



**BAM!**  
BOOKS-A-MILLION

we're not just opening stores

**WE'RE OPENING MINDS**

Books-A-Million, Inc.  
402 Industrial Lane  
Birmingham, Alabama 35211

ANNUAL REPORT 2001

## FIVE-YEAR HIGHLIGHTS

<i>(In thousands, except per share amounts and operational data)</i>	Fiscal Year Ended				
	2/3/01	1/29/00	1/30/99	1/31/98	2/1/97
	53 Weeks	52 Weeks	52 Weeks	52 Weeks	52 Weeks
<b>Statement of Operations Data</b>					
Net sales	\$ 418,606	\$ 404,057	\$ 347,877	\$ 324,762	\$ 278,613
Net income	3,066	5,942	4,514	6,969	5,792
Earnings per share - diluted	0.17	0.33	0.26	0.40	0.33
Weighted average shares - diluted	17,991	18,250	17,554	17,428	17,580
EBITDA	24,542	27,624	24,690	27,160	21,708
Capital investment	12,417	13,462	15,682	14,355	23,674
<b>Balance Sheet Data</b>					
Working capital	\$ 104,124	\$ 93,872	\$ 84,022	\$ 82,771	\$ 70,629
Property and equipment, net	60,659	64,232	67,377	65,814	63,147
Total assets	292,541	286,785	271,551	245,816	233,539
Long-term debt	41,526	35,936	36,944	45,240	37,645
Debt to total capital ratio	0.25	0.23	0.24	0.30	0.28
Stockholders' investment	123,230	121,405	115,022	103,485	96,420
<b>Operational Data</b>					
Total number of stores	185	180	173	165	151
Number of Books-A-Million Superstores	145	135	124	107	91
Number of Bookland stores	37	43	47	57	60
Number of Joe Muggs Newsstands	3	2	2	1	0

## LETTER TO STOCKHOLDERS



Fiscal 2001 was a challenging year for Books-A-Million. Meeting our comparable store sales growth objective proved difficult as we cycled through the impact of the turn of the millennium and the Pokémon phenomenon from fiscal year 2000. Nonetheless, our entire team worked hard, in a difficult retail environment, to control costs and deliver sales in the fourth quarter. We started the new year once again focused on the fundamentals and determined to build on the positive trend in our core book business.

Although comparable store sales were down, there were some positive trends. Our core book business held up well as we continued to make progress in enhancing our inventory management and replenishment systems. In particular, we saw strong growth in our religious and inspirational books, children's books, and in our Joe Muggs coffee business.

Our plans for the new year include the integration of the recently acquired Crown stores, the expansion of our Joe Muggs Newsstand concept, and the continued development of our e-commerce operations.

In March we purchased the assets of 18 bookstores from Crown Books, the Washington D.C.-based bookstore chain that had sought bankruptcy protection under Chapter 11. We have now begun to integrate these Washington D.C. and Chicago locations into the Books-A-Million organization. We believe these stores fit well into our strategic plan and serve to expand the Books-A-Million brand in two important markets. With this acquisition, we now operate 155 total superstores and 201 stores overall. In addition, our plans for the year are to open four to five additional superstores.

Due to the success of our Joe Muggs Newsstand concept, we are ready to move forward in expanding this exciting store model. The prototype store is 2,000 to 2,500 square feet and features Joe Muggs coffee and over 3,000 magazine and newspaper titles. This simple mixture of magazines and coffee has met with great enthusiasm and acceptance in the markets of Atlanta and Birmingham. We are planning to open eight stores this year, with a particular focus in the Atlanta market.

Our e-commerce efforts have continued to surpass our expectations and to deliver benefits to our larger organization. Booksamillion.com had an excellent year, exceeding our sales projections while holding expenses below budget. Our Internet development group at NetCentral made an important contribution to the retail stores by delivering an Internet-based customer service system built on the infrastructure we had developed to support our e-commerce and direct-to-consumer fulfillment operations. This system is a valuable new tool for our store associates, who now have the power of the Internet at their fingertips.

Our wholesale group also had a successful year. American Wholesale Book Company met the challenges of our growing core business and expanding direct-to-consumer fulfillment volume. Our BookSmart bargain book wholesale division achieved healthy sales, a reduction in inventory and excellent expense control.

Despite these achievements, no one on our team was pleased with our financial results in fiscal year 2001. As we move ahead, we will build on the positive trends in our book business, remain disciplined in inventory management and cost control, and continue to pursue new opportunities to grow our business profitably.

Thank you for your continued support. We hope you will visit one of our stores soon and we invite you to visit us on the web at [www.booksamillion.com](http://www.booksamillion.com).

Sincerely,

Clyde B. Anderson  
Chairman and Chief Executive Officer

### Financial Highlights

<i>(In thousands, except per share amounts)</i>	Fiscal Year Ended	
	2/3/01	1/29/00
Net sales	\$ 418,606	\$ 404,057
EBITDA	24,542	27,624
Operating profit	9,749	13,794
Net income	3,066	5,942
Net income per share - diluted	0.17	0.33

<i>(In thousands)</i>	As of	
	2/3/01	1/29/00
Working capital	\$ 104,124	\$ 93,872
Total assets	292,541	286,785
Stockholders' investment	123,230	121,405



