

Michaels Companies, Inc.  
Form 10-Q  
August 28, 2015  
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

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FORM 10-Q

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

For the quarterly period ended August 1, 2015

Commission file number 001-36501

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THE MICHAELS COMPANIES, INC.

A Delaware Corporation

IRS Employer Identification No. 37-1737959

8000 Bent Branch Drive

Irving, Texas 75063

(972) 409-1300

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The Michaels Companies, Inc. (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.

The Michaels Companies, Inc. has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

The Michaels Companies, Inc. is a non-accelerated filer.

The Michaels Companies, Inc. is not a shell company (as defined in Rule 12b-2 of the Exchange Act).

As of August 21, 2015, 207,999,586 shares of The Michaels Companies, Inc.'s common stock were outstanding.

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THE MICHAELS COMPANIES, INC.

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## Part I—FINANCIAL INFORMATION

## Item 1. Financial Statements

## THE MICHAELS COMPANIES, INC.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands, except per share data)

(Unaudited)

|   | 13 Weeks Ended    |                   | 26 Weeks Ended    |                   |
|---|-------------------|-------------------|-------------------|-------------------|
|   | August 1,<br>2015 | August 2,<br>2014 | August 1,<br>2015 | August 2,<br>2014 |
| Net sales   | \$ 984,270        | \$ 948,150        | \$ 2,061,870      | \$ 2,000,198      |
| Cost of sales and occupancy expense                             | 610,949           | 590,953           | 1,246,752         | 1,214,258         |
| Gross profit  | 373,321           | 357,197           | 815,118           | 785,940           |
| Selling, general and administrative                             | 275,699           | 272,888           | 571,270           | 557,871           |
| Related party expenses  | —                 | 32,354            | —                 | 35,682            |
| Store pre-opening costs   | 1,040             | 1,063             | 3,284             | 2,295             |
| Operating income  | 96,582            | 50,892            | 240,564           | 190,092           |
| Interest expense  | 34,311            | 60,635            | 72,127            | 117,726           |
| Losses on early extinguishment of debt and<br>refinancing costs | 6,072             | 67,980            | 6,072             | 67,980            |
| Other expense (income), net                                     | (136)             | (161)             | 59                | (210)             |
| Income (loss) before income taxes                               | 56,335            | (77,562)          | 162,306           | 4,596             |
| Provision for income taxes                                      | 20,624            | (28,919)          | 59,857            | 7,825             |
| Net income (loss)   | \$ 35,711         | \$ (48,643)       | \$ 102,449        | \$ (3,229)        |
| Other comprehensive income (loss), net of tax:                  |                   |                   |                   |                   |
| Foreign currency translation adjustment and other               | (7,223)           | 1,801             | (2,907)           | 677               |
| Comprehensive income (loss)                                     | \$ 28,488         | \$ (46,842)       | \$ 99,542         | \$ (2,552)        |
| Earnings (loss) per share:                                      |                   |                   |                   |                   |
| Basic   | \$ 0.17           | \$ (0.26)         | \$ 0.49           | \$ (0.02)         |
| Diluted   | \$ 0.17           | \$ (0.26)         | \$ 0.49           | \$ (0.02)         |
| Weighted-average shares outstanding:                            |                   |                   |                   |                   |
| Basic   | 206,941           | 184,927           | 206,283           | 180,024           |
| Diluted   | 209,691           | 184,927           | 209,541           | 180,024           |

See accompanying notes to consolidated financial statements.

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## THE MICHAELS COMPANIES, INC.

## CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

(Unaudited)

|  | August 1,<br>2015 | January 31,<br>2015 | August 2,<br>2014 |
|--|-------------------|---------------------|-------------------|
| <b>ASSETS</b>                                  |                   |                     |                   |
| Current Assets:                                |                   |                     |                   |
| Cash and equivalents                           | \$ 70,368         | \$ 378,295          | \$ 89,503         |
| Merchandise inventories                        | 1,073,722         | 958,171             | 936,892           |
| Prepaid expenses and other                     | 83,244            | 84,894              | 100,698           |
| Deferred income taxes                          | 38,473            | 38,345              | 37,103            |
| Income tax receivables                         | 53,499            | 2,418               | 75,481            |
| Total current assets                           | 1,319,306         | 1,462,123           | 1,239,677         |
| Property and equipment, at cost                | 1,632,755         | 1,579,446           | 1,530,972         |
| Less accumulated depreciation and amortization | (1,238,069)       | (1,193,074)         | (1,165,351)       |
| Property and equipment, net                    | 394,686           | 386,372             | 365,621           |
| Goodwill                                       | 94,290            | 94,290              | 94,290            |
| Debt issuance costs, net                       | 33,800            | 40,613              | 47,933            |
| Deferred income taxes                          | 20,203            | 20,245              | 23,618            |
| Other assets                                   | 1,673             | 1,638               | 1,775             |
| Total assets                                   | \$ 1,863,958      | \$ 2,005,281        | \$ 1,772,914      |

## LIABILITIES AND STOCKHOLDERS' DEFICIT

## Current Liabilities:

|                                   |            |            |            |
|-----------------------------------|------------|------------|------------|
| Accounts payable                  | \$ 418,745 | \$ 447,165 | \$ 317,824 |
| Accrued liabilities and other     | 349,777    | 391,997    | 335,739    |
| Current portion of long-term debt | 48,900     | 24,900     | 47,900     |
| Income taxes payable              | 873        | 25,570     | 1,241      |
| Total current liabilities         | 818,295    | 889,632    | 702,704    |
| Long-term debt                    | 2,931,008  | 3,124,374  | 3,316,909  |
| Deferred income taxes             | 16,180     | 9,580      | 1,163      |
| Other liabilities                 | 91,032     | 93,220     | 86,186     |
| Total liabilities                 | 3,856,515  | 4,116,806  | 4,106,962  |

## Commitments and contingencies

## Stockholders' Deficit:

|  |         |         |         |
|--|---------|---------|---------|
| Common Stock, \$0.06775 par value, 350,000 shares authorized;<br>208,011 shares issued and outstanding at August 1, 2015;<br>205,803 shares issued and outstanding at January 31, 2015; and<br>203,952 shares issued and outstanding at August 2, 2014 | 13,952  | 13,799  | 13,768  |
| Additional paid-in-capital   | 577,104 | 557,831 | 545,311 |

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|   |              |              |              |
|---|--------------|--------------|--------------|
| Accumulated deficit                         | (2,568,901)  | (2,671,350)  | (2,894,002)  |
| Accumulated other comprehensive loss        | (14,712)     | (11,805)     | 875          |
| Total stockholders' deficit                 | (1,992,557)  | (2,111,525)  | (2,334,048)  |
| Total liabilities and stockholders' deficit | \$ 1,863,958 | \$ 2,005,281 | \$ 1,772,914 |

See accompanying notes to consolidated financial statements.

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## THE MICHAELS COMPANIES, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

|  | 26 Weeks Ended    |                   |
|--|-------------------|-------------------|
|  | August 1,<br>2015 | August 2,<br>2014 |
| Cash flows from operating activities:  |                   |                   |
| Net income (loss)  | \$ 102,449        | \$ (3,229)        |
| Adjustments to reconcile net income (loss) to net cash used in operating activities: |                   |                   |
| Depreciation and amortization  | 55,949            | 53,173            |
| Share-based compensation   | 6,225             | 9,663             |
| Debt issuance costs amortization   | 4,366             | 5,602             |
| Accretion of long-term debt, net   | (66)              | (431)             |
| Deferred income taxes  | 6,514             | 4,844             |
| Losses on early extinguishment of debt and refinancing costs                         | 6,072             | 67,980            |
| Excess tax benefits from share-based compensation                                    | (12,952)          | (479)             |
| Other  | —                 | (23)              |
| Changes in assets and liabilities:   |                   |                   |
| Merchandise inventories  | (115,198)         | (37,254)          |
| Prepaid expenses and other   | 1,659             | (5,238)           |
| Other assets   | (86)              | (1,731)           |
| Accounts payable   | (10,686)          | (37,624)          |
| Accrued interest   | 89                | (45,689)          |
| Accrued liabilities and other  | (53,634)          | (30,603)          |
| Income taxes   | (75,779)          | (102,390)         |
| Other liabilities  | (2,067)           | (1,307)           |
| Net cash used in operating activities  | (87,145)          | (124,736)         |
| Cash flows used in investing activities:   |                   |                   |
| Additions to property and equipment  | (63,241)          | (64,770)          |
| Cash flows from financing activities:  |                   |                   |
| Payment of PIK notes   | (184,467)         | (443,542)         |
| Borrowings on restated revolving credit facility                                     | 24,000            | 23,000            |
| Borrowings on restated term loan credit facility                                     | —                 | 845,750           |
| Payments on restated term loan credit facility                                       | (12,450)          | (8,200)           |
| Payment of 2018 senior notes   | —                 | (1,057,208)       |
| Issuance of 2020 senior subordinated notes   | —                 | 255,000           |
| Issuance of common stock   | —                 | 445,660           |
| Payment of debt issuance costs   | —                 | (10,900)          |
| Payment of dividends   | (443)             | (480)             |
| Change in cash overdraft   | (9,832)           | (8,070)           |
| Proceeds from stock options exercised  | 32,521            | 6,243             |

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|  |           |           |
|--|-----------|-----------|
| Common stock repurchased                                     | (19,822)  | (7,587)   |
| Excess tax benefits from share-based compensation            | 12,952    | 479       |
| Net cash (used in) provided by financing activities          | (157,541) | 40,145    |
| Net change in cash and equivalents                           | (307,927) | (149,361) |
| Cash and equivalents at beginning of period                  | 378,295   | 238,864   |
| Cash and equivalents at end of period                        | \$ 70,368 | \$ 89,503 |
| See accompanying notes to consolidated financial statements. |           |           |

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THE MICHAELS COMPANIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. BASIS OF PRESENTATION

All expressions of the “Company”, “us”, “we”, “our”, and all similar expressions are references to The Michaels Companies, Inc. and our consolidated, wholly-owned subsidiaries, unless otherwise expressly stated or the context otherwise requires. Our consolidated financial statements include the accounts of The Michaels Companies, Inc. and our wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated.

