

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

(MARK ONE)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED JANUARY 30, 1999

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED) FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NUMBER 000-21250

THE GYMBOREE CORPORATION  
(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

94-2615258  
(I.R.S. Employer  
Identification No.)

700 AIRPORT BOULEVARD, SUITE 200, BURLINGAME, CALIFORNIA  
(Address of principal executive offices)

94010-1912  
(Zip Code)

Registrant's telephone number, including area code: (650)-579-0600

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class	Name of each exchange on which registered
COMMON STOCK, \$0.001 PAR VALUE	NASDAQ NATIONAL MARKET

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

NONE.

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), 12 months and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the voting stock held by non-affiliates of the registrant as of April 5, 1999, was approximately \$248,725,680, based upon the last price reported for such date on the NASDAQ National Market.

As of April 5, 1999, 24,265,920 shares of the registrant's common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Annual Report to Stockholders for the fiscal year ended January 30, 1999 (hereinafter referred to as the "1998 Annual Report to Stockholders") are incorporated into Parts II and IV.

Portions of the Registrant's Proxy Statement for the Annual Meeting of

Stockholders to be held on May 26, 1999 (hereinafter referred to as the "1998 Proxy Statement") are incorporated into Part III.

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THE GYMBOREE CORPORATION

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PART 1

ITEM 1. BUSINESS

The Gymboree Corporation is a leading specialty retailer of high quality apparel and accessories for children ages newborn to preteen. Gymboree operates an international chain of stores, primarily in regional shopping malls, and in selected suburban and urban locations. As of January 30, 1999, Gymboree operated 564 stores. Under the GYMBOREE(R) brand name, we design and contract manufacture children's active-wear for sale exclusively by Gymboree. Our apparel is characterized by fashionable colors, charming prints, complex embroidery, comfort, functionality and durability. Gymboree also offers directed parent-child developmental play programs for children ages newborn to 4 years old at 398 franchised and Gymboree-operated locations.

Gymboree was organized in October, 1979, as a California corporation, and re-incorporated in Delaware in June, 1992.

This annual report on Form 10-K contains certain forward-looking statements reflecting Gymboree's current expectations. Our actual future performance may not meet such expectations. Factors that could cause future performance to vary from current expectations include, but are not limited to, the factors discussed in the "Business" section, and in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of the 1998 Annual Report to Stockholders incorporated by reference in this annual report on Form 10-K.

BUSINESS STRATEGY

Gymboree's business strategy consists of the following principal elements:

- HIGH QUALITY APPAREL. We strive to offer our customers high quality apparel with an excellent price/value relationship. We design the merchandise to be comfortable, functional, safe and durable by placing particular emphasis on high quality fabrics and detailed garment construction.
- BRAND NAME RECOGNITION. Gymboree has developed a clearly recognizable brand image through its distinctive design, merchandising and retailing. Customers associate Gymboree with high quality and appealing, colorful

children's clothing sold in an attractive and friendly environment.

- INTEGRATED OPERATIONS: DESIGN, CONTRACT PRODUCTION AND RETAILING. We believe that the vertical integration of our operations enables us to identify and respond to market trends, maintain rigorous product quality standards and closely monitor the distribution of our products.
- EXCLUSIVE DISTRIBUTION CHANNEL. Our products are sold exclusively through Gymboree retail stores and, to a limited extent, through our play program sites. During fiscal 1998, we continued to build the Gymboree Gift Center at [www.gymboree.com](http://www.gymboree.com) which began in 1997. This web site allows customers to purchase selected items.
- MERCHANDISE FOCUS. Gymboree apparel is designed, contract manufactured and merchandised by line. Merchandise is displayed in each Gymboree store in a manner designed to enhance visual appeal and maximize customer convenience by enabling customers to select among an assortment of coordinated apparel items, accessories and shoes. We offer a broad range of styles, themes and colors, as opposed to relying primarily on certain key items. To maintain the freshness of the merchandise, Gymboree introduces between 30 and 40 new lines of boy's, girl's and infant's apparel each year.
- RESPONSIVE CUSTOMER SERVICE. Customer service and satisfaction are defining features of the Gymboree corporate culture. Assisting customers in merchandise selection and outfit coordination is the top priority of Gymboree team members. We believe that this customer service in combination with our merchandise encourages multiple item purchases per customer.

#### STORE EXPANSION STRATEGY

Gymboree seeks to strategically increase our current store base by opening new stores in major metropolitan malls, certain secondary regional malls and in select downtown street locations that satisfy certain demographic and financial return criteria. In fiscal 1998, Gymboree opened 129 new stores and relocated and/or expanded 25 existing stores. Over the past year, the average size of new stores was approximately 1,700 square feet. We plan to open 40 to 50 new stores during fiscal 1999. As indicated in the table below Gymboree has achieved increasing geographic diversification within the United States in recent years. We have continued our international expansion by opening 4 additional retail stores in Canada and 18 additional stores in Europe during fiscal 1998. During fiscal 1999, we are planning to open approximately 4 to 5 stores in Europe and 3 to 5 stores in Canada. Our ability to continue to expand successfully in the future will depend on a number of factors, including the availability of suitable store locations, the negotiation of acceptable lease terms, our financial resources and the ability to control the operational aspects of this growth.

Gymboree expanded from 2 stores in California in 1986 to 525 stores in 50 states and the District of Columbia, 15 stores in Canada and 24 stores in Europe, as of January 30, 1999. The following table sets forth, by geographic region, the net number of stores opened and closed during each of the periods indicated:

	Fiscal Year								TOTAL
	PRIOR TO 1992	1992	1993	1994	1995	1996	1997	1998	
East	35	8	9	14	14	17	23	30	150
Midwest	7	10	9	12	19	25	10	24	116
South	6	9	10	23	26	12	29	39	154
West	32	5	12	8	11	16	7	14	105
Europe	0	0	0	0	0	0	6	18	24
Canada	0	0	0	0	0	5	6	4	15
TOTAL	80	32	40	57	70	75	81	129	564

SITE SELECTION. In selecting new store sites, Gymboree typically looks for high traffic locations ranging from 1,500 to 3,000 square feet in regional malls, specialty centers and suburban main street locations. Our real estate department conducts extensive analysis of potential store sites and bases its selection on the performance of other specialty retail tenants, size of the market and demographics of the surrounding area. In evaluating a store location, placement of the store relative to retail traffic patterns and the number of children in the trade area are important considerations. Although our current stores are located primarily in regional malls, we have opened stores in alternative locations. In addition, we plan to relocate some higher volume stores within the same malls where we anticipate receiving a competitive advantage. There can be no assurance that Gymboree will continue to be successful in either obtaining favorable sites for our new stores or negotiating favorable lease terms for such sites.

NEW STORE ECONOMICS. Gymboree's average cost for leasehold improvements, furniture and fixtures for stores opened in fiscal 1998 was approximately \$250,000 per store, before landlord construction allowances. In addition, working capital requirements on these same stores, consisting almost entirely of inventory purchases, averaged approximately \$60,000 per store. Average pre-opening costs per store, which are expensed as incurred, were \$17,000 during fiscal 1998. Gymboree stores have typically achieved profitability at the store operating level within their first six months of operation, although there can be no assurance that new stores will continue to achieve the same levels of profitability.

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#### PRODUCTS AND MERCHANDISING

Gymboree's merchandise has evolved significantly over time. Prior to 1988, Gymboree offered unisex apparel for children ages 6 months to 5 years and a selection of non-apparel products, including toys. Since 1989, we have broadened our apparel merchandise assortment by developing separate boy's and girl's lines, distinguishing assortments for appropriate ages: CradleGym(R) - newborn to 12 months; GymBaby(R) - newborn to 3 years and GymKids(R) - for children ages 3 to 7 years. Gymboree currently offers customers an assortment of high quality, comfortable, fully coordinated lines of GYMBOREE(R) brand apparel and accessories, consisting primarily of pants, tops, overalls, dresses, socks, hats, crib shoes, swimwear, sweaters, outerwear, underwear and shoes. Our merchandising strategy focuses upon the quality and design of the apparel products and planned introduction of new product lines. Gymboree strives to create a distinctive look for its merchandise to enhance brand recognition and stimulate repeat purchases. Gymboree apparel is designed, manufactured, purchased and merchandised by line on a seasonal basis.

Each of Gymboree's stores features 11 major merchandising lines per year. Each merchandise line generally consists of approximately 60 clothing items, encompassing matching tops and bottoms, with similar color palettes, patterns and designs. Additionally, each line features a wide selection of related accessories that complement the apparel, such as coordinated socks, hats, crib shoes and hair accessories. In order to maintain the freshness of its merchandise, Gymboree regularly updates the assortments by rotating each line on an 11- to 13-week selling cycle. Although Gymboree generally is unable to reorder items after a line has been purchased, we carefully monitor the rotation schedule, and we have the ability to move up the set-up of new lines based on selling demand. Merchandise in each line generally flows through a structured markdown process.

Gymboree's customized wall systems display each merchandise line as a separate coordinated group. This presentation maximizes customer convenience in selection, creates a visually attractive selling environment and assists team members in the process of wardrobing, which, we believe, stimulates multiple purchases of matching items. Boy's and girl's lines are generally displayed on opposite walls and accessories are located adjacent to the coordinated line. A typical store offers approximately 200 to 250 styles of apparel and approximately 100 to 120 accessories and other non-apparel items.

#### FASHION TRENDS AND CHANGING CONSUMER PREFERENCES

Gymboree's sales and profitability depend upon the continued demand by customers for our apparel and accessories. We believe that our success depends in large part upon our ability to anticipate, gauge and respond in a timely manner to changing consumer demands and fashion trends and upon the appeal of our products. There can be no assurance that the demand for Gymboree's apparel or accessories will not decline or that we will be able to anticipate, gauge and respond to changes in fashion trends. If demand for our apparel and accessories were to decline or if we were to misjudge fashion trends, Gymboree's business, financial condition and results of operations could be materially adversely affected.

#### DESIGN, SOURCING AND CONTRACT MANUFACTURING

Gymboree apparel is characterized by colorful and distinctive designs, quality fabrications and construction and an excellent price/value relationship. Gymboree sources soft, comfortable and durable fabrics. Our merchandising and design team creates unique color combinations and original patterns for these fabrics and emphasizes functional features such as grow cuffs, which allow for extended use of tops, pants and overalls as children grow.

Gymboree manages the production of apparel from the initial product concept, through color and pattern design, fabric development and testing, sample approval and testing and garment manufacturing. We believe that the vertical integration of operations and the coordinated efforts of our merchandising and design, production, and financial planning teams enable Gymboree to create distinctive offerings. The merchandising and design team determines the styles for merchandise based on an evaluation of current style trends as well as a review of the popularity of the prior year's products. This team works closely with Gymboree's financial planning team to select garment styles for each season. In conjunction with foreign buying agents, the production team arranges fabric sourcing and garment production while the quality team ensures that the final products satisfy Gymboree's detailed specifications and strict quality and safety standards. The process from initial product concept/design to receipt of finished product requires approximately 10 months. Fabric and production commitments are made approximately 6 months before receipt of the finished garments at our distribution center.

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Throughout the design process, Gymboree's financial planning team prepares financial plans for each line of clothing on an item-by-item basis. Certain proposed items in a line may be revised or replaced as a result of this team's financial analysis. This team also monitors inventories on a daily basis, prepares seasonal plans and develops unit production forecasts.

The majority of Gymboree apparel is manufactured to our specifications by approximately 150 independent manufacturers. Key countries in the Far East include China, Indonesia, Philippines, Thailand and Sri Lanka. Other manufacturing regions include Central America, Israel, Mexico and the United States. Gymboree sources its fabric from approximately 15 vendors. In fiscal 1998, our product assortment was approximately 65% knit and 35% woven. Gymboree purchases all products in U.S. dollars, and we have not historically experienced any material difficulties as a result of any foreign political, economic or social instabilities, although there can be no assurance that we will not experience such difficulties in the future. We have no long-term contracts with suppliers and typically transact business on an order-by-order basis.

Gymboree's quality control team arranges with independent testing laboratories to test fabrics prior to cutting against established performance standards for quality and safety. During the prototype sampling stage and following manufacturing, the technical teams subject the merchandise to tests which ensure that construction, workmanship and fit, as well as the style and appearance of the garments, satisfy Gymboree's stringent specifications. Subsequently, the production and quality control teams review the garment test and bulk production inspection results to verify that the quality is consistent with Gymboree's high standards. Gymboree generally does not purchase its finished apparel products until manufacturing has been completed and the products have been approved by independent testing labs and Gymboree's quality control and production teams.

#### DEPENDENCE ON NEW PRODUCTS

Gymboree's continued growth and success depend in large part on our ability to successfully develop and introduce new products that are perceived to represent an improvement in style, functionality or value compared to products available in the marketplace. Failure to regularly develop and introduce new products successfully could materially and adversely impact future growth and profitability. In addition, in 1999 Gymboree will introduce certain new products and concepts such as Zutopia, targeted for children ages 6 - 12, that represent a shift in concept, design and target market demographics from our traditional products. These new products may have shorter life cycles, thereby requiring more frequent product introductions than Gymboree's traditional product lines. Furthermore, these products and the introduction of more products could dilute Gymboree's image as a leading supplier of children's apparel in the newborn - 7 years age range and lead to a reduced demand for its existing products.

#### RELIANCE ON FOREIGN AND UNAFFILIATED MANUFACTURERS

Gymboree currently relies on unaffiliated manufacturers to produce substantially all of its products. Gymboree has no long-term contracts with its manufacturing sources, and we compete with other companies for production facilities and import quota capacity. Gymboree's products are currently manufactured to specifications by independent factories located primarily in the Far East, as well as Central America, Israel, Mexico and the United States. In the event any of our key manufacturers were unable or unwilling to continue to manufacture Gymboree's products, Gymboree would have to rely on other current manufacturing sources or identify and qualify new unaffiliated manufacturers. In such event, there can be no assurance that Gymboree would be able to qualify such manufacturers for existing or new products in a timely manner or that such manufacturers would allocate sufficient capacity to Gymboree in order to meet its requirements. Any significant delay in our ability to obtain adequate supplies of products from our current or alternative sources, would materially and adversely affect the business and results of operations. Although Gymboree believes that we have good relationships with our unaffiliated principal mills and manufacturing sources and we maintain good control with respect to product specifications and quality, our future success will depend in large measure upon our ability to maintain such relationships both directly and through our independent agents, and there can be no assurance that these manufacturers will continue to produce products that are consistent with Gymboree's standards. In this regard, Gymboree has occasionally received, and may in the future continue to receive, shipments of product from unaffiliated manufacturers that fail to conform to our quality control standards. In such event, unless we are able to obtain replacement products in a timely manner, Gymboree risks the loss of revenue resulting from the sale of such products and related increased administrative and shipping costs. The failure of any key unaffiliated manufacturer to supply products that conform to Gymboree's standards could materially and adversely affect our results of operations and our reputation in the marketplace.

Although Gymboree believes that we have good relationships with our principal manufacturing sources, our future success is substantially dependent upon our ability to maintain such relationships. If Gymboree experiences significant increased demand, which

cannot be assured, or if an existing unaffiliated manufacturer needs to be replaced, we will need to significantly expand manufacturing capacity, both from current and new manufacturing sources. There can be no assurance that such additional manufacturing capacity will be available when required on terms that are acceptable to Gymboree. In addition, in fiscal 1998, one vendor accounted for approximately 70% of our cotton knit fabric purchases. Although we believe that other sources could be identified to satisfy our requirements for cotton knit fabrics, the loss of this vendor, or a delay in obtaining fabric from this vendor, could have a material adverse effect on our business and operating results.

Gymboree's business is subject to the risks generally associated with doing business abroad, such as foreign governmental regulations, political unrest, disruptions or delays in shipments and changes in economic conditions in countries in which our vendor mills and manufacturing sources are located. Gymboree cannot predict the effect that such factors will have on our business arrangements with foreign mills and manufacturing sources. If any such factors were to render the conduct of business in a particular country undesirable or

impractical, or if our current foreign manufacturing sources or mills were to cease doing business with us for any reason, Gymboree's business and operating results could be adversely affected. Our business is also subject to the risks associated with the imposition of additional United States legislation and regulations relating to imported apparel products, including quotas, duties, taxes and other charges or restrictions on imported apparel. We cannot predict whether additional United States quotas, duties, taxes or other charges or restrictions will be imposed upon the importation of our products in the future, or what effect any such actions would have on our business, financial position and results of operations.