(In thousands, except per share amounts)	Fiscal Year Ended				
	2/3/01	1/29/00	1/30/99	1/31/98	2/1/97
<b>Statement of Operations Data:</b>					
Net sales	\$ 418,606	\$ 404,057	\$ 347,877	\$ 324,762	\$ 278,613
Cost of products sold	309,397	296,316	256,793	238,342	206,269
Gross profit	109,209	107,741	91,084	86,420	72,344
Operating, selling and administrative expenses	84,667	80,117	66,394	59,260	50,636
Depreciation and amortization	14,793	13,830	12,974	11,588	9,540
Operating profit	9,749	13,794	11,716	15,572	12,168
Interest expense, net	4,804	4,211	4,435	4,331	2,826
Income before income taxes	4,945	9,583	7,281	11,241	9,342
Provision for income taxes	1,879	3,641	2,767	4,272	3,550
Net income	\$ 3,066	\$ 5,942	\$ 4,514	\$ 6,969	\$ 5,792
Weighted average number of shares outstanding - basic	17,955	17,981	17,497	17,425	17,405
Net income per share - basic	\$ 0.17	\$ 0.33	\$ 0.26	\$ 0.40	\$ 0.33
Weighted average number of shares outstanding - diluted	17,991	18,250	17,554	17,428	17,580
Net income per share - diluted	\$ 0.17	\$ 0.33	\$ 0.26	\$ 0.40	\$ 0.33

(In thousands)	As of				
	2/3/01	1/29/00	1/30/99	1/31/98	2/1/97
<b>Balance Sheet Data:</b>					
Working capital	\$ 104,124	\$ 93,872	\$ 84,022	\$ 82,771	\$ 70,629
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Total assets	292,541	286,785	271,551	245,816	233,539
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Stockholders' investment	123,230	121,405	115,022	103,485	96,420

**Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995**

This document contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, that involve a number of risks and uncertainties. A number of factors could cause actual results, performance, achievements of the Company, or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These factors include, but are not limited to, the competitive environment in the book retail industry in general and in the Company's specific market areas; inflation; economic conditions in general and in the Company's specific market areas; the number of store openings and closings; the profitability of certain product lines; capital expenditures and future liquidity; liability and other claims asserted against the Company; uncertainties related to the Internet and the Company's Internet operations; and other factors referenced herein. In addition, such forward-looking statements are necessarily dependent upon assumptions, estimates and dates that may be incorrect or imprecise and involve known and unknown risks, uncertainties and other factors. Accordingly, any forward-looking statements included herein do not purport to be predictions of future events or circumstances and may not be realized. Given these uncertainties, stockholders and prospective investors are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the results of any of the forward-looking statements contained herein to reflect future events or developments.



**General**

The Company was founded in 1917 and currently operates 201 retail bookstores, including 155 superstores, concentrated in the southeastern United States.

The Company's growth strategy is focused on opening superstores in new and existing market areas, particularly in the Southeast. In addition to opening new stores, management intends to continue its practice of reviewing the profitability trends and prospects of existing stores and closing or relocating underperforming stores or converting stores to different formats.

**Results of Operations**

The following table sets forth statement of operations data expressed as a percentage of net sales for the periods presented.

	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
Net sales	100.0%	100.0%	100.0%
Gross profit	26.1%	26.6%	26.2%
Operating, selling, and administrative expenses	20.2%	19.8%	19.1%
Depreciation and amortization	3.5%	3.4%	3.7%
Operating profit	2.4%	3.4%	3.4%
Interest expense, net	1.2%	1.0%	1.3%
Income before income taxes	1.2%	2.4%	2.1%
Provision for income taxes	0.5%	0.9%	0.8%
Net income	0.7%	1.5%	1.3%

**Fiscal 2001 Compared to Fiscal 2000**

Net sales increased \$14.5 million, or 3.6%, to \$418.6 million in fiscal 2001 from \$404.1 million in fiscal 2000. Comparable store sales decreased 2.9% for fiscal year 2001. The increase in net sales resulted from net sales generated by twelve new stores opened during fiscal 2001, and five new stores opened in the second half of fiscal 2000. In addition, the Company closed seven underperforming stores in fiscal 2001.

The factors affecting the future trend of comparable store sales include, among others, overall demand for products the Company sells, the Company's marketing programs, pricing strategies, store operations and competition.

Gross profit increased \$1.5 million, or 1.4%, to \$109.2 million in fiscal 2001 from \$107.7 million in fiscal 2000. Gross profit as a percentage of net sales decreased to 26.1% in fiscal 2001 from 26.6% in fiscal 2000, primarily due to increased occupancy costs and higher warehouse distribution costs as a percentage of net sales.

Operating, selling and administrative expenses increased \$4.6 million, or 5.7%, to \$84.7 million in fiscal 2001, from \$80.1 million in fiscal 2000. Operating, selling and administrative expenses as a percentage of net sales increased to 20.2% in fiscal 2001 from 19.8% in fiscal 2000, primarily due to the lower comparable store sales for fiscal 2001.



Depreciation and amortization increased \$1.0 million, or 7.0%, to \$14.8 million in fiscal 2001 from \$13.8 million in fiscal 2000. Depreciation and amortization as a percentage of net sales increased to 3.5% in fiscal 2001 from 3.4% in fiscal 2000, primarily due to increased investment in information systems technology.

Net interest expense increased \$0.6 million, or 14.1%, to \$4.8 million in fiscal 2001 from \$4.2 million in fiscal 2000, primarily due to increased average borrowings during fiscal 2001.

#### Fiscal 2000 Compared to Fiscal 1999

Net sales increased \$56.2 million, or 16.1%, to \$404.1 million in fiscal 2000 from \$347.9 million in fiscal 1999. Comparable store sales increased 8.2% for fiscal year 2000. The increase in net sales resulted from net sales generated by twelve new stores opened during fiscal 2000, and eleven new stores opened in the second half of fiscal 1999. In addition, the Company closed five underperforming stores in fiscal 2000.

