
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
WASHINGTON, DC 20549

FORM 10-Q
**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES
EXCHANGE ACT OF 1934**

For the quarterly period ended November 3, 2018

Commission file number 001-36501

THE MICHAELS COMPANIES, INC.
A Delaware Corporation

IRS Employer Identification No. 37-1737959

8000 Bent Branch Drive
Irving, Texas 75063
(972) 409-1300

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 every Interactive Data File required to be submitted 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 large accelerated filer.

The Michaels Companies, Inc. is not (1) a shell company, (2) a small reporting company or (3) an emerging growth company (as defined in Rule 12b-2 of the Exchange Act).

As of November 27, 2018, 157,694,568 shares of The Michaels Companies, Inc.'s common stock were outstanding.

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
(in thousands, except per share data)
(Unaudited)

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Net sales	\$ 1,274,058	\$ 1,240,196	\$ 3,482,835	\$ 3,471,352
Cost of sales and occupancy expense	795,104	756,088	2,173,990	2,117,100
Gross profit	478,954	484,108	1,308,845	1,354,252
Selling, general and administrative	340,593	329,298	970,191	970,561
Restructure charge	—	—	44,278	—
Store pre-opening costs	1,196	952	3,995	2,592
Operating income	137,165	153,858	290,381	381,099
Interest expense	37,798	32,818	109,493	94,305
Losses on early extinguishments of debt and refinancing costs	—	—	1,835	—
Other (income) expense, net	(121)	(360)	(2,646)	950
Income before income taxes	99,488	121,400	181,699	285,844
Income taxes	15,719	41,640	43,557	98,314
Net income	<u>\$ 83,769</u>	<u>\$ 79,760</u>	<u>\$ 138,142</u>	<u>\$ 187,530</u>
Other comprehensive income, net of tax:				
Foreign currency translation adjustment and other	3,016	(4,418)	(3,230)	4,254
Comprehensive income	<u>\$ 86,785</u>	<u>\$ 75,342</u>	<u>\$ 134,912</u>	<u>\$ 191,784</u>
Earnings per common share:				
Basic	\$ 0.50	\$ 0.44	\$ 0.79	\$ 1.01
Diluted	\$ 0.50	\$ 0.44	\$ 0.78	\$ 1.00
Weighted-average common shares outstanding:				
Basic	165,975	180,710	174,949	185,521
Diluted	166,570	181,987	175,851	186,775

See accompanying notes to consolidated financial statements.

THE MICHAELS COMPANIES, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)
(Unaudited)

ASSETS	November 3, 2018	February 3, 2018	October 28, 2017
Current Assets:			
Cash and equivalents	\$ 102,670	\$ 425,896	\$ 176,771
Merchandise inventories	1,440,875	1,123,288	1,404,206
Prepaid expenses and other	100,791	97,830	95,993
Accounts receivable, net	42,997	26,207	30,936
Income taxes receivable	6,544	3,761	5,792
Total current assets	<u>1,693,877</u>	<u>1,676,982</u>	<u>1,713,698</u>
Property and equipment, at cost	1,642,838	1,593,683	1,545,004
Less accumulated depreciation and amortization	<u>(1,189,442)</u>	<u>(1,173,663)</u>	<u>(1,143,112)</u>
Property and equipment, net	453,396	420,020	401,892
Goodwill	119,074	119,074	119,074
Other intangible assets, net	20,591	21,769	22,253
Deferred income taxes	23,367	34,538	36,946
Other assets	28,730	27,832	12,233
Total assets	<u>\$ 2,339,035</u>	<u>\$ 2,300,215</u>	<u>\$ 2,306,096</u>
LIABILITIES AND STOCKHOLDERS' DEFICIT			
Current Liabilities:			
Accounts payable	\$ 645,469	\$ 483,002	\$ 674,222
Accrued liabilities and other	407,684	370,457	400,138
Current portion of long-term debt	240,261	24,900	140,125
Income taxes payable	476	79,586	16,673
Total current liabilities	<u>1,293,890</u>	<u>957,945</u>	<u>1,231,158</u>
Long-term debt	2,690,302	2,701,764	2,707,120
Other liabilities	144,694	150,001	100,656
Total liabilities	<u>4,128,886</u>	<u>3,809,710</u>	<u>4,038,934</u>
Commitments and contingencies			
Stockholders' Deficit:			
Common stock, \$0.06775 par value, 350,000 shares authorized; 158,616 shares issued and outstanding at November 3, 2018; 181,919 shares issued and outstanding at February 3, 2018; and 181,263 shares issued and outstanding at October 28, 2017	10,700	12,206	12,159
Additional paid-in-capital	—	21,740	7,722
Treasury stock	(12,168)	—	—
Accumulated deficit	(1,781,493)	(1,539,781)	(1,742,749)
Accumulated other comprehensive loss	(6,890)	(3,660)	(9,970)
Total stockholders' deficit	<u>(1,789,851)</u>	<u>(1,509,495)</u>	<u>(1,732,838)</u>
Total liabilities and stockholders' deficit	<u>\$ 2,339,035</u>	<u>\$ 2,300,215</u>	<u>\$ 2,306,096</u>

See accompanying notes to consolidated financial statements.

THE MICHAELS COMPANIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	39 Weeks Ended	
	November 3, 2018	October 28, 2017
Cash flows from operating activities:		
Net income	\$ 138,142	\$ 187,530
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	89,933	86,232
Share-based compensation	20,780	18,232
Debt issuance costs amortization	3,759	3,823
Accretion of long-term debt, net	(385)	(379)
Restructure charge	44,278	—
Deferred income taxes	7,710	529
Losses on early extinguishments of debt and refinancing costs	1,835	—
Changes in assets and liabilities:		
Merchandise inventories	(338,260)	(275,086)
Prepaid expenses and other	(2,886)	(8,818)
Accounts receivable	(18,269)	(7,721)
Other assets	(1,314)	(1,010)
Accounts payable	150,088	150,947
Accrued interest	7,850	(314)
Accrued liabilities and other	1,077	12,685
Income taxes	(79,258)	(61,628)
Other liabilities	734	1,405
Net cash provided by operating activities	<u>25,814</u>	<u>106,427</u>
Cash flows used in investing activities:		
Additions to property and equipment	<u>(119,553)</u>	<u>(72,640)</u>
Cash flows from financing activities:		
Common stock repurchased	(430,509)	(253,595)
Payments on term loan credit facility	(17,356)	(18,675)
Borrowings on asset-based revolving credit facility	307,400	357,200
Payments on asset-based revolving credit facility	(89,400)	(248,200)
Payment of debt refinancing costs	(1,117)	—
Payment of dividends	(317)	(408)
Proceeds from stock options exercised	1,812	7,849
Net cash used in financing activities	<u>(229,487)</u>	<u>(155,829)</u>
Net change in cash and equivalents	(323,226)	(122,042)
Cash and equivalents at beginning of period	425,896	298,813
Cash and equivalents at end of period	<u>\$ 102,670</u>	<u>\$ 176,771</u>
Supplemental cash flow information:		
Cash paid for interest	\$ 98,864	\$ 91,794
Cash paid for taxes	\$ 115,724	\$ 159,013

See accompanying notes to consolidated financial statements.

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 February 3, 2018 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 2018” relate to the 52 weeks ending February 2, 2019 and references to “fiscal 2017” relate to the 53 weeks ended February 3, 2018. In addition, all references to “the third quarter of fiscal 2018” relate to the 13 weeks ended November 3, 2018 and all references to “the third quarter of fiscal 2017” relate to the 13 weeks ended October 28, 2017. Finally, all references to “the nine months ended November 3, 2018” relate to the 39 weeks ended November 3, 2018 and all references to “the nine months ended October 28, 2017” relate to the 39 weeks ended October 28, 2017. Because of the seasonal nature of our business, the results of operations for the 13 and 39 weeks ended November 3, 2018 are not indicative of the results to be expected for the entire year.

Aaron Brothers

In March 2018, we closed substantially all of our Aaron Brothers stores and began the process of repositioning our Aaron Brothers brand as a store-within-a-store, providing custom framing services in all Michaels stores. In the first nine months of fiscal 2018, we recorded a restructure charge totaling \$44.3 million, consisting primarily of costs associated with the termination of the remaining lease obligations, the write-off of fixed assets and employee-related expenses. For the nine months ended November 3, 2018 and October 28, 2017, Aaron Brothers net sales totaled approximately \$12.9 million and \$78.0 million, respectively. Excluding the restructure charge, Aaron Brothers did not have a material impact on the Company’s operating income in the periods presented.

Share Repurchase Program

In September 2018, the Board of Directors authorized a new share repurchase program for the Company to purchase \$500.0 million of the Company’s common stock on the open market or through accelerated share repurchase transactions. The share repurchase program does not have an expiration date, and the timing and number of repurchase transactions under the program will depend on market conditions, corporate considerations, debt agreements and regulatory requirements. Shares repurchased under the program are held as treasury shares until retired. In June 2018, the Company entered into an accelerated share repurchase agreement (“ASR Agreement”) with JPMorgan Chase Bank, N.A. (“JPMorgan”). Under the ASR Agreement, we paid JPMorgan a purchase price of \$250.0 million for delivery of 12.4 million shares of our common stock. The total number of shares repurchased was based upon a volume weighted average price of our stock over a predetermined period. The ASR agreement was completed on August 30, 2018. During the nine

months ended November 3, 2018, we repurchased 23.6 million shares under our share repurchase programs for an aggregate amount of \$434.2 million, inclusive of the ASR Agreement. As of November 3, 2018, we had \$416.0 million of availability remaining under our current share repurchase program.