#### STORE OPERATIONS

The primary objective of store management is to maximize sales by providing superior customer service. Store management is principally responsible for sales training and implementing performance evaluation systems. In a continuing effort to minimize team members' time away from customers, operational procedures are reviewed and streamlined by the store operations team prior to implementation at the store level. This team is also responsible for field and store staffing, daily sales motivation and central office to store communications. Our merchandising team also interacts with store personnel and is responsible for developing merchandise presentation plans that can be effectively implemented at the store level.

Store operations are managed through 46 operating districts, divided into 6 geographic regions. Each District Team Leader is responsible for approximately 8 stores. Stores are typically staffed with a team leader, two assistant team leaders and several team members, which varies with store volume. During the holiday selling season, team member levels are substantially increased to accommodate peak traffic levels.

A number of Gymboree programs offer incentives to both team members and team leaders. Team members receive compensation primarily in the form of hourly wages. Incentive structures are designed to maximize team members' average sales transactions. Scheduling procedures allocate payroll hours to team members based upon sales performance rather than simple availability. Other programs provide bonuses or cash awards to high achieving team members during contest periods, or to all team members of a store based on store sales achievements. District Team Leaders and Regional Team Directors receive compensation in the form of salaries, performance-based bonuses and stock options.

#### CUSTOMER SERVICE

Customer service is a defining feature of the Gymboree corporate culture. We believe that knowledgeable and enthusiastic team members have a direct impact on profitability. Gymboree places great emphasis on the selling function through consistent and on-going training and evaluation systems which are initiated by the central office and administered by field management at all levels. Our store Managers, District Team Leaders and Regional Team Directors spend the majority of their work week on Gymboree selling floors, providing leadership by coaching the sales staff and assisting customers.

Customer service is a high priority for Gymboree store team members. Gymboree's customer focus is emphasized in recruiting and, as measured by sales, is the primary component in the on-going evaluation of team members. Gymboree minimizes team members' time spent on administrative functions by centrally determining merchandise display and replenishment, markdowns and basic labor scheduling. By emphasizing friendliness, product knowledge and personal attention, we believe that Gymboree has established a reputation for excellent customer service.

#### STORE ENVIRONMENT

Gymboree stores are designed to create an energetic and enjoyable shopping environment. The brightly lit stores and glass store fronts allow the colorful in-store environments to attract customers from the outside. Stores are constructed in an open manner which enables customers to see virtually all product offerings from the store's entrance.

Customers enter the stores under natural wood arches supported by giant

children's building blocks. The dramatic archways and Gymboree logo attract the customer's attention, even from a distance. Gymboree believes that the playful image created by our store fronts is carried into the stores and maintained through product presentation and enthusiastic store personnel.

Inside the store, merchandise is displayed on store walls by coordinated apparel lines, which allows easy accessibility and provides ample floor space for customers to maneuver strollers within the store. While parents shop, children are encouraged to play with small toys throughout the store and to enjoy Gymboree videos which run continuously throughout the day.

#### MARKETING AND PROMOTION

Whereas Gymboree previously relied on word of mouth advertising, in 1998 we continued development through strategic marketing of the Gymboree brand. An increased focus on synergy between the stores and Play Programs helped fuel more successful direct marketing, advertising and promotional efforts. Cross-promotional activities with other large strategically appropriate brands like Gruner and Jahr's Parents Magazine were also successfully executed.

#### ELECTRONIC COMMERCE

Gymboree launched its first web site at [www.gymboree.com](http://www.gymboree.com) during fiscal 1997. This web site, also known as the Gymboree Gift Center, is designed to assist customers as a one-stop shopping connection for Gymboree gift sets for children between the ages of newborn and 7 years old. During 1998, products were selectively added to the Gift Center. We will continue to develop our web presence for corporate identification and expansion of sales.

#### MERCHANDISE DISTRIBUTION

Gymboree's merchandise is shipped primarily via ocean carriers from foreign ports to the Port of Oakland, California, for distribution to U.S. stores, to Toronto, Ontario, for distribution to Canadian stores, and to Shannon, Ireland for our European stores. Contract manufacturers or vendors are required to complete manufacturing and deliver merchandise to our foreign consolidator within a designated ship window. This ship window ensures timely delivery of the product to Gymboree's U.S., Canadian and Irish distribution centers using cost-effective ocean transportation. A multi-country consolidation program was established in 1997 which enables us to bring full ocean containers into those countries, thereby minimizing shipping cost per unit.

Our transportation department coordinates the transportation of all purchase orders and monitors the timeliness of these shipments. Customs clearance takes place at the Port of Oakland for U.S. goods, Toronto for Canadian goods, and Shannon, Ireland for European goods. Samples of all items are reviewed by U.S. or local Customs agents prior to the actual shipment of merchandise. This process reduces the customs clearance time and speeds the delivery of the merchandise to Gymboree.

Our U.S. merchandise is received, checked, processed and distributed through the new U.S. distribution center in Dixon, California. This distribution center is a Gymboree-owned 300,000 square foot facility which opened on schedule in January, 1998. New lines are received at the distribution center "just in time." The merchandise is processed, packed by store and delivered on a targeted in-store date approximately once per month. Merchandise is then replenished on a weekly basis based on store sell-through. Merchandise for distribution to Europe is shipped directly from the factory to a 26,000 square foot leased facility in Shannon, Ireland, where it is processed for delivery to the stores. Merchandise destined for Canadian stores is shipped directly to a third-party distribution center in Toronto, Canada.

Outbound transportation is coordinated by our transportation team. Store orders are consolidated by region and shipped via truckload carriers into the downstream terminals of regional less-than-truckload carriers. This allows Gymboree to build full trailers, thereby reducing the delivery cost per unit.

#### MANAGEMENT INFORMATION SYSTEMS

Gymboree's information systems provide integration of store, merchandising,

distribution and financial systems. These systems operate on Unix and NT platforms. Sales and other inventory management information are updated daily in the merchandise reporting systems by communicating with each store's point-of-sale system. Merchandise is automatically replenished in response to the specific unit inventory requirements of each store. Gymboree evaluates information obtained through daily reporting to implement merchandising decisions regarding markdowns and allocation of merchandise.

Gymboree believes that our information systems are essential in achieving our growth plans and maintaining a competitive industry position. We are committed to utilizing technology as a competitive advantage.

YEAR 2000

The information required by this item is incorporated herein by reference to page 15 of the 1998 Annual Report to Stockholders filed as Exhibit 13.1 to this Annual Report on Form 10-K.

#### PLAY PROGRAMS

As of January 30, 1999, Gymboree's Play Programs included 18 Company-operated play centers in California and 380 franchisee-operated play centers, of which approximately 80% are located in the United States, and the remaining 20% are located in foreign countries, including Australia, Canada, Colombia, France, Indonesia, Korea, Mexico, Singapore and Taiwan. In addition to generating income, we believe that the Play Programs provide attractive cross-marketing opportunities for Gymboree stores and further strengthen the GYMBOREE(R) brand name recognition with retail customers. See "Marketing and Promotion."

The Gymboree Play Programs are designed to enhance early childhood development through fun-filled sensory and motor activities, which engage children through sight, touch, sound and movement. Motor skill development is stimulated through physical play and exercise in an exciting, safe environment which includes proprietary, colorful, developmentally appropriate play equipment. The Gymboree Play Program involves weekly 45-minute classes offered throughout the year. Classes are designed to interest and challenge children through activities that are tailored to enhance mental and physical development as well as to provide opportunities for socializing. In addition to sliding, climbing, jumping and running, classes include music, structured play activities, games and often a finale featuring a colorful parachute, songs, bubbles and GYMBO(R) the clown. Parents are present at play classes and participate in the activities with their children.

Gymboree classes are offered to children ages newborn to 4 years old. GymBabies (for ages newborn to 6 months) introduce sensory play with special props and equipment. GymCrawlers (6 to 12 months) develop upper-body stability, strength and coordination. GymWalkers (10 to 18 months) emphasize pre-walking and early walking skills and enhance strength, socialization, walking, balance and coordination. GymRunners (14 to 28 months) encourage exploration and build motor skills. GymExplorers (for 2 year olds) explore movement, stories, puppetry and songs. GymKids (3 year olds) learn non-competitive skills like catching, throwing, kicking and tumbling. GymPairs classes are designed for parents with two mobile children; activities are modified to serve the needs of each participant.

Gymboree's standard franchise agreement provides for an initial term of 10 years. Upon signing the franchise agreement, each domestic and Canadian franchisee currently pays an initial fee ranging from \$35,000 for the franchisee's first play center location to \$20,000 for the fourth (and each subsequent) location, and each international (excluding Canadian) franchisee pays an initial fee ranging from \$75,000 to \$500,000. The franchises are renewable for 1 additional 10-year term, and Gymboree receives no fee upon the renewal of the franchise from domestic franchisees. Gymboree receives a royalty of 6% of each domestic franchisee's gross receipts from operations, and a fee of approximately \$10,500 upon the transfer of a franchise from one domestic franchisee to another. Currently, Gymboree supplies the franchisees with program aids, equipment and consumer products at a cost to the franchisee and conducts initial and ongoing training programs.

Gymboree will continue offering franchises for sale in fiscal 1999.

## TRADEMARKS AND SERVICE MARKS

Gymboree is the owner in the United States of the trademark and service mark "GYMBOREE", and the trademarks "GYMBO" and "GYMBABY", among others. These marks and certain other of Gymboree's marks are registered in the United States Patent and Trademark Office, and the mark "GYMBOREE" is also registered, or is the subject of pending applications, in approximately 45 foreign countries. Each federal registration is renewable indefinitely if the mark is still in use at the time of renewal. Gymboree's rights in the "GYMBOREE" mark and other marks are a significant part of the business. Accordingly, we intend to maintain the mark and the related registrations. Gymboree is not aware of any material claims of infringement or other challenges to our right to use the mark in the United States.

Gymboree uses a number of trademarks, certain of which have been registered with the United States Patent and Trademark Office and in certain foreign countries. We believe that our registered and common law trademarks have significant value and that some of our trademarks are instrumental to our ability to create and sustain demand for and market our products. We believe that there are no currently pending material challenges to the use or registration of any of Gymboree's registered trademarks. There can be no assurance, however, that our trademarks do not or will not violate the proprietary rights of others, that they would be upheld if challenged or that Gymboree would, in such an event, not be prevented from using our trademarks, any of which could have a material adverse effect on Gymboree and the business. In addition, we could incur substantial costs to defend legal actions taken against Gymboree relating to our use of trademarks, which could have a material adverse effect on our results of operations and financial position.

From time to time, Gymboree discovers products in the marketplace that are counterfeit reproductions of our products or that otherwise infringe upon trademark rights held by Gymboree. If Gymboree is unsuccessful in challenging a third party's products on the basis of trademark infringement, continued sales of such product by that or any other third party could adversely impact the Gymboree brand, result in the shift of consumer preferences away from Gymboree and generally have a material adverse effect on our results of operations and financial condition.

## COMPETITION

The children's apparel segment of the specialty retail business is highly competitive. Gymboree competes on a national level with GapKids (a division of The Gap, Inc.) and certain leading department stores as well as certain discount retail chains such as Kids 'R' Us (a division of Toys 'R' Us, Inc.). Gymboree also competes with a wide variety of local and regional specialty stores and with certain other retail chains. Many of these competitors are larger and have substantially greater financial, marketing and other resources than Gymboree. Increased competition may reduce sales and gross margins, increase operating expenses and decrease profit margins. We may not be able to compete successfully in the future.

## ECONOMIC CONDITIONS; DEPENDENCE ON CONSUMER SPENDING

Gymboree's financial performance is also sensitive to changes in overall economic conditions, which have an impact on consumer spending trends. The success of our operations depends upon a number of factors relating to consumer spending, including future economic conditions affecting disposable consumer income such as employment, business conditions, interest rates and tax rates. There can be no assurance that consumer spending will not decline in response to economic conditions, thereby adversely affecting our growth, net sales and profitability. Gymboree's stores are located primarily in enclosed regional malls. Consequently, our ability to sustain the level of sales is dependent in part on a high volume of mall traffic. Mall traffic may be adversely affected by, among other things, economic downturns, the closing of anchor department stores or changes in consumer preferences, all of which are beyond our control. Shifts in consumer discretionary spending to other products or a general reduction in the level of such spending could also adversely affect Gymboree. These factors may adversely impact our business, financial position and results of operations in the future.

## DEPENDENCE ON KEY PERSONNEL; NEW MANAGEMENT

In the past year, we have made significant changes in our executive officers and management team. These new senior personnel, among others, have extensive

national retail and wholesale experience and have effected certain product development, merchandising, marketing and operational strategy changes. There can be no assurance that Gymboree will successfully assimilate these new executives and make strategic modifications to certain of its past operating policies in a timely and efficient manner. Furthermore, the

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continued success of Gymboree is largely dependent on the personal efforts and abilities of our senior management and certain other key personnel and on our ability to retain current management and to attract and retain qualified personnel in the future. The loss of certain key employees or Gymboree's inability to retain other qualified employees could have a material adverse effect on the results of operations and financial position.

#### NEED FOR ADDITIONAL CAPITAL

Various elements of our business and growth strategies, including plans to broaden existing product lines and introduce new products and concepts, such as Zutopia, which may require us to maintain higher inventory levels which could require additional capital. There can be no assurance that funds will be available to Gymboree on terms that are satisfactory. To the extent that we raise additional equity capital, a dilutive effect on existing stockholders could result.

#### TEAM MEMBERS

As of January 30, 1999, Gymboree had over 6,500 team members. In addition, a significant number of seasonal team members are hired during each holiday selling season. None of our team members is represented by a labor union, and we believe that our relationship with our team members is good.

#### EXECUTIVE OFFICERS

The following table sets forth information regarding our executive officers.

Stuart G. Moldaw	71	Chairman of the Board of Directors
Gary White	46	Chief Executive Officer and Vice-Chair of the Board of Directors
Melanie Bordeaux Cox	39	President
Lawrence H. Meyer	46	Senior Vice President and Chief Financial Officer
Edward Loseman	48	Senior Vice President, Sourcing and Logistics
Kenneth F. Meyers	36	Senior Vice President, Human Resources

Stuart G. Moldaw has been our Chairman of the Board of Directors since January 1994, and has been a director of Gymboree since May 1982. Mr. Moldaw previously served as Chairman of the Board of Directors of Gymboree from January 1990 through January 1993. From 1980 to 1990, Mr. Moldaw served as a general partner of U.S. Venture Partners. From 1987 through 1988, Mr. Moldaw served as Chief Executive Officer of Ross Stores, Inc., an off-price retailer, and is currently a director and Chairman Emeritus of Ross Stores, Inc.

Gary White has been our Vice-Chair of the Board of Directors and Chief Executive Officer since February 1999, and was Chief Executive Officer and President and a director beginning in February 1997. Mr. White served as a Senior Vice President and the Chief Operating Officer of Gymboree from January 1996 until February 1997. Prior to joining Gymboree, Mr. White served as Executive Vice President of Mervyn's, a division of Dayton Hudson Corporation. Mr. White was employed by Dayton Hudson Corporation since 1976 having served in various positions as an officer with Dayton Hudson Corporation from 1988 to 1996.

Melanie Bordeaux Cox joined Gymboree as President in March 1999. Prior to joining, she was General Merchandise Manager of Urban Outfitters, Inc. since 1995. Before that, Ms. Cox was Executive Vice President, General Merchandise Manager, of Contempo Casuals from 1994 to 1995, General Merchandise Manager of Clothetime Stores, Inc. from 1990 to 1994, and prior to 1990 was Merchandise Manager of Product Development of The Wet Seal, Inc.

Lawrence H. Meyer joined Gymboree as Senior Vice President and Chief Financial Officer in September 1998. Previously, Mr. Meyer was Chief Financial Officer and later was Vice President, Business Development, of Toys "R" Us International, from 1991 to 1998. Before that, Mr. Meyer was Vice President and Chief Financial Officer of Nielsen Marketing Research from 1989 to 1991, and held several financial positions with PepsiCo, Inc. from 1978 to 1989.

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Mr. Edward A. Loseman joined Gymboree as Senior Vice President of Sourcing and Logistics in January 1998. Prior to joining Gymboree, Mr. Loseman was Vice President of Sourcing for GUESS? Inc. from 1996, and Vice President of Manufacturing Services for Polo/Ralph Lauren from 1992 to 1996.

Mr. Kenneth F. Meyers joined Gymboree as Senior Vice President, Human Resources in March, 1997. Previously, Mr. Meyers was Vice President, Human Resources at Walt Disney Imagineering from 1995 to 1997. Prior to Disney, Mr. Meyers held executive positions in human resources at United Technologies Corporation.