The factors affecting the future trend of comparable store sales include, among others, overall demand for products the Company sells, the Company's marketing programs, pricing strategies, store operations and competition.

Gross profit increased \$16.6 million, or 18.3%, to \$107.7 million in fiscal 2000 from \$91.1 million in fiscal 1999. Gross profit as a percentage of net sales increased to 26.6% in fiscal 2000 from 26.2% in fiscal 1999, primarily due to decreased occupancy costs and lower warehouse distribution costs as a percentage of net sales.

Operating, selling and administrative expenses increased \$13.7 million, or 20.7%, to \$80.1 million in fiscal 2000, from \$66.4 million in fiscal 1999. Operating, selling and administrative expenses as a percentage of net sales increased to 19.8% in fiscal 2000 from 19.1% in fiscal 1999, primarily due to costs incurred related to the development of new business opportunities.

Depreciation and amortization increased \$0.8 million, or 6.6%, to \$13.8 million in fiscal 2000 from \$13.0 million in fiscal 1999. Depreciation and amortization as a percentage of net sales decreased to 3.4% in fiscal 2000 from 3.7% in fiscal 1999, primarily the result of lower capital expenditures due to fewer stores opened in fiscal 2000 than in the previous year.

Net interest expense was relatively constant in fiscal year 2000, at \$4.2 million, versus \$4.4 million in fiscal year 1999.

#### Seasonality and Quarterly Results

Similar to many retailers, the Company's business is seasonal, with its highest retail sales, gross profit and net income historically occurring in the fourth fiscal quarter. This seasonal pattern reflects the increased demand for books and gifts experienced during the year-end holiday selling season. Working capital requirements are generally highest during the third fiscal quarter and the early part of the fourth fiscal quarter due to the seasonality of the Company's business.



In addition, the Company's results of operations may fluctuate from quarter to quarter as a result of the amount and timing of sales and profits contributed by new stores as well as other factors. New stores require the Company to incur pre-opening expenses and often require several months of operation before generating acceptable sales volumes. Accordingly, the addition of a large number of new stores in a particular quarter could adversely affect the Company's results of operations for that quarter.

#### Liquidity and Capital Resources

The Company has a revolving credit facility that allows borrowings up to \$90.0 million, for which no principal repayments are due until the facility expires on June 18, 2003, and an unsecured working capital line of credit for \$15.0 million, which is subject to annual renewal. As of February 3, 2001, \$33.3 million was outstanding under these facilities combined. Additionally, as of February 3, 2001, the Company has outstanding borrowings associated with the issuance of an industrial revenue bond totaling \$7.5 million.

The Company's capital expenditures totaled \$12.4 million in fiscal 2001. These expenditures were primarily used to open new stores, perform renovations and make improvements to existing stores, expand existing warehouse facilities and invest in management information systems. Management estimates that capital expenditures for fiscal 2002 will be approximately \$14.8 million and that such amounts will be used primarily for new stores, renovation and improvements to existing stores and investments in management information systems. Management believes that existing cash balances and net cash from operating activities, together with borrowings under the Company's credit facilities, will be adequate to finance the Company's planned capital expenditures and to meet the Company's working capital requirements for fiscal 2002.

#### Related-Party Activities

As discussed in Note 6 of Notes to Consolidated Financial Statements, the Company conducts business with other entities in which certain officers, directors and principal stockholders of the Company have controlling ownership interests. The most significant related-party transactions include inventory purchases from, and sales to, related parties. Related-party inventory purchases decreased in fiscal 2001 due to lower magazine purchases. Related-party sales transactions increased in fiscal 2001 due to higher bargain book sales. Management believes the terms of these related-party transactions are substantially equivalent to those available from unrelated parties and, therefore, have no significant impact on gross profit.

#### Financial Position

During fiscal 2001, the Company opened twelve new stores. The store openings resulted in increased inventory balances at February 3, 2001, as compared to January 29, 2000. Reduced capital expenditures, as compared to fiscal 2000, and the closing of seven stores during fiscal 2001 resulted in lower net property and equipment balances at February 3, 2001, as compared to January 29, 2000.

Consolidated Balance  
Sheets

(As of 2/3/01 and 1/29/00)