Accounting Pronouncements Recently Adopted

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 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 March 2016, the FASB issued ASU 2016-08, “*Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*” which is intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU 2016-10, “*Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*” which provides further guidance on identifying performance obligations and improves the operability and understandability of the licensing implementation guidance. In May 2016, the FASB issued ASU 2016-12, “*Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*” which narrowly amended the revenue recognition guidance regarding collectability, noncash consideration, presentation of sales tax and transition. We used the modified retrospective transition method to adopt ASU 2014-09 in the first quarter of fiscal 2018 with no adjustments required to our opening retained earnings. The adoption did not have a material impact to the consolidated financial statements; however, it did result in additional disclosures.

Recent Accounting Pronouncements Not Yet Adopted

In October 2018, the FASB issued ASU 2018-16, “*Derivatives and Hedging (Topic 815): Inclusion of the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as a Benchmark Interest Rate for Hedge Accounting Purposes*” (“ASU 2018-16”). ASU 2018-16 allows for the use of the Overnight Index Swap (“OIS”) rate based on the Secured Overnight Financing Rate (“SOFR”) as a U.S. benchmark interest rate for purposes of applying hedge accounting under Accounting Standard Codification (“ASC”) 815, *Derivatives and Hedging*. ASU 2018-16 is effective for fiscal years beginning after December 15, 2018, with early adoption permitted. We are currently evaluating the new standard but do not anticipate a material impact to the consolidated financial statements once implemented.

In August 2018, the FASB issued ASU 2018-15, “*Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract*,” (“ASU 2018-15”). ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). ASU 2018-15 is effective for annual reporting periods beginning after December 15, 2019, including interim periods within that reporting period, with early adoption permitted. The standard is to be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. We are currently evaluating the impact that ASU 2018-15 will have on the consolidated financial statements and related disclosures.

In August 2018, the FASB issued ASU 2018-13, “*Fair Value Measurement (Topic 820): Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement*” (“ASU 2018-13”). ASU 2018-13 removes, modifies and adds certain disclosure requirements for fair value measurements under ASC 820, *Fair Value Measurements* (“ASC 820”). ASU 2018-13 is effective for annual reporting periods beginning after December 15, 2019, including interim periods within that reporting period, with early adoption permitted. We do not anticipate a material impact to the consolidated financial statements once implemented.

In January 2017, the FASB issued ASU 2017-04, “*Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*” (“ASU 2017-04”). ASU 2017-04 simplifies the measurement of goodwill impairment by removing the second step of the goodwill impairment test, which requires the determination of the fair value of individual assets and liabilities of a reporting unit. Under ASU 2017-04, goodwill impairment is to be measured as the amount by which a reporting unit’s carrying value exceeds its fair value with the loss recognized not to exceed the total amount of goodwill allocated to the reporting unit. ASU 2017-04 is effective for fiscal years beginning after December 15, 2019, with early adoption permitted for interim or annual goodwill impairment tests performed after January 1, 2017. The standard is to be applied on a prospective basis. We do not anticipate a material impact to the consolidated financial statements once implemented.

In February 2016, the FASB issued ASU 2016-02, “*Leases (Topic 842)*” (“ASU 2016-02”). Under ASU 2016-02, an entity will be required to recognize right-of-use assets and lease liabilities on its balance sheet and disclose key information about leasing arrangements. ASU 2016-02 offers specific accounting guidance for a lessee, a lessor and sale and leaseback transactions. Lessees and lessors are required to disclose qualitative and quantitative information about leasing arrangements to enable a user of the financial statements to assess the amount, timing and uncertainty of cash flows arising from leases. The lease standard requires companies to use a modified retrospective transition approach as of the beginning of the earliest comparable period presented in the company’s financial statements. In July 2018, the FASB issued ASU 2018-11, “*Leases (Topic 842): Targeted Improvements*” which provided an additional transition option that allows companies to continue applying the guidance under the current lease standard in the comparative periods presented in the consolidated financial statements. The Company has elected to adopt this transition option and will record a cumulative-effect adjustment to the opening balance of retained earnings on the date of adoption. The guidance under these standards is effective for annual reporting periods beginning after December 15, 2018, including interim periods within that reporting period, with early adoption permitted. We are currently evaluating the impact that ASU 2016-02 will have on the consolidated financial statements and related disclosures. We believe the most significant impact relates to our accounting for real estate leases, which will be recorded as right-of-use assets and lease liabilities on our balance sheet upon adoption. We do not expect a material impact on our consolidated statements of comprehensive income or our consolidated statements of cash flows once implemented.

2. REVENUE RECOGNITION

Our revenue is primarily associated with sales of merchandise to customers within our stores, customers utilizing our e-commerce platforms and through our Darice wholesale business (“Darice”). Revenue is measured based on the amount of consideration that we expect to receive, reduced by estimates for return allowances, point-of-sale coupons and discounts. Revenue also excludes any amounts collected on behalf of third parties, including sales tax. Revenue from sales of our merchandise is recognized when the customer takes possession of the merchandise. Payment for our retail sales is typically due at the time of the sale.

Right of Return

We allow for merchandise to be returned under most circumstances up to 180 days after purchase. A sales return reserve is established using historical customer return behavior and reduces both revenue and cost of goods sold. Historically, the sales returns reserve was presented net of cost of sales in other current liabilities in the consolidated balance sheets. As a result of adopting ASU 2014-09, the Company presents the gross sales return reserve in other current liabilities and the estimated value of the merchandise expected to be returned in prepaid expenses and other in the consolidated balance sheets. The change did not have a material impact on our consolidated balance sheet as of November 3, 2018.

Customer Receivables

As of November 3, 2018, February 3, 2018 and October 28, 2017, receivables from customers, which consist primarily of trade receivables related to Darice, were approximately \$30.5 million, \$19.2 million and \$23.5 million, respectively, and are included in accounts receivable, net in the consolidated balance sheets.

Gift Cards

We record a gift card liability on the date we issue the gift card to the customer. We record revenue and reduce the gift card liability as the customer redeems the gift card or when the likelihood of redemption by the customer is remote (“gift card breakage”). We estimate gift card breakage using the expected value method based on customers’ historical redemption rates and patterns. Gift card breakage income is recorded in net sales in the consolidated statements of comprehensive income over the estimated redemption period. The gift card liability is included in accrued liabilities and other in the consolidated balance sheets.

The following table includes activity related to gift cards (in thousands):

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Balance at beginning of period	\$ 50,513	\$ 44,185	\$ 56,729	\$ 49,869
Issuance of gift cards	12,077	11,582	36,873	36,536
Revenue recognized ⁽¹⁾	(12,403)	(11,678)	(41,541)	(41,190)
Gift card breakage	(749)	(454)	(2,623)	(1,580)
Balance at end of period	\$ 49,438	\$ 43,635	\$ 49,438	\$ 43,635

(1) Revenue recognized from the beginning liability during the third quarters of fiscal 2018 and fiscal 2017 totaled \$7.1 million. Revenue recognized from the beginning liability during the first nine months of fiscal 2018 and fiscal 2017 totaled \$19.9 million and \$19.4 million, respectively.

3. FAIR VALUE MEASUREMENTS

As defined in 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.

Impairment losses related to store-level property and equipment are calculated using significant unobservable inputs including the present value of future cash flows expected to be generated using a risk-adjusted weighted-average

cost of capital and comparable store sales growth assumptions and, therefore, are classified as a Level 3 measurement in the fair value hierarchy.

The carrying value of cash and cash equivalents, accounts receivable and accounts payable approximates their estimated fair values due to the short maturities of these instruments.

The table below provides the fair values of our senior secured term loan facility (“Amended Term Loan Credit Facility”), our 5.875% senior subordinated notes maturing in 2020 (“2020 Senior Subordinated Notes”) and our interest rate swaps executed in April 2018.

	November 3, 2018	February 3, 2018	October 28, 2017
(in thousands)			
Assets			
Interest rate swaps	\$ 5,028	\$ —	\$ —
Liabilities			
Term loan credit facility	\$ 2,195,613	\$ 2,246,302	\$ 2,250,412
Senior subordinated notes	510,000	518,288	520,838
Interest rate swaps	571	—	—

The fair values of our Amended Term Loan Credit Facility and our 2020 Senior Subordinated Notes were determined based on quoted market prices which are considered Level 1 inputs within the fair value hierarchy.

The fair value of our interest rate swaps was calculated using significant observable inputs including the present value of estimated future cash flows using the applicable interest rate curves and, therefore, were classified as Level 2 inputs within the fair value hierarchy.

