

LLR Invests \$18M In Kids' Dollar Store Five Below

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RETAIL

5/9/2005 – Five Below Inc. stores offer decidedly inexpensive items like \$1 candy bars, \$3 nail polish and \$5 coolers - but LLR Partners Inc. sees great value in the company.

The Philadelphia-based buyout firm has contributed \$18 million in growth capital to Five Below's latest financing round, along with \$2 million from the company's existing investors.

LLR owns less than 50% of the company. Its existing investors - including owners and individual sponsors of its earlier private rounds - hold the rest, said Howard Ross, an LLR founding partner.

Five Below, also of Philadelphia, operates 25 stores that sell what it calls "extreme-value merchandise" - basketballs, video games, candies, snacks, stationery, trinkets, novelty gifts and the like - that cost no more than \$5 each. The stores target "tweens," or children between 8 and 12 years old, as well as teenagers.

"They are dollar stores for kids," said Ross. He said there are 23 million "tweens" in the U.S., who spend \$10 billion to \$11 billion a year - mostly from allowances. Their numbers are growing twice as fast as the entire population and could peak at around 30 million in 2010, Ross said. Teenagers are spending even more.

LLR likes the company's discount model, which it says is similar to that of Wal-Mart Stores Inc. Five Below ensures low prices by striking special deals with suppliers and getting hold of cancelled shipments by larger retail chains at much lower prices. The result: a Guinness World Records 2005 book, for instance, which would go for \$30 elsewhere, sells for only \$5 at Five Below stores, according to Ross.

Ross is also well-acquainted with Five Below's founders, David Schlessinger and Tom Vellios, having known them for more than a decade. In the early 1990s, Schlessinger and Vellios founded Zany Brainy Inc., a chain that sold educational toys to children younger than 12. Zany Brainy went public in 1999, backed by venture capital, and eventually became part of FAO Inc., the parent of FAO Schwartz. FAO Inc. liquidated the Zany Brainy stores as part of its bankruptcy filing in 2003.

Five Below has expansion plans in the works: The company intends to add another 25 stores this year, build at least 40 new stores in 2006 and add 100 more in 2007. "It has huge growth opportunity," Ross said. "I don't see why it can't have 1,000 stores" in the next five to eight years. Scale is essential for the company to turn a profit by the end of next year, according to Ross. Right now, Five Below is profitable at the store level but not at the corporate level.

Down the road, LLR is most likely to take Five Below public. A sale to a larger retailer is also possible. Dollar General, Dollar Tree Stores Inc., 99 Cents Only Stores, and Family Dollar Stores are among the major publicly-traded discount retailers.

LLR's only previous retail investment went awry. In 2000, the firm invested \$5 million in New Weathervane Retail Corp., which sold clothes to teenage girls. The company later filed for bankruptcy.

The firm believe Five Below is different, as it is not a clothing retailer prone to the whim of fashion. Five Below's discount model and a wider variety of offerings also distinguish it from Weathervane, Ross said.

"Retail is risky," Ross said. "But not all retailers are the same."