(In thousands)	As Of	
	2/3/01	1/29/00
<b>Assets</b>		
<b>Current Assets:</b>		
Cash and temporary cash investments	\$ 5,282	\$ 4,920
Accounts receivable, net of allowance for doubtful accounts of \$787 and \$1,489, respectively	8,417	8,781
Related party receivables	2,358	4,161
Inventories	205,986	194,624
Prepayments and other	4,521	3,339
Deferred income taxes	3,791	5,084
<b>Total Current Assets</b>	<b>230,355</b>	<b>220,909</b>
<b>Property and Equipment:</b>		
Land	628	628
Buildings	5,986	5,442
Equipment	48,252	40,646
Furniture and fixtures	38,350	35,904
Leasehold improvements	41,562	42,235
Construction in process	123	599
	134,901	125,454
Less accumulated depreciation and amortization	74,242	61,222
<b>Net Property and Equipment</b>	<b>60,659</b>	<b>64,232</b>
<b>Other Assets:</b>		
Goodwill, net	1,410	1,453
Other	117	191
<b>Total Other Assets</b>	<b>1,527</b>	<b>1,644</b>
<b>Total Assets</b>	<b>\$ 292,541</b>	<b>\$ 286,785</b>
<b>Liabilities and Stockholders' Investment</b>		
<b>Current Liabilities:</b>		
Accounts payable:		
Trade	\$ 95,006	\$ 94,090
Related party	7,504	9,415
Accrued income taxes	650	2,092
Accrued expenses	22,611	20,970
Current portion of long-term debt	460	470
<b>Total Current Liabilities</b>	<b>126,231</b>	<b>127,037</b>
<b>Long-term Debt</b>	<b>41,526</b>	<b>35,936</b>
<b>Deferred Income Taxes</b>	<b>1,554</b>	<b>2,407</b>
<b>Commitments and Contingencies</b>	<b>—</b>	<b>—</b>
<b>Stockholders' Investment:</b>		
Preferred stock, \$.01 par value; 1,000,000 shares authorized, no shares outstanding	—	—
Common stock, \$.01 par value; 30,000,000 shares authorized, 18,092,001 and 18,080,646 shares issued and outstanding at February 3, 2001 and January 29, 2000, respectively	181	181
Additional paid-in capital	70,634	70,564
Treasury stock at cost (597,600 shares at February 3, 2001 and 81,600 shares at January 29, 2000)	(1,563)	(252)
Retained earnings	53,978	50,912
<b>Total Stockholders' Investment</b>	<b>123,230</b>	<b>121,405</b>
<b>Total Liabilities and Stockholders' Investment</b>	<b>\$ 292,541</b>	<b>\$ 286,785</b>

The accompanying notes are an integral part of these consolidated balance sheets.

Consolidated Statements  
of Operations

(For the fiscal years ended 2/3/01, 1/29/00 and 1/30/99)

(In thousands, except per share data)	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
	53 Weeks	52 Weeks	52 Weeks
Net sales	\$ 418,606	\$ 404,057	\$ 347,877
Cost of products sold, including warehouse distribution and store occupancy costs <sup>(1)</sup>	309,397	296,316	256,793
<b>Gross profit</b>	<b>109,209</b>	<b>107,741</b>	<b>91,084</b>
Operating, selling and administrative expenses	84,667	80,117	66,394
Depreciation and amortization	14,793	13,830	12,974
<b>Operating profit</b>	<b>9,749</b>	<b>13,794</b>	<b>11,716</b>
Interest expense, net	4,804	4,211	4,435
<b>Income before income taxes</b>	<b>4,945</b>	<b>9,583</b>	<b>7,281</b>
Provision for income taxes	1,879	3,641	2,767
<b>Net income</b>	<b>\$ 3,066</b>	<b>\$ 5,942</b>	<b>\$ 4,514</b>
Weighted average number of shares outstanding - basic	17,955	17,981	17,497
<b>Net income per share - basic</b>	<b>\$ 0.17</b>	<b>\$ 0.33</b>	<b>\$ 0.26</b>
Weighted average number of shares outstanding - diluted	17,991	18,250	17,554
<b>Net income per share - diluted</b>	<b>\$ 0.17</b>	<b>\$ 0.33</b>	<b>\$ 0.26</b>

<sup>(1)</sup> Inventory purchases from related parties were \$34,128, \$34,548 and \$36,836, respectively, for the periods presented above.

The accompanying notes are an integral part of these consolidated statements.



(As of February 3, 2001)

(In thousands)	Common Stock		Additional	Treasury Stock		Retained
	Shares	Amount	Paid-In Capital	Shares	Amount	Earnings
<b>Balance, January 31, 1998</b>	17,428	\$ 174	\$ 62,925	—	\$ —	\$ 40,386
Net Income	—	—	—	—	—	4,514
Issuance of stock for employee stock purchase plan	16	—	78	—	—	—
Purchase of treasury stock	—	—	—	82	(252)	—
Exercise of stock options	461	5	4,132	—	—	—
Tax benefit from exercise of stock options	—	—	2,333	—	—	—
Issuance of stock for acquisition						
accounted for as pooling of interests	112	1	2	—	—	70
Contributions from certain stockholders	—	—	1,054	—	—	—
Tax provision for contributions						
from certain stockholders	—	—	(400)	—	—	—
<b>Balance, January 30, 1999</b>	18,017	180	70,124	82	(252)	44,970
Net Income	—	—	—	—	—	5,942
Issuance of stock for employee stock purchase plan	16	—	77	—	—	—
Exercise of stock options	48	1	306	—	—	—
Tax benefit from exercise of stock options	—	—	57	—	—	—
<b>Balance, January 29, 2000</b>	18,081	181	70,564	82	(252)	50,912
Net Income	—	—	—	—	—	3,066
Purchase of treasury stock	—	—	—	516	(1,311)	—
Issuance of stock for employee stock purchase plan	11	—	70	—	—	—
<b>Balance, February 3, 2001</b>	18,092	\$ 181	\$ 70,634	598	\$ (1,563)	\$ 53,978

The accompanying notes are an integral part of these consolidated statements.