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. Therefore, these financial statements should be read in conjunction with our annual report on Form 10-K for the fiscal year ended January 31, 2015 filed with the Securities and Exchange Commission (“SEC”) pursuant to section 13 or 15(d) under the Securities Exchange Act of 1934. In the opinion of management, all adjustments (consisting of normal recurring accruals and other items) considered necessary for a fair presentation have been included.

We report on the basis of a 52- or 53-week fiscal year, which ends on the Saturday closest to January 31. All references to fiscal year mean the year in which that fiscal year began. References to “fiscal 2015” relate to the 52 weeks ended January 30, 2016 and references to “fiscal 2014” relate to the 52 weeks ended January 31, 2015. In addition, all references to “the second quarter of fiscal 2015” relate to the 13 weeks ended August 1, 2015 and all references to “the second quarter of fiscal 2014” relate to the 13 weeks ended August 2, 2014. Finally, all references to “the six months ended August 1, 2015” relate to the 26 weeks ended August 1, 2015 and all references to “the six months ended August 2, 2014” relate to the 26 weeks ended August 2, 2014. Because of the seasonal nature of our business, the results of operations for the 13 and 26 weeks ended August 1, 2015 are not indicative of the results to be expected for the entire year.

Recent Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2015-03, “Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs” (“ASU 2015-03”). ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. Amortization of the costs will continue to be reported as interest expense. ASU 2015-03 is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period and is to be applied retrospectively, with early application permitted. As of August 1, 2015, the reduction to our long-term assets and debt would be approximately \$29 million. We are currently evaluating the requirements of the standard to determine when we will adopt and implement its provisions.

In April 2015, the FASB issued ASU 2015-05, “Intangibles — Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement” (“ASU 2015-05”). ASU 2015-05 provides guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The new guidance does not change the accounting for a customer’s accounting for service contracts. ASU 2015-05 is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period. We are currently

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evaluating the impact, if any, of the adoption of this new standard on our consolidated financial statements and related disclosures.

In May 2014, the FASB issued ASU No. 2014-09, “Revenue from Contracts with Customers” (“ASU 2014-09”). ASU 2014-09 supersedes the revenue recognition requirements in “Revenue Recognition (Topic 605)”, and requires entities to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. In July 2015, the FASB decided to delay the effective date of ASU 2014-09 by one year. ASU 2014-09 is therefore now effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The standard is to be applied retrospectively, with early application permitted for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. We are evaluating the new standard, but do not anticipate a material impact to the consolidated financial statements once implemented.

In July 2015, the FASB issued ASU No. 2015-11, “Inventory (Topic 330): Simplifying the Measurement of Inventory” (“ASU 2015-11”). ASU 2015-11 provides guidance for the subsequent measurement of inventory and requires that inventory that is measured using average cost be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. When evidence exists that the net realizable value of inventory is lower than its cost, the difference will be recognized as a loss in earnings in the period in which it occurs. ASU 2015-11 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period and is to be applied prospectively, with early application permitted. We are currently evaluating the impact of the adoption of this new standard on our consolidated financial statements and related disclosures.

## 2. FAIR VALUE MEASUREMENTS

As defined in Accounting Standards Codification (“ASC”) 820, Fair Value Measurements (“ASC 820”), fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 establishes a three-level valuation hierarchy for fair value measurements. These valuation techniques are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect less transparent active market data, as well as internal assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1—Quoted prices for identical instruments in active markets;
- Level 2—Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose significant inputs are observable; and

- Level 3—Instruments with significant unobservable inputs.

The table below provides the carrying and fair values of our senior secured term loan facility (“Restated Term Loan Credit Facility”) and our 5.875% senior subordinated notes maturing in 2020 (“2020 Senior Subordinated Notes”) as of August 1, 2015. The fair values of our Restated Term Loan Credit Facility and our 2020 Senior Subordinated Notes were determined based on quoted market prices which are considered Level 2 inputs within the fair value hierarchy.

|                                    | Carrying<br>Value<br>(In thousands) | Fair<br>Value |
|------------------------------------|-------------------------------------|---------------|
| Restated term loan credit facility | \$ 2,441,648                        | \$ 2,446,704  |
| Senior subordinated notes          | 514,260                             | 538,050       |

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## 3. DEBT

Long-term debt consists of the following (in thousands):

|                                    | Interest Rate   | August 1,<br>2015 | January 31,<br>2015 | August 2,<br>2014 |
|------------------------------------|-----------------|-------------------|---------------------|-------------------|
| Restated term loan credit facility | Variable        | \$ 2,441,648      | \$ 2,453,770        | \$ 2,466,086      |
| Restated revolving credit facility | Variable        | 24,000            | —                   | 23,000            |
| Senior subordinated notes          | 5.875 %         | 514,260           | 514,654             | 514,873           |
| PIK notes                          | 7.50 % / 8.25 % | —                 | 180,850             | 360,850           |
| Total debt                         |                 | 2,979,908         | 3,149,274           | 3,364,809         |
| Less current portion               |                 | (48,900)          | (24,900)            | (47,900)          |
| Long-term debt                     |                 | \$ 2,931,008      | \$ 3,124,374        | \$ 3,316,909      |

Cash paid for interest totaled \$67.7 million and \$158.4 million for the 26 weeks ended August 1, 2015 and August 2, 2014, respectively.

## 7.50%/8.25% PIK Toggle Notes

On April 6, 2015, an irrevocable notice of redemption was delivered to the holders of the 7.50%/8.25% PIK Toggle Notes due 2018 (“PIK Notes”). Pursuant to the notice, the remaining \$180.9 million in principal of the PIK Notes was redeemed on May 6, 2015. In the second quarter of fiscal 2015, the Company recorded \$6.1 million of debt extinguishment costs, which consists of a 2% redemption premium and \$2.5 million of unamortized debt issuance costs. This final payment retired the PIK Notes and discharged the obligations under the indenture governing the PIK Notes.

## Restated Revolving Credit Facility

As of August 1, 2015, the borrowing base of our senior secured asset-based revolving credit facility (“Restated Revolving Credit Facility”) was \$650.0 million, of which Michaels Stores, Inc. (“MSI”) had \$564.0 million of unused borrowing capacity. Outstanding standby letters of credit, which reduce our borrowing base, totaled \$62.0 million as of August 1, 2015. There was \$24.0 million of outstanding borrowings under the Restated Revolving Credit Facility

as of August 1, 2015.

Debt Issuance Costs

Accumulated amortization of debt issuance costs was \$57.6 million, \$54.6 million, and \$50.8 million as of August 1, 2015, January 31, 2015 and August 2, 2014, respectively.

4. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following table includes detail regarding changes in the composition of accumulated other comprehensive income (loss) (in thousands):

|   | 13 Weeks Ended |                | 26 Weeks Ended |                |
|---|----------------|----------------|----------------|----------------|
|   | August 1, 2015 | August 2, 2014 | August 1, 2015 | August 2, 2014 |
| Beginning of period                               | \$ (7,489)     | \$ (926)       | \$ (11,805)    | \$ 198         |
| Foreign currency translation adjustment and other | (7,223)        | 1,801          | (2,907)        | 677            |
| End of period                                     | \$ (14,712)    | \$ 875         | \$ (14,712)    | \$ 875         |



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## 5. INCOME TAXES

Income tax expense totaled \$20.6 million in the second quarter of fiscal 2015 as compared to an income tax benefit of \$28.9 million in the second quarter of fiscal 2014. Income tax expense for the six months ended August 1, 2015 was \$59.9 million compared to \$7.8 million in the same period in the prior year. The increase in income tax expense in both periods was due to higher pre-tax income as compared to the same periods in the prior year. The current year income tax expense was partially offset by our assertion to indefinitely reinvest fiscal 2015 earnings of our Canadian subsidiary into our operations outside the U.S. Accordingly, we have not provided for U.S. federal or foreign income taxes, including withholding taxes, on fiscal 2015 earnings of our Canadian subsidiaries' undistributed earnings. However, if any portion were to be distributed, the related U.S. tax liability may be reduced by foreign income taxes paid on those earnings. We currently estimate our annualized effective tax rate for fiscal 2015 to be approximately 36.7%.