4. DEBT

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

	Interest Rate	November 3, 2018	February 3, 2018	October 28, 2017
Term loan credit facility	Variable	\$ 2,214,994	\$ 2,232,350	\$ 2,244,800
Asset-based revolving credit facility	Variable	218,000	—	109,000
Senior subordinated notes	5.875 %	510,000	510,000	510,000
Total debt		2,942,994	2,742,350	2,863,800
Less unamortized discount/premium and debt costs		(12,431)	(15,686)	(16,555)
Total debt, net		2,930,563	2,726,664	2,847,245
Less current portion		(240,261)	(24,900)	(140,125)
Long-term debt		<u>\$ 2,690,302</u>	<u>\$ 2,701,764</u>	<u>\$ 2,707,120</u>

Revolving Credit Facility

As of November 3, 2018 and October 28, 2017, the borrowing base under our senior secured asset-based revolving credit facility was \$850.0 million, of which Michaels Stores, Inc. (“MSI”) had unused borrowing capacity of \$567.0 million and \$675.7 million, respectively. As of November 3, 2018 and October 28, 2017, outstanding standby letters of credit, which reduce our borrowing base, totaled \$65.0 million and \$65.3 million, respectively.

Term Loan Credit Facility

On May 23, 2018, MSI entered into an amendment with JPMorgan and other lenders to amend and restate our term loan credit facility. The amended and restated credit agreement, together with the related security, guarantee and other agreements, is referred to as the “Amended and Restated Term Loan Credit Facility”. Borrowings under the Amended and Restated Term Loan Credit Facility bear interest at a rate per annum, at MSI’s option, of either (a) a margin of 1.50% plus a base rate defined as the highest of (1) the prime rate of JPMorgan, (2) the federal funds effective rate plus 0.5%, and (3) the one-month London Interbank Offered Rate (“LIBOR”) plus 1% or (b) a margin of 2.50% plus the applicable LIBOR. MSI is required to make scheduled quarterly payments equal to 0.25% of the original principal amount of the term loans (subject to adjustments relating to the incurrence of additional term loans) for the first four years and two quarters of the Amended and Restated Term Loan Credit Facility, with the balance to be paid on January 28, 2023. All other terms under the Amended Term Loan Credit Facility have remained unchanged. As a result of this refinancing, we recorded a loss on the early extinguishment of debt of \$1.8 million during the second quarter of fiscal 2018.

Interest Rate Swaps

In April 2018, we executed two interest rate swaps with an aggregate notional value of \$1.0 billion associated with our outstanding Amended Term Loan Credit Facility. The interest rate swaps have a maturity date of April 30, 2021 and were executed for risk management and are not held for trading purposes. The objective of the interest rate swaps is to hedge the variability of cash flows resulting from fluctuations in the one-month LIBOR. The swaps replaced the one-month LIBOR with a fixed interest rate of 2.7765% and payments are settled monthly. The swaps qualify as cash flow hedges and changes in the fair values are recorded in accumulated other comprehensive income in the consolidated balance sheet. The changes in fair value are reclassified from accumulated other comprehensive income to interest expense in the same period that the hedged items affect earnings. We reclassified \$1.6 million and \$3.7 million from accumulated other comprehensive income to interest expense during the three and nine months ended November 3, 2018, respectively. As of November 3, 2018, the fair value of the interest rate swaps was a net asset of \$4.5 million, consisting of \$5.0 million recorded in other assets and \$0.6 million recorded in accrued liabilities in our consolidated balance sheets.

5. ACCUMULATED OTHER COMPREHENSIVE LOSS

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

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Beginning of period	\$ (9,906)	\$ (5,552)	\$ (3,660)	\$ (14,224)
Foreign currency translation adjustment and other	(942)	(4,418)	(6,528)	4,254
Interest rate swaps	3,958	—	3,298	—
End of period	\$ (6,890)	\$ (9,970)	\$ (6,890)	\$ (9,970)

6. INCOME TAXES

The effective tax rate was 15.8% for the third quarter of fiscal 2018 compared to 34.3% for the third quarter of fiscal 2017 and 24.0% for the nine months ended November 3, 2018 compared to 34.4% for the same period in the prior year. The effective tax rate for both the third quarter of fiscal 2018 and the nine months ended November 3, 2018 were lower than the comparable period in the prior year due to benefits recognized related to the enactment of the Tax Cuts and Jobs Act (“Tax Act”) in the fourth quarter of fiscal 2017, including the reduction of the federal statutory tax rate from 35% to 21%. In addition, a provisional charge of \$5.0 million was recognized for the nine months ended November 3, 2018 related to repatriation taxes for accumulated earnings of our foreign subsidiaries, partially offset by a provisional benefit of \$4.0 million related to the revaluation of our net deferred tax assets as a result of the Tax Act. The U.S. Treasury is

expected to issue additional regulations and guidance in connection with the Tax Act, which may alter interpretations of the new tax law and could materially change our estimated provisional adjustments.

7. EARNINGS PER SHARE

The Company’s unvested restricted stock awards contain non-forfeitable rights to dividends and meet the criteria of a participating security as defined by ASC 260, “*Earnings Per Share*”. In applying the two-class method, net income is allocated to both common and participating securities based on their respective weighted-average shares outstanding for the period. Basic earnings per share is computed by dividing net income allocated to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted earnings per share is computed by dividing income available to common shareholders by the weighted-average common shares outstanding plus the potential dilutive impact from stock options and restricted stock units. Common equivalent shares are excluded from the computation if their effect is anti-dilutive. There were 8.4 million and 5.8 million anti-dilutive shares during the third quarters of fiscal 2018 and fiscal 2017, respectively. There were 7.1 million and 6.0 million anti-dilutive shares during the nine months ended November 3, 2018 and October 28, 2017, respectively.

The following table sets forth the computation of basic and diluted earnings per common share (in thousands, except per share data):

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Basic earnings per common share:				
Net income	\$ 83,769	\$ 79,760	\$ 138,142	\$ 187,530
Less income related to unvested restricted shares	(138)	(297)	(285)	(789)
Income available to common shareholders - Basic	<u>\$ 83,631</u>	<u>\$ 79,463</u>	<u>\$ 137,857</u>	<u>\$ 186,741</u>
Weighted-average common shares outstanding - Basic	<u>165,975</u>	<u>180,710</u>	<u>174,949</u>	<u>185,521</u>
Basic earnings per common share	\$ 0.50	\$ 0.44	\$ 0.79	\$ 1.01
Diluted earnings per common share:				
Net income	\$ 83,769	\$ 79,760	\$ 138,142	\$ 187,530
Less income related to unvested restricted shares	(138)	(295)	(284)	(784)
Income available to common shareholders - Diluted	<u>\$ 83,631</u>	<u>\$ 79,465</u>	<u>\$ 137,858</u>	<u>\$ 186,746</u>
Weighted-average common shares outstanding - Basic	165,975	180,710	174,949	185,521
Effect of dilutive stock options and restricted stock units	<u>595</u>	<u>1,277</u>	<u>902</u>	<u>1,254</u>
Weighted-average common shares outstanding - Diluted	<u>166,570</u>	<u>181,987</u>	<u>175,851</u>	<u>186,775</u>
Diluted earnings per common share	\$ 0.50	\$ 0.44	\$ 0.78	\$ 1.00

8. SEGMENTS AND GEOGRAPHIC INFORMATION

We consider Michaels-U.S., Michaels-Canada, Aaron Brothers, Pat Catan's and Darice 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 Michaels-U.S., Michaels-Canada, Aaron Brothers and Pat Catan's have similar economic characteristics and meet the aggregation criteria set forth in ASC 280. Therefore, we combine these operating segments into one reporting segment. Darice does not meet the materiality criteria in ASC 280 and, therefore, is not disclosed separately as a reportable segment. Our chief operating decision makers evaluate historical operating performance and forecast future periods' operating performance based on operating income.

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

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
United States ⁽¹⁾	\$1,153,784	\$1,117,626	\$3,158,393	\$3,152,048
Canada	120,274	122,570	324,442	319,304
Total	\$1,274,058	\$1,240,196	\$3,482,835	\$3,471,352

(1) In March 2018, we closed substantially all of our Aaron Brothers stores. There were no Aaron Brothers net sales in the third quarter of fiscal 2018 and net sales totaled approximately \$25.2 million in the third quarter of fiscal 2017. For the nine months ended November 3, 2018 and October 28, 2017, Aaron Brothers net sales totaled approximately \$12.9 million and \$78.0 million, respectively.

9. CONTINGENCIES

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 employee. The lawsuit was 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 alleged 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 sought 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.*, in the U.S. District Court for the Northern District of Texas, *Michelle Bercut v. Michaels Stores, Inc.* in the Superior Court of California for Sonoma County, *Raini Burnside v. Michaels Stores, Inc.*, in the U.S. District Court for the Western District of Missouri, *Sue Gettings v. Michaels Stores, Inc.*, in the U.S. District Court for the Southern District of New York, and *Barbara Horton v. Michaels Stores, Inc.*, in the U.S. District Court for the Central District of California. All of the plaintiffs alleged violations of the FCRA. In addition, the *Castro*, *Horton* and *Janice Bercut* lawsuits also alleged violations of California's unfair competition law. The *Burnside*, *Horton* and *Gettings* lawsuits, as well as the claims by Michele Castro, have been dismissed. The *Graham*, *Janice Bercut* and *Michelle Bercut* lawsuits were transferred for centralized pretrial proceedings to the District of New Jersey. On January 24, 2017, the Company's motion to dismiss for lack of standing was granted, and the court declined to rule on the merits of plaintiffs' claims. The dismissal order was stayed for 30 days to allow the plaintiffs to amend their complaints. Because there were no amendments filed, two of the three centralized cases were dismissed and subsequently appealed to the U.S. Court of Appeals for the Third Circuit, and the remaining case (*Michelle Bercut*) was remanded to

California Superior Court. The parties reached a class settlement which was approved by the California Superior Court on October 10, 2018. The resolution of the lawsuits did not 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.

