BUILD A BEAR WORKSHOP INC
Form 10-Q
May 10, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-Q

(Mark One)

þ **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended March 31, 2007

OR

o **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from __________ to __________

Commission file number: 001-32320

BUILD-A-BEAR WORKSHOP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**43-1883836**
(State or Other Jurisdiction of Incorporation or Organization)	*(I.R.S. Employer Identification No.)*
1954 Innerbelt Business Center Drive St. Louis, Missouri	**63114**
(Address of Principal Executive Offices)	*(Zip Code)*

(314) 423-8000

(Registrant s Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (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.

Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer o Accelerated Filer þ Non-Accelerated Filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes þ No o

As of May 4, 2007, there were 20,607,648 issued and outstanding shares of the registrant s common stock.

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PART I-FINANCIAL INFORMATION

Item 1. Financial Statements.

BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(Dollars in thousands, except share and per share data)

	March 31, 2007	December 30, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 42,375	$ 53,109
Inventories	48,013	50,905
Receivables	6,028	7,389
Prepaid expenses and other current assets	17,854	11,805
Deferred tax assets	2,437	2,388
Total current assets	116,707	125,596
Property and equipment, net	129,455	130,347
Goodwill	36,374	36,927
Other intangible assets, net	2,984	2,873
Other assets, net	4,972	4,027
Total Assets	$ 290,492	$ 299,770
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 44,167	$ 46,761
Accrued expenses	12,378	16,301
Gift cards and customer deposits	20,295	28,128
Deferred revenue	6,613	6,454
Total current liabilities	83,453	97,644
Deferred franchise revenue	2,418	2,297
Deferred rent	36,466	34,754
Other liabilities	308	352
Deferred tax liabilities	460	459
Stockholders equity:		
Preferred stock, par value $0.01, Shares authorized: 15,000,000; No shares issued or outstanding at March 31, 2007 and December 30, 2006		
Common stock, par value $0.01, Shares authorized: 50,000,000; Issued and outstanding: 20,594,729 and 20,537,421 shares, respectively	206	205
Additional paid-in capital	84,796	88,866
Other comprehensive income	(1,868)	(997)
Retained earnings	84,253	76,190

Total stockholders equity		167,387		164,264
Total Liabilities and Stockholders Equity	$	290,492	$	299,770

See accompanying notes to condensed consolidated financial statements.

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BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(Dollars in thousands, except share and per share data)

	Thirteen weeks ended	
	March 31, 2007	**April 1, 2006**
Revenues:		
Net retail sales	$ 115,883	$ 97,730
Franchise fees	695	690
Licensing revenue	236	211
Total revenues	116,814	98,631
Costs and expenses:		
Cost of merchandise sold	62,140	49,860
Selling, general and administrative	41,544	35,451
Store preopening	688	615
Interest expense (income), net	(545)	(866)
Total costs and expenses	103,827	85,060
Income before income taxes	12,987	13,571
Income tax expense	4,922	5,225
Net income	$ 8,065	$ 8,346
Earnings per common share:		
Basic	$ 0.40	$ 0.42
Diluted	$ 0.39	$ 0.41
Shares used in computing common per share amounts:		
Basic	20,281,820	20,078,876
Diluted	20,525,347	20,401,378

See accompanying notes to condensed consolidated financial statements.

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BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(in thousands)

	Thirteen weeks ended	
	March 31, 2007	**April 1, 2006**
Cash flows from operating activities:		
Net income	$ 8,065	$ 8,346
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	6,260	4,782
Deferred taxes	39	(847)
Tax benefit from stock option exercises	(159)	(405)
Loss (gain) on disposal of property and equipment	10	(13)
Stock-based compensation	587	493
Change in assets and liabilities:		
Inventories	4,057	(3,435)
Receivables	1,358	(667)
Prepaid expenses and other assets	(6,952)	(504)
Accounts payable	(4,424)	(2,731)
Accrued expenses and other liabilities	(9,808)	(6,772)
Net cash used in operating activities	(967)	(1,753)
Cash flows from investing activities:		
Purchases of property and equipment	(4,944)	(9,662)
Purchases of other assets and other intangible assets	(644)	(301)
Escrow Deposit		(36,893)
Net cash used in investing activities	(5,588)	(46,856)
Cash flows from financing activities:		
Exercise of employee stock options and employee stock purchases	347	652
Purchases of Company s common stock	(4,670)	
Tax benefit from stock option exercises	159	405
Net cash (used in) provided by financing activities	(4,164)	1,057
Effect of exchange rates on cash	(15)	
Net decrease in cash and cash equivalents	(10,734)	(47,552)
Cash and cash equivalents, beginning of period	53,109	90,950
Cash and cash equivalents, end of period	$ 42,375	$ 43,398
Supplemental disclsoure of cash flow information:		
Cash paid during the period for:		
Income taxes	$ 8,106	$ 7,326

Noncash Transactions:				
Return of common stock in lieu of tax witholdings and option exercises	$	494	$	211

See accompanying notes to condensed consolidated financial statements.

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1. Basis of Presentation

The condensed consolidated financial statements included herein are unaudited and have been prepared by Build-A-Bear Workshop, Inc. and its subsidiaries (collectively, the Company) pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to such rules and regulations. The condensed consolidated balance sheet of the Company as of December 30, 2006 was derived from the Company s audited consolidated balance sheet as of that date. All other condensed consolidated financial statements contained herein are unaudited and reflect all adjustments which are, in the opinion of management, necessary to summarize fairly the financial position of the Company and the results of the Company s operations and cash flows for the periods presented. All of these adjustments are of a normal recurring nature. All significant intercompany balances and transactions have been eliminated in consolidation. Because of the seasonal nature of the Company s operations, results of operations of any single reporting period should not be considered as indicative of results for a full year. These condensed consolidated financial statements should be read in conjunction with the Company s audited consolidated financial statements for the fiscal year ended December 30, 2006 included in the Company s annual report on Form 10-K filed with the SEC on March 15, 2007.

2. Business Acquisition

On April 2, 2006, the Company acquired all of the outstanding shares of The Bear Factory Limited (Bear Factory), a stuffed animal retailer in the United Kingdom, and Amsbra Limited (Amsbra), the Company s former U.K. franchisee (collectively, the U.K. Acquisition). The results of the U.K. Acquisition operations have been included in the consolidated financial statements since that date. In conjunction with those transactions, we obtained 40 retail locations in the United Kingdom and Ireland. The aggregate cash purchase price for the U.K. Acquisition was $39.4 million, excluding cash acquired of $0.3 million. In addition to the cash purchase price, the Company had previously advanced $4.5 million to Amsbra as a note receivable. The amount of this note receivable and the related accrued interest is a component of the purchase price.