#### ITEM 2. PROPERTIES

As of January 1999, Gymboree's corporate campus is located in 3 office buildings in Burlingame, California, which we occupy under leases expiring between 1999 and 2003.

During 1997, we completed construction of a new 300,000 square foot distribution center on 15 acres located in Dixon, California. Gymboree has an option agreement on contiguous land for an additional 6 acres. Beginning in January, 1998, we started distributing all products to our stores located in the United States from this facility. Gymboree leases a distribution center in Shannon, Ireland for European operations, and utilizes a third-party owned and operated distribution center in Toronto, Ontario, Canada for Canadian operations.

At January 30, 1999, Gymboree's 564 stores included an aggregate of approximately 939,000 square feet of space. Our stores are all leased, typically for a 10-year term. In most cases, Gymboree pays a minimum rent plus a percentage rent based on the store's net sales in excess of a certain threshold. Substantially all of the leases require us to pay insurance, utilities, real estate taxes and repair and maintenance expenses. See Note 2 of Notes to Consolidated Financial Statements.

#### ITEM 3. LEGAL PROCEEDINGS

Gymboree has been named as a defendant in two lawsuits relating to sourcing of products from Saipan (Commonwealth of Northern Mariana Islands). A complaint was filed on January 13, 1999 in California Superior Court in San Francisco by the Union of Needletrades Industrial and Textile Employees, AFL-CIO; Global Exchange; Sweatshop Watch; and Asian Law Caucus against Gymboree and 17 other parties. The plaintiffs allege violations of California's unlawful, fraudulent and unfair business practices and untrue and misleading advertising statutes in connection with labeling of product and labor practices regarding workers of factories that make product for Gymboree in Saipan. The plaintiffs seek injunctive relief, restitution, disgorgement of profits and other damages. On March 29, 1999, Gymboree, along with other defendants, filed a demurrer in California Superior Court in San Francisco, seeking dismissal of the complaint.

A second complaint was filed on January 13, 1999 in Federal District Court, Central District of California, by various unidentified worker plaintiffs against Gymboree and 25 other parties. Those unidentified worker plaintiffs seek class-action status and allege, among other things, that Gymboree (and other defendants) violated the Racketeer Influenced and Corrupt Organizations Act in connection with the labor practices and treatment of workers of factories in Saipan that make product for us. The plaintiffs seek injunctive relief as well as actual and punitive damages. On March 29, 1999, Gymboree, along with several other defendants, filed a motion in Federal District Court, Central District of California, to transfer the venue of the case to the Commonwealth of the Northern Mariana Islands. Additionally, on April 12, 1999, Gymboree, along with several other defendants, filed a motion to dismiss the federal complaint.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On February 8, 1999 a Special Meeting of stockholders was held to vote upon a proposal to approve Gymboree's Amended and Restated 1993 Stock Option Plan (the "Plan"). Specifically, the Plan was amended to:

- (a) increase the aggregate number of shares of Common Stock authorized for issuance under the Plan by 2,000,000 shares raising the number of shares reserved under the plan since its inception to 6,025,000;
- (b) impose annual limits on the number of shares subject to stock option grants, so as to qualify the compensation associated with such grants as "performance-based" compensation within the meaning of Section 162(m) of the Internal Revenue Code;
- (c) impose an annual maximum limit of 200,000 shares that may be issued pursuant to Stock Purchase Rights;
- (d) impose a minimum 3 year vesting schedule for all Stock Purchase Rights;
- (e) remove language from the 1993 Plan that contemplated option re-pricings and exchanges.

The number of votes cast for the proposal was 11,885,691, the number of votes cast against the proposal was 6, 289,356, and the number of abstentions and broker non-votes was 117,519. The proposal was approved and the Plan was adopted.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Gymboree's Common Stock is traded on the NASDAQ National Market System under the symbol "GYMB". The following table sets forth the quarterly high and low sale prices per share, as reported on the NASDAQ National Market System.

	FISCAL 1998		FISCAL 1997		FISCAL 1996	
	HIGH	LOW	HIGH	LOW	HIGH	LOW
First Quarter	23.375	18.250	27.250	21.750	29.000	17.750
Second Quarter	19.031	12.000	27.625	22.625	35.750	20.125
Third Quarter	10.500	4.063	27.750	23.875	33.675	23.375
Fourth Quarter	8.500	4.875	28.875	23.875	34.750	21.250

As of April 5, 1999, the number of holders of record of Gymboree's Common Stock was approximately 764. Gymboree has never declared or paid cash dividends on its Common Stock and anticipates that all future earnings will be retained for development of its business. The payment of any future dividends will be at the discretion of Gymboree's Board of Directors and will depend upon, among other things, future earnings, capital requirements, our financial position and general business conditions.

As of January 30, 1999, 1,111,909 shares of Common Stock had been issued upon exercise of options and pursuant to restricted stock purchase agreements, and 2,842,996 shares of Common stock were issuable upon exercise of outstanding options under Gymboree's Amended and Restated 1993 Stock Option Plan.

## ITEM 6. SELECTED FINANCIAL DATA

The information required by this item is incorporated herein by reference to page 11 of the 1998 Annual Report to Stockholders filed as Exhibit 13.1 to this Annual Report on Form 10-K.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The information required by this item is incorporated herein by reference to pages 12 through 15 of the 1998 Annual Report to Stockholders filed as Exhibit 13.1 to this Annual Report on Form 10-K.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information required by this item is incorporated herein by reference to page 14 of the 1998 Annual Report to Stockholders filed as Exhibit 13.1 to this Annual Report on Form 10-K.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The information required by this item is incorporated herein by reference to pages 16 through 27 of the 1998 Annual Report to Stockholders filed as Exhibit 13.1 to this Annual Report on Form 10-K.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

None.

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PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required by this item is incorporated herein by reference to the sections entitled "Election of Directors - Nominees" and "Additional Information-Compliance with Section 16(a) of the Securities Exchange Act" in the 1998 Proxy Statement. See also Item 1.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this item is incorporated herein by reference to the sections entitled "Election of Directors - Compensation of Directors" and "Additional Information - Executive Compensation" in the 1998 Proxy Statement.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required by this item is incorporated herein by reference to the section entitled "Additional Information - Security Ownership" in the 1998 Proxy Statement.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this item is incorporated herein by reference to the sections entitled "Additional Information - Employment Contracts and Termination of Employment and Change-in-Control Arrangements" and "Additional Information - Compensation Committee Interlocks and Insider Participation" in the 1998 Proxy Statement.

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PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENTS, AND REPORTS ON FORM 8-K

(A) (1) FINANCIAL STATEMENTS

The following documents are incorporated by reference to pages 16 through 27 of the 1998 Annual Report to Stockholders filed as Exhibit 13.1 to this Annual Report on Form 10-K.

Consolidated Balance Sheets as of January 30, 1999 and January 31, 1998

Consolidated Statements of Income for each of the three fiscal years ended January 30, 1999

Consolidated Statements of Cash Flows for the three fiscal years ended January 30, 1999

Consolidated Statements of Stockholders' Equity for the three fiscal years ended January 30, 1999

Notes to Consolidated Financial Statements

Independent Auditors' Report

(A) (2) FINANCIAL STATEMENT SCHEDULES

Financial statement schedules have been omitted because they are not required or are not applicable.

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(A) (3) EXHIBITS

EXHIBIT NUMBER -----	DESCRIPTION -----
3.1	Restated Certificate of Incorporation of Registrant.(1)
3.2	Bylaws of Registrant.(1)
4.1	Article III of Restated Certificate of Incorporation of Registrant (See Exhibits 3.1). (1)
4.2	Form of certificate for Common Stock. (1)
10.1	1983 Incentive Stock Option Plan, with form of stock Option Agreement. (1)
10.2	1993 Stock Option Plan, with form of Stock Option Agreement.(4)
10.3	1993 Employee Stock Purchase Plan. (1)
10.4	Amended Line of Credit Agreement with Bank of America dated October 27, 1995. (3)
10.5	Line of Credit Agreement with CoreStates Bank dated August 2, 1994.(2)
10.6	Amended Lease Agreement for 700 Airport Blvd., Suite 200, Burlingame, California. (2)
10.7	Amended Lease Agreement for distribution center. (3)
10.8	California Uniform Franchise Offering Circular, including form of Franchise Agreement.(1)
10.11	Restricted Stock Purchase Agreement with Nancy J. Pedot. (2)
10.12	Lease Agreement for 770 Airport Blvd., Burlingame, CA. (5)

- 10.13 Deferred Compensation Agreement. (5)
- 10.14 Lease Agreement for Bays 140-141, Shannon Free Zone, Shannon, Ireland, dated May 6, 1997. (6)
- 10.15 Lease Agreement for 111 Anza Blvd., Burlingame, CA dated January 8, 1998. (6)
- 10.16 Amendment No. 1 to the Amended and Restated Line of Credit Agreement with Bank of America, dated July 17, 1997. (6)
- 10.17 Amendment No. 2 to the Amended and Restated Line of Credit Agreement with Bank of America, dated August 11, 1997. (6)
- 10.18 Amendment No. 3 to the Amended and Restated Line of Credit Agreement and Waiver with Bank of America, dated January 9, 1998. (6)
- 10.19 Amendment No. 4 to the Amended and Restated Line of Credit Agreement with Bank of America, dated January 30, 1998. (6)

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- 10.20 Amendment No. 5 to the Amended and Restated Line of Credit Agreement with Bank of America, dated March 9, 1998. (6)
- 10.21 Amendment No. 6 to Amended and Restated Line of Credit Agreement with Bank of America, dated March 9, 1998. (6)
- 10.22 Acquisition and Development Agreement for Dixon, California Distribution Facility with Carl D. Panattoni and Wickland Properties, dated November, 1996. (6)
- 10.23 Standard Form of Contractor Agreement with DPR Construction, Inc. for construction of Dixon, California Distribution Facility dated May 5, 1997. (6)
- 10.24 Amendment No. 7 to the Amended and Restated Line of Credit Agreement with Bank of America, dated June 26, 1998. (7)
- 10.25 Amendment No. 8 to the Amended and Restated Line of Credit Agreement with Bank of America, dated August 14, 1998. (7)
- 10.26 Management Change of Control Plan. (8)
- 10.27 Management Severance Plan. (8)
- 10.28 Term Loan and Security Agreement with Transamerica Equipment Financial Services, Inc., dated December 28, 1998.
- 10.29 Commitment Letter for the Amended and Restated Line of Credit Agreement with Bank of America, dated March 11, 1999.
- 10.30 Amended 1993 Stock Option Plan, with form of Stock Option Agreement, dated March 8, 1999. (9)
- 11.1 Statement re Computation of Income Per Share.
- 13.1 1998 Annual Report to Stockholders.
- 21.1 Subsidiaries of the Registrant.
- 23.1 Independent Auditors' Consent.
- 24.1 Power of Attorney (included in Part IV of this Form 10-K under the caption "Signatures").
- 27.1 Financial Data Schedule.

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(B) REPORTS ON FORM 8-K

None.

- (1) Incorporated by reference to the Registrant's Registration Statement on Form S-1 filed with the Commission on February 18, 1993 (File No. 33-58322), as amended.
- (2) Incorporated by reference to the Registrant's 1994 Annual Report on Form 10-K filed with the Commission on April 24, 1995.
- (3) Incorporated by reference to the Registrant's 1995 Annual Report on Form 10-K filed with the Commission on May 2, 1996.
- (4) Incorporated by reference to the Registrant's Registration Statement on Form S-1 filed with the Commission on February 18, 1993 (File No. 33-58322), as amended by numbers 33-60310, 33-90452, 33-94594 and 333-10811.
- (5) Incorporated by reference to the Registrant's 1996 Annual Report on Form 10-K filed with the Commission on May 5, 1997.
- (6) Incorporated by reference to the Registrant's 1997 Annual Report on Form 10-K filed with the Commission on April 20, 1998.
- (7) Incorporated by reference to the Registrant's August 1, 1998 Quarterly Report on Form 10-Q ("1998 Q2 10-Q") filed with the Commission on September 11, 1998.
- (8) Incorporated by reference to the Registrant's October 31, 1998 Quarterly Report on Form 10-Q ("1998 Q3 10-Q") filed with the Commission on December 21, 1998.
- (9) Incorporated by reference to the Registrant's Registration Statement on Form S-8 filed with the Commission on March 11, 1999 (File No. 333-74269).

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THE GYMBOREE CORPORATION

SIGNATURES

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

THE GYMBOREE CORPORATION

April 26, 1999

By: /s/ Gary White

(Date)

Gary White  
Vice-Chair,  
Chief Executive Officer  
and Director

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENT:

That the undersigned officers and directors of Gymboree Corporation, a Delaware corporation, do hereby constitute and appoint Gary White the lawful attorney and agent, with power and authority to do any and all acts and things and to execute any and all instruments which said attorney and agent determine may be necessary or advisable or required to enable said corporation to comply with the Securities Act, and any rules or regulations or requirements of the Securities and Exchange Commission in connection with this Form 10-K. Without limiting the generality of the foregoing power and authority, the powers granted include the power and authority to sign the names of the undersigned officers and directors in the capacities indicated below to this Form 10-K, to any and all amendments, and supplements to this Form 10-K, to any and all instruments or documents filed as part of or in conjunction with this Form 10-K or amendments or supplements thereof, and each of the undersigned hereby ratifies and confirms all that said attorney and agent shall do or cause to be done by virtue hereof. This Power of Attorney may be signed in several counterparts.

IN WITNESS WHEREOF, each of the undersigned has executed this Power of Attorney as of the date indicated.

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Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

NAME -----	TITLE -----	DATE -----
/s/ Stuart G. Moldaw ----- Stuart G. Moldaw	Chairman of the Board of Directors	April 26, 1999
/s/ Gary White ----- Gary White	Vice Chair, Chief Executive Officer and Director	April 26, 1999
/s/ Melanie B. Cox ----- Melanie B. Cox	President	April 26, 1999
/s/ Lawrence H. Meyer ----- Lawrence H. Meyer	Senior Vice President and Chief Financial Officer (Principal financial and accounting officer of the registrant)	April 26, 1999
/s/ Walter F. Loeb ----- Walter F. Loeb	Director	April 26, 1999
/s/ Barbara L. Rambo ----- Barbara L. Rambo	Director	April 26, 1999
/s/ Deborah A. Sorondo ----- Deborah A. Sorondo	Director	April 26, 1999
/s/ William U. Westerfield ----- William U. Westerfield	Director	April 26, 1999
/s/ Carole J. Whitacre ----- Carole J. Whitacre	Director	April 26, 1999

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THE GYMBOREE CORPORATION

EXHIBIT INDEX

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TERM LOAN AND SECURITY AGREEMENT

AMONG

THE GYMBOREE CORPORATION  
AND  
GYMBOREE MANUFACTURING, INC.,  
AS GUARANTORS

GYMBOREE LOGISTICS PARTNERSHIP,  
AS BORROWER

AND

TRANSAMERICA BUSINESS CREDIT CORPORATION,  
AS LENDER

CLOSING DATE: DECEMBER 28, 1998

AGGREGATE PRINCIPAL AMOUNT: \$12,000,000

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TERM LOAN AND SECURITY AGREEMENT

THIS TERM LOAN AND SECURITY AGREEMENT, made, entered into and effective as of the Closing Date (defined below), by and among THE GYMBOREE CORPORATION, a Delaware corporation ("Guarantor One"), GYMBOREE MANUFACTURING, INC., a California corporation ("Guarantor Two"; Guarantor One and Guarantor Two each, individually, a "Guarantor" and, collectively, the "Guarantors"), GYMBOREE LOGISTICS PARTNERSHIP, a California general partnership ("Borrower"), and TRANSAMERICA BUSINESS CREDIT CORPORATION, a Delaware corporation ("Lender");

W I T N E S S E T H :

WHEREAS, Borrower has applied to Lender for financing, in the form of two term loans, described more particularly below, to be secured by liens on, and security interests in, certain real property, machinery and equipment of Borrower and Guarantors, as likewise described more particularly below;

WHEREAS, the making of such term loans by Lender to Borrower will inure to the direct and material benefit of Guarantor One as the owner, directly or indirectly, of all of the equity interests in Borrower, and to Guarantor Two as an affiliate of Guarantor One and Borrower who conducts its business as a common enterprise with Guarantor One and Borrower, and, to induce Lender to make such term loans to Borrower, Guarantors are willing to guaranty Borrower's payment and performance of its obligations to Lender; and

WHEREAS, Lender has considered Borrower's request for such financing and is willing to extend such financing to Borrower for such purposes in accordance with the terms of this Agreement upon the execution of this Agreement by Borrower and Guarantors and, compliance by Borrower and Guarantors with all of the terms and provisions of this Agreement and fulfillment by Borrower and Guarantors of all conditions precedent to Lender's obligations herein contained;

NOW, THEREFORE, in consideration of the foregoing premises, to induce Lender to extend the financing provided for herein, and for other good and valuable consideration, the sufficiency and receipt of all of which are acknowledged by Guarantors and Borrower, Lender, Guarantors and Borrower agree as follows:

1. DEFINITIONS, TERMS AND REFERENCES.

1.1. CERTAIN DEFINITIONS. In addition to such other terms as are elsewhere defined herein, as used in this Agreement and in any Exhibits, the following terms shall have the following meanings, unless the context requires otherwise:

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"Agreement" shall mean this Term Loan and Security Agreement, as amended

or supplemented from time to time.