10. RELATED PARTY TRANSACTIONS

Affiliates of, or funds advised by, Bain Capital Private Equity, L.P. (“Bain Capital”) and The Blackstone Group L.P. (“The Blackstone Group”, together with Bain Capital and their applicable affiliates, the “Sponsors”) owned approximately 46% of our outstanding common stock as of November 3, 2018.

The Blackstone Group owns a majority equity position in RGIS, a vendor we utilized until February 2018 to count our store inventory. There were no payments associated with this vendor during the third quarter of fiscal 2018. Payments associated with this vendor during the third quarter of fiscal 2017 were \$2.3 million. Payments associated with this vendor during the nine months ended November 3, 2018 and October 28, 2017 were \$0.7 million and \$6.0 million, respectively. These expenses are included in selling, general and administrative (“SG&A”) in the consolidated statements of comprehensive income.

The Blackstone Group owns a majority equity position in Excel Trust, Inc., Blackstone Real Estate DDR Retail Holdings III, LLC and Blackstone Real Estate RC Retail Holdings, LLC, vendors we utilize to lease certain properties. Payments associated with these vendors during the third quarters of fiscal 2018 and fiscal 2017 were \$1.4 million and \$2.0 million, respectively. Payments made during the nine months ended November 3, 2018 and October 28, 2017 were \$4.7 million and \$5.4 million, respectively. These expenses are included in cost of sales and occupancy expense in the consolidated statements of comprehensive income.

The Blackstone Group owns a majority equity position in JDA Software Group, Inc., a vendor we utilize for transportation and supply chain software. Payments associated with this vendor during the third quarters of fiscal 2018 and fiscal 2017 were \$0.3 million. Payments made during the nine months ended November 3, 2018 and October 28, 2017 were \$2.2 million and \$1.0 million, respectively. These expenses are included in SG&A in the consolidated statements of comprehensive income.

Three of our current directors, Joshua Bekenstein, Ryan Cotton and Peter F. Wallace, are affiliates of either 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 November 3, 2018, affiliates of The Blackstone Group held \$93.2 million of our Amended Term Loan Credit Facility.

11. 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.

Michaels Stores, Inc.
Condensed Consolidated Balance Sheets
(in thousands)

ASSETS	November 3, 2018	February 3, 2018	October 28, 2017
Current assets:			
Cash and equivalents	\$ 101,895	\$ 425,129	\$ 176,007
Merchandise inventories	1,440,875	1,123,288	1,404,206
Prepaid expenses and other current assets	146,317	127,656	131,695
Total current assets	<u>1,689,087</u>	<u>1,676,073</u>	<u>1,711,908</u>
Property and equipment, net	453,396	420,020	401,892
Goodwill	119,074	119,074	119,074
Other assets	73,088	84,537	72,036
Total assets	<u>\$ 2,334,645</u>	<u>\$ 2,299,704</u>	<u>\$ 2,304,910</u>
LIABILITIES AND STOCKHOLDERS' DEFICIT			
Current liabilities:			
Accounts payable	\$ 645,469	\$ 483,002	\$ 674,222
Accrued liabilities and other	407,252	369,647	399,363
Current portion of long-term debt	240,261	24,900	140,125
Other current liabilities	41,948	124,881	60,884
Total current liabilities	<u>1,334,930</u>	<u>1,002,430</u>	<u>1,274,594</u>
Long-term debt	2,690,302	2,701,764	2,707,120
Other liabilities	156,770	165,662	108,112
Total stockholders' deficit	<u>(1,847,357)</u>	<u>(1,570,152)</u>	<u>(1,784,916)</u>
Total liabilities and stockholders' deficit	<u>\$ 2,334,645</u>	<u>\$ 2,299,704</u>	<u>\$ 2,304,910</u>

Michaels Stores, Inc.
Condensed Consolidated Statements of Comprehensive Income
(in thousands)

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Net sales	\$ 1,274,058	\$ 1,240,196	\$ 3,482,835	\$ 3,471,352
Cost of sales and occupancy expense	795,104	756,088	2,173,990	2,117,100
Gross profit	478,954	484,108	1,308,845	1,354,252
Selling, general and administrative	340,375	328,855	969,500	969,793
Restructure charge	—	—	44,278	—
Store pre-opening costs	1,196	952	3,995	2,592
Operating income	137,383	154,301	291,072	381,867
Interest and other expense	37,680	32,460	106,857	95,261
Losses on early extinguishment of debt and refinancing costs	—	—	1,835	—
Income before income taxes	99,703	121,841	182,380	286,606
Income taxes	15,771	41,806	43,722	98,601
Net income	\$ 83,932	\$ 80,035	\$ 138,658	\$ 188,005
Other comprehensive income, net of tax:				
Foreign currency translation adjustment and other	3,016	(4,418)	(3,230)	4,254
Comprehensive income	\$ 86,948	\$ 75,617	\$ 135,428	\$ 192,259

Michaels Stores, Inc.
Condensed Consolidated Statements of Cash Flows
(in thousands)

	39 Weeks Ended	
	November 3, 2018	October 28, 2017
Cash flows from operating activities:		
Net cash provided by operating activities	\$ 22,855	\$ 109,782
Cash flows used in investing activities:		
Additions to property and equipment	(119,553)	(72,640)
Cash flows from financing activities:		
Net repayments of debt	(106,756)	(266,875)
Net borrowings of debt	307,400	357,200
Payment of debt refinancing costs	(1,117)	—
Payment of dividend to Michaels Funding, Inc.	(426,063)	(245,514)
Net cash used in financing activities	(226,536)	(155,189)
Net change in cash and equivalents	(323,234)	(118,047)
Cash and equivalents at beginning of period	425,129	294,054
Cash and equivalents at end of period	\$ 101,895	\$ 176,007

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), 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 February 3, 2018 (“Annual Report”) filed with the Securities and Exchange Commission (“SEC”) pursuant to Section 13 or 15(d) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) on March 22, 2018.

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 2018” relate to the 52 weeks ending February 2, 2019 and references to “fiscal 2017” relate to the 53 weeks ended February 3, 2018. In addition, all references to “the third quarter of fiscal 2018” relate to the 13 weeks ended November 3, 2018 and all references to “the third quarter of fiscal 2017” relate to the 13 weeks ended October 28, 2017. Finally, all references to “the nine months ended November 3, 2018” relate to the 39 weeks ended November 3, 2018 and all references to “the nine months ended October 28, 2017” relate to the 39 weeks ended October 28, 2017. Because of the seasonal nature of our business, the results of operations for the 13 and 39 weeks ended November 3, 2018 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, Aaron Brothers and Pat Catan’s. We also operate an international wholesale business under the Darice brand name and a market-leading, vertically-integrated custom framing business under the Artistree brand name. As of November 3, 2018, we operated 1,256 Michaels stores and 36 Pat Catan’s stores.

In March 2018, we closed substantially all of our Aaron Brothers stores and began the process of repositioning our Aaron Brothers brand as a store-within-a-store, providing custom framing services in all Michaels stores. In the first nine months of fiscal 2018, we recorded a restructure charge totaling \$44.3 million, consisting primarily of costs associated with the termination of the remaining lease obligations, the write-off of fixed assets and employee-related expenses. For the nine months ended November 3, 2018 and October 28, 2017, Aaron Brothers net sales totaled approximately \$12.9 million and \$78.0 million, respectively. Excluding the restructure charge, Aaron Brothers did not have a material impact on the Company’s operating income in the periods presented.

Net sales for the third quarter of fiscal 2018 increased 2.7% compared to the same period in the prior year. The increase in net sales was due to a 3.8% increase in comparable store sales (4.3% at constant exchange rates) and a \$12.5 million increase related to 19 additional Michaels stores opened (net of closures) since the third quarter of fiscal 2017. The increase was partially offset by the closure of substantially all of our Aaron Brothers stores. Gross profit as a percent of net sales decreased 140 basis points to 37.6% during the third quarter of fiscal 2018 due primarily to higher distribution related costs and an increase in inventory reserves recorded during the quarter. Operating income as a percent of net sales decreased to 10.8% for the third quarter of fiscal 2018 compared to 12.4% in the same period in the prior year.

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. All Aaron Brothers stores have been excluded from comparable stores sales in fiscal 2018.

Operating Information

The following table sets forth certain operating data:

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Michaels stores:				
Open at beginning of period	1,251	1,230	1,238	1,223
New stores	6	8	21	16
Relocated stores opened	4	4	20	12
Closed stores	(1)	(1)	(3)	(2)
Relocated stores closed	(4)	(4)	(20)	(12)
Open at end of period	1,256	1,237	1,256	1,237
Aaron Brothers stores:				
Open at beginning of period	—	101	97	109
Closed stores	—	(3)	(97)	(11)
Open at end of period	—	98	—	98
Pat Catan's stores:				
Open at beginning of period	36	35	36	35
New stores	—	1	—	1
Open at end of period	36	36	36	36
Total store count at end of period	1,292	1,371	1,292	1,371
Other Operating Data:				
Average inventory per Michaels store (in thousands) ⁽¹⁾	\$ 1,039	\$ 1,028	\$ 1,039	\$ 1,028
Comparable store sales	3.8 %	1.0 %	1.4 %	0.1 %
Comparable store sales, at constant currency	4.3 %	0.5 %	1.4 %	— %

(1) The calculation of average inventory per Michaels store excludes our Aaron Brothers and Pat Catan's stores.

