P	2007P	2008P	2009P	2010P	
<i>Fiscal year end date</i>	1/31/04	1/29/05	1/31/06	1/31/07	1/31/08	1/31/09	1/31/10	
Accounts receivable, EOP	146.0	153.0	154.5	156.8	160.0	164.0	168.9	
AR as % of sales	1.3%	1.4%	1.4%	1.4%	1.4%	1.4%	1.4%	
Inventory, EOP	2,094.0	1,884.0	1,900.9	1,915.7	1,949.4	1,991.1	2,041.9	
Inventory as % of COGS	27.4%	25.1%	25.1%	25.1%	25.1%	25.1%	25.1%	
Other current assets, EOP	962.0	636.0	642.4	652.0	665.0	681.7	702.1	
Other current assets as % of sales	8.5%	5.7%	5.7%	5.7%	5.7%	5.7%	5.7%	
Accounts payable, EOP	1,022.0	1,023.0	1,032.2	1,040.2	1,058.5	1,081.2	1,108.8	
AP as % of COGS	13.4%	13.6%	13.6%	13.6%	13.6%	13.6%	13.6%	
Accrued expenses , EOP	866.0	881.0	889.8	903.2	921.2	944.3	972.6	
As % of sales	7.7%	7.9%	7.9%	7.9%	7.9%	7.9%	7.9%	
<i>Net Working Capital</i>	<i>1,314.0</i>	<i>769.0</i>	<i>775.8</i>	<i>781.2</i>	<i>794.7</i>	<i>811.4</i>	<i>831.6</i>	

LONG LIVED ASSETS

	Historical			Forecasts				
Fiscal year	2004A	2005A	2006P	2007P	2008P	2009P	2010P	
<i>Fiscal year end date</i>	1/31/04	1/29/05	1/31/06	1/31/07	1/31/08	1/31/09	1/31/10	
PP&E	4,743.0	4,439.0	4,339.0	4,246.2	4,176.1	4,129.5	4,106.2	4,106.2
Capital expenditures	385.0	221.0	228.0	224.5	226.3	225.4	225.8	225.6
Depreciation	(337.0)	(359.8)	(345.8)	(317.3)	(296.4)	(272.0)	(249.1)	(225.6)
Capex as a % of revenue	3.4%	2.0%	2.1%	2.1%	2.1%	2.1%	2.1%	2.1%
Depreciation as a % of capex	87.5%	162.8%	151.7%	141.3%	131.0%	120.7%	110.3%	100.0%
Costs of Computer Software	243.0	284.0	316.8	357.8	398.8	439.8	480.8	521.8
Purchases	10.0	41.0	41.0	41.0	41.0	41.0	41.0	41.0

Smoothing?

Yes

(10%)

Amortization	(2.0)	(8.2)	(8.2)	(8.2)	(8.2)	(8.2)	(8.2)	(8.2)
Purchases as a % of revenue	0.1%	0.4%	0.4%	0.4%	0.4%	0.4%	0.3%	0.3%
Amortization as straight lined	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%
Goodwill and other assets	916.0	621.0	553.0	553.0	553.0	553.0	553.0	553.0
Other liabilities	282.0	505.0	481.0	422.7	422.7	422.7	422.7	422.7

CASH FLOW STATEMENT

<i>Fiscal year</i>	2006P	2007P	2008P	2009P	2010P
<i>Fiscal year end date</i>	<i>1/31/06</i>	<i>1/31/07</i>	<i>1/31/08</i>	<i>1/31/09</i>	<i>1/31/10</i>
Net income	74.5	97.6	157.5	232.8	306.6
Depreciation and amortization (Add Back)	309.1	288.2	263.8	240.9	217.4
Stock based compensation(Add Back)	0.0	0.0	0.0	0.0	0.0
Changes in net working capital(subtract)	(6.8)	(5.4)	(13.5)	(16.7)	(20.3)
Other assets & liabilities	(58.3)	0.0	0.0	0.0	0.0
Cash from operating activities	332.0	391.2	434.8	490.4	544.2
Capital expenditures	(224.5)	(226.3)	(225.4)	(225.8)	(225.6)
Purchases of intangible assets and capitalized software development costs	(41.0)	(41.0)	(41.0)	(41.0)	(41.0)
Cash from investing activities	(265.5)	(267.3)	(266.4)	(266.8)	(266.6)
Required debt principal payments	(289.3)	(275.4)	(262.2)	(249.7)	(237.8)
Pre-revolver cash flows	(222.8)	(151.4)	(93.8)	(26.0)	39.9
Revolver Proceeds/(Payments)	222.8	75.7	84.7	55.4	7.8
Post-revolver cash flows	0.0	(75.7)	(9.0)	29.4	47.6
Discretionary paydowns	0.0	0.0	0.0	0.0	0.0
Net change in cash during period	0.0	(75.7)	(9.0)	29.4	47.6