(For the fiscal years ended 2/3/01, 1/29/00 and 1/30/99)

(Dollars in thousands)	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
<b>Cash Flows from Operating Activities:</b>			
Net income	\$ 3,066	\$ 5,942	\$ 4,514
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	14,793	13,830	12,974
(Gain) loss on sale of property	1,237	1,156	(472)
Deferred income tax provision (credit), net	440	(103)	(912)
(Increase) decrease in assets:			
Accounts receivable	364	3,501	(550)
Related party receivables	1,803	(163)	3,561
Inventories	(11,362)	(19,413)	(23,899)
Prepayments and other	(1,171)	(444)	(2,223)
Increase (decrease) in liabilities:			
Accounts payable	(995)	2,315	22,258
Accrued income taxes	(1,442)	1,673	(321)
Accrued expenses	1,641	4,178	2,817
Total adjustments	5,308	6,530	13,233
Net cash provided by operating activities	8,374	12,472	17,747
<b>Cash Flows from Investing Activities:</b>			
Proceeds from sale of property and equipment	66	1,742	1,627
Capital expenditures	(12,417)	(13,462)	(15,682)
Net cash used in investing activities	(12,351)	(11,720)	(14,055)
<b>Cash Flows from Financing Activities:</b>			
Proceeds from exercise of stock options and purchase of shares under employee stock purchase plan	70	384	4,215
Contributions from certain stockholders	—	—	1,054
Purchase of treasury stock	(1,311)	—	(252)
Issuance of other debt	—	1,409	—
Repayments of other debt	(262)	—	—
Borrowings under credit facilities	176,592	169,103	153,475
Repayments under credit facilities	(170,750)	(171,050)	(161,771)
Net cash provided by (used in) financing activities	4,339	(154)	(3,279)
<b>Net Increase in Cash and Temporary Cash Investments</b>	362	598	413
<b>Cash and Temporary Cash Investments at Beginning of Year</b>	4,920	4,322	3,909
<b>Cash and Temporary Cash Investments at End of Year</b>	\$ 5,282	\$ 4,920	\$ 4,322
<b>Supplemental Disclosures of Cash Flow Information:</b>			
Cash paid during the year for:			
Interest	\$ 4,904	\$ 4,318	\$ 4,625
Income taxes, net of refunds	\$ 2,881	\$ 1,882	\$ 4,026

The accompanying notes are an integral part of these consolidated statements.



**1. Summary of Significant Accounting Policies**

*Business*

Books-A-Million, Inc., and its subsidiaries (the "Company") are principally engaged in the sale of books, magazines and related items through a chain of retail bookstores. The Company presently operates 201 bookstores in 18 states and the District of Columbia, which are predominantly located in the southeastern United States. The Company also serves as a wholesale book distributor for certain other retailers and wholesalers and operates a retail Internet website. The Company presently consists of Books-A-Million, Inc., and its wholly owned subsidiaries, American Wholesale Book Company, Inc. ("American Wholesale") and American Internet Services, Inc ("AIS"). All significant intercompany balances and transactions have been eliminated in consolidation.

*Basis of Presentation*

The Company operates on a 52-53 week year, with the fiscal year ending on the Saturday closest to January 31. Fiscal year 2001 was a 53-week period. Fiscal years 2000 and 1999 were 52-week periods.

*Use of Estimates in the Preparation of Financial Statements*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

*Inventories*

Inventories are valued at the lower of cost or market, using the retail method, with cost determined on a first-in, first-out ("FIFO") basis and market based on the lower of replacement cost or estimated realizable value. The Company includes certain distribution and other expenses in its inventory costs.

*Property and Equipment*

Property and equipment are recorded at cost. Depreciation on equipment and furniture and fixtures is provided on the straight-line method over the estimated service lives, which range from three to seven years. Depreciation of leasehold improvements is provided on the straight-line basis over the periods of the applicable leases.

Maintenance and repairs are charged to expense as incurred. Costs of renewals and betterments are capitalized by charges to property accounts and depreciated using applicable annual rates. The cost and accumulated depreciation of assets sold, retired or otherwise disposed of are removed from the accounts, and the related gain or loss is credited or charged to income.

*Goodwill*

The Company amortizes goodwill on a straight-line basis over 40 years. As of February 3, 2001 and January 29, 2000, accumulated amortization of goodwill was \$295,000 and \$252,000, respectively. The Company continually evaluates whether events or circumstances have occurred that indicate the remaining estimated useful life of goodwill may warrant revision or that the remaining balance of goodwill may not be recoverable. When factors indicate that goodwill should be evaluated for possible impairment, the Company uses an estimate of the related operating profits over the remaining life of the goodwill in measuring recoverability.

*Store Opening Costs*

Non-capital expenditures incurred in preparation for opening new retail stores are expensed as incurred.

*Insurance Accruals*

The Company is subject to large deductibles under its workers' compensation policy. Insurance coverage is maintained in amounts management considers adequate. Amounts are accrued currently for the estimated cost of claims incurred, both reported and unreported.



*Income Taxes*

The Company recognizes deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse.

*Statements of Cash Flows*

For purposes of the consolidated statements of cash flows, the Company considers all short-term, highly liquid investments with original maturities of 90 days or less to be temporary cash investments.

*Earnings Per Share*

Basic net income per share ("EPS") excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock are exercised, converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company. Diluted EPS has been computed based on the average number of shares outstanding including the effect of outstanding stock options, if dilutive, in each respective year. A reconciliation of the weighted average shares for basic and diluted EPS is as follows:

<i>(In thousands)</i>	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
Weighted average shares outstanding:			
Basic	17,955	17,981	17,497
Dilutive effect of stock options outstanding	36	269	57
Diluted	17,991	18,250	17,554

Options outstanding of 1,391,000, 464,000 and 619,000 for the years ended February 3, 2001, January 29, 2000 and January 30, 1999, respectively, were not included in the table above as they were anti-dilutive.

*Disclosure of Fair Value of Financial Instruments*

Statement of Financial Accounting Standards ("SFAS") No. 107, Disclosure About Fair Value of Financial Instruments, requires all businesses to disclose the fair value of financial instruments, both assets and liabilities recognized and not recognized on the balance sheet, for which it is practicable to estimate fair value. Based upon their remaining term to maturity and the current interest rate environment, the estimated fair values of the Company's financial instruments recognized on the balance sheet at February 3, 2001 and January 29, 2000 approximate their carrying values at those dates.