"Applicable Rate" shall mean the Fixed Rate or the Default Rate, as made applicable to each Term Loan pursuant to Section 2.3 hereof.

"Authorized Officer" shall mean (i) for Borrower, any partner and (ii) for each Guarantor, any officer, in each case authorized to execute the Loan Documents on behalf of such entity.

"Bankruptcy Code" shall mean Title 11 of the United States Code, as amended from time to time.

"Borrower" shall have the meaning ascribed thereto in the initial recitals to this Agreement.

"Business Day" shall mean a day on which Lender is open for the conduct of business at its offices in Atlanta, Georgia and Chicago, Illinois.

"Closing Date" shall mean the date of this Agreement, as specified on the cover page of this Agreement.

"Collateral" shall mean, collectively, the Equipment Collateral, the Real Estate Collateral and any and all other property of Borrower and each Guarantor described in Article 3, or any part thereof, or elsewhere herein or in any Loan Document, all as the context shall require, in which Lender has, or is to have, or hereafter may obtain, a security interest, lien or encumbrance pursuant thereto, as security for payment of the Obligations.

"Compliance Certificate" shall mean a certificate of each Guarantor and Borrower executed by Authorized Officers of each Guarantor and Borrower, on each Guarantor's and Borrower's behalf, stating that no Event of Default or Default Condition has occurred or exists, or if an Event of Default or Default Condition has occurred or exists, specifying the nature and period of existence thereof and what action Guarantors and Borrower have taken or propose to take with respect thereto.

"Contaminant" shall mean those substances which are regulated by or form the basis of liability under federal, state or local environmental, health and safety statutes or regulations including, without limitation, asbestos, polychlorinated biphenyls ("PCBs"), radioactive substances, petroleum, petroleum products, or any other material or substance which constitutes a material health, safety or environmental hazard to any Person or Property.

"Default Condition" shall mean the occurrence of any event which, after satisfaction of any requirement for the giving of notice or the lapse of time, or both, would become an Event of Default.

"Default Rate" shall mean, as to each Term Loan, that simple interest rate equal to four percent (4%) per annum in excess of the Fixed Rate applicable to such Term Loan.

"Distribution Center" shall mean the warehouse and distribution center located at 2299 Kids Way, Dixon, California owned by Borrower and leased by it to Guarantor Two pursuant to the Intercompany Lease.

"Environmental Claim" shall mean any notice of violation, claim, suit, demand, abatement or other order or direction (conditional or otherwise) by any Governmental Authority or any Person for personal injury (including sickness, disease or death), tangible or intangible property damage, damage to the environment, nuisance, pollution, contamination or other adverse effects on the environment, or for fines, penalties or restrictions, resulting from or based upon (i) the existence, or the continuation of the existence, of a Release (including, without limitation, sudden or non-sudden, accidental or non-accidental Releases) of, or exposure to, any Contaminant, odor or audible noise or other release or emission in, into or onto the environment (including, without limitation, the air, ground, surface water, groundwater or any surface) in, by, from, or related to any Property, (ii) the environmental aspects of the transportation, storage, treatment or disposal of materials, in connection with

the operation of any Property or (iii) the violation, or alleged violation, of any statutes, ordinances, orders, rules, regulations, Permits, licenses, registrations or approvals of or from any Governmental Authority relating to environmental matters connected with any Property.

"Environmental Laws" shall mean all laws, whether domestic or foreign, or federal, state, provincial or local, relating to the environmental, safety, health and the regulation of Contaminants, including, without limitation, the Comprehensive Environmental Response, Compensation, and Liability Act (42 U.S.C. Section 9601 et seq.), the Superfund Amendments and Reauthorization Act of 1986, Public Law No. 99-499, 100 Stat. 163, the Hazardous Material Transportation Act (49 U.S.C. Section 1801 et seq.), the Resource Conservation and Recovery Act (42 U.S.C. Section 6901 et seq.), the Clean Water Act (33 U.S.C. Section 1251 et seq.), the Clean Air Act (42 U.S.C. Section 7401 et seq.), the Toxic Substances Control Act, as amended (15 U.S.C. Section 2601 et seq.), the Federal Insecticide, Fungicide, and Rodenticide Act (7 U.S.C. Section 136 et seq.), the Occupational Safety and Health Act (29 U.S.C. Section 651 et seq.), as such laws have been and hereafter may be amended or supplemented, and any analogous future federal, or present or future domestic or foreign state, provincial or local laws and all rules and regulations promulgated pursuant thereto.

"Equipment Collateral" shall mean all equipment, machinery, furniture, furnishings and fixtures of Borrower and each Guarantor, at any time or from time to time located at, or used or useful in the operation of, the Distribution Center, together with any and all extensions, additions, improvements, betterments, after-acquired property, renewals, replacements and substitutions or proceeds from a voluntary or involuntary sale, liquidation or conversion of any of the foregoing; and all attachments, additions and accessions thereto, and any and all tools, repair parts and spare parts therefor; all whether now or hereafter existing.

"Event of Default" shall mean any of the events or conditions described in Article 6, provided that any requirement for the giving of notice or the lapse of time, or both, has been satisfied.

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"Fixed Rate," as of the Closing Date shall mean that interest rate determined by Lender to be equal to (i) the then prevailing yield to maturity of a U.S. Treasury Note having a term comparable to the term of the Term Note in question, as published in the "Treasury Notes, Bonds and Bills" section of The Wall Street Journal on or as of that date closest (but prior) to the Closing Date; plus (ii) three percent (3%) per annum.

"GAAP" shall mean generally accepted accounting principles which are (a) consistent with the principles promulgated or adopted by the Financial Accounting Standards Board and its predecessors as in effect from time to time, (b) such that a certified public accountant would, insofar as the use of accounting principles is pertinent, be in a position to deliver an unqualified opinion as to financial statements in which such principles have been properly applied and (c) applied on a basis consistent with prior periods.

"Governmental Authority" shall mean any nation or government, federal, state, provincial, city, town, municipality, county, local or political subdivision thereof or thereto and any department, commission, instrumentality or agency exercising executive, legislative, judicial, regulatory or administrative functions on behalf thereof.

"Guarantor" and "Guarantors" shall have the meanings ascribed thereto in the initial recitals to this Agreement.

"Guarantor One" shall have the meaning ascribed thereto in the initial recitals to this Agreement.

"Guarantor Two" shall have the meaning ascribed thereto in the initial recitals to this Agreement.

"Headquarters" shall mean the principal place of business and chief executive office of Guarantors and Borrower, and the office where all books and records of Guarantors and Borrower are maintained, being 700 Airport Boulevard, Suite 200, Burlingame, California 94010-1912, together with any successor principal place of business and chief executive office as to which Guarantors

and Borrower have complied with the provisions of Section 3.1(h).

"Independent Accountants" shall mean any firm of independent certified public accountants selected by Guarantor and reasonably acceptable to Lender.

"Intercompany Lease" that certain lease agreement, dated as of July 15, 1997, pursuant to which Borrower leases the Distribution Center and the Equipment Collateral to Guarantor Two, as amended or modified from time to time.

"Lender" shall have the meaning ascribed thereto in the initial recitals to this Agreement. The term "Lender" shall also include any Participant to whom Lender shall assign, in whole or in part, its right, title and interest in and to the Obligations hereunder on or subsequent to the Closing Date.

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"Loan Documents" shall mean this Agreement, each Term Note, the Mortgage, each financing statement, and each and every other document, instrument, certificate and agreement executed and/or delivered by Borrower or either Guarantor in connection herewith, or any one, more, or all of the foregoing, all as the context shall require.

"Material Adverse Change" shall mean (a) any change occurring in the business, operations, properties or condition (financial or otherwise) of Borrower or either Guarantor, which materially and adversely affects (i) the ability of Borrower or such Guarantor to own or operate all, or any material portion of, its assets or conduct its business as a going concern, (ii) the collateral value to Lender of the whole of, or any material portion of, any Collateral, or (iii) the ability of Borrower to pay the Obligations as and when due and payable or otherwise perform its obligations hereunder or under the other Loan Documents; or (iv) the ability of either Guarantor to perform its obligations to Lender under its guaranty of the Obligations set forth in Section 2.10 hereof or to otherwise perform its obligations hereunder or under the other Loan Documents; or (b) the failure or inability of Borrower or either Guarantor to pay or perform its obligations to its creditors generally.

"Material Adverse Effect" shall mean an effect that has resulted in, will result in, or is reasonably likely to result in, a Material Adverse Change.

"Material Agreements," in respect of Borrower and each Guarantor, shall mean all loan and other debt instruments and agreements; all management, employment and labor agreements; all real property leases; and any other agreements, not specified hereinabove, the loss, diminution or impairment of which would have, or would reasonably be expected to have, a Material Adverse Effect; in each case, to the extent such instruments or agreements are binding on Borrower or either Guarantor or any of their respective Property.

"Mortgage" shall mean each mortgage, deed of trust or similar instrument pursuant to which Lender shall obtain a mortgage lien, security interest or security title on or in the right, title and interest of Borrower in and to the Distribution Center.

"Obligations" shall mean and include any and all indebtedness, liabilities and obligations of Borrower or either Guarantor, and each of them, jointly and severally, to Lender arising hereunder or as a result hereof, whether evidenced by the Term Notes or otherwise, and any and all extensions or renewals thereof in whole or in part; together with any and all other indebtedness, liabilities and obligations of Borrower or either Guarantor, and each of them, jointly and severally, to Lender, whether existing as of the date hereof or hereafter arising, existing or incurred, whether under a loan, lease, line of credit, letter of credit or other type of financing, whether direct, indirect, absolute or contingent, as maker, endorser, guarantor, surety or otherwise, and whether evidenced by, arising out of, or relating to, a promissory note, bill of exchange, check, draft, bond, letter of credit, guaranty agreement or otherwise issued in favor of, or acquired by, Lender.

"Participant" shall mean any Person to whom, now or hereafter, Lender sells a participation interest in, or makes an assignment of, its right, title or interest hereunder and in the Obligations (whether in whole or in part).

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"Permit" shall mean any permit, approval, authorization, license, variance, or permission required from a Governmental Authority having jurisdiction under an applicable Environmental Law.

"Person" shall mean any individual, partnership, corporation, trust, unincorporated association, business trust, sole proprietorship, or joint venture, a government or any department, agency, political subdivision or instrumentality thereof, or any other entity or organization.

"Property" or "Properties" shall mean any real or personal property owned, leased or operated by Borrower or either Guarantor.

"Real Estate Collateral" shall mean all right, title and interest of Borrower as owner in fee simple of the Distribution Center, inclusive of all buildings and other improvements thereon and all appurtenances thereto.

"Release" shall mean any actual or threatened release, spill, emission, leaking, pumping, injection, deposit, disposal, discharge, dispersal, leaching or migration into the indoor or outdoor environment or into or out of any Property, including the movement of Contaminants through or into the air, soil, subsurface strata, surface water or groundwater.

"Remedial Action" shall mean all actions required to (1) clean up, remove, treat or in any other way address Contaminants in the indoor or outdoor environment; (2) prevent the Release or threat of Release or minimize the further Release of Contaminants so they do not migrate or endanger or threaten to endanger public health or welfare or the indoor or outdoor environment; or (3) perform pre-remedial studies and investigations and post-remedial monitoring and care in respect of actions contemplated in the preceding clauses (1) and (2), in each instance in compliance with Environmental Laws.

"Subsidiary" shall mean, with respect to any Person, any corporation, association or other business entity of which more than fifty percent (50%) of the total voting power of shares of stock (or equivalent ownership or controlling interest) entitled (without regard to the occurrence of any contingency) to vote in the election of directors, managers or trustees thereof is at the time owned or controlled, directly or indirectly, by that Person or one or more of the other Subsidiaries of that Person or a combination thereof.

"Term Loan" shall mean each term loan made by Lender to Borrower pursuant to Section 2.1 below. "Term Loans" shall refer, collectively, to all such loans from time to time outstanding.

"Term Loan Facility" shall mean the term loan facility in the maximum amount of Twelve Million Dollars (\$12,000,000) established by Lender in favor of Borrower pursuant to Section 2.1.

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"Term Note" shall mean each Term Promissory Note issued by Borrower to Lender to evidence its repayment obligations associated with a given Term Loan, together with any extensions or renewals thereof, in whole or in part.

"UCC" shall mean the Uniform Commercial Code of Illinois, as in effect on the Closing Date.

1.2. USE OF DEFINED TERMS. All terms defined in this Agreement and the Exhibits shall have the same defined meanings when used in any other Loan Documents, unless the context shall require otherwise.

1.3. ACCOUNTING TERMS. All accounting terms not specifically defined herein shall have the meanings generally attributed to such terms under GAAP.

1.4. UCC TERMS. The terms "equipment", "fixtures", "proceeds" and "products", as and when used in the Loan Documents, together with any other or similar terms not specifically defined herein but which are defined in the UCC shall have the same meanings as given to such terms therein.

1.5. TERMINOLOGY. All personal pronouns used in this Agreement, whether used in the masculine, feminine or neuter gender, shall include all other genders; the singular shall include the plural, and the plural shall include the singular. Titles of Articles and Sections in this Agreement are for convenience only, and neither limit nor amplify the provisions of this Agreement, and all references in this Agreement to Articles, Sections, Subsections, paragraphs, clauses, subclauses or Exhibits shall refer to the corresponding Article, Section, Subsection, paragraph, clause, subclause of, or Exhibit attached to, this Agreement, unless specific reference is made to the articles, sections or other subdivisions divisions of, or Exhibit to, another document or instrument.

1.6. EXHIBITS. All Exhibits attached hereto are by reference made a part hereof as fully as if the contents thereof were set forth expressly herein.

## 2. THE FINANCING.

2.1. TERM LOAN FACILITY. Lender hereby creates the Term Loan Facility in favor of Borrower so that Borrower may obtain two (2) Term Loans, as follows: (i) a Term Loan of up to Three Million One Hundred Twenty-Five Thousand Dollars (\$3,125,000) in principal amount (herein, sometimes called "Term Loan A"), and (ii) a Term Loan of up to Eight Million Eight Hundred Seventy-Five Thousand Dollars (\$8,875,000) in principal amount (herein, sometimes called "Term Loan B"). The Term Loans shall be cross-collateralized and cross-defaulted to and with the other until both Term Loans are fully paid and satisfied and this Agreement is terminated. Each Term Loan so obtained shall reduce, dollar-for-dollar, the amount which may be borrowed under the Term Loan Facility. Each Term Loan shall be disbursed in its entirety on the Closing Date. No amount of either Term Loan may be reborrowed once disbursed, notwithstanding its repayment.

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2.2. AMORTIZATION. The principal amount of each Term Loan, together with accrued interest thereon at the then Applicable Rate, shall be paid as follows: (a) as to Term Loan A, in eighty-four (84) equal monthly installments of principal and interest in the amount prescribed in the amortization schedule attached to, and forming a part of, Term Note A, with payments commencing on February 1, 1999 and continuing on the first day of each month thereafter through January 1, 2006 provided that the final such payment shall, in any event, be in such amount as necessary to pay Term Loan A in full; and (b) as to Term Loan B, in one hundred nineteen (119) equal monthly installments of principal and interest, in the amount prescribed in the amortization schedule attached to and forming a part of Term Note B, with payments commencing on the February 1, 1999 and continuing on the first day of each month thereafter through December 1, 2008, followed by one (1) final, balloon payment, equal in amount to the unpaid principal balance of Term Note B, together with all accrued interest thereon, which shall be due and payable on January 1, 2009.

2.3. INTEREST. (a) Each Term Note shall bear interest at the Fixed Rate; provided, however, that, notwithstanding the foregoing, however, from and after the occurrence of any Event of Default, and continuing for so long thereafter as such Event of Default shall be continuing, Lender shall have the right to increase the interest rate payable on each Term Note to the Default Rate applicable thereto upon giving Borrowers ten (10) calendar days' advance written notice thereof, and Borrowers shall be responsible for the payment of the additional interest resulting therefrom.