Cash paid for income taxes totaled \$116.7 million and \$106.2 million for the 26 weeks ended August 1, 2015 and August 2, 2014, respectively.

## 6. EARNINGS (LOSS) PER SHARE

Basic earnings per share is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding. Diluted earnings per share is computed by dividing income available to common stockholders by the weighted-average shares outstanding plus the potential dilutive impact from the exercise of stock options and restricted shares. Common equivalent shares are excluded from the computation if their effect is anti-dilutive. There were 0.4 million and 3.8 million anti-dilutive shares during the second quarters of fiscal 2015 and fiscal 2014, respectively. There were 0.3 million and 3.7 million anti-dilutive shares during the six months ended August 1, 2015 and August 2, 2014, respectively.

The following table presents a reconciliation of the diluted weighted-average shares (in thousands, except per share data):

|  | 13 Weeks Ended    |                   | 26 Weeks Ended    |                   |
|--|-------------------|-------------------|-------------------|-------------------|
|  | August 1,<br>2015 | August 2,<br>2014 | August 1,<br>2015 | August 2,<br>2014 |
| Numerator:                                     |                   |                   |                   |                   |
| Net income (loss)                              | \$ 35,711         | \$ (48,643)       | \$ 102,449        | \$ (3,229)        |
| Income related to vested restricted shares     | 150               | —                 | 438               | —                 |
| Income (loss) available to common stockholders | \$ 35,561         | \$ (48,643)       | \$ 102,011        | \$ (3,229)        |

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|  |         |           |         |           |
|--|---------|-----------|---------|-----------|
| Denominator:                             |         |           |         |           |
| Basic weighted-average shares            | 206,941 | 184,927   | 206,283 | 180,024   |
| Effect of dilutive securities:           |         |           |         |           |
| Stock options                            | 2,482   | —         | 2,957   | —         |
| Restricted shares                        | 268     | —         | 301     | —         |
| Dilutive weighted-average shares         | 209,691 | 184,927   | 209,541 | 180,024   |
|  |         |           |         |           |
| Basic earnings (loss) per common share   | \$ 0.17 | \$ (0.26) | \$ 0.49 | \$ (0.02) |
| Diluted earnings (loss) per common share | \$ 0.17 | \$ (0.26) | \$ 0.49 | \$ (0.02) |

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## 7. SEGMENTS AND GEOGRAPHIC INFORMATION

We consider our Michaels-U.S., Michaels-Canada and Aaron Brothers to be our operating segments for purposes of determining reportable segments based on the criteria of ASC 280, Segment Reporting (“ASC 280”). We determined that each of our operating segments have similar economic characteristics and meet the aggregation criteria set forth in ASC 280. Therefore, we combine our operating segments into one reporting segment.

Our net sales by country are as follows (in thousands):

|                    | 13 Weeks Ended    |                   | 26 Weeks Ended    |                   |
|--------------------|-------------------|-------------------|-------------------|-------------------|
|                    | August 1,<br>2015 | August 2,<br>2014 | August 1,<br>2015 | August 2,<br>2014 |
| Net Sales:         |                   |                   |                   |                   |
| United States      | \$ 896,004        | \$ 858,543        | \$ 1,879,264      | \$ 1,810,342      |
| Canada             | 88,266            | 89,607            | 182,606           | 189,856           |
| Consolidated Total | \$ 984,270        | \$ 948,150        | \$ 2,061,870      | \$ 2,000,198      |

Our chief operating decision makers evaluate historical operating performance and plan and forecast future periods’ operating performance based on operating income and earnings before interest, income taxes, depreciation, amortization and losses on early extinguishment of debt and refinancing costs (“EBITDA (excluding losses on early extinguishment of debt and refinancing costs)”). We believe these metrics more closely reflect the operating effectiveness of factors over which management has control. A reconciliation of EBITDA (excluding losses on early extinguishment of debt and refinancing costs) to net income (loss) is presented below (in thousands):

|   | 13 Weeks Ended    |                   | 26 Weeks Ended    |                   |
|---|-------------------|-------------------|-------------------|-------------------|
|   | August 1,<br>2015 | August 2,<br>2014 | August 1,<br>2015 | August 2,<br>2014 |
| Net income (loss)   | \$ 35,711         | \$ (48,643)       | \$ 102,449        | \$ (3,229)        |
| Interest expense  | 34,311            | 60,635            | 72,127            | 117,726           |
| Losses on early extinguishment of debt and refinancing costs                    | 6,072             | 67,980            | 6,072             | 67,980            |
| Provision for income taxes  | 20,624            | (28,919)          | 59,857            | 7,825             |
| Depreciation and amortization   | 28,004            | 26,546            | 55,949            | 53,173            |
| Other   | (57)              | (101)             | (180)             | (169)             |
| EBITDA (excluding losses on early extinguishment of debt and refinancing costs) | \$ 124,665        | \$ 77,498         | \$ 296,274        | \$ 243,306        |

## 8. CONTINGENCIES

### Rea Claim

On September 15, 2011, MSI was served with a lawsuit filed in the California Superior Court in and for the County of Orange (“Superior Court”) by four former store managers as a class action proceeding on behalf of themselves and certain former and current store managers employed by MSI in California. The lawsuit alleges that MSI improperly classified its store managers as exempt employees and as such failed to pay all wages, overtime, waiting time penalties and failed to provide accurate wage statements. The lawsuit also alleges that the foregoing conduct was in breach of various laws, including California’s unfair competition law. On December 3, 2013, the Superior Court entered an order certifying a class of approximately 200 members. MSI successfully removed the case to the United States District Court for the Central District of California and on May 8, 2014, the class was de-certified. As a result of the decertification, we have approximately 40 individual claims pending as well as a separate representative action pending in the California Superior Court in and for the County of San Diego brought on behalf of store managers throughout the state. We believe we have

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meritorious defenses and intend to defend the lawsuits vigorously. We do not believe the resolution of the lawsuits will have a material effect on our consolidated financial statements.

### Fair Credit Reporting Claim

On December 11, 2014, MSI was served with a lawsuit, *Christina Graham v. Michaels Stores, Inc.*, filed in the U.S. District Court for the District of New Jersey by a former associate. The lawsuit is a purported class action, bringing plaintiff's individual claims, as well as claims on behalf of a putative class of applicants who applied for employment with Michaels through an online application, and on whom a background check for employment was procured. The lawsuit alleges that MSI violated the Fair Credit Reporting Act ("FCRA") and the New Jersey Fair Credit Reporting Act by failing to provide the proper disclosure and obtain the proper authorization to conduct background checks. Since the initial filing, another named plaintiff joined the lawsuit, which was amended in February 2015, *Christina Graham and Gary Anderson v. Michaels Stores, Inc.*, with substantially similar allegations. The plaintiffs seek statutory and punitive damages as well as attorneys' fees and costs.

Following the filing of the *Graham* case in New Jersey, five additional purported class action lawsuits with six plaintiffs were filed, *Michele Castro and Janice Bercut v. Michaels Stores, Inc.*, filed in the U.S. District Court in the Northern District of Texas, *Michelle Bercut v. Michaels Stores, Inc.* filed in the Superior Court of California for Sonoma County, *Raini Burnside v. Michaels Stores, Inc.*, pending in the U.S. District Court in the Western District of Missouri, *Sue Gettings v. Michaels Stores, Inc.*, in the U.S. District Court in the Southern District of New York, and *Barbara Horton v. Michaels Stores, Inc.*, in the U.S. District Court in the Central District of California. All of the plaintiffs alleged violations of the FCRA. In addition, *Castro*, *Horton* and *Janice Bercut* also alleged violations of California's unfair competition law. The *Burnside*, *Horton* and *Gettings* lawsuits have been dismissed and an offer of judgment has been accepted in the *Castro* lawsuit and will be dismissed. The *Graham*, *Janice Bercut* and *Michelle Bercut* lawsuits were transferred by the U.S. Judicial Panel on Multidistrict Litigation for centralized pretrial proceedings to the District of New Jersey.

The Company intends to defend the remaining lawsuits vigorously. We cannot reasonably estimate the potential loss, or range of loss, related to the lawsuits, if any.