Results of Operations

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

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Net sales	100.0 %	100.0 %	100.0 %	100.0 %
Cost of sales and occupancy expense	62.4	61.0	62.4	61.0
Gross profit	37.6	39.0	37.6	39.0
Selling, general and administrative	26.7	26.6	27.9	28.0
Restructure charge	—	—	1.3	—
Store pre-opening costs	0.1	0.1	0.1	0.1
Operating income	10.8	12.4	8.3	11.0
Interest expense	3.0	2.6	3.1	2.7
Losses on early extinguishments of debt and refinancing costs	—	—	0.1	—
Other (income) expense, net	—	—	(0.1)	—
Income before income taxes	7.8	9.8	5.2	8.2
Income taxes	1.2	3.4	1.3	2.8
Net income	6.6 %	6.4 %	4.0 %	5.4 %

13 Weeks Ended November 3, 2018 Compared to the 13 Weeks Ended October 28, 2017

Net Sales. Net sales increased \$33.9 million in the third quarter of fiscal 2018, or 2.7%, compared to the third quarter of fiscal 2017. The increase in net sales was due to a \$45.3 million increase in comparable store sales, a \$12.5 million increase related to 19 additional Michaels stores opened (net of closures) since the third quarter of fiscal 2017 and a \$1.0 million increase in wholesale revenue. The increase was partially offset by a \$25.2 million decrease related to the closure of substantially all of our Aaron Brothers stores. Comparable store sales increased 3.8%, or 4.3% at constant exchange rates, compared to the third quarter of fiscal 2017 due to an increase in average ticket, partially offset by a decrease in customer transactions.

Gross Profit. Gross profit was 37.6% of net sales in the third quarter of fiscal 2018 compared to 39.0% in the third quarter of fiscal 2017. The 140 basis point decrease was primarily due to higher distribution related costs and an increase in inventory reserves recorded during the quarter. The decrease was partially offset by improved occupancy cost leverage, a decrease in promotional activity and our ongoing sourcing initiatives.

Selling, General and Administrative. Selling, general and administrative (“SG&A”) was 26.7% of net sales in the third quarter of fiscal 2018 compared to 26.6% in the third quarter of fiscal 2017. SG&A increased \$11.3 million to \$340.6 million in the third quarter of fiscal 2018. The increase was primarily due to a \$6.8 million increase in performance-based compensation, a \$5.0 million increase in marketing expenses, a \$3.3 million increase in payroll costs and \$3.0 million associated with operating 19 additional Michaels stores (net of closures) since the third quarter of fiscal 2017. The increase was partially offset by a \$9.1 million decrease related to the Aaron Brothers store closures during the first quarter of fiscal 2018.

Interest Expense. Interest expense increased \$5.0 million to \$37.8 million in the third quarter of fiscal 2018 compared to the same period in the prior year. The increase was primarily due to \$3.4 million as a result of a higher interest rate on our amended term loan credit facility and \$1.6 million related to settlement payments associated with our interest rate swaps.

Income Taxes. The effective tax rate was 15.8% in the third quarter of fiscal 2018 compared to 34.3% in the third quarter of fiscal 2017. The effective tax rate in the third quarter of fiscal 2018 was lower than the same period in the prior year due to benefits recognized related to the Tax Cuts and Jobs Act of 2017 (“Tax Act”), including a decrease in the federal statutory rate from 35% to 21%, a \$4.0 million provisional benefit related to the revaluation of deferred tax assets and a \$3.1 million provisional benefit related to repatriation taxes for accumulated earnings of foreign subsidiaries.

39 Weeks Ended November 3, 2018 Compared to the 39 Weeks Ended October 28, 2017

Net Sales. Net sales increased \$11.5 million in the first nine months of fiscal 2018, or 0.3%, compared to the first nine months of fiscal 2017. The increase in net sales was due to a \$44.9 million increase in comparable store sales and a \$32.2 million increase related to 19 additional Michaels stores opened (net of closures) since the third quarter of fiscal 2017. The increase was partially offset by a \$65.0 million decrease related to the closure of substantially all of our Aaron Brothers stores and a \$1.4 million decrease in wholesale revenue. Comparable store sales increased 1.4% compared to the first nine months of fiscal 2017 due to an increase in average ticket, partially offset by a decrease in customer transactions.

Gross Profit. Gross profit was 37.6% of net sales in the first nine months of fiscal 2018 compared to 39.0% in the first nine months of fiscal 2017. The 140 basis point decrease was primarily due to higher distribution related costs, an increase in promotional activity and an increase in inventory reserves recorded during the year. The decrease was partially offset by our ongoing sourcing initiatives.

Selling, General and Administrative. SG&A was 27.9% of net sales in the first nine months of fiscal 2018 compared to 28.0% in the first nine months of fiscal 2017. SG&A decreased \$0.4 million to \$970.2 million in the first nine months of fiscal 2018. The decrease was primarily due to a \$23.4 million decrease related to the Aaron Brothers store closures during the first quarter of fiscal 2018 and a \$4.7 million decrease in performance-based compensation. The decrease was partially offset by an \$8.3 million increase associated with operating 19 additional Michaels stores (net of closures) since the third quarter of fiscal 2017, a \$6.2 million increase in marketing expenses, a \$4.4 million increase in payroll costs and \$4.4 million in professional fees related to strategic initiatives.

Restructure Charge. We recorded a restructure charge of \$44.3 million in the first nine months of fiscal 2018 primarily related to the closure of substantially all of our Aaron Brothers stores.

Interest Expense. Interest expense increased \$15.2 million to \$109.5 million in the first nine months of fiscal 2018 compared to the first nine months of fiscal 2017. The increase was primarily due to \$11.0 million as a result of a higher interest rate on our amended term loan credit facility and \$3.7 million related to settlement payments associated with our interest rate swaps.

Losses on Early Extinguishments of Debt and Refinancing Costs. We recorded a loss on the early extinguishment of debt of \$1.8 million in the first nine months of fiscal 2018 related to the refinancing of our amended and restated term loan credit facility.

Income Taxes. The effective tax rate was 24.0% in the first nine months of fiscal 2018 compared to 34.4% in the first nine months of fiscal 2017. The effective tax rate was lower than the same period in the prior year due to benefits recognized related to the Tax Act, including a decrease in the federal statutory rate from 35% to 21% and a \$4.0 million provisional benefit related to the revaluation of deferred tax assets. The decrease in the effective tax rate was partially offset by a provisional charge of \$5.0 million related to repatriation taxes for accumulated earnings of foreign subsidiaries.

Liquidity and Capital Resources

We require cash principally for day-to-day operations, to finance capital investments, purchase inventory, 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 Amended 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 Annual Report on Form 10-K for the fiscal year ended February 3, 2018 or our failure to meet our debt covenants. Our Amended Revolving Credit Facility provides senior secured financing of up to \$850.0 million, subject to a borrowing base. As of November 3, 2018, the borrowing base was \$850.0 million, of which we had \$65.0 million of outstanding standby letters of credit and \$567.0 million of unused borrowing capacity. Our cash and cash equivalents totaled \$102.7 million at November 3, 2018.

In September 2018, the Board of Directors authorized a new share repurchase program for the Company to purchase \$500.0 million of the Company’s common stock on the open market or through accelerated share repurchase transactions. The share repurchase program does not have an expiration date, and the timing and number of repurchase transactions under the program will depend on market conditions, corporate considerations, debt agreements and regulatory requirements. Shares repurchased under the program are held as treasury shares until retired. In June 2018, the Company entered into an accelerated share repurchase agreement (“ASR Agreement”) with JPMorgan Chase Bank, N.A. (“JPMorgan”). Under the ASR Agreement, we paid JPMorgan a purchase price of \$250.0 million for delivery of 12.4 million shares of our common stock. The total number of shares repurchased was based upon a volume weighted average price of our stock over a predetermined period. The ASR agreement was completed on August 30, 2018. During the nine months ended November 3, 2018, we repurchased 23.6 million shares under our share repurchase programs for an aggregate amount of \$434.2 million, inclusive of the ASR Agreement. As of November 3, 2018, we had \$416.0 million of availability remaining under our current share repurchase program.

On May 23, 2018, Michaels Stores, Inc. (“MSI”) entered into an amendment with JPMorgan and other lenders to amend and restate our term loan credit facility. The amended and restated credit agreement, together with the related security, guarantee and other agreements, is referred to as the “Amended and Restated Term Loan Credit Facility”. Borrowings under the Amended and Restated Term Loan Credit Facility bear interest at a rate per annum, at MSI’s option, of either (a) a margin of 1.50% plus a base rate defined as the highest of (1) the prime rate of JPMorgan, (2) the federal funds effective rate plus 0.5%, and (3) the one-month London Interbank Offered Rate (“LIBOR”) plus 1% or (b) a margin of 2.50% plus the applicable LIBOR. MSI is required to make scheduled quarterly payments equal to 0.25% of the original principal amount of the term loans (subject to adjustments relating to the incurrence of additional term loans) for the first four years and two quarters of the Amended and Restated Term Loan Credit Facility, with the balance to be paid on January 28, 2023. All other terms under the Amended Term Loan Credit Facility have remained unchanged. As a result of this refinancing, we recorded a loss on the early extinguishment of debt of \$1.8 million in the second quarter of fiscal 2018.