CASH & DEBT

<i>Fiscal year</i>	2003A	2004A	2005A	2006P	2007P	2008P	2009P	2010P
<i>Fiscal year end date</i>	<i>2/1/03</i>	<i>1/31/04</i>	<i>1/29/05</i>	<i>1/31/06</i>	<i>1/31/07</i>	<i>1/31/08</i>	<i>1/31/09</i>	<i>1/31/10</i>
Cash, BOP				1,000.0	1,000.0	924.3	915.3	944.6
Increases / (decreases)				0.0	(75.7)	(9.0)	29.4	47.6
Cash, EOP	1,083.0	2,003.0	2,203.0	1,000.0	924.3	915.3	944.6	992.2
Interest rate on cash		1.17%	0.90%	0.90%	0.90%	0.90%	0.90%	0.90%
Interest income		18.0	19.0	9.0	8.7	8.3	8.4	8.7
Revolver								
Cash, BOP				1,000.0	1,000.0	924.3	915.3	944.6
Less: Minimum cash desired				(1,000.0)	(1,000.0)	(1,000.0)	(1,000.0)	(1,000.0)
Equals: Excess cash at BOP				0.0	0.0	(75.7)	(84.7)	(55.4)
Plus: Free cash flows generated during period				(222.8)	(75.7)	(9.0)	29.4	47.6
Cash Surplus/(Deficit)				(222.8)	(75.7)	(84.7)	(55.4)	(7.8)

Domestic Revolver, BOP		700.0	922.8	998.5	1,083.2	1,138.6
Draws/Repayments		222.8	75.7	84.7	55.4	7.8
Revolver, EOP		922.8	998.5	1,083.2	1,138.6	1,146.3
Maximum availability	<u>% Inventory</u>	1,235.6	1,245.2	1,267.1	1,294.2	1,327.2
Compliance check	65%	In Compliance	In Compliance	In Compliance	In Compliance	In Compliance
Remaining cash (Surplus/Deficit)		0.0	0.0	0.0	0.0	0.0
<u>International Working Cap Revolver</u>						
European Working Cap, BOP		89.6	89.6	89.6	89.6	89.6
Draw/ Repayment		0.0	0.0	0.0	0.0	0.0
European Working Cap, EOP		89.6	89.6	89.6	89.6	89.6
Maximum availability	350	350	350	350	350	350
Compliance check		In Compliance	In Compliance	In Compliance	In Compliance	In Compliance
<u>Last Out Tranche (Revolver)</u>						
Last Out Tranche (Revolver), BOP		0	0.0	0.0	0.0	0.0
Draw/ Repayment		0.0	0.0	0.0	0.0	0.0
European Working Cap, EOP		0.0	0.0	0.0	0.0	0.0
Maximum availability	150	150.0	150.0	150.0	150.0	150.0
Compliance check						
<u>CMBS</u>						
CMBS, BOP		800.8	761	723	687	652
Mandatory Interest Payment \$		40	38	36	34	33
CMBS, EOP		761	723	687	652	620
Mandatory paydown (% of original)		5.00%	5.00%	5.00%	5.00%	5.00%
<u>Secured European Bridge Loan</u>						
Secured European Bridge Loan, BOP		1,001.0	951.0	903.4	858.2	815.3
Mandatory Amortization		50	48	45	43	41
Cash Sweep		0.0	0.0	0.0	0.0	0.0
Secured European Bridge Loan, EOP		951	903	858	815	775
Mandatory Paydown as(% of OG)	Available Cash	5.00%	5%	5.00%	5.00%	5.00%
Cash Available for Cash sweep	100.00%	0	0	0	0	0
<u>Unsecured European Bridge Loan</u>						
Unsecured European Bridge Loan, BOP		1,855.0	1,762.3	1,674.1	1,590.4	1,510.9
Mandatory Amortization		93	88	84	80	76
Cash Sweep		0.0	0.0	0.0	0.0	0.0
Unsecured European Bridge Loan, EOP		1,762.3	1,674.1	1,590.4	1,510.9	1,435.4
Mandatory Paydown as(% of OG)	Available Cash	5.00%	5%	5%	5%	5%
Cash Available for Cash sweep	100.00%	0.00	0.00	0.00	0.00	0.00
<u>Rolled Over Debt</u>						
Rolled Over Debt , BOP		1897	1,802.2	1,712.0	1,626.4	1,545.1
Mandatory Amortization		95	90	86	81	77
Cash Sweep		0.0	0.0	0.0	0.0	0.0
Rolled Over Debt , EOP		1,802.2	1,712.0	1,626.4	1,545.1	1,467.9
Mandatory Paydown as(% of OG)	Available Cash	5.00%	5.00%	5.00%	5.00%	5.00%
Cash Available for Cash sweep	100.00%	0.0	0.0	0.0	0.0	0.0
<u>Capitalized financing fees</u>						
Capitalized financing fees, BOP		58	46.30	34.72	23.15	11.57