### Data Security Incident

Five putative class actions were filed against MSI relating to the January 2014 data breach. The plaintiffs generally alleged that MSI failed to secure and safeguard customers' private information including credit and debit card information, and as such, breached an implied contract, and violated the Illinois Consumer Fraud Act (and other states' similar laws) and are seeking damages including declaratory relief, actual damages, punitive damages, statutory damages, attorneys' fees, litigation costs, remedial action, pre and post judgment interest, and other relief as available. The cases are as follows: *Christina Moyer v. Michaels Stores, Inc.*, was filed on January 27, 2014; *Michael and Jessica Gouwens v. Michaels Stores, Inc.*, was filed on January 29, 2014; *Nancy Maize and Jessica Gordon v. Michaels Stores, Inc.*, was filed on February 21, 2014; and *Daniel Ripes v. Michaels Stores, Inc.*, was filed on March 14, 2014. These four cases were filed in the United States District Court-Northern District of Illinois, Eastern Division. On March 18, 2014, an additional putative class action was filed in the United States District Court for the Eastern District of New York, *Mary Jane Whalen v. Michaels Stores, Inc.*, but was voluntarily dismissed by the plaintiff on April 11, 2014 without prejudice to her right to re file a complaint. On April 16, 2014, an order was entered consolidating the Illinois actions. On July 14, 2014, the Company's motion to dismiss the consolidated complaint was granted. On August 11, 2014, plaintiffs filed a motion to alter or amend the judgment, which was denied on October 14, 2014. The deadline to file a notice of appeal expired on November 13, 2014.

On December 2, 2014, Whalen filed a new lawsuit against MSI related to the data breach in the United States District Court for the Eastern District of New York, Mary Jane Whalen v. Michaels Stores, Inc., seeking damages including declaratory relief, monetary damages, statutory damages, punitive damages, attorneys' fees and costs, injunctive relief, pre and post judgment interest, and other relief as available. The Company filed a motion to dismiss and is awaiting a decision from the Court.

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The Company intends to defend these lawsuits vigorously. We cannot reasonably estimate the potential loss, or range of loss, related to the lawsuits, if any.

In connection with the breach, payment card companies and associations may seek to require us to reimburse them for unauthorized card charges and costs to replace cards and may also impose fines or penalties in connection with the data breach, and enforcement authorities may also impose fines or other remedies against us. We have also incurred other costs associated with the data breach, including legal fees, investigative fees, costs of communications with customers and credit monitoring services provided to our customers. In addition, state and federal agencies, including states' attorneys general and the Federal Trade Commission may investigate events related to the data breach, including how it occurred, its consequences and our responses. Although we intend to cooperate in these investigations, we may be subject to fines or other obligations, which may have an adverse effect on how we operate our business and our results of operations. We cannot reasonably estimate the potential loss or range of loss related to any reimbursement costs, fines or penalties that may be assessed, if any. Such amounts incurred to date are immaterial to the consolidated financial statements.

### Consumer Product Safety Commission Claim

On April 21, 2015, the United States Department of Justice, on behalf of the Consumer Product Safety Commission (the "CPSC"), filed a complaint against MSI and Michaels Stores Procurement Company, Inc. ("MSPC") in the U.S. District Court for the Northern District of Texas. The complaint seeks civil penalties for an alleged failure to timely report a potential product safety hazard to the CPSC related to the breakage of certain glass vases. The complaint also alleges the report contained a material misrepresentation and seeks injunctive relief requiring MSI and MSPC to, among other things, establish internal recordkeeping and compliance monitoring systems. The Company filed a partial motion to dismiss on June 18, 2015 seeking dismissal of the CPSC's claims for money damages, and is awaiting a decision from the Court. We believe we have meritorious defenses and intend to defend the lawsuit vigorously. We do not believe the resolution of the lawsuit will have a material effect on our consolidated financial statements.

### General

In addition to the litigation discussed above, we are now, and may be in the future, involved in various other lawsuits, claims and proceedings incident to the ordinary course of business. The results of litigation are inherently unpredictable. Any claims against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time and result in diversion of significant resources.

For some of the matters disclosed above, as well as other matters previously disclosed in the Company's filings with the SEC, the Company is able to estimate a range of losses in excess of the amounts recorded, if any, in the accompanying consolidated financial statements. As of August 1, 2015, the aggregate estimated loss is approximately \$13 million, which includes amounts recorded by the Company.

## 9. RELATED PARTY TRANSACTIONS

Bain Capital Partners, LLC (“Bain Capital”) and The Blackstone Group L.P. (“The Blackstone Group”, together with Bain Capital, the “Sponsors”) own approximately 63% of our outstanding common stock as of August 1, 2015. Prior to our initial public offering (“IPO”) on July 2, 2014, the Sponsors and another common stockholder, Highfields Capital Management LP (“Highfields”), received annual management fees of \$12.0 million and \$1.0 million, respectively. In connection with the IPO, the management agreement was terminated and the Company paid the Sponsors and Highfields an aggregate \$30.2 million termination fee. We recognized management fees and reimbursement of out-of-pocket expenses of \$32.4 million and \$35.7 million during the three and six months ended August 2, 2014, respectively. These expenses are included in related party expenses in the consolidated statements of comprehensive income (loss).

The Blackstone Group owns a majority equity position in RGIS, an external vendor we utilize to count our store inventory. Payments associated with this vendor during the second quarters of fiscal 2015 and fiscal 2014 were \$1.5 million and \$1.6 million, respectively. Payments made during the six months ended August 1, 2015 and August 2, 2014 were \$3.4



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million and \$3.6 million, respectively. These expenses are included in selling, general and administrative (“SG&A”) in the consolidated statements of comprehensive income (loss).

The Blackstone Group owns a majority equity position in Vistar, an external vendor we utilize for all of the candy-type items in our stores. Payments associated with this vendor during each of the second quarters of fiscal 2015 and fiscal 2014 were \$5.7 million and \$4.1 million, respectively. Payments made during the six months ended August 1, 2015 and August 2, 2014 were \$12.9 million and \$11.3 million, respectively. These expenses are recognized in cost of sales as the sales are incurred.

The Blackstone Group owns an equity position in Brixmor Properties Group, a vendor we utilize to lease certain properties. Payments associated with this vendor during the second quarters of fiscal 2015 and fiscal 2014 were \$0.6 million and \$0.7 million, respectively. Payments made during the six months ended August 1, 2015 and August 2, 2014 were \$1.3 million and \$1.7 million, respectively. These expenses are included in cost of sales and occupancy expense in the consolidated statements of comprehensive income (loss).

Five of our current directors, Joshua Bekenstein, Nadim El Gabbani, Lewis S. Klessel, Matthew S. Levin and Peter F. Wallace, are affiliates of Bain Capital or The Blackstone Group. As such, some or all of such directors may have an indirect material interest in payments with respect to debt securities of the Company that have been purchased by affiliates of Bain Capital and The Blackstone Group. As of August 1, 2015, affiliates of The Blackstone Group held \$43.4 million of our Restated Term Loan Credit Facility.

10. CONDENSED CONSOLIDATED FINANCIAL INFORMATION

Our debt covenants restrict MSI, and certain subsidiaries of MSI, from various activities including the incurrence of additional debt, payment of dividends and the repurchase of MSI’s capital stock (subject to certain exceptions), among other things. The following condensed consolidated financial information represents the financial information of MSI and its wholly-owned subsidiaries subject to these restrictions. The information is presented in accordance with the requirements of Rule 12-04 under the SEC’s Regulation S-X.

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Michaels Stores, Inc.

Condensed Consolidated Balance Sheets

(in thousands)

| ASSETS                                      | August 1,<br>2015 | January 31,<br>2015 | August 2,<br>2014 |
|---|-------------------|---------------------|-------------------|
| Current assets:                             |                   |                     |                   |
| Cash and equivalents                        | \$ 65,631         | \$ 373,559          | \$ 84,718         |
| Merchandise inventories                     | 1,073,722         | 958,171             | 936,892           |
| Prepaid expenses and other current assets   | 138,845           | 125,374             | 185,064           |
| Total current assets                        | 1,278,198         | 1,457,104           | 1,206,674         |
| Property and equipment, net                 | 394,686           | 386,372             | 365,621           |
| Goodwill                                    | 94,290            | 94,290              | 94,290            |
| Other assets                                | 62,413            | 64,305              | 74,140            |
| Total assets                                | \$ 1,829,587      | \$ 2,002,071        | \$ 1,740,725      |
| <br>  |                   |                     |                   |
| LIABILITIES AND STOCKHOLDERS' DEFICIT       |                   |                     |                   |
| Current liabilities:                        |                   |                     |                   |
| Accounts payable                            | \$ 418,745        | \$ 447,016          | \$ 317,824        |
| Accrued liabilities and other               | 347,983           | 388,785             | 330,620           |
| Current portion of long-term debt           | 48,900            | 24,900              | 47,900            |
| Other current liabilities                   | 2,885             | 59,885              | 1,131             |
| Total current liabilities                   | 818,513           | 920,586             | 697,475           |
| Long-term debt                              | 2,931,008         | 2,943,524           | 2,956,059         |
| Other liabilities                           | 107,325           | 102,913             | 87,868            |
| Total stockholders' deficit                 | (2,027,259)       | (1,964,952)         | (2,000,677)       |
| Total liabilities and stockholders' deficit | \$ 1,829,587      | \$ 2,002,071        | \$ 1,740,725      |

Michaels Stores, Inc.