We had total outstanding debt of \$2,943.0 million at November 3, 2018, of which \$2,433.0 million was subject to variable interest rates and \$510.0 million was subject to fixed interest rates. In April 2018, we executed two interest rate swaps with an aggregate notional value of \$1.0 billion associated with our outstanding Amended Term Loan Credit Facility. The interest rate swaps have a maturity date of April 30, 2021 and were executed for risk management and are not held for trading purposes. The objective of the interest rate swaps is to hedge the variability of cash flows resulting from fluctuations in the one-month LIBOR. The swaps replaced the one-month LIBOR with a fixed interest rate of 2.7765% and payments are settled monthly.

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 invest in growth opportunities, repurchase outstanding shares and repay portions of our indebtedness, depending on prevailing market conditions, liquidity requirements, contractual restrictions and other factors. As such, 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. If we use our excess cash flows to repay our debt, it will reduce the amount of excess cash available for additional capital expenditures.

Cash Flow from Operating Activities

Cash flows provided by operating activities were \$25.8 million in the first nine months of fiscal 2018 compared to \$106.4 million in the first nine months of fiscal 2017. The decrease in cash provided by operating activities was primarily due to additional investments in inventory to support better in-stock positions for the peak Holiday season and an increase in inventory related to our wholesale business.

Inventory at the end of the third quarter of fiscal 2018 increased \$36.7 million, or 2.6%, to \$1,440.9 million, compared to \$1,404.2 million at the end of the third quarter of fiscal 2017. The increase was primarily due to additional inventory associated with the operation of 19 additional Michaels stores (net of closures) since the third quarter of fiscal 2017, an increase in inventory related to our wholesale business and additional investments in inventory to support better in-stock positions for the peak Holiday season. The increase was partially offset by a decrease in inventory related to the Aaron Brothers store closures in the first quarter of fiscal 2018. Average inventory per Michaels store (inclusive of distribution centers, in-transit and inventory for the Company's e-commerce site) increased 1.1% to \$1,039,000 at November 3, 2018 from \$1,028,000 at October 28, 2017.

Cash Flow from Investing Activities

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

	39 Weeks Ended	
	November 3, 2018	October 28, 2017
New and relocated stores including stores not yet opened ⁽¹⁾	\$ 27,399	\$ 12,055
Existing stores	32,694	23,483
Information systems	43,602	23,929
Corporate and other	15,858	13,173
	<u>\$ 119,553</u>	<u>\$ 72,640</u>

- (1) In the first nine months of fiscal 2018, we incurred capital expenditures related to the opening of 41 Michaels stores, including the relocation of 20 stores. In the first nine months of fiscal 2017, we incurred capital expenditures related to the opening of 28 Michaels stores, including the relocation of 12 stores, and the opening of the one Pat Catan's store.

Non-GAAP Measures

The following table sets forth certain non-GAAP measures used by the Company to manage our performance and measure compliance with certain debt covenants. The Company defines "EBITDA" as net income before interest, income taxes, depreciation and amortization. The Company defines "Adjusted EBITDA" as EBITDA adjusted for certain defined amounts in accordance with the Company's Amended Term Loan Credit Facility and Amended Revolving Credit Facility (together the "Senior Secured Credit Facilities").

The Company has presented EBITDA 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 Senior Secured Credit Facilities that 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.

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As EBITDA and Adjusted EBITDA are not measures of liquidity calculated in accordance with U.S. generally accepted accounting principles (“GAAP”), these measures should not be considered in isolation of, or as substitutes for, net cash provided by operating activities as an indicator of liquidity. Our computation of EBITDA and Adjusted EBITDA may differ from similarly titled measures used by other companies.

The following table shows a reconciliation of EBITDA and Adjusted EBITDA to net income and net cash provided by operating activities (in thousands):

	13 Weeks Ended		39 Weeks Ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
Net cash provided by operating activities	\$ 112,376	\$ 110,462	\$ 25,814	\$ 106,427
Depreciation and amortization	(30,879)	(28,809)	(89,933)	(86,232)
Share-based compensation	(8,446)	(7,675)	(20,780)	(18,232)
Debt issuance costs amortization	(1,237)	(1,274)	(3,759)	(3,823)
Accretion of long-term debt, net	129	127	385	379
Restructure charge	—	—	(44,278)	—
Deferred income taxes	(6,940)	(754)	(7,710)	(529)
Losses on early extinguishments of debt and refinancing costs	—	—	(1,835)	—
Changes in assets and liabilities	18,766	7,683	280,238	189,540
Net income	83,769	79,760	138,142	187,530
Interest expense	37,798	32,818	109,493	94,305
Income taxes	15,719	41,640	43,557	98,314
Depreciation and amortization	30,879	28,809	89,933	86,232
Interest income	(137)	(190)	(2,385)	(443)
EBITDA	168,028	182,837	378,740	465,938
Adjustments:				
Losses on early extinguishments of debt and refinancing costs	—	—	1,835	—
Share-based compensation	8,446	7,675	20,780	18,232
Restructure charge	—	—	44,278	—
Severance costs	—	285	902	862
Store pre-opening costs	1,196	952	3,995	2,592
Store remodel costs	1,325	424	5,079	1,401
Foreign currency transaction (gains) losses	(149)	(355)	(950)	1,092
Store closing costs	(328)	109	3,321	2,122
Other ⁽¹⁾	754	952	2,035	2,451
Adjusted EBITDA	\$ 179,272	\$ 192,879	\$ 460,015	\$ 494,690

(1) Other adjustments primarily 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. Statements regarding sufficiency of capital resources and planned uses of excess cash flow as well as any other 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. Most of these factors are outside of our control and are difficult to predict. Such risks and uncertainties include, but are not limited to the following:

- risks related to the effect of economic uncertainty;
- risks related to our substantial indebtedness;
- restrictions in our debt agreements that limit our flexibility in operating our business;
- changes in customer demand could materially adversely affect our sales, results of operations and cash flow;
- competition, including internet-based competition, could negatively impact our business;
- a weak fourth quarter would materially adversely affect our results of operations;
- 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 results may be adversely affected by serious disruptions or catastrophic events, including geopolitical events and weather;
- 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;
- our reliance on foreign suppliers increases our risk of obtaining adequate, timely and cost-effective product supplies;
- our failure to increase comparable store sales and open new stores could impair our ability to improve our sales, profitability and cash flows;
- damage to the reputation of the Michaels brand or our private and exclusive brands could adversely affect our sales;
- 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;
- 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;
- 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;
- any difficulty executing or integrating an acquisition, a business combination or a major business initiative could adversely affect our business or results of operations;
- 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 estimates or projections used to assess fair value of intangible assets, goodwill and property and equipment may cause us to incur impairment charges that could adversely affect our results of operations;
- 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;
- failure to attract and retain quality sales, distribution center and other team members in appropriate numbers as well as experienced buying and management personnel could adversely affect our performance;
- affiliates of, or funds advised by, Bain Capital Private Equity, L.P. and The Blackstone Group L.P. own approximately 46% of the outstanding shares of our common stock and as a result will have the ability to strongly influence our decisions, and they may have interests that differ from those of other stockholders; and
- 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.

For more details on factors that may cause actual results to differ materially from such forward-looking statements 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. A 10% increase or decrease in the exchange rate of the Canadian dollar would have increased or decreased net income by approximately \$10 million for the 39 weeks ended November 3, 2018.

Interest Rate Risk

We have market risk exposure arising from changes in interest rates on our Amended Term Loan Credit Facility and our Amended Revolving Credit Facility. The interest rates on our Amended Term Loan Credit Facility and our Amended Revolving Credit Facility will reprice periodically, which will impact our earnings and cash flow. In April 2018, we executed two interest rate swap agreements with an aggregate notional value of \$1.0 billion which are intended to mitigate interest rate risk associated with future changes in interest rates for borrowings under our Amended Term Loan Credit Facility. As a result of these interest rate swaps, our exposure to interest rate volatility for \$1.0 billion of our Amended Term Loan Credit Facility was eliminated beginning in the second quarter of fiscal 2018. 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 November 3, 2018, a 100 basis point change in interest rates would impact income before income taxes by approximately \$14 million for fiscal 2018. A 100 basis point change in interest rates would impact the fair value of our long-term fixed rate debt by approximately \$21 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 Exchange Act) 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 Exchange Act, 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 November 3, 2018 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Part II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Information regarding legal proceedings is incorporated by reference from Note 9 to the consolidated financial statements in this Quarterly Report on Form 10-Q.

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 third quarter of fiscal 2018:

<u>Period</u>	<u>Total Number of Shares Purchased (a)</u>	<u>Average Price Paid per Share</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Plan (b)</u>	<u>Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plan (b) (in thousands)</u>
August 5, 2018 - September 1, 2018	1,706,167	\$ 20.09	1,697,904	\$ 100,001
September 2, 2018 - October 6, 2018	6,220,902	16.91	6,143,316	496,250
October 7, 2018 - November 3, 2018	5,001,054	16.07	5,000,500	415,994
Total	12,928,123	\$ 17.00	12,841,720	\$ 415,994

- (a) These amounts reflect the following transactions during the third quarter of fiscal 2018: (i) the repurchase of shares as part of our publicly announced share repurchase program and (ii) the surrender of shares of common stock to the Company to satisfy tax withholding obligations in connection with the vesting of employee restricted stock equity awards.
- (b) In September 2018, the Board of Directors authorized the Company to purchase up to \$500.0 million of the Company's common stock on the open market or through accelerated share repurchase transactions. The share repurchase program does not have an expiration date. The Company has retired and intends to continue to retire shares repurchased under the program.