(b) Interest shall be computed on the basis of a year consisting of twelve thirty day months. On January 1, 1999, Borrower shall make an interest only payment on each Term Note as to interest accrued for the period from the Closing Date through December 31, 1998. Thereafter, interest shall be paid as part of the combined monthly payments of principal and interest described in Section 2.2.

2.4. TERM NOTES. The indebtedness represented by each Term Loan shall be evidenced by a Term Note corresponding in principal amount thereto. Each Term Note shall be executed by Borrower and delivered to Lender on the closing date.

2.5. LATE CHARGE; LIQUIDATED DAMAGES. If payment of any principal of, or interest on, any Term Note or any other sum payable hereunder or under any other Loan Document is not received within ten (10) calendar days after its due date, Lender shall have the right to impose a late charge relative to such payment in

an amount equal to up to five percent (5%) of the amount of such past due payment, which charge, if imposed by Lender, shall be due and payable by Borrower immediately upon receipt of notice thereof. In connection with the foregoing, Borrower recognizes that any default in making, when due, any payment of principal or interest due under any Term Note or any other sum payable hereunder or under any other Loan Document, or the occurrence of any other Event of Default, will require Lender to incur additional expense in servicing and administering the Term Loans, in loss to Lender of the use of the money due and in frustration to Lender in meeting its other financial and loan commitments and that the damages caused thereby would be extremely difficult and impractical to ascertain. Borrowers agree that (a) an amount equal to the late charge described in the first sentence of this Section 2.5 plus the accrual of interest at the default rate of interest set forth in Section 2.3(f) hereof is a reasonable estimate of the damage to

Lender in the event of a late payment and (b) the accrual of interest at the default rate of interest set forth in Section 2.3(f) hereof is a reasonable estimate of the damages to Lender in the event of such other Event of Default, regardless of whether there has been acceleration of the Term Loans. Nothing herein shall be construed as an obligation on the part of Lender to accept, at any time, less than the full amount then due hereunder, or as a waiver or limitation of Lender's right to compel prompt performance.

2.6. VOLUNTARY PREPAYMENT. Provided that no Default Condition or Event of Default has occurred which is then continuing, the Term Notes may be prepaid, in whole or in part, by Borrowers at any time or from time to time after the third (3rd) anniversary of the Closing Date; provided, however, that (i) any such prepayment may be made only on a date on which a regularly scheduled payment of principal is to be made; (ii) as between Term Loans, the order of prepayment shall be, first, to Term Loan B, until it is paid in full; and then, to Term Loan A, until it is paid in full; and (iii) any such prepayment must be preceded by at least thirty (30) calendar days prior written notice thereof to Lender; and, provided, further, that, any such prepayment must be accompanied by the payment of all then accrued, but unpaid, interest on the principal amount to be prepaid and a prepayment premium, representing liquidated damages to Lender for the loss of its bargain and not a penalty, equal in amount to the product of (A) the principal amount prepaid times (B) the applicable percentage described in the table below:

If Prepayment Occurs -----	The Applicable Percentage Shall Be -----	
	Term Loan A -----	Term Loan B -----
After 3rd Anniversary of Closing Date but on or before 4th Anniversary of Closing Date	3%	3%
After 4th Anniversary of Closing Date but on or before 6th Anniversary of Closing Date	2%	2%
After 6th Anniversary of Closing Date on or before 7th Anniversary of Closing Date	1%	1%
After 7th Anniversary of Closing Date but on or before 9th Anniversary of Closing Date	N/A	1%
After 9th Anniversary of Closing Date	N/A	0%

In the event that at any time hereafter, as a result of the occurrence and continuation of any Event of Default, payment of the Term Notes is accelerated by Lender in accordance with the provisions hereof or the provisions of any other Loan Documents, Borrower shall become obligated to pay Lender, in addition to any and all other sums payable hereunder, as liquidated damages for the loss of its bargain and not as a penalty, an amount equal to the then applicable amount of the prepayment premium described above which would have been due and payable to Lender on the date on which such acceleration occurs as if, on such date, the Term Notes then outstanding had been voluntarily prepaid in full, which sum shall be added to the Obligations and be due and payable in full automatically upon such acceleration occurring.

2.7. NATURE OF CHARGES IMPOSED. Lender and Borrower hereby agree that (i) the only charges imposed by Lender upon Borrower for the use of money in connection with the Term Loan Facility are and shall be accrued interest at the rates per annum expressed in Section 2.3 hereinabove and in each Term Note and (ii) all other charges imposed by Lender upon Borrowers in connection with the Term Loan Facility, including, without limitation, the closing fee described in Section 2.9, and any prepayment premium hereafter paid by Borrower pursuant to Section 2.6, are and shall be deemed to be charges made to compensate Lender for underwriting and administrative services and costs, and other services and costs performed and incurred, and to be performed and incurred, by Lender in connection with the creation and administration of the Term Loan Facility, and shall under no circumstances be deemed to be charges for the use of money for purposes of Illinois law.

2.8. SAVINGS CLAUSE. Notwithstanding the foregoing or any provision contained in this Agreement, any Term Note or any other Loan Document to the contrary, if at any time the amount of interest computed with respect to either Term Note on the basis of the Applicable Rate would exceed the amount of such interest computed upon the basis of the maximum rate of interest permitted by applicable state or federal law in effect from time to time hereafter, after taking into account, to the extent required by applicable law, any and all fees, payments, charges and calculations provided for in this Agreement or in any other agreement between Borrower and Lender (the "Maximum Legal Rate"), the interest payable under this Agreement shall be computed upon the basis of the Maximum Legal Rate, but any subsequent reduction in the Applicable Rate shall not reduce such interest thereafter payable hereunder below the amount computed on the basis of the Maximum Legal Rate until the aggregate amount of such interest accrued and payable under this Agreement equals the total amount of interest which would have accrued if such interest had been at all times computed solely on the basis of the Applicable Rate. No agreements, conditions, provisions or stipulations contained in this Agreement, any Term Note or any other Loan Document or default of Borrower, or the exercise by the Lender of the right to accelerate the payment of the maturity of principal and interest, or to exercise any option whatsoever contained in this Agreement or any other Loan Document, or arising of any contingency whatsoever, shall entitle Lender to collect, in any event, interest exceeding the Maximum Legal Rate and in no event shall Borrower be obligated to pay interest exceeding such Maximum Legal Rate and all agreements, conditions or stipulations, if any, which may in any event or contingency whatsoever operate to bind, obligate or compel Borrower to pay a rate of interest exceeding the Maximum Legal Rate, shall be without binding force or effect, at law or in equity, to the extent only of the excess of interest over such

Maximum Legal Rate. In the event any interest is charged in excess of the Maximum Legal Rate ("Excess Interest"), Borrower acknowledges and stipulates that any such charge shall be the result of an accidental and bona fide error, and such Excess Interest shall be, first, applied to reduce the principal then unpaid hereunder; second, applied to reduce any other Obligations, until paid in full; and third, returned to Borrower, it being the intention of the parties hereto not to enter at any time into a usurious or otherwise illegal relationship. Borrower recognizes that, with fluctuations in the Maximum Legal Rate, such an unintentional result could inadvertently occur. By the execution of this Agreement, Borrower covenants that (i) the credit or return of any Excess Interest shall constitute the acceptance by the Borrower of such Excess Interest, and (ii) the Borrower shall not seek or pursue any other remedy, legal or equitable, against Lender, based in whole or in part upon the charging or receiving of any interest in excess of the maximum authorized by applicable law.

For the purpose of determining whether or not any Excess Interest has been contracted for, charged or received by Lender, all interest at any time contracted for, charged or received by the Lender in connection with this Agreement shall be amortized, prorated, allocated and spread in equal parts during the entire term of this Agreement. The provisions of this Section shall be deemed to be incorporated into each and every Term Note and other Loan Document or communication relating to the Obligations which sets forth or prescribes any account, right or claim or alleged account, right or claim of the Lender with respect to Borrower (or any other obligor in respect of Obligations), whether or not any provision of this Section is referred to therein. All such documents and communications and all figures set forth therein shall, for the sole purpose of computing the extent of the liabilities and obligations of Borrower (or any other such obligor) asserted by the Lender thereunder, be automatically recomputed by Borrower or any other obligor, and by any court considering the same, to give effect to the adjustments or credits required by this Section. If the applicable state or federal law is amended in the future to allow a greater rate of interest to be charged under this Agreement or any other Loan Documents than is presently allowed by applicable state or federal law, then the limitation of interest under this Section shall be increased to the maximum rate of interest allowed by applicable state or federal law as amended, which increase shall be effective hereunder on the effective date of such amendment, and all interest charges owing to the Lender by reason thereof shall be payable upon demand.

2.9. CLOSING FEE. Borrower shall pay to Lender on the Closing Date a closing fee of One Hundred Twenty Thousand Dollars (\$120,000), which shall be fully earned on the Closing Date, and not subject to rebate or refund once paid by Borrower.

2.10. GUARANTY. (a) THE GUARANTEE. To induce Lender to make the Term Loans to Borrower, Guarantors hereby, jointly and severally, guarantee to Lender and its successors and assigns the prompt payment in full when due (whether at stated maturity, by acceleration or otherwise) and performance of the Obligations of Borrower to Lender (such Obligations herein called, collectively, the "Guaranteed Obligations"), in each case strictly in accordance with the terms hereof. Guarantors hereby further agree, jointly and severally, that if Borrower shall fail to pay in full when due (whether at stated maturity, by acceleration or otherwise) any of the Guaranteed Obligations, Guarantors will promptly pay the same, upon demand, and that in the case of any extension of time of payment or renewal of any of the Guaranteed Obligations, the same will be

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promptly paid in full when due (whether at extended maturity, by acceleration or otherwise) in accordance with the terms of such extension or renewal.

(b) OBLIGATIONS UNCONDITIONAL. The obligations of each Guarantor hereunder are absolute, unconditional and irrevocable, joint and several, irrespective of the value, genuineness, validity, regularity or enforceability of the obligations of Borrower under this Agreement, the Term Notes or any other Loan Document or any substitution, release or exchange of any other guarantee of or security for any of the Guaranteed Obligations, and, to the fullest extent permitted by applicable law, irrespective of any other circumstance whatsoever that might otherwise constitute a legal or equitable discharge or defense of a surety or guarantor, it being the intent of this Section that the obligations of each Guarantor hereunder shall be absolute, and unconditional and irrevocable under any and all circumstances. Without limiting the generality of the foregoing, it is agreed that the occurrence of any one or more of the following shall not alter or impair the liability of each Guarantor hereunder which shall remain absolute and unconditional as described above:

(i) at any time or from time to time, without notice to Guarantors, the time for any performance of or compliance with any of the Guaranteed Obligations shall be extended, or such performance or compliance shall be waived;

(ii) any of the acts mentioned in any of the provisions of this Agreement or the Term Notes or any other agreement or instrument referred to herein or therein shall be done or omitted;

(iii) the maturity of any of the Guaranteed Obligations shall be

accelerated in accordance with the provisions of this Agreement or any other Loan Document, or any of the Guaranteed Obligations shall be modified, supplemented or amended in any respect, or any right under this Agreement or the Term Notes or any other Loan Document shall be waived or any other guarantee of any of the Guaranteed Obligations or any security therefor shall be released or exchanged in whole or in part or otherwise dealt with; or

(iv) any lien or security interest granted to, or in favor of, Lender as security for any of the Guaranteed Obligations shall fail to be created or perfected.

Each Guarantor hereby expressly waives diligence, presentment, demand of payment, protest and all notices whatsoever, and any requirement that Lender exhaust any right, power or remedy or proceed against Borrower under this Agreement or the Term Notes or any other Loan Document, or against any other Person under any other guaranty of, or security for, any of the Guaranteed Obligations.

The obligations of each Guarantor hereunder shall not be affected, modified or impaired by the occurrence of any of the following events, whether or not with notice to, or the consent of, such Guarantor: (i) the surrender, compromise, settlement, release or termination of any or all of the Guaranteed Obligations; (ii) the failure to give notice to such Guarantor of the occurrence of any breach, default of event or default under the Guaranteed Obligations; (iii) any failure, omission,

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delay or lack on the part of Lender to enforce, assert or exercise any right, power or remedy conferred on Lender under the Guaranteed Obligations; (iv) the voluntary or involuntary liquidation, dissolution, sale or other disposition of all or substantially all of the assets, marshaling of assets and liabilities, receivership, insolvency, bankruptcy, assignment for the benefit of creditors, reorganization, arrangement, composition with creditor or adjustment of debts, or other similar proceedings affecting the Borrower or either Guarantor or any of the assets of any of them; (v) the release or discharge by operation of law of the Borrower from the payment, performance, satisfaction or discharge of any or all of the Guaranteed Obligations; (vi) the release or discharge by operation of law of either Guarantor from any or all of the obligations of either Guarantor hereunder; or (vii) the invalidity or unenforceability of any or all of the Guaranteed Obligations; or (viii) the release by Lender of the other Guarantor from its obligations hereunder.

The obligations of each Guarantor hereunder are independent of the Guaranteed Obligations. Each Guarantor agrees that Lender shall have the right to proceed against such Guarantor directly and independently of the Borrower and the other Guarantor. A separate action may be brought and prosecuted against each Guarantor whether or not an action is brought against the Borrower or the other Guarantor or the Borrower or the other Guarantor is joined in any such action. Each Guarantor authorizes Lender and the Borrower, without notice to, demand of, or consent from such Guarantor and without releasing or affecting such Guarantor's liability hereunder, from time to time to amend, modify, renew, extend, supplement or replace the Guaranteed Obligations or otherwise change the terms of the Guaranteed Obligations, to take and hold collateral or security for the Guaranteed Obligations, and to enforce, waive, surrender, impair, compromise or release any such collateral or security or any or all of the Guaranteed Obligations or any person or entity liable for any or all of the Guaranteed Obligations. Each Guarantor shall be and remain bound hereunder notwithstanding any such act or omission by the Borrower or Lender.

Each Guarantor waives all rights under section 2845 of the California Civil Code and waives the right, if any, to require Lender to proceed against the Borrower, to proceed against or exhaust any collateral or security held by Lender, or to pursue any other remedy in Lender's power. Lender shall have the right to exercise or enforce any right or remedy it may have against the Borrower or any collateral or security held by Lender. Each Guarantor waives all rights under section 2849 of the California Civil Code and waives the right, if any, to the benefit of, or to direct the application of, any collateral or security held by Lender. Each Guarantor waives any defense arising from any impairment of any Collateral or security for any or all of the Guaranteed Obligations. Each Guarantor waives (i) any defense arising out of any alteration of the original

Guaranteed Obligations, (ii) any defense arising out of the absence, impairment or loss of any right of reimbursement or subrogation or other right or remedy of such Guarantor against the Borrower or any collateral or security held by Lender, and (iii) any defense arising by reason of any disability or other defense of the Borrower or by reason of the cessation or reduction from any cause whatsoever of the liability of the Borrower other than full payment, performance, satisfaction and discharge of the Guaranteed Obligations. The cessation or reduction of the liability of the Borrower for any reason whatsoever (including, without limitation, section 580d of the California Code of Civil Procedure) other than full payment, performance, satisfaction and discharge of the Guaranteed

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Obligations shall not release or affect in any way the liability of either Guarantor under this Guaranty.