The company has not completed its assessment of the U.K. Acquisition assets and liabilities. Until that assessment is complete, the allocation of the purchase price is preliminary and may be subject to revisions.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of Acquisition (in thousands):

Current assets	$ 7,670
Property and equipment	6,192
Goodwill	31,162
Intangibles	1,824
Total assets acquired	46,848
Current liabilites assumed	(9,215)
Loan previously advanced	4,517
Total purchase price	$ 42,150

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The following unaudited pro forma summary presents the Company s revenue, net income, basic earnings per share and diluted earnings per share as if the U.K. Acquisition had occurred on January 1, 2006 (in thousands, except per share data):

	Thirteen Weeks Ended	
	March 31, 2007	April 1, 2006
Revenue	$116,814	$107,764
Net Income	8,065	6,060
Basic earnings per common share:	$ 0.40	$ 0.30
Diluted earnings per common share:	$ 0.39	$ 0.30

Pro forma adjustments have been made to reflect depreciation and amortization using estimated asset values recognized after applying purchase accounting adjustments.

This pro forma information is presented for informational purposes only and is not necessarily indicative of actual results had the acquisition been effected at the beginning of the respective periods presented, and is not necessarily indicative of future results.

3. Goodwill

In connection with our U.K. Acquisition, we acquired goodwill. This asset was recorded in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, *Business Combinations* and is reported as a component of the Company s retail segment. The following table summarizes the Company s goodwill (in thousands):

U.K. Acquisition	$ 31,162
Acquisition costs	1,005
Severance costs	785
	32,952
Effect of foreign currency translation	3,422
Goodwill, as of March 31, 2007	$ 36,374

4. Stock-based Compensation

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R). SFAS 123R requires companies to recognize the cost of awards of equity instruments, such as stock options and restricted stock, based on the fair value of those awards at the date of grant and eliminates the choice to account for employee stock options under Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25). The Company adopted SFAS 123R effective January 1, 2006 using the modified prospective method.

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Under this method, in addition to reflecting compensation expense for new share-based awards, expense is also recognized to reflect the remaining service period of awards that had been included in pro forma disclosures in prior periods. Prior to January 1, 2006, the fair value of restricted stock awards was expensed by the Company over the vesting period, while compensation expense for stock options was recognized over the vesting period only to the extent that the grant date market price of the stock exceeded the exercise price of the options.

For the thirteen weeks ended March 31, 2007, selling, general and administrative expense includes $0.6 million ($0.4 million after tax) of stock-based compensation expense. For the thirteen weeks ended April 1, 2006, selling, general and administrative expenses includes $0.5 million ($0.3 million after tax) of stock-based compensation expense.

As of March 31, 2007, there was $8.9 million of total unrecognized compensation expense related to nonvested restricted stock awards and options which is expected to be recognized over a weighted-average period of 3.37 years.

Upon adoption of SFAS 123R, the Company made a policy decision that the straight-line expense attribution method would be utilized for all future stock-based compensation awards with graded vesting.

5. Stock Incentive Plans

In 2000, the Company adopted the 2000 Stock Option Plan. In 2003, the Company adopted the Build-A-Bear Workshop, Inc. 2002 Stock Incentive Plan, and, in 2004, the Company adopted the Build-A-Bear Workshop, Inc. 2004 Stock Incentive Plan (collectively, the Plans).

Under the Plans, as amended, up to 3,700,000 shares of common stock were reserved and may be granted to employees and nonemployees of the Company. The Plans allow for the grant of incentive stock options, nonqualified stock options, and restricted stock. Options granted under the Plans expire no later than 10 years from the date of the grant. The exercise price of each incentive stock option shall not be less than 100% of the fair value of the stock subject to the option on the date the option is granted. The exercise price of the nonqualified options shall be determined from time to time by the compensation committee of the board of directors (the Committee). The vesting provision of individual awards is at the discretion of the Committee and generally ranges from one to four years.

(a) Stock Options

The following table is a summary of the balances and activity for the Plans related to stock options for the thirteen weeks ended March 31, 2007:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding, December 30, 2006	529,200	$ 16.10		
Granted				
Exercised	30,505	6.88		
Forfeited	15,000	34.65		
Outstanding, March 31, 2007	483,695	$ 16.10	5.7	$ 5,498
Options Exercisable As Of:				
March 31, 2007	479,945	$ 16.05	5.6	$ 5,482

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The total intrinsic value of options exercised in the thirteen weeks ended March 31, 2007 and April 1, 2006 was approximately $0.7 million and $1.8 million, respectively. The Company generally issues new shares to satisfy option exercises.

(b) Restricted Stock

The following table is a summary of the balances and activity for the Plans related to restricted stock granted as compensation to employees and directors for the thirteen weeks ended March 31, 2007:

	Number of Shares	Weighted Average Grant Date Fair Value per Award
Outstanding, December 30, 2006	227,453	$ 30.06
Granted	215,428	27.48
Vested	51,889	29.23
Canceled or expired	400	27.82
Outstanding, March 31, 2007	390,592	$ 28.75

The total fair value of restricted shares vested during the thirteen weeks ended March 31, 2007 and April 1, 2006 was $1.4 million and $0.4 million, respectively.

(c) Associate Stock Purchase Plan

In October 2004, the Company adopted an Associate Stock Purchase Plan (ASPP). Under the ASPP, substantially all full-time employees are given the right to purchase shares of the Company s common stock, subject to certain limitations, at 85% of the lesser of the fair market value on the purchase date or the beginning of each purchase period. Up to 1,000,000 shares of the Company s common stock are available for issuance under the ASPP. The employees of the Company purchased 5,868 shares at $23.35 per share through the ASPP during the thirteen weeks ended March 31, 2007. The expense recorded related to the ASPP during the thirteen weeks ended March 31, 2007 was determined using the Black-Scholes option pricing model and the provisions of FASB Technical Bulletin 97-1, *Accounting under Statement 123 for Certain Employee Stock Purchase Plans with a Look-Back Option* (FTB 97-1), as amended by SFAS 123R. The assumptions used in the option pricing model for the thirteen weeks ended March 31, 2007 were: (a) dividend yield of 0%; (b) volatility of 20%; (c) risk-free interest rate of 6.0%; and (d) an expected life of 0.25 years.

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6. Earnings per Share

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

	Thirteen weeks ended	
	March 31, 2007	April 1, 2006
Net income allocated to common stockholders	$ 8,065	$ 8,346
Weighted average number of common shares outstanding	20,281,820	20,078,876
Effect of dilutive securities:		
Stock options	177,347	283,843
Restricted stock	66,180	38,659
Weighted average number of common shares dilutive	20,525,347	20,401,378
Earnings per share:		
Basic:	$ 0.40	$ 0.42
Diluted	$ 0.39	$ 0.41

In calculating diluted earnings per share for the thirteen weeks ended March 31, 2007, options to purchase 156,588 shares of common stock were outstanding as of the end of the period, but were not included in the computation of diluted earnings per share due to their anti-dilutive effect. An additional 215,028 shares of restricted common stock were outstanding at the end of the period, but excluded from the calculation of diluted earnings per share due to their anti-dilutive effect under the provisions of SFAS No. 128, *Earnings per Share* (SFAS No. 128).

In calculating diluted earnings per share for the thirteen weeks ended April 1, 2006, options to purchase 206,324 shares of common stock were outstanding as of the end of the period, but were not included in the computation of diluted earnings per share due to their anti-dilutive effect. An additional 202,631 shares of restricted common stock were outstanding at the end of the period, but excluded from the calculation of diluted earnings per share due to their anti-dilutive effect under the provisions of SFAS No. 128.