ITEM 6. EXHIBITS

(a) Exhibits:

Exhibit Number	Description of Exhibit
10.1	<u>Form of Restricted Stock Unit Agreement for Employees under the Second Amended and Restated 2014 Omnibus Long-Term Incentive Plan (filed herewith).</u>
31.1	<u>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 (filed herewith).</u>
31.2	<u>Certifications of Denise A. Paulonis 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 (filed herewith).</u>
32.1	<u>Certification pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002 (filed herewith).</u>
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

*Management contract or compensatory plan or agreement.

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
Chairman and Chief Executive Officer
(Principal Executive Officer)

By: /s/ Denise A. Paulonis
Denise A. Paulonis
Executive Vice President and Chief Financial
Officer
(Principal Financial Officer)

Date: December 7, 2018

Exhibit 10.1

Name:	●
Number of Restricted Stock Units:	●
Date of Grant:	●

The Michaels Companies, Inc.
2014 Omnibus Long-Term Incentive Plan

Restricted Stock Unit Agreement

This agreement (this “Agreement”) evidences the grant of restricted stock units (the “Restricted Stock Units”) by The Michaels Companies, Inc. (the “Company”) to the individual named above (the “Grantee”), pursuant to and subject to the terms of The Michaels Companies, Inc. 2014 Omnibus Long-Term Incentive Plan (as amended from time to time, the “Plan”), which is incorporated herein by reference.

1. Grant of Restricted Stock Units. The Company hereby grants to the Grantee on the date of grant set forth above (the “Date of Grant”) an award (the “Award”) consisting of the right to receive, on the terms provided herein and in the Plan, one share of Stock with respect to each Restricted Stock Unit forming part of the Award, in each case, subject to adjustment pursuant to Section 7(b) of the Plan in respect of transactions occurring after the date hereof.

2. Meaning of Certain Terms. Each initially capitalized term used but not separately defined herein has the meaning assigned to such term in the Plan. The following terms have the following meanings:

- (a) “Change of Control” means the occurrence of any of the following:
- (i) any consolidation or merger of the Company with or into any other corporation or other Person, or any other corporate reorganization or transaction (including the acquisition of capital stock of the Company), whether or not the Company is a party thereto, in which the stockholders of the Company immediately prior to such consolidation, merger, reorganization or transaction, own capital stock either (A) representing directly, or indirectly through one or more entities, less than fifty percent (50%) of the economic interests in or voting power of the Company or other surviving entity immediately after such consolidation, merger, reorganization or transaction or (B) that does not directly, or indirectly through one or more entities, have the power to elect a majority of the entire board of directors of the Company or other surviving entity immediately after such consolidation, merger, reorganization or transaction; (ii) any stock sale or other transaction or series of related transactions, whether or not the Company is a party thereto, after giving effect to which in excess of fifty percent (50%) of the Company’s voting power is owned directly, or indirectly through one or more entities, by any Person and its “affiliates” or “associates” (as such terms are defined in the rules adopted by the Securities and Exchange Commission under the

Securities Exchange Act of 1934, as in effect from time to time), other than the Investors and their respective affiliated funds, excluding, in any case referred to in clause (i) or (ii) an initial public offering or any bona fide primary or secondary public offering following the occurrence of an initial public offering; or (iii) a sale, lease or other disposition of all or substantially all of the assets of the Company.

- (b) “Investors” means Bain Capital Partners, LLC and The Blackstone Group L.P.
- (c) “Person” means any individual, partnership, corporation, company, association, trust, joint venture, limited liability company, unincorporated organization, entity or division, or any government, governmental department or agency or political subdivision thereof.

3. Vesting. The term “vest” as used herein with respect to any Restricted Stock Unit means the lapsing of the restrictions described herein with respect to such Restricted Stock Unit. Unless earlier terminated, forfeited, relinquished or expired, the Award shall vest as follows, provided in each case that the Grantee has remained in continuous Employment from the Date of Grant through the applicable vesting date:

[INSERT VESTING CRITERIA].

In the event (i) the Restricted Stock Units (or any portion thereof) are outstanding as of immediately prior to a Change of Control and the Administrator provides for the assumption or continuation of, or the substitution of a substantially equivalent award for, the Restricted Stock Units (or any portion thereof) in accordance with Section 7(a)(i) of the Plan (the “Rollover Award”) and (ii) the Grantee’s Employment is terminated by the Company (or its successor) without Cause within the twelve (12) months following the Change of Control, the Rollover Award to the extent still outstanding will vest in full on the date of the termination of the Grantee’s Employment. For the avoidance of doubt, if the Administrator does not provide for such assumption, continuation, or substitution in connection with a Change of Control, then the treatment of the Restricted Stock Units in such Change of Control will be as provided for by the Administrator in its sole discretion pursuant to Section 7(a)(2) through Section 7(a)(5) of the Plan.

4. Forfeiture Risk. If the Grantee’s Employment ceases for any reason, including death, any then outstanding and unvested Restricted Stock Units acquired by the Grantee hereunder shall be automatically and immediately forfeited, subject to Section 3(b) above.

5. Delivery of Stock. The Company shall deliver to the Grantee as soon as practicable upon the vesting of the Restricted Stock Units (or any portion thereof), but in all events no later than thirty (30) days following the date on which such Restricted Stock

Units vest, one share of Stock with respect to each such vested Restricted Stock Unit, subject to the terms of the Plan and this Agreement.

6. Dividends, etc. The Grantee shall have the rights of a shareholder with respect to a share of Stock subject to the Award only at such time, if any, as such share is actually delivered under the Award. Without limiting the generality of the foregoing and for the avoidance of doubt, the Grantee shall not be entitled to vote any share of Stock subject to the Award or to receive or be credited with any dividend or other distribution declared and payable on any such share unless such share has been actually delivered hereunder and is held by the Grantee on the record date for such vote or dividend (or other distribution), as the case may be.

7. Nontransferability. Neither the Award nor the Restricted Stock Units may be transferred.

8. Certain Tax Matters.

- (a) The Grantee expressly acknowledges and agrees that the Grantee's rights hereunder, including the right to be issued shares of Stock upon the vesting of the Restricted Stock Units (or any portion thereof), are subject to the Grantee's promptly paying, or in respect of any later requirement of withholding being liable promptly to pay at such time as such withholdings are due, to the Company in cash (or by such other means as may be acceptable to the Administrator in its discretion) all taxes required to be withheld, if any. No shares of Stock will be required to be transferred pursuant to the vesting of the Restricted Stock Units (or any portion thereof) unless and until the Grantee or the person then holding the Award has remitted to the Company an amount in cash sufficient to satisfy any federal, state, or local requirements with respect to tax withholdings then due and has committed (and by accepting the Award the Grantee shall be deemed to have committed) to pay in cash all tax withholdings required at any later time in respect of the transfer of such shares, or has made other arrangements satisfactory to the Administrator with respect to such taxes. The Grantee also authorizes the Company and its subsidiaries to withhold such amounts from any amounts otherwise owed to the Grantee, but nothing in this sentence shall be construed as relieving the Grantee of any liability for satisfying his or her obligations under the preceding provisions of this Section.
- (b) The Grantee expressly acknowledges that because the Award consists of an unfunded and unsecured promise by the Company to deliver Stock in the future, subject to the terms hereof, it is not possible to make a so-called "83(b) election" with respect to the Award.

9. Forfeiture/Recovery of Compensation. By accepting the Award the Grantee expressly acknowledges and agrees that his or her rights, and those of any permitted transferee, under the Award or to any Stock received following the vesting of the Award or proceeds from the disposition thereof, are subject to Section 6(a)(5) of the Plan (including any successor provision) and Section 10 of this Agreement. Nothing in the preceding sentence shall be construed as limiting the general application of Section 13 of this Agreement.