Condensed Consolidated Statements of Comprehensive Income (Loss)

(in thousands)

|           | 13 Weeks Ended    |                   | 26 Weeks Ended    |                   |
|-----------|-------------------|-------------------|-------------------|-------------------|
|           | August 1,<br>2015 | August 2,<br>2014 | August 1,<br>2015 | August 2,<br>2014 |
| Net sales | \$ 984,270        | \$ 948,150        | \$ 2,061,870      | \$ 2,000,198      |

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|   |           |             |            |           |
|---|-----------|-------------|------------|-----------|
| Cost of sales and occupancy expense               | 610,949   | 590,953     | 1,246,752  | 1,214,258 |
| Gross profit                                      | 373,321   | 357,197     | 815,118    | 785,940   |
| Selling, general and administrative               | 275,380   | 270,730     | 570,729    | 555,481   |
| Other operating expense                           | 1,040     | 33,417      | 3,284      | 37,977    |
| Operating income                                  | 96,901    | 53,050      | 241,105    | 192,482   |
| Interest and other expense                        | 34,063    | 100,710     | 68,415     | 141,834   |
| Income (loss) before income taxes                 | 62,838    | (47,660)    | 172,690    | 50,648    |
| Provision for income taxes                        | 23,034    | (17,534)    | 63,705     | 24,454    |
| Net income (loss)                                 | \$ 39,804 | \$ (30,126) | \$ 108,985 | \$ 26,194 |
| Other comprehensive income (loss), net of tax:    |           |             |            |           |
| Foreign currency translation adjustment and other | (7,223)   | 1,801       | (2,907)    | 677       |
| Comprehensive income (loss)                       | \$ 32,581 | \$ (28,325) | \$ 106,078 | \$ 26,871 |

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Michaels Stores, Inc.

Condensed Consolidated Statements of Cash Flows

(in thousands)

|   | 26 Weeks Ended    |                   |
|---|-------------------|-------------------|
|   | August 1,<br>2015 | August 2,<br>2014 |
| Cash flows used in operating activities:    |                   |                   |
| Net cash used in operating activities       | \$ (84,245)       | \$ (58,722)       |
| Cash flows used in investing activities:    |                   |                   |
| Additions to property and equipment         | (63,241)          | (64,770)          |
| Cash flows from financing activities:       |                   |                   |
| Net repayments of debt                      | (12,450)          | (1,065,408)       |
| Net borrowings of debt                      | 24,000            | 1,123,750         |
| Payment of dividend to Holdings             | (188,046)         | (60,333)          |
| Other financing activities                  | 16,054            | (23,959)          |
| Net cash used in financing activities       | (160,442)         | (25,950)          |
| Net change in cash and equivalents          | (307,928)         | (149,442)         |
| Cash and equivalents at beginning of period | 373,559           | 234,160           |
| Cash and equivalents at end of period       | \$ 65,631         | \$ 84,718         |

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

This discussion and analysis should be read in conjunction with the unaudited consolidated financial statements of the Company (and the related notes thereto included elsewhere in this quarterly report), and the audited consolidated financial statements of the Company (and the related notes thereto) and the Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2015 ("Annual Report") filed with the Securities and Exchange Commission ("SEC") pursuant to Section 13 or 15(d) under the Securities Act of 1934 on March 19, 2015.

All of the "Company", "us", "we", "our", and similar expressions are references to The Michaels Companies, Inc. ("Michaels") and our consolidated wholly-owned subsidiaries, unless otherwise expressly stated or the context otherwise requires.

We report on the basis of a 52- or 53-week fiscal year, which ends on the Saturday closest to January 31. All references to fiscal year mean the year in which that fiscal year began. References to "fiscal 2015" relate to the 52 weeks ended January 30, 2016 and references to "fiscal 2014" relate to the 52 weeks ended January 31, 2015. In addition, all references to "the second quarter of fiscal 2015" relate to the 13 weeks ended August 1, 2015 and all references to "the second quarter of fiscal 2014" relate to the 13 weeks ended August 2, 2014. Finally, all references to "the six months ended August 1, 2015" relate to the 26 weeks ended August 1, 2015 and all references to "the six months ended August 2, 2014" relate to the 26 weeks ended August 2, 2014. Because of the seasonal nature of our business, the results of operations for the 13 and 26 weeks ended August 1, 2015 are not indicative of the results to be expected for the entire year.

Overview

We are the largest arts and crafts specialty retailer in North America (based on store count) providing materials, project ideas and education for creative activities, under the retail brands of Michaels and Aaron Brothers. We also

operate a market-leading vertically-integrated custom framing business. At August 1, 2015, we operated 1,186 Michaels stores and 118 Aaron Brothers stores.

Net sales for the second quarter of fiscal 2015 increased 3.8% compared to the same period in the prior year. The increase in net sales was due primarily to the opening of 40 additional stores (net of closures) since August 2, 2014. Comparable stores sales increased 1.6% during the second quarter of fiscal 2015, or 2.9% at constant exchange rates. Gross profit as a percent of sales increased 20 basis points to 37.9% during the second quarter of fiscal 2015 primarily related to the timing of distribution expenses, partially offset by a planned increase in costs compared to last year to exit select merchandise as part of our on-going department resets that occurred later in fiscal 2015 due to the West Coast port slowdown and unfavorable shrink experience. Operating income increased \$45.7 million to \$96.6 million during the second quarter of fiscal 2015. The increase was due primarily to an improvement in gross profit and a reduction in related party expenses due to the termination of the management services agreement in July 2014.

On April 6, 2015, an irrevocable notice of redemption was delivered to the holders of the 7.50%/8.25% PIK Toggle Notes due 2018 ("PIK Notes"). Pursuant to the notice, the remaining \$180.9 million in principal of the PIK Notes was redeemed on May 6, 2015. In the second quarter of fiscal 2015, the Company recorded \$6.1 million of debt extinguishment costs, which consists of a 2% redemption premium and \$2.5 million of unamortized debt issuance costs. This final payment retired the PIK Notes and discharged the obligations under the indenture governing the PIK Notes.

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## Comparable Store Sales

Comparable store sales represents the change in net sales for stores open the same number of months in the comparable period of the previous year, including stores that were relocated or expanded during either period, as well as e-commerce sales. A store is deemed to become comparable in its 14th month of operation in order to eliminate grand opening sales distortions. A store temporarily closed more than two weeks is not considered comparable during the month it is closed. If a store is closed longer than two weeks but less than two months, it becomes comparable in the month in which it reopens, subject to a mid-month convention. A store closed longer than two months becomes comparable in its 14th month of operation after its reopening.

## Operating Information

The following table sets forth certain operating data:

|   | 13 Weeks Ended    |                   | 26 Weeks Ended    |                   |
|---|-------------------|-------------------|-------------------|-------------------|
|   | August 1,<br>2015 | August 2,<br>2014 | August 1,<br>2015 | August 2,<br>2014 |
| Michaels stores:  |                   |                   |                   |                   |
| Open at beginning of period                             | 1,177             | 1,144             | 1,168             | 1,136             |
| New stores  | 9                 | 3                 | 19                | 11                |
| Relocated stores opened                                 | 3                 | 5                 | 13                | 10                |
| Closed stores   | —                 | —                 | (1)               | —                 |
| Relocated stores closed                                 | (3)               | (5)               | (13)              | (10)              |
| Open at end of period                                   | 1,186             | 1,147             | 1,186             | 1,147             |
| Aaron Brothers stores:                                  |                   |                   |                   |                   |
| Open at beginning of period                             | 118               | 118               | 120               | 121               |
| Closed stores   | —                 | (1)               | (2)               | (4)               |
| Open at end of period                                   | 118               | 117               | 118               | 117               |
| Total store count at end of period                      | 1,304             | 1,264             | 1,304             | 1,264             |
| Other Operating Data:                                   |                   |                   |                   |                   |
| Average inventory per Michaels store (in thousands) (1) | \$ 880            | \$ 782            | \$ 880            | \$ 782            |
| Comparable store sales                                  | 1.6 %             | 3.2 %             | 0.9 %             | 3.5 %             |
| Comparable store sales, at constant currency            | 2.9 %             | 3.6 %             | 2.1 %             | 4.1 %             |

(1) The calculation of average inventory per Michaels store excludes our Aaron Brothers stores.