*Legal*

The Company is a party to various legal proceedings incidental to its business. In the opinion of management, after consultation with legal counsel, the ultimate liability, if any, with respect to those proceedings is not presently expected to materially affect the financial position or results of operations of the Company.

*Accounting for Derivative Instruments and Hedging Activities*

In June 1998, the Financial Accounting Standards Board ("FASB") issued SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, amended by SFAS No. 137, Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FASB Statement No. 133, and SFAS No. 138, Accounting for Certain Derivatives and Certain Hedging Activities. SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded in the balance sheet as either an asset or liability measured at its fair value. SFAS No. 133 requires that changes in the derivative's fair value be recognized currently in



earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the income statement, and requires that a company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting. The adoption of these statements may increase volatility of earnings. The Company adopted these statements on February 4, 2001, which will result in decreasing retained earnings by \$465,000 in the first quarter of fiscal 2002.

**Contributions from Certain Stockholders**

In fiscal 1999, contributions of short-swing profits from certain stockholders were received by the Company totaling \$1,054,000 with a related tax provision of \$400,000 charged to paid-in capital.

**Prior Year Reclassifications**

Certain prior year amounts have been reclassified to conform to the current year presentation.

**2. Income Taxes**

A summary of the components of the income tax provision is as follows (*dollars in thousands*):

	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
Current:			
Federal	\$ 1,386	\$ 3,448	\$ 3,337
State	53	296	342
	<u>1,439</u>	<u>3,744</u>	<u>3,679</u>
Deferred taxes arising from:			
Depreciation	(871)	1,270	(321)
Accruals	593	(522)	(443)
Inventory	(110)	(113)	25
Other	828	(738)	(173)
	<u>440</u>	<u>(103)</u>	<u>(912)</u>
Provision for income taxes	<u>\$ 1,879</u>	<u>\$ 3,641</u>	<u>\$ 2,767</u>

A reconciliation of the federal statutory income tax rate to the effective income tax rate is as follows:

	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
Federal statutory income tax rate	34.0%	34.0%	34.0%
State income tax provision	1.0%	2.8%	3.1%
Other	3.0%	1.2%	0.9%
Effective income tax rate	<u>38.0%</u>	<u>38.0%</u>	<u>38.0%</u>

Temporary differences which created deferred tax assets and liabilities at February 3, 2001 and January 29, 2000, are detailed below (*dollars in thousands*):

	As of 2/3/01		As of 1/29/00	
	Current	Noncurrent	Current	Noncurrent
Depreciation	\$ —	\$ (1,404)	\$ —	\$ (2,275)
Accruals	2,543	—	3,136	—
Inventory	988	—	878	—
Other	260	(150)	1,070	(132)
Deferred tax asset (liability)	<u>\$ 3,791</u>	<u>\$ (1,554)</u>	<u>\$ 5,084</u>	<u>\$ (2,407)</u>

No valuation allowance is deemed necessary by management, as the realization of recorded deferred tax assets is considered more likely than not.



**3. Debt and Lines of Credit**

The Company has a revolving credit facility that allows borrowings up to \$90 million for which no principal repayments are due until the facility expires on June 18, 2003, and an unsecured working capital line of credit for \$15 million, increased from \$10 million in September, 2000, which is subject to annual renewal. Both credit facilities have certain financial and non-financial covenants with which the Company is in compliance. As of February 3, 2001 and January 29, 2000, \$33.3 million and \$27.5 million, respectively, were outstanding under these credit facilities. The maximum and average outstanding balances during fiscal 2001 were \$81.0 million and \$64.1 million, respectively. The outstanding borrowings as of February 3, 2001, had interest rates ranging from 6.41% to 7.20%.

The Company is subject to interest rate fluctuations involving its credit facilities. However, the Company uses both fixed and variable debt to manage this exposure. On February 9, 1998, the Company entered into an interest rate swap agreement with a five year term that carries a notional principal amount of \$30.0 million. The swap effectively fixes the interest rate on \$30.0 million of variable rate debt at 6.78%. The swap agreement expires on February 11, 2003. The counter party to the interest rate swap is one of the Company's primary banks. The Company believes the credit and liquidity risk of the counter party failing to meet its obligation is remote as the Company settles its interest position with the bank on a quarterly basis.

During fiscal 1996 and fiscal 1995, the Company financed the acquisition and construction of certain warehouse and distribution facilities through loans, obtained from the proceeds of an industrial development revenue bond (the "Bond"), which are secured by a mortgage interest in these facilities. As of February 3, 2001 and January 29, 2000, there was \$7.5 million of borrowings outstanding under these arrangements, at variable rates. The Bond has a maturity date of December 1, 2019, with a purchase provision obligating the Company to repurchase the Bond on May 11, 2005, unless extended by the bondholder. Such an extension may be renewed annually by the bondholder, at the Company's request, to a date no more than five years from the renewal date. The Company maintains a \$7.5 million interest rate swap that effectively fixes the interest rate on the Bond at 7.98%. The swap was entered into in May 1996 and has a term of ten years.

**4. Leases**

The Company leases the premises for its retail bookstores under operating leases, which expire in various years through the year 2013. Many of these leases contain renewal options and require the Company to pay executory costs (such as property taxes, maintenance, and insurance). In addition to fixed minimum rentals, some of the Company's leases require contingent rentals based on a percentage of sales, which the Company records throughout the year based upon best available information.