7. Comprehensive Income

Comprehensive income for the thirteen weeks ended March 31, 2007 and April 1, 2006 was $7.2 million and $8.3 million, respectively. The difference between comprehensive income and net income resulted from foreign currency translation adjustments.

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8. Property and Equipment

Property and equipment consist of the following (in thousands):

	March 31, 2007	December 30, 2006
Land	$ 2,261	$ 2,261
Furniture and fixtures	33,221	33,938
Computer hardware	15,862	15,649
Building	14,970	14,970
Leasehold improvements	123,847	122,043
Computer software	14,410	12,988
Construction in progress	4,085	2,200
	208,656	204,049
Less accumulated depreciation	79,201	73,702
	$ 129,455	$ 130,347

9. Income Taxes

The Company adopted the provisions of Financial Standards Accounting Board Interpretation No. 48 Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48) on December 31, 2006. The implementation of FIN 48 did not result in an adjustment to the liability for unrecognized income tax benefits. At the adoption date of December 31, 2006, there was approximately $1,207,000 of unrecognized tax benefits, all of which would affect the Company s effective tax rate if recognized. At March 31, 2007, there is approximately $1,207,000 of unrecognized tax benefits. In the short-term, management of the Company does not reasonably expect any significant changes.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. As of March 31, 2007, there is approximately $86,000 of accrued interest related to uncertain tax positions.

The tax years 2003-2006 remain open to examination by the major taxing jurisdictions to which the Company is subject.

10. Segment Information

The Company s operations are conducted through three reportable segments consisting of retail, international franchising, and licensing and entertainment. The retail segment includes the operating activities of company-owned stores in the United States, Canada, the United Kingdom and Ireland, and other retail delivery operations, including the Company s web store and non-traditional store locations such as baseball ballparks. The international franchising segment includes the licensing activities of the Company s franchise agreements with store locations in Europe, Asia, and Australia. The licensing and entertainment segment has been established to market the naming and branding rights of the Company s intellectual properties for third party use. These operating segments represent the basis on which the Company s chief operating decision-maker regularly evaluates the business in assessing performance, determining the allocation of resources and the pursuit of future growth opportunities. The operating segments have discrete sources of revenue, different capital structures and different cost structures. The reporting segments follow the same accounting policies used for the Company s consolidated financial statements.

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Following is a summary of the financial information for the Company s reporting segments (in thousands):

	Retail	International Franchising	Licensing & Entertainment	Total
Thirteen weeks ended March 31, 2007				
Net sales to external customers	$115,883	$ 695	$ 236	$116,814
Income before income taxes	12,622	294	71	12,987
Capital expenditures	4,941		3	4,944
Depreciation and amortization	6,126	122	12	6,260
Thirteen weeks ended April 1, 2006				
Net sales to external customers	97,730	690	211	98,631
Income before income taxes	13,170	271	130	13,571
Capital expenditures	9,660	2		9,662
Depreciation and amortization	4,634	146	2	4,782
Total Assets as of:				
March 31, 2007	$286,134	$ 2,427	$ 1,931	$290,492
April 1, 2006	236,472	7,718	1,174	245,364

The Company s reportable segments are primarily determined by the types of products and services that they offer. Each reportable segment may operate in many geographic areas. The Company allocates revenues to geographic areas based on the location of the customer or franchisee. The following schedule is a summary of the Company s sales to external and long-lived assets by geographic area (in thousands):

	North America	United Kingdom & Ireland	Other	Total
Thirteen weeks ended March 31, 2007				
Net sales to external customers	$105,320	$ 10,799	$695	$116,814
Property and equipment, net	113,708	15,731	16	129,455
Thirteen weeks ended April 1, 2006				
Net sales to external customers	97,941		690	98,631
Property and equipment, net	95,172		22	95,194

11. New Accounting Pronouncements

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on assumptions that market participants would use in pricing the asset or liability. The Company is required to adopt SFAS 157 in the first quarter of 2008. The Company is currently assessing the financial impact of SFAS 157 on its consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits an entity to measure certain financial assets and liabilities at fair value. The statement s objective is to improve financial reporting by allowing entities to mitigate volatility in reported earnings caused by the measurement of related assets and liabilities using different attributes, without having to apply complex hedge accounting provisions. This statement becomes effective for fiscal years beginning after November 15, 2007 and should be applied prospectively. It is expected that this statement will not have a material effect on the Company s financial statements.

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12. Subsequent Event

The Company holds a minority interest in Retail Entertainment Concepts, LLC (REC). REC is an early-stage company that has developed an interactive retail concept targeted primarily to boys and their families. REC conducts business under the Ridemakerz ™ brand name. On April 30, 2007, the Company entered into a series of agreements whereby an additional equity investment was made and the Company agreed to perform operational support services for REC. In accordance with the agreements, the Company invested approximately $2.4 million on April 30, 2007, bringing the total investment in REC to approximately $3.0 million. In exchange for performing operational support services the Company will receive additional equity in REC.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.

The following Management s Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from the results discussed in the forward-looking statements. These risks and uncertainties include, without limitation, those detailed under the caption Risk Factors in our annual report on Form 10-K for the year ended December 30, 2006, as filed with the SEC, and the following: we may be unable to generate interest in and demand for our interactive retail experience, or to identify and respond to consumer preferences in a timely fashion; our marketing initiatives may not be effective in generating sufficient levels of brand awareness and guest traffic; we may be unable to generate comparable store sales growth; we may be unable to open new stores or may be unable to effectively manage our growth; we may be unable to effectively manage our international franchises or laws relating to those franchises may change; we may be unable to realize some of the expected benefits of the acquisition of Amsbra and Bear Factory including making these operations profitable; customer traffic may decrease in the shopping malls where we are located, on which we depend to attract guests to our stores; general economic conditions may deteriorate, which could lead to disproportionately reduced consumer demand for our products, which represent relatively discretionary spending; our market share could be adversely affected by a significant, or increased, number of competitors; we may lose key personnel, be unable to hire qualified additional personnel, or experience turnover of our management team; the ability of our principal vendors to deliver merchandise may be disrupted; the availability and costs of our products could be adversely affected by risks associated with international manufacturing and trade; high petroleum products prices could increase our inventory transportation costs and adversely affect our profitability; we may be unable to realize the anticipated benefits from our company-owned distribution center; fluctuations in our quarterly results of operations could cause the price of our common stock to substantially decline; we may fail to renew, register or otherwise protect our trademarks or other intellectual property; we may have disputes with, or be sued by, third parties for infringement or misappropriation of their proprietary rights; we may be unable to renew or replace our store leases, or enter into leases for new stores on favorable terms or in favorable locations, or may violate the terms of our current leases; we may suffer negative publicity or be sued due to violations of labor laws or unethical practices by manufacturers of our merchandise; and we may improperly obtain or be unable to protect information from our guests in violation of privacy or security laws or expectations.

These risks, uncertainties and other factors may adversely affect our business, growth, financial condition or profitability, or subject us to potential liability, and cause our actual results, performance or achievements to be materially different from those expressed or implied by our forward-looking statements. We do not undertake any obligation or plan to update these forward-looking statements, even though our situation may change.