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## Results of Operations

The following table sets forth the percentage relationship to net sales of line items of our consolidated statements of comprehensive income (loss). This table should be read in conjunction with the following discussion and with our consolidated financial statements, including the related notes.

|   | 13 Weeks Ended    |   |                   |   | 26 Weeks Ended    |   |                      |   |
|---|-------------------|---|-------------------|---|-------------------|---|----------------------|---|
|   | August 1,<br>2015 |   | August 2,<br>2014 |   | August 1,<br>2015 |   | August<br>2,<br>2014 |   |
|   |                   | % |                   | % |                   | % |                      | % |
| Net sales   | 100.0             | % | 100.0             | % | 100.0             | % | 100.0                | % |
| Cost of sales and occupancy expense                             | 62.1              |   | 62.3              |   | 60.5              |   | 60.7                 |   |
| Gross profit  | 37.9              |   | 37.7              |   | 39.5              |   | 39.3                 |   |
| Selling, general and administrative                             | 28.0              |   | 28.8              |   | 27.7              |   | 27.9                 |   |
| Related party expenses  | —                 |   | 3.4               |   | —                 |   | 1.8                  |   |
| Store pre-opening costs   | 0.1               |   | 0.1               |   | 0.2               |   | 0.1                  |   |
| Operating income  | 9.8               |   | 5.4               |   | 11.7              |   | 9.5                  |   |
| Interest expense  | 3.5               |   | 6.4               |   | 3.5               |   | 5.9                  |   |
| Losses on early extinguishment of debt and<br>refinancing costs | 0.6               |   | 7.2               |   | 0.3               |   | 3.4                  |   |
| Other expense (income), net                                     | —                 |   | —                 |   | —                 |   | —                    |   |
| Income (loss) before income taxes                               | 5.7               |   | (8.2)             |   | 7.9               |   | 0.2                  |   |
| Provision for income taxes                                      | 2.1               |   | (3.1)             |   | 2.9               |   | 0.4                  |   |
| Net income (loss)   | 3.6               | % | (5.1)             | % | 5.0               | % | (0.2)                | % |

## 13 Weeks Ended August 1, 2015 Compared to the 13 Weeks Ended August 2, 2014

**Net Sales.** Net sales increased \$36.1 million in the second quarter of fiscal 2015, or 3.8%, compared to the second quarter of fiscal 2014. The increase in net sales was due to a \$21.4 million increase primarily related to 40 additional stores opened (net of closures) since August 2, 2014 and a \$14.8 million increase in comparable store sales. Comparable store sales increased 1.6%, or 2.9% at constant exchange rates, due primarily to an increase in customer transactions and our average ticket.

**Gross Profit.** Gross profit was 37.9% of net sales in the second quarter of fiscal 2015 compared to 37.7% in the second quarter of fiscal 2014. The 20 basis point improvement was due primarily to the timing of distribution expenses, partially offset by a planned increase in costs compared to last year to exit select merchandise as part of our on-going department resets that occurred later in fiscal 2015 due to the West Coast port slowdown and unfavorable shrink experience.

Selling, General and Administrative. SG&A was 28.0% of net sales for the second quarter of fiscal 2015 compared to 28.8% in the second quarter of fiscal 2014. SG&A increased \$2.8 million to \$275.7 million for the second quarter of fiscal 2015. The increase was due primarily to a \$5.0 million increase in costs associated with operating 40 additional stores (net of closures) and a \$1.9 million increase in performance-based compensation. The increase was partially offset by \$2.1 million of costs incurred in prior year related to our Initial Public Offering (“IPO”) completed in July 2014.

Related Party Expenses. Related party expenses decreased \$32.4 million in the second quarter of fiscal 2015 compared to the same period in the prior year due to the termination of the management services agreement in connection with our IPO completed in July 2014.

Interest Expense. Interest expense decreased \$26.3 million to \$34.3 million in the second quarter of fiscal 2015 compared to the second quarter of fiscal 2014. The decrease was primarily attributable to \$14.8 million of interest savings from the redemption of the PIK Notes during the fourth quarter of fiscal 2014 and the second quarter of fiscal 2015 and

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\$11.0 million of interest savings from the refinancing of the 7.75% Senior Notes due 2018 (“2018 Senior Notes”) in the second quarter of 2014.

Losses on Early Extinguishment of Debt and Refinancing Costs. We recorded a loss on the early extinguishment of debt of \$6.1 million during the second quarter of fiscal 2015 related to the redemption of our remaining outstanding PIK Notes, consisting of \$3.6 million of redemption premiums and \$2.5 million to write off related debt issuance costs. We recorded a loss on the early extinguishment of debt of \$68.0 million during the second quarter of fiscal 2014 related to the redemption of our 2018 Senior Notes and PIK Notes, consisting of \$55.2 million of redemption premiums and \$17.9 million to write off related debt issuance costs. The loss during the second quarter of fiscal 2014 was partially offset by a \$5.1 million write off of the unamortized net premium.

Provision for Income Taxes. Income tax expense totaled \$20.6 million in the second quarter of fiscal 2015 as compared to a tax benefit of \$28.9 million in the second quarter of fiscal 2014. The increase was primarily due to higher pre-tax income as compared to the same period in the prior year. The current year income tax expense was partially offset by our assertion to indefinitely reinvest fiscal 2015 earnings of our Canadian subsidiary into our operations outside the U.S., which is taxed at a lower rate than the U.S.

26 Weeks Ended August 1, 2015 Compared to the 26 Weeks Ended August 2, 2014

Net Sales. Net sales increased \$61.7 million in the first six months of fiscal 2015, or 3.1%, compared to the first six months of fiscal 2014. The increase in net sales was due to a \$43.8 million increase primarily related to 40 additional stores opened (net of closures) since August 2, 2014 and a \$17.8 million increase in comparable store sales. Comparable store sales increased 0.9%, or 2.1% at constant exchange rates, due primarily to an increase in our average ticket, partially offset by a decrease in customer transactions.

Gross Profit. Gross profit was 39.5% of net sales for the first six months of fiscal 2015 compared to 39.3% for the first six months of fiscal 2014. The 20 basis point improvement was due primarily to the timing of distribution expenses. The improvement was partially offset by a planned increase in costs compared to last year to exit select merchandise as part of our on-going department resets that occurred later in fiscal 2015 due to the West Coast port slowdown, unfavorable shrink experience and higher promotional activity that occurred primarily during the first quarter of fiscal 2015.

Selling, General and Administrative. SG&A was 27.7% of net sales for the first six months of fiscal 2015 compared to 27.9% for the first six months of fiscal 2014. SG&A increased \$13.4 million to \$571.3 million for the first six months of fiscal 2015. The increase was due primarily to a \$9.8 million increase in costs associated with operating 40 additional stores (net of closures) and a \$4.1 million increase in performance-based compensation. The increase was partially offset by \$2.1 million of costs incurred in prior year related to our IPO completed in July 2014.

**Related Party Expenses.** Related party expenses decreased \$35.7 million in the first six months of fiscal 2015 compared to the same period in the prior year due to the termination of the management services agreement in connection with our IPO completed in July 2014.

**Interest Expense.** Interest expense decreased \$45.6 million to \$72.1 million in the first six months of fiscal 2015 compared to the first six months of fiscal 2014. The decrease was due primarily to \$26.4 million of interest savings from the redemption of the PIK Notes during the fourth quarter of fiscal 2014 and the second quarter of fiscal 2015 and \$18.4 million of interest savings from the refinancing of the 2018 Senior Notes in the second quarter of 2014.

**Losses on Early Extinguishment of Debt and Refinancing Costs.** We recorded a loss on the early extinguishment of debt of \$6.1 million during the first six months of fiscal 2015 related to the redemption of our remaining outstanding PIK Notes, consisting of \$3.6 million of redemption premiums and \$2.5 million to write off related debt issuance costs. We recorded a loss on the early extinguishment of debt of \$68.0 million during the first six months of fiscal 2014 related to

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the redemption of our 2018 Senior Notes and PIK Notes, consisting of \$55.2 million of redemption premiums and \$17.9 million to write off related debt issuance costs. The loss during the first six months of fiscal 2014 was partially offset by a \$5.1 million write off of the unamortized net premium.

Provision for Income Taxes. Income tax expense for the first six months of fiscal 2015 was \$59.9 million compared to \$7.8 million in the same period in the prior year. The increase was primarily due to higher pre-tax income as compared to the same period in the prior year. The current year income tax expense was partially offset by our assertion to indefinitely reinvest fiscal 2015 earnings of our Canadian subsidiary into our operations outside the U.S., which is taxed at a lower rate than the U.S.

Liquidity and Capital Resources

We require cash principally for day-to-day operations, to finance capital investments, to purchase inventory, to service our outstanding debt and for seasonal working capital needs. We expect that our available cash, cash flow generated from operating activities and funds available under our senior secured asset-based revolving credit facility (“Restated Revolving Credit Facility”) will be sufficient to fund planned capital expenditures, working capital requirements, debt repayments, debt service requirements and anticipated growth for the foreseeable future. Our ability to satisfy our liquidity needs and continue to refinance or reduce debt could be adversely affected by the occurrence of any of the events described under Item 1A. Risk Factors of our Report on Form 10-K for the fiscal year ended January 31, 2015 or our failure to meet our debt covenants. Our Restated Revolving Credit Facility provides senior secured financing of up to \$650.0 million, subject to a borrowing base. As of August 1, 2015, the borrowing base was \$650.0 million, of which we had \$62.0 million of outstanding standby letters of credit, \$24.0 million of outstanding borrowings and \$564.0 million of unused borrowing capacity. Our cash and cash equivalents totaled \$70.4 million at August 1, 2015.

We had total outstanding debt of \$2,979.9 million at August 1, 2015, of which \$2,465.6 million was subject to variable interest rates and \$514.3 million was subject to fixed interest rates.