EACH GUARANTOR HEREBY SPECIFICALLY AGREES THAT SUCH GUARANTOR SHALL NOT BE RELEASED FROM LIABILITY HEREUNDER BY ANY ACTION TAKEN OR OMITTED TO BE TAKEN BY LENDER, BORROWER OR ANY OF THEIR RESPECTIVE AFFILIATES, EMPLOYEES, AGENTS OR REPRESENTATIVES, INCLUDING WITHOUT LIMITATION, A NON-JUDICIAL SALE OF COLLATERAL UNDER ANY SECURITY AGREEMENT, MORTGAGE OR DEED OF TRUST THAT WOULD AFFORD A BORROWER OR A GUARANTOR A DEFENSE BASED UPON THE LAWS (INCLUDING THE ANTI-DEFICIENCY LAWS) OF ANY STATE. EACH GUARANTOR EXPRESSLY WAIVES (i) ANY DEFENSE TO THE RECOVERY OF A DEFICIENCY AGAINST BORROWER OR A GUARANTOR HEREUNDER AFTER SUCH NON-JUDICIAL SALE, NOTWITHSTANDING THAT SUCH SALE MAY RESULT IN A LOSS BY A GUARANTOR OF THE RIGHT TO RECOVER FROM THE BORROWER OF ANY SUCH DEFICIENCY, (ii) ANY DEFENSE OR BENEFITS THAT MAY BE DERIVED FROM CALIFORNIA CODE OF CIVIL PROCEDURE SECTIONS 580(A), 580(D) OR 726, OR SIMILAR LAWS OF OTHER JURISDICTIONS, AND (iii) ALL SURETYSHIP DEFENSES THAT IT WOULD OTHERWISE HAVE UNDER THE LAWS OF ANY JURISDICTION. WITHOUT LIMITING THE FOREGOING, EACH GUARANTOR UNDERSTANDS THAT IN THE ABSENCE OF THE WAIVERS MADE HEREIN, INCLUDING THOSE MADE IN THIS PARAGRAPH, SUCH GUARANTOR MIGHT HAVE A DEFENSE AGAINST AN ACTION BY LENDER TO RECOVER A DEFICIENCY FROM SUCH GUARANTOR HEREUNDER FOLLOWING A NON-JUDICIAL FORECLOSURE SALE OF REAL PROPERTY OR OTHER COLLATERAL SECURING THE LOAN, AND EACH GUARANTOR IS SPECIFICALLY WAIVING THESE DEFENSES AND ALL OTHER DEFENSES. EACH GUARANTOR EXPRESSLY AGREES THAT SUCH GUARANTOR SHALL BE AND REMAIN LIABLE FOR ANY DEFICIENCY REMAINING AFTER FORECLOSURE OF ANY MORTGAGE OR SECURITY INTEREST SECURING ANY OF THE OBLIGATIONS, WHETHER OR NOT THE LIABILITY OF BORROWER WITH RESPECT TO ANY OF THE OBLIGATIONS FOR SUCH DEFICIENCY IS DISCHARGED PURSUANT TO STATUTE OR JUDICIAL DECISION.

(c) REINSTATEMENT. The obligations of each Guarantor hereunder shall be automatically reinstated if and to the extent that for any reason any payment by or on behalf of Borrower in respect of the Guaranteed Obligations is rescinded or must be otherwise restored by any holder of any of the Guaranteed Obligations, whether as a result of any proceedings in bankruptcy or reorganization or otherwise and Guarantors, jointly and severally, agree that they will indemnify Lender on demand for all reasonable costs and expenses (including, without limitation, fees of counsel) incurred by Lender in connection with such rescission or restoration, including any such costs and expenses incurred in defending against any claim alleging that such payment constituted a preference, fraudulent transfer or similar payment under any bankruptcy, insolvency or similar law.

(d) SUBROGATION. Each Guarantor hereby subordinates to the indefeasible payment in full of the Obligations all rights of subrogation or contribution against Borrower, whether arising by contract or operation of law (including, without limitation, any such right arising under the Bankruptcy Code) or otherwise by reason of any payment by it pursuant to the provisions hereof and agrees that, unless and until the Obligations are indefeasibly paid in full, it will not exercise any such right.

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(e) REMEDIES. Each Guarantor agrees that, as between Guarantor and Lender, the Guaranteed Obligations may be declared to be forthwith due and payable as provided herein (and shall be deemed to have become automatically due and payable in the circumstances provided herein) for purposes hereof,

notwithstanding any stay, injunction or other prohibition preventing such declaration (or such obligations from becoming automatically due and payable) as against Borrower and that, in the event of such declaration (whether or not due and payable by the Borrower) shall forthwith become due and payable by Guarantors for purposes hereof.

(f) INSTRUMENT FOR THE PAYMENT OF MONEY. Each Guarantor hereby acknowledges that its guaranty herein constitutes an instrument for the payment of money.

(g) CONTINUING GUARANTY. The guaranty set forth herein is a continuing guaranty, and shall apply to all Guaranteed Obligations, whenever and howsoever arising.

(h) ACKNOWLEDGMENTS. Each Guarantor assumes the responsibility for being and keeping itself informed of the financial condition of the Borrower and of all other circumstances bearing upon the risk of failure to pay, perform, satisfy or discharge any of the Guaranteed Obligations that diligent inquiry would reveal, and each Guarantor agrees that Lender has no duty to advise such Guarantor of information known to Lender regarding such condition or any such circumstance. Each Guarantor acknowledges that repeated and successive demands may be made and payments or performances required hereunder in response to such demands as and when, from time to time, the Borrower defaults in the payment performance, satisfaction or discharge of the Guaranteed Obligations. Notwithstanding any such payments and performances hereunder, each Guarantor's obligations hereunder shall remain in full force and effect and shall apply to any and all subsequent defaults by the Borrower. It is not necessary for Lender to inquire into the capacity, authority or powers of the Borrower or the partners, directors, officers, employees, agents or representatives acting or purporting to act on behalf of the Borrower, and all of the Guaranteed Obligations made or created in reliance upon the purported exercise of such powers shall be guaranteed hereunder.

(i) REPRESENTATIONS. Each Guarantor represents and warrants to Lender as of the date hereof as follows: such Guarantor has received reasonably equivalent value in exchange for the execution, delivery and performance of this guaranty. Each Guarantor is solvent and will not become insolvent as a result of the execution, delivery or performance of this guaranty.

(j) RIGHTS OF CONTRIBUTION. Guarantors hereby agree, as between themselves, that if any Guarantor shall become an "Excess Funding Guarantor" (as defined below) by reason of the payment by such Guarantor of any Guaranteed Obligations, the other Guarantor shall, on demand of such Excess Funding Guarantor (but subject to the next sentence), pay to such Excess Funding Guarantor an amount equal to such Guarantor's "Pro Rata Share" (as defined below and determined, for this purpose, without reference to the properties, debts and liabilities of such Excess Funding Guarantor) of the "Excess Payment" (as defined below) in respect of such Guaranteed Obligations. The payment obligation of a Guarantor to any Excess Funding Guarantor under this Section shall be subordinate and subject in right of payment to the prior payment in full of the obligations of such

Guarantor under the other provisions of this Section 2.10 and such Excess Funding Guarantor shall not exercise any right or remedy with respect to such excess until payment and satisfaction in full of all such obligations. For purposes hereof, (i) "Excess Funding Guarantor" means, in respect of any Guaranteed Obligations, a Guarantor that has paid an amount in excess of its Pro Rata Share of such Guaranteed Obligations, (ii) "Excess Payment" means, in respect of any Guaranteed Obligations, the amount paid by an Excess Funding Guarantor in excess of its Pro Rata Share of such Guaranteed Obligations, (iii) "Pro Rata Share" means, for any Guarantor, the ratio (expressed as a percentage) of (x) the amount by which the aggregate present fair saleable value of all assets of such Guarantor (excluding any shares of stock of any other Guarantor) exceeds the amount of all the debts and liabilities of such Guarantor (including contingent, subordinated, unmaturred and unliquidated liabilities, but excluding the obligations of such Guarantor hereunder and any obligations of any other Guarantor that have been guaranteed by such Guarantor) to (y) the amount by which the aggregate fair saleable value of all assets of all of the Guarantors exceeds the amount of all the debts and liabilities (including contingent, subordinated, unmaturred and unliquidated liabilities, but excluding the

obligations of such Guarantor hereunder) of the Guarantors, determined as of the Closing Date.

(k) GENERAL LIMITATION ON GUARANTEED OBLIGATIONS. In any action or proceeding involving any state corporate law, or any state or Federal bankruptcy, insolvency, reorganization or other law affecting the rights of creditors generally, if the obligations of a Guarantor hereunder, after giving effect to the contribution rights provided in Section 2.10(j), would otherwise be held or determined to be void, invalid or unenforceable, or subordinated to the claims of any other creditors, on account of the amount of its liability hereunder, then, notwithstanding any other provision hereof to the contrary, the amount of such liability shall, without any further action by any Guarantor, any Lender or any other Person, be automatically limited and reduced to the highest amount that is valid and enforceable and not subordinated to the claims of other creditors as determined in such action or proceeding.

30 SECURITY INTEREST -- COLLATERAL. As security for the payment of the Term Notes and all other Obligations, Borrower and each Guarantor hereby grant to Lender a first priority, continuing, general lien upon, security interest in, and security title to the Equipment Collateral owned by Borrower or such Guarantor, together with any and all products and proceeds of the foregoing, including, without limitation, insurance proceeds. The foregoing shall be in addition to, and be cumulative with, the Real Estate Collateral obtained by Lender pursuant to the Mortgage.

3.1. REPRESENTATIONS AND WARRANTIES. With respect to the Collateral, Borrower and each Guarantor hereby represents, warrants and covenants to Lender as follows:

(a) GOOD TITLE; NO EXISTING ENCUMBRANCES. Borrower or a Guarantor owns the Collateral free and clear of any prior security interest, lien or encumbrance thereon other than liens in favor of Lender and those liens listed on Exhibit A attached hereto and incorporated herein by reference (collectively, "Permitted Encumbrances"), and no financing statements, registration statements, certificates of title or other evidences of the grant of a security interest respecting the

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Collateral exist on any public records as of the date hereof, other than any in favor of Lender and those evidencing Permitted Encumbrances.

(b) RIGHT TO GRANT SECURITY INTEREST; NO FURTHER ENCUMBRANCES. Borrower and each Guarantor has the right to grant the security interest in the Collateral prescribed hereinabove in this Article 3; Borrower or a Guarantor will pay all sales, use, franchise and other taxes and other charges against the Collateral; neither Borrower nor either Guarantor will use the Collateral illegally or allow the Collateral to be encumbered except for the security interest in favor of Lender granted herein and except for any Permitted Encumbrances (as described in Section 3.1(a)).

(c) CONDITION OF COLLATERAL; CASUALTY. All Equipment Collateral is in good working order and repair as of the Closing Date. Borrower and each Guarantor will maintain the Equipment Collateral in good working order and repair subsequent to the Closing Date, ordinary wear and tear excepted, and subject to Borrower's right to replace Equipment Collateral as provided in Section 3.1(d) hereof. Borrower and each Guarantor further will take such actions subsequent to the Closing Date as may be necessary to keep any manufacturer's warranty in effect with respect to the Equipment Collateral. Borrower and each Guarantor further will promptly report to Lender any material loss, damage, theft or other casualty to any Equipment Collateral, and whether Borrower or Guarantor has repaired (or caused to be repaired) or replaced, or intends to repair (or cause to be repaired) or replace, such Equipment Collateral.

(d) NO SALE OF COLLATERAL. Neither Borrower nor either Guarantor will sell, assign, lease, license, exchange, mortgage, encumber, hypothecate, grant a security interest in, or otherwise dispose of its right, title or interest in any of the Collateral, without in each case first obtaining the prior written consent of Lender thereto; provided, however, that (i) Borrower may obtain purchase money financing of equipment purchases secured by liens on such equipment to the extent permitted pursuant to Section 3.2, (ii) Borrower

may replace Collateral consisting of obsolete or worn out equipment and machinery in the ordinary course of its business and consistent with past practice so long as (x) the replacement Collateral has a value equal to or greater than that of the Collateral being replaced, and (y) Lender has a perfected first priority security interest in the replacement Collateral, subject to no other security interests, liens or encumbrances and (iii) so long as no Default Condition or Event of Default has occurred and is continuing, Borrower may dispose of obsolete or worn out equipment and machinery in the ordinary course of its business and consistent with past practice without replacing same so long as the aggregate value of equipment so disposed of in any calendar year does not exceed Twenty-Five Thousand Dollars (\$25,000).

(e) WAIVERS. Borrower and Guarantors agree to obtain, on Lender's behalf, such waivers or consents from third parties, including, without limitation, any lessor, licensor, operator, servicer or vendor, as Lender may reasonably request at any time, in order to assure Lender in regard to the perfection and priority of its security interest in, and ability to realize on, any Collateral.

(f) FURTHER ASSURANCES. Borrower and each Guarantor further shall duly execute and/or deliver (or cause to be duly executed and/or delivered) to Lender any instrument, invoice, registration certificate, certificate of title, application, document, document of title, dock warrant,

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dock receipt, warehouse receipt, bill of lading, order, financing statement, assignment, waiver, consent or other writing which may be necessary to Lender to carry out the terms of this Agreement and any of the other Loan Documents and to perfect its security interest in and facilitate its realization on the Collateral. Borrower and each Guarantor shall perform or cause to be performed such acts as Lender may reasonably request to establish and maintain for Lender a valid and perfected first priority security interest in the Collateral, free and clear of any liens, encumbrances or security interests other than in favor of Lender and other than Permitted Encumbrances.

(g) RIGHT TO INSPECT. Lender or any Participant shall have the right to call at the Headquarters or the Distribution Center at any reasonable time, and, without hindrance or delay, inspect, audit and check the Collateral and make extracts from each Guarantor's and Borrower's books, records, journals, orders, receipts and any correspondence and other data relating to the transactions contemplated herein and to the Collateral. As long as no Default Condition or Event of Default has occurred and is continuing, Lender shall give Borrower three (3) days advance notice of any such visit. No notice of any such visit shall be required at any time when a Default Condition or Event of Default has occurred and is continuing.

(h) CHANGE OF NAME. Borrower and each Guarantor hereby acknowledges and agrees that if, at any time hereafter, Borrower or either Guarantor elects to move its chief executive office and principal place of business from the Headquarters, or elects to change its name, identity or its organization structure, Borrower or such Guarantor will notify Lender in writing at least thirty (30) days prior thereto (provided that the foregoing shall not be deemed a consent to any action otherwise prohibited by the terms of this Agreement or any of the other Loan Documents) and execute (or cause to be executed) such financing statements, or amendments thereto, or other documents as Lender then may require in response to such changed condition in accordance with Sections 3.1(e) and 3.1(f).

(i) CHANGE OF LOCATION. Borrower and each Guarantor further agree not to remove any Collateral from the Distribution Center to any other location.

3.2. PURCHASE MONEY LIENS; RELEASE PROVISION. Notwithstanding anything contained herein to the contrary, Borrower may permit purchase money liens to be placed on items of equipment acquired by it after the Closing Date if and to the extent that (i) at the time of the incurrence of any indebtedness to be secured by such lien, no Default Condition or Event of Default shall have occurred and be continuing, (ii) the aggregate amount of such purchase money indebtedness incurred during the term of this Agreement, together with the cost of all items of equipment purchased by Borrower with cash as to which Borrower has requested releases pursuant to the next sentence hereof, shall not exceed \$500,000, and (iii) each item of equipment shall secure only the indebtedness incurred to

purchase such item, shall be readily distinguishable (by using serial numbers and other identification) from the other Equipment Collateral and shall not serve as a replacement for any item of Equipment Collateral existing on the Closing Date or acquired thereafter. Upon Borrower's written request, (i) Lender shall release its security interest in any item of equipment financed with purchase money financing as to which all of the conditions set forth in the preceding sentence have been satisfied and (ii) Lender shall release its security interest in any

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item of equipment purchased by Borrower after the Closing Date with cash if and to the extent that (A) no Default Condition or Event of Default shall have occurred and be continuing, (B) the aggregate amount of all purchase money indebtedness as described in the preceding sentence and the cost of equipment purchased by Borrower with cash and requested to be released hereby during the term of this Agreement shall not exceed Five Hundred Thousand Dollars (\$500,000), and (iii) each item of equipment requested to be released hereby shall be readily distinguishable (by using serial numbers and other identification) and shall not serve as a replacement for any item of Equipment Collateral existing on the Closing Date or acquired thereafter.

40 GENERAL REPRESENTATIONS AND WARRANTIES. In order to induce Lender to enter into this Agreement, each Guarantor and Borrower hereby represents and warrants to Lender as set forth in Sections 4.1 through 4.6, inclusive.

4.1. EXISTENCE. Borrower is a general partnership duly organized, validly existing and in good standing under the laws of the State of California. Guarantor One is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and is qualified to do business and in good standing under the laws of the State of California. Guarantor Two is a corporation duly organized, validly existing and in good standing under the laws of the State of California. The principal place of business and chief executive office of each Guarantor and Borrower is located at the Headquarters. Borrower and Guarantors keep their books and records concerning the Collateral at the Headquarters. Borrower has no Subsidiaries. Guarantor One has only those Subsidiaries listed on Exhibit B attached hereto and incorporated herein by reference. Guarantor Two has no Subsidiaries.