The Company also leases certain office, warehouse and retail store space from related parties. Rental expense under these leases was approximately \$658,000, \$674,000 and \$624,000 in fiscal 2001, 2000 and 1999, respectively. Total minimum future rental payments under these leases are \$1,479,000.

Minimum future rental payments under non-cancelable operating leases having remaining terms in excess of one year as of February 3, 2001, are as follows (*in thousands*):

Fiscal Year	
2002	\$ 27,728
2003	24,168
2004	22,364
2005	20,981
2006	18,408
Subsequent years	42,124
Total	<u>\$ 155,773</u>



Rental expense for all operating leases consisted of the following (*in thousands*):

	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
Minimum rentals	\$ 26,084	\$ 23,458	\$ 21,151
Contingent rentals	496	596	425
Total	\$ 26,580	\$ 24,054	\$ 21,576

## 5. Employee Benefit Plans

### 401(k) Profit-Sharing Plan

The Company and its subsidiaries maintain a 401(k) plan covering all employees who have completed 12 months of service and who are at least 21 years of age, and permit participants to contribute from 2% to 15% of compensation to the plan. Company matching and supplemental contributions are made at management's discretion. The expense under this plan was \$335,000, \$554,000 and \$333,000 in fiscal 2001, 2000 and 1999, respectively.

### Stock Option Plan

The Company maintains a stock option plan reserving 3,300,000 shares of the Company's common stock for grants to executive officers, directors, and key employees. Prior to January 9, 2001, all options granted to employees become exercisable in equal annual increments over a five-year period and expire on the sixth anniversary of the date of grant. On January 9, 2001, the Compensation Committee approved an amendment to the Stock Option Plan that allows all options granted after that date to vest in equal annual increments over a three-year period and expire on the tenth anniversary of the date of the grant. All stock options have exercise prices generally equal to the fair market value of the common stock on the date of grant. A summary of the status of the Company's stock option plan is as follows (*shares in thousands*):

	Fiscal Year Ended					
	February 3, 2001		January 29, 2000		January 30, 1999	
	Shares	Exercise Price	Shares	Exercise Price	Shares	Exercise Price
Outstanding at beginning of year	1,562	\$ 8.26	1,335	\$ 8.25	1,571	\$ 7.57
Granted	804	1.87	632	8.21	432	10.83
Exercised	—	—	(49)	6.31	(461)	8.98
Forfeited	(174)	9.84	(356)	8.44	(207)	7.25
Outstanding at end of year	2,192	\$ 5.79	1,562	\$ 8.20	1,335	\$ 8.25
Exercisable at end of year	736	\$ 7.57	363	\$ 8.62	315	\$ 8.58
Weighted average fair value of options granted		\$ 1.75		\$ 7.33		\$ 9.30

During fiscal years 2001, 2000 and 1999, the Company recognized tax benefits related to the exercise of stock options in the amount of \$0, \$57,000 and \$2,333,000, respectively. The tax benefits were credited to paid-in capital in the respective years.

The following table summarizes information about stock options outstanding at February 3, 2001 (*shares in thousands*):

Range of Exercise Price	Options Outstanding			Options Exercisable		
	Number Outstanding at February 3, 2001	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable at February 3, 2001	Weighted Average Exercise Price	
\$ 1.38 - \$ 6.50	1,252	6.93	\$ 3.28	377	\$ 5.80	
\$ 6.51 - \$ 13.00	940	4.30	\$ 9.13	359	\$ 9.44	



In October 1995, the FASB issued SFAS No. 123, Accounting for Stock-Based Compensation. SFAS No. 123 established financial accounting and reporting standards for stock-based compensation and for transactions in which an entity issues its equity instruments to acquire goods and services for non-employees. In accordance with SFAS No. 123, the Company continues to account for and record compensation expense under APB No. 25. However, the Company adopted the disclosure only provisions of SFAS No. 123, as required. If the Company had recorded compensation expense in accordance with SFAS No. 123 under the fair value based method, the Company's net income and net income per share would have been as indicated below:

	Fiscal Year Ended		
	2/3/01	1/29/00	1/30/99
( <i>In thousands except per share data</i> )			
Net income-as reported	\$ 3,066	\$ 5,942	\$ 4,514
Net income-pro forma	2,024	5,307	4,257
Net income per share-diluted, as reported	0.17	0.33	0.26
Net income per share-diluted, pro forma	0.11	0.29	0.24

For the purposes of the foregoing calculation, the fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. The assumptions used in connection with this model show no expected dividend yield, a five-year or ten-year expected life of the options, and an expected stock price volatility rate of 1.20 with risk-free interest rates ranging from 4.99% to 6.76%.

### Employee Stock Purchase Plan

The Company maintains an employee stock purchase plan under which 200,000 shares of the Company's common stock are reserved for purchase by employees at 85% of the fair market value of the common stock. Of the total reserved shares, 90,414 shares have been purchased as of February 3, 2001.

## 6. Related Party Transactions

Certain stockholders of the Company have controlling ownership interests in other entities with which the Company conducts business. Transactions between the Company and these various other entities ("related parties") are summarized in the following paragraphs and Note 4.

The Company purchases a portion of its inventories for resale from related parties; such purchases amounted to \$34,128,000, \$34,548,000 and \$36,836,000 in fiscal 2001, 2000 and 1999, respectively. The Company sells a portion of its inventories to related parties; such sales amounted to \$3,940,000, \$2,841,000 and \$5,301,000 in fiscal 2001, 2000 and 1999, respectively. The Company also purchases logistics services from a related party that amounted to \$250,000, \$445,000 and \$128,000 in fiscal 2001, 2000 and 1999, respectively.