Amortization	(12)	(12)	(12)	(12)	(12)
Capitalized financing fees, EOP	46.30	34.72	23.15	11.57	0.00

INTEREST EXPENSE

Fiscal year	2003A	2004A	2005A	2006P	2007P	2008P	2009P	2010P
Fiscal year end date	2/1/03	1/31/04	1/29/05	1/31/06	1/31/07	1/31/08	1/31/09	1/31/10
3-Month LIBOR Rate (bps)				230	245	300	320	330
	<u>LIBOR Spread</u>	<u>LIBOR floor</u>						
Domestic Revolver	L + 3%	1.0%		41.0	50.0	59.8	66.1	69.1
International Revolver	L + 2%	1.0%		3.6	3.8	4.3	4.4	4.5
CMBS	L + 1%	1.0%		28.1	27.8	30.3	30.1	29.3
Senior Secured Bridge Loan	L + 2%	1.0%		37.1	36.6	39.6	39.3	38.2
Senior Unsecured Bridge Loan	L + 5%	1.0%		136.6	132.3	134.7	131.0	126.0
Rolled Over Debt	L + 5%	1.0%		125.8	122.1	125.2	122.1	117.5

EXIT VALUATION

Assumed exit on January 31, 2010

	Step	7.0x	7.5x	8.0x	8.5x	9.0x
EBITDA multiple at exit	0.5x					
EBITDA at exit		1,062.7	1,062.7	1,062.7	1,062.7	1,062.7
Enterprise value		7,439.0	7,970.3	8,501.7	9,033.1	9,564.4
<u>Net debt:</u>						
Domestic Revolver		1,146.3	1,146.3	1,146.3	1,146.3	1,146.3
International Revolver		89.6	89.6	89.6	89.6	89.6
CMBS		619.6	619.6	619.6	619.6	619.6
Senior Secured Bridge Loan		774.6	774.6	774.6	774.6	774.6
Senior Unsecured Bridge Loan		1,435.4	1,435.4	1,435.4	1,435.4	1,435.4
Rolled Over Debt		1,467.9	1,467.9	1,467.9	1,467.9	1,467.9
Cash		(992.2)	(992.2)	(992.2)	(992.2)	(992.2)
Equity value		2,897.9	3,429.2	3,960.6	4,491.9	5,023.3
Sponsor equity	<u>Initial equity inv.</u>	1,103	2,897.9	3,429.2	4,491.9	5,023.3
Mgmt equity	<u>% ownership</u>	0	0.0	0.0	0.0	0.0
Pref. stock	<u>Fully diluted</u>		0.0	0.0	0.0	0.0
Sub. Note			0.0	0.0	0.0	0.0

RETURNS

	Cash-on-cash	IRR	Initial	2006P	2007P	2008P	2009P	2010P
Sponsor's Equity at exit EBITDA multiple of:								
7.0x	2.63x	21%	(1,103.5)	0.0	0.0	0.0	0.0	2,897.9
7.5x	3.11x	25%	(1,103.5)	0.0	0.0	0.0	0.0	3,429.2
8.0x	3.59x	29%	(1,103.5)	0.0	0.0	0.0	0.0	3,960.6
8.5x	4.07x	32%	(1,103.5)	0.0	0.0	0.0	0.0	4,491.9
9.0x	4.55x	35%	(1,103.5)	0.0	0.0	0.0	0.0	5,023.3