4.2. AUTHORITY. Each Guarantor and Borrower has the power to make, deliver and perform under this Agreement, the Term Notes and the other Loan Documents to which it is party, and, in the case of Borrower, to borrow hereunder, and has taken all necessary and appropriate legal action to authorize the execution, delivery and performance of all such Loan Documents. This Agreement constitutes, and the Term Notes and the remainder of the Loan Documents to which each is party, when executed and delivered by a Guarantor or Borrower for value received, will constitute, the valid obligations of such Guarantor and Borrower, legally binding upon each of them and enforceable against each of them in accordance with their respective terms, to the extent that each is party thereto. The Persons whose names are inscribed below are Authorized Officers of Guarantors and Borrower duly authorized and empowered to execute, attest and deliver this Agreement, the Term Notes and the remainder of the Loan Documents to which each is party, for and on behalf of Guarantors and Borrower, and to bind Guarantors and Borrower accordingly thereby.

4.3. NO MATERIAL LITIGATION. Except as set forth on Exhibit C attached hereto and incorporated herein by reference, there are no proceedings pending or, so far as either Guarantor or Borrower knows, threatened, against either Guarantor or Borrower, before any court, arbitration panel or administrative agency, no material disputes with any contract party and no pending or threatened labor action which, in each case, if decided adversely to either Guarantor or Borrower, would have a Material Adverse Effect.

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4.4. PAYMENT OF TAXES. Each Guarantor and Borrower has filed or caused to be filed any federal income tax returns required to be filed by it, and all other tax returns required to be filed by it, and has paid all taxes shown to be due and payable by it on said returns or on any assessments made against it.

Neither of Guarantors nor Borrower has participated in any "prohibited transaction" (as defined in Section 4975 of the Internal Revenue Code of 1986) that could subject either Guarantor or Borrower to any tax or penalty.

4.5. NO VIOLATIONS, GENERALLY. The execution, delivery and performance by each Guarantor and Borrower of this Agreement, the Term Notes and the other Loan Documents to which each is party do not and will not require any consent or approval of any Person, except to the extent obtained by a Guarantor or Borrower on or prior to the Closing Date; or violate either Guarantor's certificate of incorporation or bylaws or Borrower's partnership agreement or any provision of any law, rule, regulation, order, writ, judgment, injunction, decree, determination or award presently in effect having applicability to either Guarantor or Borrower; or result in a breach of or constitute a default under any agreement that is material to either Guarantor's or Borrower's business; and, to the best of each Guarantor's and Borrower's knowledge following diligent inquiry, neither of Guarantors nor Borrower is in default under any such law, rule, regulation, order, writ, judgment, injunction, decree, determination or award or material agreement.

#### 4.6. POLLUTION AND ENVIRONMENTAL CONTROL.

(a) To the best knowledge of Guarantors and Borrower after due inquiry, the business operations of each Guarantor and Borrower comply in all material respects with all applicable Environmental Laws; each Guarantor and Borrower has obtained all environmental, health and safety Permits necessary for the operation of such Guarantor's and Borrower's businesses; and all such permits are valid, and in good standing and Guarantors and Borrower are in compliance in all material respects with all terms and conditions of such Permits.

(b) Further, to the best knowledge of Guarantors and Borrower after due inquiry, (i) neither of Guarantors nor Borrower is subject to any outstanding written order or agreement with any Governmental Authority or with any private Person with respect to (A) any Environmental Laws, (B) any Remedial Actions, or (C) any Environmental Claims arising from the Release of a Contaminant into the environment with respect to the Distribution Center; (iii) none of the operations of either Guarantor or Borrower at the Distribution Center is subject to any judicial or administration proceeding alleging a violation of any Environmental Law; (iv) none of the operations of either Guarantor or Borrower is the subject of any federal or state investigation evaluating whether any Remedial Action is needed to respond to a Release of any Contaminant into the environment under any applicable law; (v) neither of Guarantors or Borrower nor any predecessor of either Guarantor or Borrower has filed any notice under any federal or state law indicating past or present treatment, storage, or disposal of a hazardous waste or reporting a spill or Release of a Contaminant into the environment under any applicable law; (vi) neither of Guarantors nor Borrower has any contingent liability in connection with any Release of any Contaminant into the environment; (vii) neither of Guarantors' nor Borrower's business operations involve the generation, transportation, treatment or disposal of any hazardous waste, as defined under 40 C.F.R.

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Parts 260-270 or any state equivalent (other than any done in compliance with all Environmental Laws); (viii) neither of Guarantors nor Borrower has disposed of any Contaminant by placing it in or on the ground, groundwater or surface water, and, with regard to the Distribution Center, neither has any lessee, prior owner, or other Person; and (ix) no Lien in favor of any Governmental Authority for (A) any liability under Environmental Laws or regulations, or (B) damages arising from or costs incurred by such governmental authority in response to a Release of a Contaminant into the environment has been filed or attached to any Property.

50 COVENANTS. Guarantors and Borrower agree that, so long as any Obligations are outstanding and this Agreement has not been terminated in writing by Lender, each Guarantor and Borrower will comply with the following covenants:

5.1. BOOKS AND RECORDS. Guarantors and Borrower shall maintain, at all times, true and complete books, records and accounts in which true and correct entries are made of their transactions in accordance with GAAP.

5.2. PERIODIC FINANCIAL STATEMENTS. Guarantors and Borrower shall, as

soon as practicable, and in any event within sixty (60) days after the end of each fiscal quarter, furnish (or cause to be furnished) to Lender and each Participant unaudited financial statements of Guarantor One and its consolidated Subsidiaries, including, in each instance, balance sheets, income statements and cash flow statements, on a consolidated and consolidating basis, as of and for the quarterly period then ended and for their fiscal year to date, prepared in accordance with GAAP, certified as to truth and accuracy by Authorized Officers of Guarantor One and Borrower, together with a copy of Guarantor One's 10-Q quarterly report filed with the Securities and Exchange Commission incorporating such financial statements.

5.3. ANNUAL FINANCIAL STATEMENTS. Guarantors and Borrower shall, as soon as practicable, and in any event within ninety (90) days after the end of each fiscal year, furnish (or cause to be furnished) to Lender and each Participant annual financial statements of Guarantor One and its consolidated Subsidiaries, including, in each instance, balance sheets, income statements and cash flow statements for the fiscal year then ended, on a consolidated and consolidating basis, which have been audited by Guarantor One's Independent Accountants, together with a copy of Guarantor One's 10-K annual report filed with the Securities and Exchange Commission incorporating such financial statements.

5.4. COMPLIANCE CERTIFICATES. Together with each of the financial statements described in Sections 5.2 and 5.3 above, and more frequently, if requested by Lender, Guarantors and Borrower shall deliver a Compliance Certificate and a covenant compliance worksheet to Lender, including calculations of the financial tests set forth in Section 6.14, each signed by Authorized Officers of Guarantors and Borrower.

5.5. PAYMENT OF TAXES. Each Guarantor and Borrower shall pay and discharge all taxes, assessments and governmental charges pertaining to Collateral, and the Distribution Center and all other material taxes, assessments and governmental charges upon each of them, their respective

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income and properties prior to the date on which penalties attach thereto, unless and to the extent only that (i) such taxes, assessments and governmental charges are being contested in good faith and by appropriate proceedings by Borrower and (ii) the applicable Guarantor or Borrower maintains reasonable reserves on its books therefor.

5.6. MAINTENANCE OF INSURANCE. Guarantors and Borrower shall insure the Collateral against fire, theft and such other risks (including, but not limited to boiler and machinery) as Lender shall require from time to time at the full replacement cost thereof, and maintain at least six (6) months of business interruption or loss of rental income insurance, with Lender shown by endorsement and named on a certificate of insurance as loss payee, additional insured and mortgagee thereof, with responsible insurance companies rated "A-" or better by A.M. Best Company. As to other Properties and risks, including, without limitation, liability coverage, Guarantors and Borrower shall maintain such insurance, with such insurers (having the minimum qualifications described above) on such Properties, in such amounts and against such risks as is customarily maintained by similar businesses operating in the same vicinity; provided that such insurance shall not be less, in terms of insurers, amounts, coverages or limitations, than the insurance being maintained by Guarantors and Borrower on the Closing Date; and, provided, further, that such insurance shall include, in any event, at all times, comprehensive general liability (inclusive of products liability coverage), in aggregate combined single limit coverage acceptable to Lender; and, provided, further, that Lender shall be shown by endorsement and named on a certificate of insurance as "additional insured" thereon and with breach of warranty endorsement favoring Lender. All such insurance in existence on the Closing Date shall not be cancellable or modifiable by Guarantors or Borrower, thereafter, unless with the prior written consent of Lender, or by Guarantors' or Borrower's insurer, unless with at least thirty (30) days advance written notice to Lender thereof (except as may be necessary to bring such insurance into compliance herewith from time to time). Guarantors and Borrower shall file with Lender on the Closing Date and at least annually thereafter or, at Lender's request at any time from and after the occurrence of, and during the continuance of, any Event of Default, upon its request, an insurer's certificate evidencing Guarantors' and Borrower's compliance with the requirements of this Section 5.6. All casualty insurance proceeds paid with respect to the Collateral shall, after deduction of

reasonable expenses of Lender actually incurred in collecting such proceeds (if any), at Lender's option be (i) applied (upon compliance with such terms and conditions as may be required by Lender) to repair or restoration, either partly or entirely, of the Collateral or (ii) applied to the payment of the Obligations in such order and manner as Lender may elect, whether or not due. In the event that, notwithstanding the foregoing, Borrower or either Guarantor receives any such insurance proceeds directly or that a check for such proceeds is made payable to Borrower or a Guarantor and Lender jointly, Borrower or such Guarantor shall take all actions necessary to convey such proceeds to Lender. In the event that pursuant hereto such proceeds are to be used for repair or restoration of the Collateral, at its option, Lender will either release such proceeds directly to Borrower or use such proceeds to pay directly invoices for repair or restoration work, in each case upon compliance with such terms and conditions as it may require.

5.7. PRESERVATION OF EXISTENCE. Each Guarantor and Borrower shall preserve and maintain its existence, rights, franchises and privileges, in each local jurisdiction in which the Distribution Center exists and in each other jurisdiction where the nature of the business conducted therein or the

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location of any Property therein requires that such rights, franchises and privileges be preserved and maintained; and obtain and maintain for itself all Permits, licenses, certificates of convenience and necessity, operating rights, authorizations and consents as shall be necessary or advisable to permit it to continue to operate its business in the manner contemplated to be conducted by it on the Closing Date.

5.8. COMPLIANCE WITH LAWS. Each Guarantor and Borrower shall comply with the requirements of all applicable laws, rules, regulations, permits, hearings, approvals and clearances and orders of any Governmental Authority, including particularly, but without limitation, in respect of Environmental Laws.

5.9. ENVIRONMENTAL LAW COMPLIANCE.

(a) On or before the Closing Date, Borrower will provide Lender with the environmental assessment described in Section 9(g)(7) below together with copies of any environmental assessments or similar reports made by or on behalf of Borrower with respect to any of the Real Estate Collateral within the preceding five (5) years (if any); and, subsequent to the Closing Date, Borrower will provide Lender with copies of any such assessments or reports thereafter made by or on behalf of Borrower with respect to any location where Collateral is located, promptly as and when made or received by Borrower, but not later than thirty (30) days thereafter.

(b) Each Guarantor and Borrower will notify Lender in writing of any Environmental Claim as to which a Guarantor or Borrower is reasonably likely to have liability in excess of Fifty Thousand Dollars (\$50,000) or any accusation or allegations which may give rise to such an Environmental Claim hereafter made against it or received by it within fifteen (15) days after it first obtains knowledge or notice thereof. Each such notice to Lender shall include a copy of any claim, citation, order, notice or other communication (to the extent in writing) received by a Guarantor or Borrower from the person making such Environmental Claim, allegation or accusation, a description of the nature of such Environmental Claim, allegation or accusation, the name of the Person making such Environmental Claim, allegation or accusation; such Guarantor's or Borrower's anticipated defense to such Environmental Claim, allegation or accusation or the action such Guarantor or Borrower proposes to take in respect of such Environmental Claim, allegation or accusation and the anticipated costs to be incurred by such Guarantor or Borrower in connection with such Environmental Claim, allegation or accusation (including, with limitation, that amount of any anticipated damages, the costs of defending such Environmental Claims and the costs of any cleanup or corrective action).

(c) In addition, each Guarantor and Borrower will promptly notify Lender of any Release with regard to any Property if such Release would or would reasonably be expected to have a Material Adverse Effect or of material change in the nature or extent of any Contaminants used, transported or stored by either Guarantor or Borrower or any Subsidiary, and allow no material change in the use thereof or either Guarantor's or Borrower's or any Subsidiary's operations that would increase in any material amount the risk of violation of

the Environmental Laws without the express prior written approval of Lender.

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(d) Guarantors and Borrower, jointly and severally, further agree to indemnify and hold Lender, each Participant and the officers, directors, agents, employees, affiliates and representatives of Lender and each Participant (individually an "Indemnified Party" and collectively the "Indemnified Parties") harmless from and against any and all damages, penalties, fines, claims, liens, suits, liabilities, costs (including necessary and actual clean-up and response costs), judgments, and expenses (including reasonable attorneys' fees and any consultants' or other experts' fees and expenses) of every kind and nature suffered by or asserted against any Indemnified Party (i) under or on account of the Environmental Laws, including, without limitation, as a result of the past, present or future institution of any suits, claims, actions, or proceedings by any person against Borrower, either Guarantor or Lender in respect of any alleged violation of the Environmental Laws by Borrower, either Guarantor or Borrower's or either Guarantor's use, storage or disposition of Contaminants, (ii) with respect to any past, present or future Release of Contaminants affecting any Property, whether or not the same originates or emanates from any Property or any contiguous real estate, (iii) with respect to any other past, present, or future matters affecting any Property within the jurisdiction of any Governmental Authority administering the Environmental Laws or (iv) with respect to any past, present or future requirement under the Environmental Laws which requires the elimination or removal of any Contaminants or other substances regulated pursuant to any Environmental Laws, rules, or regulations of any Governmental Authority having jurisdiction over Borrower or either Guarantor, whether attributable to events occurring before or after the Closing Date. Any payments required to be made hereunder shall be due and payable on demand.

(e) The agreements contained in this Section shall survive the termination of this Agreement and shall continue in full force and effect for so long as the prospect of any loss or liability covered by the indemnity contained in such clause (d) above exists.

5.10. NOTICE OF LITIGATION; EVENTS OF DEFAULT, ETC. Promptly, after receipt of notice or knowledge thereof, but not later than ten (10) days thereafter, each Guarantor and Borrower will report to Lender: (i) any lawsuit or administrative proceeding or arbitration proceeding in which Borrower or either Guarantor is a defendant wherein the amount of damages claimed against Borrower or either Guarantor exceeds One Hundred Thousand Dollars (\$100,000) or in which the validity of this Agreement or any Loan Document or any action taken or to be taken pursuant hereto or thereto is questioned; (ii) any strike, walkout, lockout or other related legal action, whether pending or threatened pertaining to Borrower or either Guarantor which could have a Material Adverse Effect; (iii) the existence and nature of any Default Condition or Event of Default; and (iv) any Environmental Claim or an accusation or allegation which may give rise to an Environmental Claim hereafter made against Borrower or either Guarantor, or received by Borrower or either Guarantor or of which it obtains knowledge, whether or not made against it, which either (A) relates to the Distribution Center or (B) could reasonably be expected to result in liability to Borrower or a Guarantor in excess of One Hundred Thousand Dollars (\$100,000).

5.11. YEAR 2000 COMPLIANCE. Each Guarantor and Borrower shall take all actions necessary or advisable to assure that its business operations will handle date information involving any and all dates before, during and after January 1, 2000, including, accepting and storing input,

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providing output and performing date calculations, without any change in performance or reliability from that existing on the Closing Date for dates shorter than January 1, 2000.

5.12. INTERCOMPANY LEASE. Guarantor Two and Borrower shall keep the Intercompany Lease in effect at all times until the Obligations have been paid in full and shall not, amend or modify in any material respect, or terminate, or acquiesce in any amendment or modification in a material respect, or termination

of, the Intercompany Lease without Lender's prior written consent.

6. EVENTS OF DEFAULT. The occurrence of any events or conditions shall constitute an Event of Default hereunder, provided that any requirement for the giving of notice or the lapse of time, or both, has been satisfied.

6.1. TERM NOTES. Borrower or a Guarantor shall fail to make any payments of principal of, or interest on, either Term Note, within ten (10) calendar days after the same shall become due and payable.

6.2. OTHER OBLIGATIONS. Borrower or a Guarantor shall fail to pay any Obligations (other than as evidenced by the Term Notes) to Lender, within ten (10) calendar days after the same shall become due and payable (unless a longer or shorter grace period is provided therefor in any document, instrument or agreement evidencing, pertaining to or securing the repayment of such other Obligations, in which event such other grace period shall apply).