Our substantial indebtedness could adversely affect our ability to raise additional capital, limit our ability to react to changes in the economy or our industry, expose us to interest rate risk and prevent us from meeting our obligations. Management reacts strategically to changes in economic conditions and monitors compliance with debt covenants to seek to mitigate any potential material impacts to our financial condition and flexibility.

We intend to use excess operating cash flows to repay portions of our indebtedness, depending on market conditions, and to invest in growth opportunities. If we use our excess cash flows to repay our debt, it will reduce the amount of excess cash available for additional capital expenditures.

On April 6, 2015, an irrevocable notice of redemption was delivered to the holders of the PIK Notes. Pursuant to the notice, the remaining \$180.9 million in principal of the PIK Notes was redeemed on May 6, 2015. In the second quarter of fiscal 2015, the Company recorded \$6.1 million of debt extinguishment costs, which consists of a 2% redemption premium and \$2.5 million of unamortized debt issuance costs. This final payment retired the PIK Notes and discharged the obligations under the indenture governing the PIK Notes.

We and our subsidiaries, affiliates and significant shareholders may, from time to time, seek to retire or purchase our outstanding debt (including publicly issued debt) through cash purchases and/or exchanges, in open market purchases, privately negotiated transactions, by tender offer or otherwise. Such repurchases or exchanges, if any, will depend on prevailing market conditions, liquidity requirements, contractual restrictions and other factors.

#### Cash Flow from Operating Activities

Cash flows used in operating activities was \$87.1 million in the first six months of fiscal 2015 and \$124.7 million in the first six months of fiscal 2014. The decrease in cash used in operating activities was primarily due to a \$50.5 million

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increase in operating income for the first six months of fiscal 2015 compared to the same period in the prior year and interest savings from the redemption of the remaining outstanding PIK Notes in the second quarter of fiscal 2015. The decrease was partially offset by higher inventory levels.

Average inventory per Michaels store (including e-commerce and distribution centers) increased 12.5% to \$880,000 at August 1, 2015, from \$782,000 at August 2, 2014. The increase is due to a strategic decision to increase inventory levels of core products as well as the early receipt of certain Holiday products. The decision to receive certain products early was made prior to the resolution of the West Coast port slow down and was influenced by the large number of private brand products sold at our stores and the corresponding lead times needed to produce this product.

## Cash Flow from Investing Activities

The following table includes capital expenditures paid during the periods presented (in thousands):

|  | 26 Weeks Ended       |                      |
|--|----------------------|----------------------|
|  | August<br>1,<br>2015 | August<br>2,<br>2014 |
| New and relocated stores and stores not yet opened (1) | \$ 13,890            | \$ 13,805            |
| Existing stores  | 26,670               | 18,685               |
| Information systems                                    | 18,557               | 23,612               |
| Corporate and other                                    | 4,124                | 8,668                |
|  | \$ 63,241            | \$ 64,770            |

(1) In the first six months of fiscal 2015, we incurred capital expenditures related to the opening of 32 Michaels stores, including the relocation of 13 Michaels stores. In the first six months of fiscal 2014, we incurred capital expenditures related to the opening of 21 Michaels stores, including the relocation of 10 Michaels stores.

## Non-GAAP Measures

The following table sets forth certain non-GAAP measures the Company uses to manage our performance and measure compliance with certain debt covenants. The Company defines “EBITDA (excluding losses on early extinguishment of debt and refinancing costs)” as net income (loss) before interest, income taxes, depreciation, amortization, and losses on early extinguishment of debt and refinancing costs. The Company defines “Adjusted EBITDA” as EBITDA (excluding losses on early extinguishment of debt and refinancing costs) adjusted for certain

defined amounts in accordance with the Company's senior secured term loan facility ("Restated Term Loan Credit Facility") and Restated Revolving Credit Facility (collectively, the "Adjustments").

The Company has presented EBITDA (excluding losses on early extinguishment of debt and refinancing costs) and Adjusted EBITDA to provide investors with additional information to evaluate our operating performance and our ability to service our debt. Adjusted EBITDA is a required calculation under the Company's Restated Term Loan Credit Facility and its Restated Revolving Credit Facility (together the "Senior Secured Credit Facilities"). As it relates to the Senior Secured Credit Facilities, Adjusted EBITDA is used in the calculations of fixed charge coverage and leverage ratios, which, under certain circumstances determine mandatory repayments or maintenance covenants and may restrict the Company's ability to make certain payments (characterized as restricted payments), investments (including acquisitions) and debt repayments.

As EBITDA (excluding losses on early extinguishment of debt and refinancing costs) and Adjusted EBITDA are not measures of operating performance or liquidity calculated in accordance with U.S. generally accepted accounting principles ("GAAP"), these measures should not be considered in isolation of, or as a substitute for, net income (loss), as an indicator of operating performance, or net cash provided by operating activities as an indicator of liquidity. Our computation of EBITDA (excluding losses on early extinguishment of debt and refinancing costs) and Adjusted EBITDA may differ from similarly titled measures used by other companies.



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The following table shows a reconciliation of EBITDA (excluding losses on early extinguishment of debt and refinancing costs) and Adjusted EBITDA to net income (loss) and net cash used in operating activities (in thousands):

|   | 13 Weeks Ended    |                   | 26 Weeks Ended    |                   |
|---|-------------------|-------------------|-------------------|-------------------|
|   | August 1,<br>2015 | August 2,<br>2014 | August 1,<br>2015 | August 2,<br>2014 |
| Net cash used in operating activities   | \$ (10,925)       | \$ (50,377)       | \$ (87,145)       | \$ (124,736)      |
| Depreciation and amortization   | (28,004)          | (26,546)          | (55,949)          | (53,173)          |
| Share-based compensation  | (3,505)           | (5,980)           | (6,225)           | (9,663)           |
| Debt issuance costs amortization  | (2,089)           | (2,744)           | (4,366)           | (5,602)           |
| Accretion of long-term debt, net  | 33                | 103               | 66                | 431               |
| Deferred income taxes   | (1,410)           | 1,059             | (6,514)           | (4,844)           |
| Losses on early extinguishment of debt and refinancing costs                    | (6,072)           | (67,980)          | (6,072)           | (67,980)          |
| Excess tax benefits from share-based compensation                               | 2,753             | 271               | 12,952            | 479               |
| Changes in assets and liabilities   | 84,930            | 103,551           | 255,702           | 261,859           |
| Net income (loss)   | 35,711            | (48,643)          | 102,449           | (3,229)           |
| Interest expense  | 34,311            | 60,635            | 72,127            | 117,726           |
| Losses on early extinguishment of debt and refinancing costs                    | 6,072             | 67,980            | 6,072             | 67,980            |
| Provision for income taxes  | 20,624            | (28,919)          | 59,857            | 7,825             |
| Depreciation and amortization   | 28,004            | 26,546            | 55,949            | 53,173            |
| Other   | (57)              | (101)             | (180)             | (169)             |
| EBITDA (excluding losses on early extinguishment of debt and refinancing costs) | 124,665           | 77,498            | 296,274           | 243,306           |
| Adjustments:  |                   |                   |                   |                   |
| Share-based compensation  | 3,505             | 5,980             | 6,225             | 9,663             |
| Management fees to Sponsors and others  | —                 | 32,354            | —                 | 35,682            |
| Retention costs   | —                 | —                 | —                 | 340               |
| Severance costs   | 302               | 883               | 1,162             | 994               |
| Store pre-opening costs   | 1,047             | 1,081             | 3,310             | 2,341             |
| Store remodel costs   | 1,167             | (38)              | 1,827             | 3,403             |
| Foreign currency transaction losses (gains)                                     | 14                | 53                | (23)              | 301               |
| Store closing costs   | 332               | 439               | (361)             | 1,058             |
| IPO costs   | —                 | 2,134             | —                 | 2,134             |
| Other (1)   | 1,449             | 1,013             | 2,476             | 1,627             |
| Adjusted EBITDA   | \$ 132,481        | \$ 121,397        | \$ 310,890        | \$ 300,849        |

(1) Other adjustments relate to items such as moving and relocation expenses, franchise taxes, sign on bonuses and certain legal expenses.