## 7. Subsequent Events (Unaudited)

During March 2001, the Company acquired the assets and assumed the leases of 18 retail bookstores from Crown Books Corporation. The stores are located in the Washington, D.C. and Chicago metropolitan areas. The results of operations for the acquired stores will be reflected in the consolidated financial statements for the Company beginning in the first quarter of fiscal 2002.



To Books-A-Million, Inc.:

We have audited the accompanying consolidated balance sheets of Books-A-Million, Inc. (a Delaware corporation), and its subsidiaries as of February 3, 2001, and January 29, 2000, and the related consolidated statements of operations, stockholders' investment, and cash flows for each of the three fiscal years in the period ended February 3, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Books-A-Million, Inc. and its subsidiaries as of February 3, 2001, and January 29, 2000, and the results of their operations and their cash flows for each of the three fiscal years in the period ended February 3, 2001, in conformity with accounting principles generally accepted in the United States.

ARTHUR ANDERSEN LLP

Birmingham, Alabama  
March 19, 2001



	Fiscal Year Ended February 3, 2001				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
<i>(In thousands, except per share amounts)</i>					
Net sales	\$ 93,099	\$ 93,629	\$ 90,133	\$ 141,745	\$ 418,606
Gross profit	24,700	24,344	22,235	37,930	109,209
Operating profit (loss)	1,793	342	(1,295)	8,909	9,749
Net income (loss)	471	(568)	(1,637)	4,800	3,066
Net income (loss) per share - basic <sup>(1)</sup>	0.03	(0.03)	(0.09)	0.27	0.17
Net income (loss) per share - diluted <sup>(1)</sup>	0.03	(0.03)	(0.09)	0.27	0.17

	Fiscal Year Ended January 29, 2000				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
<i>(In thousands, except per share amounts)</i>					
Net sales	\$ 85,127	\$ 89,878	\$ 91,162	\$ 137,890	\$ 404,057
Gross profit	22,357	23,364	22,081	39,939	107,741
Operating profit (loss)	1,517	1,196	(319)	11,400	13,794
Net income (loss)	310	19	(924)	6,537	5,942
Net income (loss) per share - basic	0.02	0.00	(0.05)	0.36	0.33
Net income (loss) per share - diluted	0.02	0.00	(0.05)	0.36	0.33

<sup>(1)</sup> The sum of quarterly per share amounts are different from the annual per share amounts because of differences in the weighted average number of common and common equivalent shares used in the quarterly and annual computations.

**Board of Directors**

**Clyde B. Anderson**  
*Chairman of the Board  
and Chief Executive Officer*

**Charles C. Anderson**  
*Retired Chairman*

**Terry C. Anderson**  
*President,  
American Promotional Events, Inc.*

**Ronald G. Bruno**  
*President,  
Bruno Capital Management Corporation*

**Dr. J. Barry Mason**  
*Dean, Culverhouse College of Commerce  
The University of Alabama*

**William H. Rogers, Jr.**  
*Executive Vice President,  
SunTrust Banks, Inc.*

**Corporate Officers**

**Clyde B. Anderson**  
*Chairman of the Board  
and Chief Executive Officer*

**Sandra B. Cochran**  
*President and Secretary*

**Terrance G. Finley**  
*President,  
American Internet Services, Inc.*

**Richard S. Wallington**  
*Chief Financial Officer*

**CORPORATE DATA**

**Corporate Office**  
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Birmingham, Alabama 35211  
(205) 942-3737

**Transfer Agent**  
Bank of New York  
(800) 524-4458

**Stockholder Inquiries:**  
Stockholder Relations Department - 11E  
P.O. Box 11258  
Church Street Station  
New York, NY 10286  
E-Mail address: [shareowner-svcs@bankofny.com](mailto:shareowner-svcs@bankofny.com)  
Bank of New York's Stock Transfer Website:  
<http://stock.bankofny.com>

**Certificates for Transfer and Address Changes to:**  
Receive and Deliver Department - 11W  
P.O. Box 11002  
Church Street Station  
New York, NY 10286

**Independent Public Accountants**  
Arthur Andersen LLP  
Birmingham, Alabama

**Form 10-K and Investor Contact**

A copy of the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2001, as filed with the Securities and Exchange Commission is available without charge to stockholders upon written request. Such requests and other investor inquiries should be directed to Richard S. Wallington, the Company's Chief Financial Officer, or you can view the Company's Annual Report at [www.booksamillioninc.com](http://www.booksamillioninc.com).

**Market and Dividend Information**

**Common Stock**  
The Common Stock of Books-A-Million, Inc., is traded in the Nasdaq National Market under the symbol BAMM. The chart below sets forth the high and low stock prices for each quarter of the fiscal years ending February 3, 2001, and January 29, 2000.

Quarter Ended	High	Low
January 2001	\$ 3.25	\$ 1.38
October 2000	3.75	2.25
July 2000	4.75	3.13
April 2000	8.25	4.00
January 2000	\$ 12.00	\$ 7.63
October 1999	12.19	7.50
July 1999	16.63	7.00
April 1999	17.00	8.00

The closing price on April 17, 2001, was \$2.36. No cash dividends have been declared since completion of the Company's initial public offering in 1992. As of April 17, 2001, Books-A-Million, Inc. had approximately 13,600 stockholders based on the number of individual participants represented by security position listings.

**Annual Meeting of Stockholders**

The annual meeting of stockholders will be held on June 7, 2001, at 10:00 a.m. Central time at The Harbert Center, 2019 Fourth Avenue North, Birmingham, Alabama 35203. Stockholders of record as of April 17, 2001, are invited to attend this meeting.