Overview

We are the leading, and only international, company providing a make your own stuffed animal interactive entertainment experience under the Build-A-Bear Workshop brand, in which our guests stuff, fluff, dress, accessorize and name their own teddy bears and other stuffed animals. Our concept, which we developed primarily for mall-based retailing, capitalizes on what we believe is the relatively untapped demand for experience-based shopping as well as the widespread appeal of stuffed animals. The Build-A-Bear Workshop experience appeals to a broad range of age groups and demographics, including children, teens, their parents and grandparents. As of March 31, 2007, we operated 237 stores in 44 states and Canada, 40 stores in the United Kingdom and Ireland, and had 37 franchised stores operating internationally under the Build-A-Bear Workshop brand. In addition to our stores, we market our products and build our brand through our website, which simulates our interactive shopping experience, as well as non-traditional store locations in Major League Baseball® ballparks, one location in a zoo and one in a science center, and our presence at event-based locations through our mobile store.

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On April 2, 2006, the Company acquired all of the outstanding shares of The Bear Factory Limited (Bear Factory), a stuffed animal retailer in the United Kingdom, and Amsbra Limited (Amsbra), the Company s former U.K. franchisee (collectively, the U.K. Acquisition). The results of the U.K. Acquisition operations have been included in the consolidated financial statements since that date. In conjunction with those transactions, we obtained 40 retail locations in the United Kingdom and Ireland. Four of those locations closed during 2006. Of those four locations, two closed due to overlapping store locations in the Amsbra and Bear Factory portfolios, and the other two locations are concessions within department stores which is a format that we have chosen not to continue. The Company expects to improve sales performance and adopt best practices in the areas of merchandising, marketing, purchasing and store operations, across the acquired store base.

We operate in three reportable segments (retail, international franchising, and licensing and entertainment) that share the same infrastructure, including management, systems, merchandising and marketing, and generate revenues as follows:

Company-owned retail stores located in the United States, Canada, the United Kingdom and Ireland retail stores, two webstores and seasonal, event-based locations;

International stores operated under franchise agreements; and

License arrangements with third parties which manufacture and sell to other retailers merchandise carrying the Build-A-Bear Workshop brand.

Selected financial data attributable to each segment for the thirteen weeks ended March 31, 2007 and April 1, 2006 are set forth in the notes to our condensed consolidated financial statements included elsewhere in this quarterly report on Form 10-Q.

Store contribution, for our consolidated operations, was 24.4% for the thirteen weeks ended March 31, 2007 and 27.7% for the thirteen weeks ended April 1, 2006 and consolidated net income as a percentage of total revenues was 6.9% for the thirteen weeks ended March 31, 2007 and 8.5% for the thirteen weeks ended April 1, 2006. See Non-GAAP Financial Measures for a definition of store contribution and a reconciliation of store contribution to net income. The decrease in our store contribution over the prior year was primarily due to the decline in gross margin. The decrease in gross margin was anticipated and primarily resulted from higher occupancy costs as a percentage of net retail sales at the U.K. stores. We have maintained what we believe to be a high store contribution level through the creation of economies of scale which allow us to decrease the cost of our product on a per unit basis and continued expense management through labor planning and the monitoring of store supplies and other expenses.

We use comparable store sales as one of the performance measures for our business. Comparable store sales decreased by 6.9% in the thirteen weeks ended March 31, 2007 compared to a decrease of 3.8% for the thirteen weeks ended April 1, 2006. The decline in comparable store sales was attributed primarily to changing customer preferences. Our repeat customers, many of whom have built a sizable collection of Build-A-Bear Workshop stuffed animals, have become more product discriminating. Also contributing to the decline in comparable store sales was a decrease in customer traffic in our stores and the more difficult macro economic conditions generally impacting customers.

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Expansion and Growth Potential

Company-owned stores:

The table below sets forth the number of Build-A-Bear Workshop Company-owned stores in the United States, Canada, the United Kingdom and Ireland for the periods presented:

	Thirteen weeks ended	
	March 31, 2007	April 1, 2006
Beginning of period	271	200
Opened	6	2
Closed		
End of period	277	202

During fiscal 2007, we anticipate opening 39 Build-A-Bear Workshop stores in the United States and Canada, and 7 to 10 new stores in the United Kingdom and Ireland. We believe there is a market potential for at least 350 Build-A-Bear Workshop stores in the United States and Canada and approximately 70 to 75 stores in the United Kingdom and Ireland. Additionally, we expect to expand our Company-owned store base in 2007 to France, which previously had one franchised store in operation. We expect to open three new stores in France during fiscal 2007.

In fiscal 2003, we began testing in certain markets our initial brand expansion initiative, our proprietary Friends 2B Made line of make-your-own dolls and related products. As of March 31, 2007, we operated one stand-alone Friends 2B Made store and eight Friends 2B Made stores adjacent to or within Build-A-Bear Workshop stores in the United States. Other than the one stand-alone store, these Friends 2B Made stores are not considered new stores but rather expansions of Build-A-Bear Workshop stores.

Non-store locations:

In fiscal 2004, we began offering merchandise in seasonal, event-based locations such as Major League Baseball® ballparks, as well as at temporary locations such as at the NBA All-Star Jam Session. We expect to expand our future presence at select seasonal, event-based locations contingent on their availability. As of the end of March 31, 2007, we had a total of five ballpark locations and one store within a zoo. We also opened our first store within a science center during the thirteen weeks ended March 31, 2007.

International Franchise Revenue:

Our first franchised location opened in November 2003. The number of international, franchised stores for the periods presented below can be summarized as follows:

	Thirteen weeks ended	
	March 31, 2007	April 1, 2006
Beginning of period	34	30
Opened	4	
Closed	(1)	
End of period	37	30

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As of March 31, 2007, we had 13 master franchise agreements, which typically grant franchise rights for a particular country or countries, covering 16 countries. We anticipate signing additional master franchise agreements in the future. We expect our current and future franchisees to open a total of 20 to 25 stores in fiscal 2007. We believe there is a market potential for approximately 300 franchised stores outside of the United States, Canada, the United Kingdom and Ireland.

Results of Operations

The following table sets forth, for the periods indicated, selected statement of operation data expressed as a percentage of total revenues, except where otherwise indicated. Percentages will not total due to the cost of merchandise sold being expressed as a percentage of net retail sales and rounding:

	Thirteen weeks ended	
	March 31, 2007	**April 1, 2006**
Revenues:		
Net retail sales	99.2	99.1
Franchise fees	0.6	0.7
Licensing revenue	0.2	0.2
Total revenues	100.0	100.0
Costs and expenses:		
Cost of merchandise sold (1)	53.6	51.0
Selling, general and administrative	35.6	35.9
Store preopening	0.6	0.6
Interest expense (income), net	(0.5)	(0.9)
Total costs and expenses	88.9	86.2
Income before income taxes	11.1	13.8
Income tax expense	4.2	5.3
Net income	6.9	8.5
Gross Margin % (2)	46.4%	49.0%

(1) Cost of merchandise sold is expressed as a percentage of net retail sales.