10. Non-Competition/Non-Solicitation. The Grantee hereby acknowledges that the Company and its Affiliates have invested and continue to invest considerable resources in developing Company Information (as defined below) and trade secrets, and in establishing and maintaining relationships with customers, employees, and vendors. The Grantee hereby further acknowledges that the Award is being furnished to the Grantee as good and valuable consideration, among other consideration, in exchange for the below covenants, which are necessary to protect the Company Information, trade secrets, and goodwill of the Company and its Affiliates:

- (a) *Non-Competition.* The Grantee covenants and agrees that during the Grantee's Employment and for a period of twelve (12) months (and such period shall be tolled on a day-to-day basis for each day during which the Grantee participates in any activity in violation of the restrictions set forth in this Section 10(a)) following the termination of the Grantee's Employment, whether such termination occurs at the insistence of the Company or its Affiliates or the Grantee (for whatever reason), the Grantee will not, directly or indirectly, alone or in association with others, anywhere in the Territory (as defined below), own, manage, operate, control or participate in the ownership, management, operation or control of, or be connected as an officer, employee, investor, principal, joint venturer, shareholder, partner, director, consultant, agent or otherwise with, or have any financial interest (through stock or other equity ownership, investment of capital, the lending of money or otherwise) in, any business, venture or activity that directly or indirectly competes, or is in planning, or has undertaken any preparation, to compete, with the Business of the Company or any of its Immediate Affiliates (any Person who engages in any such business venture or activity, a "Competitor"), except that nothing contained in this Section 10(a) shall prevent the Grantee's wholly passive ownership of two percent (2%) or less of the equity securities of any Competitor that is a publicly-traded company. For purposes of this Section 10(a), the "Business of the Company or any of its Immediate Affiliates." is that of arts and crafts, or framing specialty retailer or wholesaler providing materials, ideas and education for creative activities, or framing, as well as any other business that the Company or any of its Immediate Affiliates conducts or is actively planning to conduct at any time during the Grantee's Employment, or with respect to the Grantee's obligations following the termination of the Grantee's Employment the twelve (12) months immediately preceding the termination of the Grantee's Employment; provided, that the term

“Competitor” shall not include any business, venture or activity whose gross receipts derived from the retail or wholesale sale of arts and crafts, or framing products and services (aggregated with the gross receipts derived from the retail and wholesale sale of such products or any related business, venture or activity) are less than ten percent (10%) of the aggregate gross receipts of such businesses, ventures or activities. For purposes of this Section 10(a), the “Territory” is comprised of those states within the United States, those provinces of Canada, and any other geographic area in which the Company or any of its Immediate Affiliates was doing business or actively planning to do business at any time during the Grantee’s Employment, or with respect to the Grantee’s obligations following his or her termination of Employment the twelve (12) months immediately preceding the termination of the Grantee’s Employment. For purposes of this Section, “Immediate Affiliates” means those Affiliates which are one of the following: (i) a direct or indirect subsidiary of the Company, (ii) a parent to the Company or (iii) a direct or indirect subsidiary of such a parent.

- (b) *Non-Solicitation.* The Grantee covenants and agrees that during the Grantee’s Employment and for a period of twelve (12) months (and such period shall be tolled on a day-to-day basis for each day during which the Grantee participates in any activity in violation of the restrictions set forth in this Section 10(b)) after the termination of the Grantee’s Employment, whether such termination occurs at the insistence of the Company or the Grantee (for whatever reason), the Grantee shall not, and shall not assist any other Person to, (i) hire or solicit for hire any employee of the Company or any of its Immediate Affiliates or seek to persuade any employee of the Company or any of its Immediate Affiliates to discontinue employment or (ii) solicit or encourage any independent contractor providing services to the Company or any of its Immediate Affiliates to terminate or diminish its relationship with them; provided, however, that after termination of the Grantee’s Employment, these restrictions shall apply only with respect to employees of, and independent contractors providing services to, the Company or any of its Immediate Affiliates who were such on the date that the Grantee’s Employment terminated or at any time during the nine (9) months immediately preceding such termination date.
- (c) *Goodwill and Company Information.* The Grantee acknowledges the importance to the Company and its Affiliates of protecting their legitimate business interests, including without limitation the valuable Company Information and goodwill that they have developed or acquired at considerable expense. The Grantee acknowledges and agrees that in the course of the Grantee’s Employment, the Grantee has acquired: (i) confidential information including without limitation information received by the Company (or any of its Affiliates) from third parties, under confidential conditions, (ii) other technical, product, business, financial or

development information from the Company (or any of its Affiliates), the use or disclosure of which reasonably might be construed to be contrary to the interest of the Company (or any of its Affiliates), or (iii) any other proprietary information or data, including but not limited to identities, responsibilities, contact information, performance and/or compensation levels of employees, costs and methods of doing business, systems, processes, computer hardware and software, compilations of information, third-party IT service providers and other Company or its Affiliates' vendors, records, sales reports, sales procedures, financial information, customer requirements and confidential negotiated terms, pricing techniques, customer lists, price lists, information about past, present, pending and/or planned Company or its Affiliates' transactions not publically disclosed and other confidential information which the Grantee may have acquired during the Grantee's Employment (hereafter collectively referred to as "Company Information") which are owned by the Company or its Affiliates and regularly used in the operation of its business, and as to which precautions are taken to prevent dissemination to persons other than certain directors, officers and employees and if disclosed, would assist in competition against the Company or any of its Affiliates. The Grantee understands and agrees that such Company Information was and will be disclosed to the Grantee in confidence and for use only in performing work for the Company or its Affiliates. The Grantee understands and agrees that the Grantee: (x) will keep such Company Information confidential at all times, (y) will not disclose or communicate Company Information to any third party, and (z) will not make use of Company Information on the Grantee's own behalf, or on behalf of any third party. In view of the nature of the Grantee's Employment and the nature of Company Information the Grantee receives during the course of the Grantee's Employment, the Grantee agrees that any unauthorized disclosure to third parties of Company Information would cause irreparable damage to the confidential or trade secret status of Company Information. The Grantee further acknowledges and agrees that the restrictions on his or her activities set forth above are necessary to protect the goodwill, Company Information and other legitimate interests of the Company and its Affiliates and that the Grantee's acceptance of these restrictions is a condition of receipt of the Award, to which the Grantee would not otherwise be entitled, and the Award is good and sufficient consideration to support the Grantee's agreement to and compliance with these covenants.

- (d) *Remedies.* In the event of a breach or threatened breach by the Grantee of any of the covenants contained in Section 10(a), 10(b) or 10(c):
- (i) the Grantee hereby consents and agrees that (x) any unvested Restricted Stock Units and (y) all shares of Stock held by the Grantee following the vesting of the Restricted Stock Units shall be forfeited effective as of the date of such breach or

threatened breach, unless sooner terminated by operation of another term or condition of this Agreement or the Plan;

(ii) the Grantee hereby consents and agrees that if the Grantee has sold any shares of Stock upon or following the vesting of the Restricted Stock Units within twelve (12) months prior to the date of such breach or threatened breach, the Grantee shall pay to the Company the gross proceeds realized by the Grantee in connection with such sale; and

(iii) the Grantee hereby consents and agrees that the Company shall be entitled to seek, in addition to other available remedies, a temporary or permanent injunction or other equitable relief against such breach or threatened breach from any court of competent jurisdiction, without the necessity of showing any actual damages or that money damages would not afford an adequate remedy, and without the necessity of posting any bond or other security. The aforementioned equitable relief shall be in addition to, not in lieu of, legal remedies, monetary damages or other available forms of relief.

- (e) *General.* The Grantee agrees that the above restrictive covenants are completely severable and independent agreements supported by good and valuable consideration and, as such, shall survive the termination of this Agreement for whatever reason. The Company and the Grantee agree that any invalidity or unenforceability of any one or more of such restrictions on competition shall not render invalid or unenforceable any remaining restrictive covenants. Should a court of competent jurisdiction determine that the scope of any provision of this Section 10 is too broad to be enforced as written, the Company and the Grantee intend that the court reform the provision to such narrower scope as it determines to be reasonable and enforceable.

11. Form S-8 Prospectus. The Grantee acknowledges having received and reviewed a copy of the prospectus required by Part I of Form S-8 relating to shares of Stock that may be issued under the Plan.

12. Governing Law. Notwithstanding anything to the contrary in the Plan, Section 10 of this Agreement shall be governed by and construed in accordance with the laws of the State of Texas, without giving effect to any choice or conflict of law provision or rule that would cause the application of the laws of any other jurisdiction, except where preempted by federal law. Both parties hereby consent and submit to the jurisdiction of the state and federal courts in Dallas County, Texas in all questions and controversies arising out of this Agreement.

13. Acknowledgments. By accepting the Award, the Grantee agrees to be bound by, and agrees that the Award is, and the Restricted Stock Units are, subject in all

respects to, the terms of the Plan. The Grantee further acknowledges and agrees that (a) the signature to this Agreement on behalf of the Company is an electronic signature that will be treated as an original signature for all purposes hereunder, and (b) such electronic signature will be binding against the Company and will create a legally binding agreement when this Agreement is countersigned by the Grantee.

[The remainder of this page is intentionally left blank]

Executed as of the ___ day of [●], [●].

Company:

THE MICHAELS COMPANIES, INC.

By: _____

Name:

Title:

Grantee:

Name:

Address:

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Exhibit 31.1

CERTIFICATIONS

I, Carl S. Rubin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of The Michaels Companies, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: December 7, 2018

/s/ Carl S. Rubin
Carl S. Rubin
Chairman and Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATIONS

I, Denise A. Paulonis, certify that:

1. I have reviewed this quarterly report on Form 10-Q of The Michaels Companies, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: December 7, 2018

/s/ Denise A. Paulonis

Denise A. Paulonis
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

Exhibit 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. § 1350, AS ADOPTED PURSUANT TO § 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the filing of the Quarterly Report on Form 10-Q of The Michaels Companies, Inc., a Delaware corporation (the "Company"), for the period ended November 3, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned officers of the Company certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to such officer's knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: December 7, 2018

/s/ Carl S. Rubin
Carl S. Rubin
Chairman and Chief Executive Officer
(Principal Executive Officer)

/s/ Denise A. Paulonis
Denise A. Paulonis
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

The foregoing certification is being furnished solely pursuant to 18 U.S.C. § 1350 and is not being filed as part of the Report or as a separate disclosure document.