Disclosure Regarding Forward-Looking Information

The above discussion, as well as other portions of this Quarterly Report on Form 10-Q, contains forward-looking statements that reflect our plans, estimates and beliefs. Any statements contained herein (including, but not limited to, statements to the effect that Michaels or its management “anticipates”, “plans”, “estimates”, “expects”, “believes”, “intends” and other similar expressions) that are not statements of historical fact should be considered forward-looking statements and should be read in conjunction with our Annual Report. Such forward-looking statements are based upon management’s current knowledge and assumptions about future events and involve risks and uncertainties that could cause actual results, performance or achievements to be materially different from anticipated results, prospects, performance or achievements expressed or implied by such forward-looking statements. Such risks and uncertainties include, but are not limited to the following:

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- risks related to the effect of economic uncertainty;
  
- our substantial outstanding indebtedness of \$3.0 billion could adversely affect our ability to raise additional capital to fund our operations, limit our ability to react to changes in the economy or our industry, expose us to interest rate risk to the extent of our \$2.5 billion variable rate debt and prevent us from meeting our obligations under our notes and credit facilities;
  
- restrictions in our debt agreements that limit our flexibility in operating our business, as our senior secured credit facilities and the indentures governing our notes contain various covenants that limit our ability to engage in specified types of transactions and require that we maintain specified financial ratios upon the occurrence of certain events;
  
- changes in customer demand could materially adversely affect our sales, results of operations, and cash flow;
  
- our failure to adequately maintain security and prevent unauthorized access to electronic and other confidential information, which could result in an additional data breach, could materially adversely affect our financial condition and operating results;
  
- competition, including internet-based competition, could negatively impact our business;
  
- our reliance on foreign suppliers increases our risk of not obtaining adequate, timely, and cost-effective product supplies;
  
- how well we manage our business;
  
- our ability to open new stores and increase comparable store sales growth, as our growth depends on our strategy of expanding our base of retail stores; and, if we are unable to continue this strategy, our ability to increase our sales, profitability, and cash flow could be impaired;
  
- damage to the reputation of the Michaels brand or our private and exclusive brands could adversely affect our sales;
  
- a weak fourth quarter would materially adversely affect our results of operations;
  
- risks associated with the suppliers from whom our products are sourced may fail us and transitioning to other qualified vendors could materially adversely affect our revenue and profit growth;
  
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unexpected or unfavorable consumer responses to our promotional or merchandising programs could materially adversely affect our sales, results of operations, cash flows and financial condition;

- our marketing programs, e-commerce initiatives and use of consumer information are governed by an evolving set of laws and enforcement trends and unfavorable changes in those laws or trends, or our failure to comply with existing or future laws, could substantially harm our business and results of operations;
- product recalls and/or product liability, as well as changes in product safety and other consumer protection laws, may adversely impact our operations, merchandise offerings, reputation, results of operation, cash flow, and financial condition;
- changes in regulations or enforcement, or our failure to comply with existing or future regulations, may adversely impact our business;

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- significant increases in inflation or commodity prices such as petroleum, natural gas, electricity, steel, wood, and paper may adversely affect our costs, including cost of merchandise;
- we may be subject to information technology system failures or network disruptions, or our information systems may prove inadequate, resulting in damage to our reputation, business operations and financial condition;
- improvements to our supply chain may not be fully successful;
- changes in newspaper subscription rates may result in reduced exposure to our circular advertisements;
- disruptions in the capital markets could increase our costs of doing business;
- our real estate leases generally obligate us for long periods, which subjects us to various financial risks;
- we have co-sourced certain of our information technology, accounts payable, payroll, accounting and human resources functions, and may co-source other administrative functions, which makes us more dependent upon third parties;
- we are exposed to fluctuations in exchange rates between the U.S. and Canadian dollar, which is the functional currency of our Canadian subsidiaries;
- we are dependent upon the services of our senior management team;
- failure to attract and retain quality sales, distribution center and other associates in appropriate numbers as well as experienced buying and management personnel could adversely affect our performance;
- our results may be adversely affected by serious disruptions or catastrophic events, including geo-political events and weather;
- our holding company structure makes us, and certain of our direct and indirect subsidiaries, dependent on the operations of our, and their, subsidiaries to meet our financial obligations; and
- investment funds affiliated with the Sponsors own approximately 63% of the outstanding shares of our common stock and as a result will have the ability to control the outcome of matters submitted for stockholder approval, including the ability to direct the election of all of the members of our Board of Directors, and they may have

interests that differ from those of other stockholders.

For more details on factors that may cause actual results to differ materially from such forward-looking statements, please see the Risk Factors section of our Annual Report. Except as required by applicable law, we disclaim any intention to, and undertake no obligation to, update or revise any forward-looking statement.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

#### Foreign Currency Risk

We are exposed to fluctuations in exchange rates between the U.S. and Canadian dollar, which is the functional currency of our Canadian subsidiaries. Our sales, costs and expenses of our Canadian subsidiaries, when translated into U.S. dollars, can fluctuate due to exchange rate movement. As of August 1, 2015, a 10% increase or decrease in the

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exchange rate of the Canadian dollar would increase or decrease net income by approximately \$1 million for the 26 weeks ended August 1, 2015.

Interest Rate Risk

We have market risk exposure arising from changes in interest rates on our Restated Term Loan Credit Facility and our Restated Revolving Credit Facility. The interest rates on our Restated Term Loan Credit Facility and our Restated Revolving Credit Facility will reprice periodically, which will impact our earnings and cash flow. The interest rate on our 2020 Senior Subordinated Notes is fixed. Based on our overall interest rate exposure to variable rate debt outstanding as of August 1, 2015, a 1% increase or decrease in interest rates would increase or decrease income before income taxes by approximately \$25 million. A 1% increase or decrease in interest rates would decrease or increase the fair value of our long-term fixed rate debt by approximately \$13 million. A change in interest rates would not materially affect the fair value of our variable rate debt as the debt reprices periodically.

Inflation Risk

We do not believe inflation and changing commodity prices have had a material impact on our net sales, income from continuing operations, plans for expansion or other capital expenditures for any period presented in this report. However, we cannot be sure inflation and changing commodity prices will not have an adverse impact on our operating results, financial condition, plans for expansion or other capital expenditures in future periods.

ITEM 4. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

We maintain a set of disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated by the SEC under the Securities Exchange Act of 1934) designed to provide reasonable assurance that information, which is required to be timely disclosed, is accumulated and communicated to management in a timely fashion. We note the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

An evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls are effective to provide reasonable assurance that information required to be disclosed in the reports that we file or submit under the Securities and Exchange Act of 1934, as amended, is accumulated and communicated to management, including our Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosure and are effective to provide reasonable assurance that such information is recorded, processed, summarized, and reported within the time periods specified by the SEC's rules and forms.

#### Change in Internal Control Over Financial Reporting

There have been no changes in our internal controls over financial reporting during the quarter ended August 1, 2015 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.



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## Part II—OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS.

Information regarding legal proceedings is incorporated by reference from Note 8 to the consolidated financial statements.

## Item 1A. RISK FACTORS

There have been no material changes to the Risk Factors described in the Annual Report on Form 10-K.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

The following table provides certain information with respect to our purchases of shares of the Company's common stock during the second quarter of fiscal 2015:

| Period                        | Total Number of<br>Shares Purchased (a) | Average<br>Price<br>Paid per<br>Share | Total Number of<br>Shares Purchased<br>as Part of Publicly<br>Announced Plan | Approximate Dollar<br>Value<br>of Shares That May<br>Yet Be Purchased<br>Under the Plan |
|-------------------------------|---|---------------------------------------|--|---|
| May 3, 2015 - May 30, 2015    | —                                       | \$ —                                  | —  | \$ —  |
| May 31, 2015 - July 4, 2015   | 16,185                                  | 27.00                                 | —  | —   |
| July 5, 2015 - August 1, 2015 | —                                       | —                                     | —  | —   |
| Total                         | 16,185                                  | \$ 27.00                              | —  | \$ —  |

(a) These amounts reflect the surrender of shares of common stock to the Company to satisfy tax withholding obligations in connection with employee restricted stock awards that vested during the second quarter of fiscal 2015.

## ITEM 5. OTHER INFORMATION.

Iran Threat Reduction and Syria Human Rights Act of 2012

Pursuant to Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012, which added Section 13(r) of the Exchange Act, the Company hereby incorporates by reference herein Exhibit 99.1 of this Quarterly Report on Form 10-Q, which includes disclosures publicly filed and/or provided to The Blackstone Group L.P., one of our Sponsors, by Travelport Worldwide Limited which may be considered its affiliate.

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Item 6. EXHIBITS

(a) Exhibits:

| Exhibit<br>Number | Description of Exhibit  |
|-------------------|---|
| 31.1              | Certifications of Carl S. Rubin pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002        |
| 31.2              | Certifications of Charles M. Sonstebly pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002 |
| 32.1              | Certification pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002  |
| 99.1              | Section 13(r) Disclosure  |
| 101.INS           | XBRL Instance Document  |
| 101.SCH           | XBRL Taxonomy Extension Schema  |
| 101.CAL           | XBRL Taxonomy Extension Calculation Linkbase  |
| 101.DEF           | XBRL Taxonomy Extension Definition Linkbase   |
| 101.LAB           | XBRL Taxonomy Extension Label Linkbase  |
| 101.PRE           | XBRL Taxonomy Extension Presentation Linkbase   |

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE MICHAELS COMPANIES, INC.

By: /s/ Carl S. Rubin  
Carl S. Rubin  
Chief Executive Officer  
(Principal Executive Officer)

By: /s/ Charles M. Sonstebly  
Charles M. Sonstebly  
Chief Administrative Officer & Chief Financial Officer  
  
(Principal Financial Officer)

Date: August 28, 2015