(2) Gross margin represents net retail sales less cost of merchandise

sold. Gross margin percentage represents gross margin divided by net retail sales.

Thirteen weeks ended March 31, 2007 compared to thirteen weeks ended April 1, 2006

Total revenues. Net retail sales increased to $115.9 million for the thirteen weeks ended March 31, 2007 from $97.7 million for the thirteen weeks ended April 1, 2006, an increase of $18.2 million, or 18.6%. Net retail sales for new stores in North America contributed a $12.6 million increase in net retail sales. U.K. sales contributed $10.8 million. Sales over the Internet increased by $0.6 million, or 24.0%. Comparable store sales decreased $6.5 million, or 6.9%. The decline in comparable store sales was attributed primarily to a change in preferences from our repeat customers who have become more product discriminating. Also contributing to the decline in comparable store sales was a decrease in customer traffic in our stores and the more difficult macro economic conditions generally impacting customers.

Revenue from franchise fees was $0.6 million for both the thirteen weeks ended March 31, 2007 and thirteen weeks ended April 1, 2006.

Gross margin. Gross margin increased to $53.7 million for the thirteen weeks ended March 31, 2007 from $47.9 million for the thirteen weeks ended April 1, 2006, an increase of $5.8 million, or 12.1%. As a percentage of net retail sales, gross margin decreased to 46.4% for the thirteen weeks ended March 31, 2007 from 49.0% for the thirteen weeks ended April 1, 2006, a decrease of 2.6%. This decrease was anticipated and primarily resulted from higher occupancy costs as a percentage of net retail sales in the U.K. Improved merchandise margins partially offset the decrease in gross margin percentage.

Selling, general and administrative. Selling, general and administrative expenses were $41.6 million for the thirteen weeks ended March 31, 2007 as compared to $35.5 million for the thirteen weeks ended April 1, 2006, an increase of $6.1 million, or 17.2%. As a percentage of total revenues, selling, general and administrative expenses decreased to 35.6% for the thirteen weeks ended March 31, 2007 as compared to 35.9% for the thirteen weeks ended April 1, 2006, a decrease of 0.3%. The dollar increase was primarily due to higher selling, general and administrative costs associated with the acquired operations of the U.K., and having 75 more stores in operation at March 31, 2007 as compared to April 1, 2006. Additionally, during the thirteen weeks ended March 31, 2007 the Company incurred bad debt expense of $0.3 million associated with receivables owed by our former franchisee in France. The operations of the one franchised store in France ceased in April 2007. The decrease in selling, general and administrative expenses as a percent of revenue was primarily due to the leveraging of store payroll over a larger revenue base and a decline in central office management payroll resulting primarily from lower performance-based bonus expense.

Store preopening. Store preopening expense was $0.7 million for the thirteen weeks ended March 31, 2007 as compared to $0.6 million for the thirteen weeks ended April 1, 2006. Contributing to the higher expense during the thirteen weeks ended March 31, 2007 was U.K. preopening expenses of $0.2 million. Preopening expenses include expenses for stores that opened in the current period as well as some expenses incurred for stores that will be opened in future periods.

Interest expense (income), net. Interest income, net of interest expense, was $0.5 million for the thirteen weeks ended March 31, 2007 as compared to $0.9 million for the thirteen weeks ended April 1, 2006. This decrease was due to lower cash balances in the fiscal 2007 first quarter as compared to the fiscal 2006 first quarter.

Provision for income taxes. The provision for income taxes was $4.9 million for the thirteen weeks ended March 31, 2007 as compared to $5.2 million for the thirteen weeks ended April 1, 2006. The effective tax rate was 37.9% for the thirteen weeks ended March 31, 2007 compared to 38.5% for the thirteen weeks ended April 1, 2006. The decrease in the effective tax rate is attributable to tax benefits associated with our company-owned distribution center. We expect the effective tax rate for full year 2007 to be approximately 38.0% compared to approximately 39.0% in fiscal year 2006.

Non-GAAP Financial Measures

We use the term store contribution in this quarterly report on Form 10-Q. Store contribution consists of income before income tax expense, interest, store depreciation and amortization, store preopening expense and general and administrative expense, excluding franchise fees, income from licensing activities and contribution from our webstore and seasonal and event-based locations. This term, as we define it, may not be comparable to similarly titled measures used by other companies and is not a measure of performance presented in accordance with U.S. generally accepted accounting principles (GAAP).

We use store contribution as a measure of our stores operating performance. Store contribution should not be considered a substitute for net income, net income per store, cash flows provided by operating activities, cash flows provided by operating activities per store, or other income or cash flow data prepared in accordance with GAAP.

We believe store contribution is useful to investors in evaluating our operating performance because it, along with the number of stores in operation, directly impacts our profitability. Historically, central office general and administrative expenses and preopening expenses have increased at a rate of less than our total net retail sales increases. Therefore, as we have opened additional new stores and leveraged our central office and general and administrative and preopening expenses over this larger store base and sales volume, we have been able to increase our net income each year.

The following table sets forth a reconciliation of store contribution to net income for our company-owned stores located in the U.S. and Canada (North America), stores located in the U.K. and Ireland (United Kingdom), and for our consolidated store base (Total) (in thousands):

	Thirteen weeks ended March 31, 2007			Thirteen weeks ended April 1, 2006		
	North America	United Kingdom	Total	North America	United Kingdom	Total
Net income	$ 10,296	$ (2,231)	$ 8,065	$ 8,346	$	$ 8,346
Income tax expense	4,922		4,922	5,225		5,225
Interest expense (income)	(545)		(545)	(866)		(866)
Store depreciation and amortization (1)	4,148	545	4,693	3,912		3,912
Store preopening expense	513	175	688	615		615
General and administrative expense (2)	10,084	861	10,945	9,852		9,852
Franchising and licensing contribution (3)	(539)		(539)	(457)		(457)
Non-store activity contribution (4)	(1,016)		(1,016)	(403)		(403)
Store contribution	$ 27,863	$ (650)	$ 27,213	$ 26,224	$	$ 26,224
Total revenues	$ 106,015	$ 10,799	$ 116,814	$ 98,631	$	$ 98,631
Franchising and licensing revenues	(931)		(931)	(901)		(901)
Revenues from non-store activities (4)	(3,985)	(197)	(4,182)	(3,001)		(3,001)
Store location net retail sales	$ 101,099	$ 10,602	$ 111,701	$ 94,729	$	$ 94,729
Store contribution as a percentage of store location net retail sales	27.6%	-6.1%	24.4%	27.7%	0.0%	27.7%
Total net income as a percentage of total revenues	9.7%	-20.7%	6.9%	8.5%	0.0%	8.5%

(1) Store depreciation and amortization includes depreciation and amortization of all capitalized assets in store locations, including leasehold improvements, furniture and fixtures, and computer hardware and software.

(2) General and administrative expenses consist of non-store, central office general and administrative functions such as management payroll and related benefits, travel, information systems, accounting, purchasing and legal costs as well as the depreciation and amortization of central office leasehold improvements, furniture and fixtures, computer hardware and software and intellectual property. General and administrative expenses also include a central office marketing department, primarily payroll and related benefits expense, but exclude advertising expenses, such as direct mail catalogs and television advertising, which are included in store contribution.

(3) Franchising and licensing contribution

includes franchising and licensing revenues and all expenses attributable to the international franchising and licensing and entertainment segments other than depreciation, amortization and interest expense/income. Depreciation and amortization related to franchising and licensing is included in the general and administrative expense caption. Interest expense/income related to franchising and licensing is included in the interest expense (income) caption.

(4) Non-store activities include our webstore, and seasonal and event-based locations.

Seasonality and Quarterly Results

Our operating results for one period may not be indicative of results for other periods, and may fluctuate significantly because of a variety of factors, including: (1) the timing of our new store openings and related expenses; (2) the profitability of our stores; (3) increases or decreases in our comparable store sales; (4) the timing and frequency of our marketing initiatives; (5) changes in general economic

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conditions and consumer spending patterns; (6) changes in consumer preferences; (7) the effectiveness of our inventory management; (8) the actions of our competitors or mall anchors and co-tenants; (9) seasonal shopping patterns and holiday and vacation schedules; (10) the timing and frequency of national media appearances and other public relations events; and (11) weather conditions.

The timing of new store openings may result in fluctuations in quarterly results as a result of the revenues and expenses associated with each new store location. We typically incur most preopening costs for a new store in the three months immediately preceding the store s opening. We expect our growth, operating results and profitability to depend in some degree on our ability to increase our number of stores.

Historically, for North American stores (U.S. and Canada) open more than twelve months, seasonality has not been a significant factor in our results of operations, although we cannot assure you that this will continue to be the case. U.K.-based store sales have historically been weighted more heavily in the fourth quarter as compared to North American stores. In addition, for accounting purposes, the quarters of each fiscal year consist of 13 weeks, although we will have a 14-week quarter approximately once every six years.

Liquidity and Capital Resources

Our cash requirements are primarily for the opening of new stores, information systems and working capital. Historically, we have met these requirements through capital generated from the sale and issuance of our securities to private investors and through our initial public offering, cash flow provided by operations and our revolving line of credit.

Operating Activities. Cash used in operating activities was $1.0 million for the thirteen weeks ended March 31, 2007 as compared with cash used in operating activities of $1.8 million for the thirteen weeks ended April 1, 2006, or an decrease of $0.8 million. This increase over the year ago period was primarily due to the timing of inventory purchases through better inventory management partially offset by the increase of cash used in the prepayment of rent in the U.K.

Investing Activities. Cash used in investing activities was $5.6 million for the thirteen weeks ended March 31, 2007 as compared to $46.9 million for the thirteen weeks ended April 1, 2006. The decrease in cash used for investing activities relates primarily to cash held in escrow for the U.K. Acquisition of $36.9 million for the thirteen weeks ended April 1, 2006. Additionally, cash flows from investing activities decreased for the periods presented as the thirteen weeks ended April 1, 2006 included cash expenditures for the construction of the company-owned distribution center. As the distribution center was completed in fiscal 2006, first quarter 2007 capital expenditures had no additional cash outflows related to this project.

Financing Activities. Cash used in financing activities was $4.2 million in the thirteen weeks ended March 31, 2007 which consisted of cash spent for the repurchase of the Company s common stock and slightly offset by proceeds from the exercise of employee stock options and the tax benefit from the exercise of stock options. Cash flows provided by financing activities of $1.1 million for the thirteen weeks ended April 1, 2006 consisted primarily of proceeds from the exercise of employee stock options and the tax benefit from the exercise of stock options. No borrowings were made under our line of credit in either the thirteen weeks ended March 31, 2007 or the thirteen weeks ended April 1, 2006.

Capital Resources. As of March 31, 2007, we had a cash balance of $42.4 million. We also have a line of credit, which we can use to finance capital expenditures and seasonal working capital needs throughout the year. The credit agreement is with U.S. Bank, National Association and was amended effective June 30, 2006 to include a seasonal overline from July 1 to December 31 each year during which the line availability increases from $15 million to $30 million. Borrowings under the credit agreement are not collateralized, but availability under the credit agreement can be limited by the vendor based on our

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level of accounts receivable, inventory, and property and equipment. The credit agreement expires on September 30, 2007 and contains various restrictions on indebtedness, liens, guarantees, redemptions, mergers, acquisitions or sale of assets, loans, transactions with affiliates, and investments. It also prohibits us from declaring dividends without the bank s prior consent, unless such payment of dividends would not violate any terms of the loan agreement. Borrowings bear interest at our option of prime minus 1.0% or LIBOR plus 1.5%. Financial covenants include maintaining a minimum tangible net worth, maintaining a minimum fixed charge cover ratio (as defined in the credit agreement) and not exceeding a maximum funded debt to earnings before interest, depreciation and amortization ratio. As of March 31, 2007, we were in compliance with these covenants. There were no borrowings under our line of credit as of March 31, 2007. There was a standby letter of credit of approximately $1.1 million outstanding under the credit agreement as of March 31, 2007. Accordingly, there was approximately $28.9 million available for borrowing under the line of credit as of March 31, 2007.

Most of our retail stores are located within shopping malls and all are operated under leases classified as operating leases. Our leases in North America typically have a ten-year term and contain provisions for base rent plus percentage rent based on defined sales levels. Many of the leases contain a provision whereby either we or the landlord may terminate the lease after a certain time, typically in the third to fourth year of the lease, if a certain minimum sales volume is not achieved. In addition, some of these leases contain various restrictions relating to change of control of our company. Our leases also subject us to risks relating to compliance with changing mall rules and the exercise of discretion by our landlords on various matters, including rights of termination in some cases.

Our leases in the U.K. typically have terms of 10-15 years and generally contain a provision whereby every fifth year the rental rate can be adjusted to reflect the current market rates. The leases typically provide the lessee with the first right for renewal at the end of the lease. We may also be required to make deposits and rent guarantees to secure new leases as we expand. Real estate taxes also change according to government time schedules to reflect current market rental rates for the locations we lease.

In fiscal 2007, we expect to spend a total of $35 to $40 million on capital expenditures. Capital spending through the thirteen weeks ended March 31, 2007 totaled $5.6 million. Capital spending in fiscal 2007 is primarily for the opening of approximately 44 new stores (38 in North America and 7 to 10 in the United Kingdom), and the continued installation and upgrades of central office information technology systems. In fiscal 2006, the average investment per new store, which includes leasehold improvements, fixtures, equipment and inventory, was approximately $0.5 million. We anticipate the investment per store in fiscal 2007 will be approximately the same as fiscal 2006.

We believe that cash generated from operations and borrowings under our credit agreement will be sufficient to fund our working capital and other cash flow requirements for at least the next 18 months. Our credit agreement expires on September 30, 2007.

Off-Balance Sheet Arrangements

We do not have any arrangements classified as off-balance sheet arrangements.

Inflation

We do not believe that inflation has had a material adverse impact on our business or operating results during the periods presented. We cannot provide assurance, however, that our business will not be affected by inflation in the future.

Critical Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles requires the appropriate application of certain accounting policies, many of which require us to make estimates and assumptions about future events and their impact on amounts reported in our financial statements and related notes. Since future events and their impact cannot be determined with certainty, the actual results will inevitably differ from our estimates. Such differences could be material to the financial statements.

We believe our selection and application of accounting policies, and the estimates inherently required therein, is reasonable. These accounting policies and estimates are periodically reevaluated, and adjustments are made when facts and circumstances dictate a change. Historically, we have found our application of accounting policies to be appropriate, and actual results have not differed materially from those determined using necessary estimates.

Our accounting policies and use of estimates are discussed in and should be read in conjunction with the annual consolidated financial statements and notes included in our annual report on Form 10-K, as filed with the Securities and Exchange Commission on March 15, 2007, which includes audited consolidated financial statements for our 2006, 2005 and 2004 fiscal years. We have identified certain critical accounting policies which are described below.

Inventory

Inventory is stated at the lower of cost or market, with cost determined on an average cost basis. Historically, we have not conducted sales whereby we offer significant discounts or markdowns, nor have we experienced significant occurrences of obsolete or slow moving inventory. However, future changes in circumstances, such as changes in guest merchandise preference, could cause reclassification of inventory as obsolete or slow-moving inventory. The effect of this reclassification would be the recording of a reduction in the value of inventory to realizable values.

Throughout the year we record an estimated cost of shortage based on past historical results. Periodic physical inventories are taken and any difference between the actual physical count of merchandise and the recorded amount in our records are adjusted and recorded as shortage. Historically, the timing of the physical inventory has been near the end of the fiscal year so that no material amount of shortage was required to be estimated on activity between the date of the physical count and year-end. However, future physical counts of merchandise may not be at times at or near the end of a fiscal quarter or fiscal year-end, and our estimate of shortage for the intervening period may be material based on the amount of time between the date of the physical inventory and the date of the fiscal quarter or year-end.

Long-Lived Assets

If facts and circumstances indicate that a long-lived asset, including property and equipment, may be impaired, the carrying value is reviewed. If this review indicates that the carrying value of the asset will not be recovered as determined based on projected undiscounted cash flows related to the asset over its remaining life, the carrying value of the asset is reduced to its estimated fair value.

Goodwill and Other Intangible Assets

Intangible assets deemed to have indefinite lives and goodwill are not subject to amortization. All other intangible assets are amortized over their estimated useful lives. Goodwill and other intangible assets not subject to amortization are tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. This testing requires comparison of carrying values to fair values, and when appropriate, the carrying values of impaired assets is reduced to

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fair value. We reviewed our goodwill and other intangible assets as of December 30, 2006 and determined that no impairment existed.

Revenue Recognition

Revenues from retail sales, net of discounts and excluding sales tax, are recognized at the time of sale. Guest returns have not been significant. Revenues from gift certificates are recognized at the time of redemption. Unredeemed gift cards are included in current liabilities on the consolidated balance sheets.

We have an automated frequent shopper program in the United States, the Stuff Fur Stuff® club, whereby guests enroll in the program and receive one point for every dollar or partial dollar spent and after reaching 100 points receive a $10 discount on a future purchase. This program was automated in July 2006 and replaced our former Buy Stuff Program, which was a manual punch card system with limited tracking capability. The reward earned under the new program did not change. An estimate of the obligation related to the program, based on historical redemption rates, is recorded as deferred revenue and a reduction of net retail sales at the time of purchase. The deferred revenue obligation is reduced, and a corresponding amount is recognized in net retail sales, in the amount of and at the time of redemption of the $10 discount.

Under the previous Buy Stuff Program, the first card had no expiration date. Beginning in June 2002, and continuing each summer up to July 1, 2006, a series of cards was issued that had an expiration date of December 31 of the year following the year in which that series of cards was first issued. Beginning in July 2006, the automated Stuff Fur Stuff® club was introduced which provides greater visibility to the rewards earned by our guests and the historical redemption rates. We track redemptions of these various cards and use actual redemption rates by card series and historical results to estimate how much revenue to defer. We review these redemption rates and assess the adequacy of the deferred revenue account at the end of each fiscal quarter. Due to the estimates involved in these assessments, adjustments to the deferral rate are generally made no more often than bi-annually in order to allow time for more definite trends to emerge.

Based upon an assessment at the end of fiscal 2003, the deferred revenue account was adjusted downward by $1.1 million with a corresponding increase to net retail sales, an increase in net income of $0.7 million. Additionally, the amount of revenue being deferred beginning in fiscal 2004 was decreased by 0.2%, and by another 0.5% beginning with the third quarter of 2004, to give effect to the change in redemption experience. The changes made to the deferral rate in fiscal 2004 were prospective in nature with no impact on previously reported results of operations. Beginning with the second quarter of fiscal 2005, the amount of revenue being deferred was reduced by 0.1% on a prospective basis from its then current level due to further changes in the Company s redemption experience.

Based on the most recent assessment at the end of fiscal 2006, the deferred revenue account was adjusted downward by $3.6 million, effective at the beginning of fiscal 2006, with a corresponding increase to net sales, and a $2.2 million increase in net income. Additionally, the amount of revenue being deferred for future periods has been decreased by 0.6%, to give effect to the change in redemption experience and the increased visibility of the redemptions with the automated system. An additional 0.1% adjustment of the ultimate redemption rate at the end of fiscal 2006 for the current cards expiring on December 30, 2006 and December 29, 2007 would have an approximate impact of $0.5 million on the deferred revenue balance and net retail sales.

Leases

We lease all of our store locations and our corporate headquarters. We account for our leases under the provisions of FASB Statement No. 13, *Accounting for Leases* (SFAS 13) and subsequent amendments, which require that our leases be evaluated and classified as operating or capital leases for financial reporting purposes. All of our store leases are classified as operating leases pursuant to the requirements of SFAS 13. We disburse cash for leasehold improvements and furniture fixtures and equipment to build out and equip our leased premises. We may also expend cash for permanent improvements that we make to leased premises that generally are reimbursed to us by our landlords as construction allowances (also known as tenant improvement allowances) pursuant to agreed-upon terms in our leases. Landlord allowances can take the form of up-front cash, full or partial credits against minimum or percentage rents otherwise payable by us, or a combination thereof. Under the provisions of FASB Technical Bulletin No. 88-1, Issues Relating to Accounting for Leases, we account for these landlord allowances as lease incentives resulting in a deferred credit to be recognized over the term of the lease as a reduction of rent expense.

New Accounting Pronouncements

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on assumptions that market participants would use in pricing the asset or liability. We are required to adopt SFAS 157 in the first quarter of 2008. We are currently assessing the financial impact of SFAS 157 on our consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits an entity to measure certain financial assets and liabilities at fair value. The statement s objective is to improve financial reporting by allowing entities to mitigate volatility in reported earnings caused by the measurement of related assets and liabilities using different attributes, without having to apply complex hedge accounting provisions. This statement becomes effective for fiscal years beginning after November 15, 2007 and should be applied prospectively. It is expected that this statement will not have a material effect on the our financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Our market risks relate primarily to changes in interest rates. We bear this risk in two specific ways. First, our revolving credit facility carries a variable interest rate that is tied to market indices and, therefore, our results of operations and our cash flows could have been impacted by changes in interest rates. We had no borrowings outstanding under our revolving credit facility during the thirteen weeks ended March 31, 2007. Accordingly, a 100 basis point change in interest rates would result in no material change to our recorded interest expense. The second component of interest rate risk involves the short term investment of excess cash in short term, investment grade interest-bearing securities. These investments are considered to be cash equivalents and are shown that way on our balance sheet. If there are changes in interest rates, those changes would affect the investment income we earn on these investments and, therefore, impact our cash flows and results of operations.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures: The Company s management, with the participation of the Company s Chief Executive Bear and Chief Financial Bear, has evaluated the effectiveness of the Company s disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this report. Based on such evaluation, the Company s management, including the Chief Executive Bear and Chief Financial Bear, have concluded that the Company s disclosure controls and procedures were effective as of March 31, 2007, the end of the period covered by this quarterly report.

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It should be noted that our management, including the Chief Executive Bear and the Chief Financial Bear, does not expect that the Company s disclosure controls and procedures or internal controls will prevent all error and all fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. 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; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Changes in Internal Control Over Financial Reporting: The Company s management, with the participation of the Company s Chief Executive Bear and Chief Financial Bear, also conducted an evaluation of the Company s internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) to determine whether any changes occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting. Based on that evaluation, there has been no such change during the period covered by this report.

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PART II OTHER INFORMATION

Item 1A. Risk Factors.

There have been no material changes to our Risk Factors as disclosed in our Annual Report on Form 10-K for the year ended December 30, 2006 as filed with the SEC on March 15, 2007.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

ISSUER PURCHASES OF EQUITY SECURITIES

Period		(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Program	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
Dec. 31, 2006	**Jan. 27, 2007**		N/A		
Jan. 28, 2007	**Feb. 24, 2007 (1)**	30,000	$ 27.54	30,000	$ 24,173,677
Feb. 25, 2007	**March 31, 2007(1) (2)**	164,093	$ 26.34	146,500	$ 20,333,516
Total		194,093	$ 26.52	176,500	$ 20,333,516

(1) On February 20, 2007, we announced a $25 million share repurchase program of our outstanding common stock over the next twelve months. The program was authorized by our board of directors. Purchases may be made in the open market or in privately

negotiated transactions, with the level and timing of activity depending on market conditions, other investment opportunities, and other factors. Purchases may be increased, decreased or discontinued at any time without notice. Shares purchased under the program were subsequently retired.

(2) Represents shares of our common stock delivered to us in satisfaction of the tax withholding obligation of holders of restricted shares which vested during the quarter. Our equity incentive plans provide that the value of shares delivered to us to pay the withheld to cover tax obligations is calculated as the average of the high and low trading price of our common

stock on the date the relevant transaction occurs.

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Item 5. Other Information

(a) The following individuals maintain Rule 10b5-1 trading plans (each, a Plan and together, the Plans)(1) Maxine Clark, Chairman, Board of Directors and Chief Executive Bear, (2) Scott Seay, President and Chief Operating Bear, (3) Tina Klocke, Chief Financial Bear, Treasurer and Secretary, and (4) Teresa Kroll, Chief Marketing. Barry Erdos terminated his Rule 10b5-1 plan in conjunction with his departure on January 5, 2007. Barney Ebsworth, Director Emeritus, terminated his Rule 10b5-1 plan effective April 30, 2007.

Chief Executive Bear Maxine Clark s Plan was adopted under the name of Smart Stuff, Inc. Ms. Clark controls the voting and/or investment power for the shares held by Smart Stuff, Inc, as its president and sole shareholder. Ms. Clark currently owns 3,071,529 shares (including vested options and the shares she owns through Smart Stuff, Inc.). Ms. Clark s Plan permits no more than a maximum of 8% of her current share holdings (including vested options) to be sold per year (in each of 2007 and 2008). Accordingly, Ms. Clark will continue to have a significant ownership interest in the Company,

The participants in the Plans will have no control over the timing of any sales under their respective Plans and there can be no assurance that the shares covered by the Plans actually will be sold. The participants entered into the Plans in order to diversify their respective financial holdings.

The Plans are intended to comply with Rule 10b5-1 of the Securities Exchange Act of 1934 and the Company s insider trading policy. Rule 10b5-1 allows corporate insiders to establish prearranged written plans to buy or sell a specified number of shares of a company stock over a set period of time. The specified number of shares sold may be determined pursuant to a formula or may be at the discretion of a third party, so long as such person is not aware of material non-public information. Among other things, the Company s insider trading policy allows insiders to implement a written trading plan provided such person is not in possession of material non-public information about the Company at the time the plan is entered into, consistent with Rule 10b5-1. The Plans were established during an open window under the Company s insider trading policy.

Except as may be required by law, the Company does not undertake to report written trading plans established by other Company officers or directors, nor to report modifications, terminations, transactions or other activities under the Plans or the plan of any other officer or director. Actual sales made pursuant to the Plans will be disclosed publicly through Form 4 and Form 144 filings with the Securities and Exchange Commission.

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Item 6. Exhibits.

The following is a list of exhibits filed as a part of the quarterly report on Form 10-Q:

Exhibit No.	Description
10.1	Rules of the Build-A-Bear Workshop, Inc. U.K. Share Option Scheme, incorporated by reference to Build-A-Bear Workshop, Inc. Form 8-K filed on February 9, 2007, Exhibit 10.1
10.2	Employment, Confidentiality, and Non-compete Agreement between Build-a-Bear Workshop, Inc. and Paul Bundonis dated January 16, 2007, incorporated by reference to Build-A-Bear Workshop, Inc. Form 8-K filed on January 18, 2007, Exhibit 10.1
10.3	Separation Agreement and General Release by and between Build-A-Bear Workshop, Inc. and Barry Erdos dated January 5, 2007, incorporated by reference to Build-A-Bear Workshop, Inc. Form 8-K filed on January 5, 2007, Exhibit 10.1
10.4	Second Amendment to the Employment, Confidentiality, and Non-Compete Agreement between Build-A-Bear Workshop, Inc. and Scott Seay dated January 5, 2007, incorporated by reference to Build-A-Bear Workshop, Inc. Form 8-K filed January 5, 2007, Exhibit 10.2
31.1	Rule 13a-14(a)/15d-14(a) certification (pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, executed by the Chief Executive Bear)
31.2	Rule 13a-14(a)/15d-14(a) certification (pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, executed by the Chief Financial Bear)
32.1	Section 1350 Certification (pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, executed by the Chief Executive Bear)
32.2	Section 1350 Certification (pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, executed by the Chief Financial Bear)

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SIGNATURES

Pursuant to the requirements 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.

Date: May 10, 2007

BUILD-A-BEAR WORKSHOP, INC.
(Registrant)

By: /s/ Maxine Clark
Maxine Clark
Chairman of the Board and Chief Executive Bear

By: /s/ Tina Klocke
Tina Klocke
Chief Financial Bear, Treasurer and Secretary