6.3. MISREPRESENTATIONS. Borrower or a Guarantor shall make any representation or warranty, respectively, in this Agreement or any of the Loan Documents or in any certificate or statement furnished at any time hereunder or in connection with this Agreement or any of the Loan Documents which proves to have been untrue or misleading in any material respect when made or furnished.

6.4. COVENANTS. Borrower or a Guarantor shall default in the observance or performance of any covenant or agreement contained in Section 5; or Borrower or a Guarantor shall default in the observance or performance of any other covenant or agreement contained in this Agreement or any of the Loan Documents, except for any default of the types described in Sections 6.1, 6.2 or 6.3 above, and such default shall continue for a period of thirty (30) calendar days from the date of receipt by Borrower or a Guarantor of written notice from Lender specifying such default (unless a longer or shorter cure period is provided therefor in any such Loan Document, in which case such other grace period shall apply), without such default being waived or cured.

6.5. OTHER DEBTS. Borrower or a Guarantor shall default under any agreement for indebtedness in excess of Two Hundred Fifty Thousand Dollars (\$250,000) under which it is a borrower or guarantor if such default (i) consists of the failure to pay any debt when due or to perform any other obligation thereunder, (ii) gives the holder of the debt the right to accelerate the debt and (iii) the holder has accelerated the debt and commenced the exercise of remedies.

6.6. VOLUNTARY BANKRUPTCY. Borrower or a Guarantor shall file a voluntary petition in bankruptcy or a voluntary petition or answer seeking liquidation, reorganization, arrangement, readjustment of its debts, or for any other relief under the Bankruptcy Code, or under any other act or law pertaining to insolvency or debtor relief, whether state, federal, or foreign, now or hereafter existing; or Borrower or a Guarantor shall enter into any agreement indicating its consent to, approval of, or acquiescence in, any such petition or proceeding; or Borrower or a Guarantor shall apply for or permit the appointment by consent or acquiescence of a receiver, custodian or trustee for all or a substantial part of its property; or Borrower or a Guarantor shall make an assignment for the benefit of creditors; or Borrower or a Guarantor shall be unable or shall fail to pay its debts generally as such debts become due; or Borrower or a Guarantor shall admit, in writing, its inability or failure to pay its debts generally as such debts become due.

6.7. INVOLUNTARY BANKRUPTCY. There shall have been filed against Borrower or a Guarantor an involuntary petition in bankruptcy or seeking liquidation, reorganization, arrangement, readjustment of its debts or for any other relief under the Bankruptcy Code, or under any other act or law pertaining to insolvency or debtor relief, whether state, federal or foreign, now or hereafter existing; or Borrower or a Guarantor shall suffer or permit the involuntary appointment of a receiver, custodian or trustee or for all or a substantial part of its property; or Borrower or a Guarantor shall suffer or permit the issuance of a warrant of attachment, execution or similar process against all or any substantial part of its property; unless, in each such case, such petition, appointment or process is fully bonded against, vacated or dismissed within sixty (60) days from its effective date, but not later than ten (10) days prior to any proposed disposition of any assets pursuant to any such

proceeding.

6.8. JUDGMENTS. If one or more final, nonappealable judgments or decrees in excess of Two Hundred Fifty Thousand Dollars (\$250,000) shall be entered against Borrower or a Guarantor and such judgments or decrees shall not have been vacated, discharged, stayed or bonded pending appeal within forty-five (45) days from the date such judgment becomes nonappealable.

6.9. CHANGE OF CONTROL. If: (i) except as and to the extent consented to by Lender in writing, Guarantor One shall cease to own, directly or indirectly, all of the issued and outstanding equity interests of Borrower and Guarantor Two; or (ii) except as and to the extent consented to by Lender in writing, either Guarantor or Borrower shall merge with, or consolidate into, any other corporation, partnership, company or other entity (except for a merger of Borrower or Guarantor Two into Guarantor One if Guarantor One is the surviving corporation); or (iii) either Guarantor or Borrower shall sell all, or substantially all, of its assets.

6.10. LOSS OF COLLATERAL. If all or any material portion of the Collateral: (i) suffers any loss, damage, theft or other casualty, in a single occurrence or series of related occurrences not fully covered by insurance as prescribed in Section 5.6 (provided that Borrower shall have the right to cure one such loss in an amount not in excess of \$250,000 by either prepaying the Term Loans, together with any applicable prepayment premium pursuant to Section 2.6 hereof, in such amount as Lender determines to be necessary in connection with such loss or providing to Lender substitute collateral satisfactory to Lender in all respects in which Lender shall have a first priority security

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interest); or (ii) becomes subject to any lien, claim or encumbrance not being contested, in good faith, and, in any event, removed within ninety (90) days of its imposition; or (iii) is made the subject of any proceeding in which the existence, scope, coverage, or priority of the security interest of Lender therein is disputed by the Borrower or Guarantor.

6.11. GUARANTOR. If either Guarantor shall default in its observance or performance of any term of its guaranty of the Obligations set forth in Section 2.10 hereof.

6.12. MATERIAL AGREEMENTS. If (a) Borrower or Guarantor Two shall default in the payment or performance of the Intercompany Lease or (b) Borrower or a Guarantor shall default in the payment or performance of any Material Agreement (other than the Intercompany Lease) which default described in this clause (b) entitles the other party or parties thereto to terminate or repudiate such contract.

6.13. MATERIAL ADVERSE EFFECT. The occurrence of any Material Adverse Effect.

6.14. FINANCIAL DEFAULTS.

(a) If Guarantor One's Net Worth (as defined below and measured quarterly) shall be less than: (i) \$155,000,000 at any time from the Closing Date through January 31, 2000, (ii) \$160,000,000, at any time from February 1, 2000 through January 31, 2001 or (iii) \$175,000,000 at any time from and after January 31, 2001.

(b) If Guarantor One's Fixed Charge Coverage Ratio (as defined below) shall be less than: (i) 1.50:1, for each fiscal quarter during Guarantor One's fiscal year ended January 31, 2000, (ii) 1.75:1.00 for each fiscal quarter during Guarantor One's fiscal year ending January 31, 2001 or (iii) 1.85:1.00 for each fiscal quarter of Guarantor One thereafter.

The tests described in this Section 6.13 shall be measured quarterly, at the end of each fiscal quarter of Guarantor One, on a consolidated basis, for Guarantor One and its consolidated Subsidiaries. In addition thereto:

(a) "NET WORTH" shall mean total shareholder's equity, as determined in accordance with GAAP; and

(b) "FIXED CHARGE COVERAGE RATIO" shall mean the ratio which:

(i) the net income of Guarantor One and its consolidated Subsidiaries, determined without regard to any extraordinary gains or losses, plus the following, to the extent included in the computation thereof, taxes, interest expense, depreciation and amortization and rent/operating lease expenses, determined on a rolling four (4) quarters' basis, bears to (ii) the sum of interest expense of Guarantor One and its consolidated Subsidiaries, plus the current maturities of long-term debt (including capital leases) of Guarantor One and its consolidated Subsidiaries plus cash paid for rent/operating leases of Guarantor One and its consolidated Subsidiaries, each for the same four fiscal quarters.

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An example computation of each such test is set forth on Exhibit D attached hereto.

7. REMEDIES. Upon the occurrence or existence of any Event of Default, or at any time thereafter, without prejudice to the rights of Lender to enforce its claims against each Guarantor and Borrower for damages for failure by Guarantors and Borrower to fulfill any of their obligations hereunder, subject only to prior receipt by Lender of payment in full of all Obligations then outstanding in a form acceptable to Lender, Lender shall have all of the rights and remedies described in Sections 7.1 through 7.4, inclusive, and it may exercise any one, more, or all of such remedies, in its sole discretion, without thereby waiving any of the others.

7.1. ACCELERATION OF THE OBLIGATIONS. Lender, at its option, may declare all of the Obligations (including but not limited to that portion thereof evidenced by the Term Notes) to be immediately due and payable, whereupon the same shall become immediately due and payable without presentment, demand, protest, notice of nonpayment or any other notice required by law relative thereto, all of which are hereby expressly waived by Borrower, anything contained herein to the contrary notwithstanding and, in connection therewith, if Lender so elects, by further written notice to Borrower, Lender may increase the rate of interest charged on each Term Note then outstanding for so long thereafter as Lender further shall elect to the Default Rate. Thereafter, Lender, at its option, may, but shall not be obligated to, accept less than the entire amount of Obligations due, if tendered, provided, however, that unless then agreed to in writing by Lender, no such acceptance shall or shall be deemed to constitute a waiver of any Event of Default or a reinstatement of any commitments of Lender hereunder.

7.2. REMEDIES OF A SECURED PARTY. Lender shall thereupon have the rights and remedies of a secured party under the UCC in effect on the date thereof (regardless of whether the same has been enacted in the jurisdiction where the rights or remedies are asserted), including, without limitation, the right to take possession of any of the Collateral or the proceeds thereof, to sell or otherwise dispose of the same, to apply the proceeds therefrom to any of the Obligations in such order as Lender, in its sole discretion, may elect. Lender shall give Borrower and Guarantors written notice of the time and place of any public sale of the Collateral or the time after which any other intended disposition thereof is to be made. The requirement of sending reasonable notice shall be met if such notice is given to Borrower and Guarantors pursuant to Section 8.9 at least ten (10) days before such disposition. Expenses of retaking, holding, insuring, preserving, protecting, preparing for sale or selling or the like with respect to the Collateral shall include, in any event, reasonable attorneys' fees and other legally recoverable collection expenses, all of which shall constitute Obligations.

7.3. REPOSSESSION OF THE COLLATERAL. Lender may take the Collateral or any portion thereof into its possession, by such means (without breach of the peace) and through agents or otherwise as it may elect (and, in connection therewith, demand that Borrower and Guarantors assemble the Collateral at a place or places and in such manner as Lender shall prescribe), and sell, lease or otherwise dispose of the Collateral or any portion thereof in its then condition or following any commercially reasonable preparation or processing, which disposition may be by public or private proceedings, by one or more contracts, as a unit or in parcels, at any time and place and on any

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terms, so long as the same are commercially reasonable. To facilitate the foregoing, Borrower and Guarantors agree to make available to Lender the Distribution Center or any other premises then owned or leased by Borrower or a Guarantor on which any Collateral then may be situated for such purposes, without charge or undue delay, and on such terms as Lender then may reasonably request (including, without limitation, if Lender so requests, the temporary or permanent vacation by Borrower or a Guarantor of any leased premises).

7.4. OTHER REMEDIES. Unless and except to the extent expressly provided for to the contrary herein, the rights of Lender specified herein shall be in addition to, and not in limitation of, Lender's rights under the UCC, as amended from time to time, or any other statute or rule of law or equity, or under any other provision of any of the Loan Documents, or under the provisions of any other document, instrument or other writing executed by Borrower, a Guarantor or any third party in favor of Lender, all of which may be exercised successively or concurrently.

7.5. NOTICE TO GUARANTORS. Lender shall send to each Guarantor in the manner provided in Section 8.9 a copy of any written notice of the occurrence of an Event of Default which it sends to Borrower.

#### 8. MISCELLANEOUS.

8.1. WAIVER. Each and every right granted to Lender under this Agreement, or any of the other Loan Documents, or any other document delivered hereunder or in connection herewith or allowed it by law or in equity, shall be cumulative and may be exercised from time to time. No failure on the part of Lender to exercise, and no delay in exercising, any right shall operate as a waiver thereof, nor shall any single or partial exercise by Lender of any right preclude any other or future exercise thereof or the exercise of any other right. No waiver by Lender of any Default Condition or Event of Default shall constitute a waiver of any subsequent Default Condition or Event of Default.

8.2. GOVERNING LAW. THIS AGREEMENT AND, UNLESS OTHERWISE EXPRESSLY PROVIDED THEREIN, THE TERM NOTES AND THE OTHER LOAN DOCUMENTS, AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES HEREUNDER AND THEREUNDER, SHALL BE GOVERNED BY, AND CONSTRUED AND INTERPRETED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF ILLINOIS.

8.3. SURVIVAL. All representations, warranties and covenants made herein and in the other Loan Documents shall survive the execution and delivery of this Agreement and such other Loan Documents. On the Closing Date, each Guarantor and Borrower shall be deemed to have restated, renewed and reaffirmed as of each such date all of such representations, warranties and covenants. The terms and provisions of this Agreement shall continue in full force and effect, notwithstanding the payment of the Term Notes, until all of the Obligations have been paid in full and Lender has terminated this Agreement in writing.

8.4. NO ASSIGNMENT BY EITHER GUARANTOR OR BORROWER; LENDER MAY ASSIGN. No assignment hereof shall be made by either Guarantor or Borrower without the prior written consent of Lender. Lender may assign, or sell participations in, its right, title and interest herein and in the Loan Documents at any time hereafter without notice to or consent of either Guarantor or Borrower to any Participant having at least Fifty Million Dollars (\$50,000,000) in assets and with the written consent of Guarantors and Borrower, to any Participant. Upon any assignment by Lender, the assignee shall be entitled to all the rights, powers, privileges and remedies of Lender to the extent assigned, and the obligations of each Guarantor or Borrower shall not be subject, as against any such assignee, to any defense, set-off or counterclaim available to Guarantor or Borrower against Lender and any such defense, set-off or counterclaim may be asserted only against Lender.

8.5. COUNTERPARTS. This Agreement may be executed in two or more counterparts, each of which when fully executed shall be an original, and all of said counterparts taken together shall be deemed to constitute one and the same agreement.

8.6. REIMBURSEMENT. Guarantors and Borrower, jointly and severally,

agree to reimburse Lender for its out-of-pocket expenses, actually incurred, including, without limitation, the reasonable fees and disbursements of its legal counsel (including a reasonable allocation of the costs, compensation and expenses of internal counsel), incurred in connection with the preparation of the Loan Documents and any and all other documents, notes, and agreements pursuant hereto, including the furnishing of any opinions which may be requested of such counsel by the Lender on questions incident to this transaction, which costs, exclusive of survey, title insurance and appraisal costs, are not expected to exceed \$20,000. Guarantors and Borrower will pay all expenses incurred by Guarantors and Borrower in this transaction. If any taxes, fees or other costs shall be payable on account of the execution, issuance, delivery or recording of any of the Loan Documents, by reason of any existing or hereafter enacted federal or state statute, Guarantors and Borrower, jointly and severally, agree to pay all such taxes (other than taxes imposed on or measured by Lender's net income), fees or other costs, including any applicable interest and penalty, and to indemnify and hold Lender harmless from and against liability in connection therewith. If any attorney (including, without limitation, internal counsel) is engaged (a) to collect the Obligations, whether or not legal proceedings are thereafter instituted by Lender, (b) to represent Lender in any bankruptcy, reorganization, receivership or other proceedings affecting creditors' rights and involving a claim under this Agreement or any of the other Loan Documents, (c) to protect the lien of the Mortgage or any of the other Loan Documents, (d) to represent Lender in any other proceedings whatsoever in connection with this Agreement, the Mortgages or any other Loan Documents, including, without limitation, post judgment proceedings to enforce any judgment related to the Loan Documents, or (e) in connection with seeking of an out-of-court workout or settlement of any of the foregoing, then Guarantors and Borrower, jointly and severally, agree to pay to Lender all costs, attorneys' fees and expenses in connection therewith (including a reasonable allocation of the costs, compensation and expenses of internal counsel), in addition to all other amounts due hereunder. This provision is separate and several and shall survive the merger of this provision into any judgment.

8.7. SUCCESSORS AND ASSIGNS. This Agreement and every Loan Document shall be binding upon and inure to the benefit of the successors and permitted assigns of the parties hereto and

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thereto. The foregoing shall expressly include, without limitation, in the case of Lender, any Participant.

8.8. SEVERABILITY. If any provision of this Agreement or of the Loan Documents or the application thereof to any party thereto or circumstances shall be invalid or unenforceable to any extent, the remainder of such Loan Documents and the application of such provisions to any other party thereto or circumstance shall not be affected thereby and shall be enforced to the greatest extent permitted by law.

8.9. NOTICES. All notices, requests and demands to or upon the respective parties hereto shall be deemed to have been given or made when personally delivered or deposited in the mail, registered or certified mail, postage prepaid, or delivered by overnight courier, addressed as follows or to such other address as may be designated hereafter in writing by the respective parties hereto (which, in the case of Lender, may include the name and address of each Participant):

Guarantor or Borrower:

The Gymboree Corporation  
700 Airport Boulevard  
Suite 200  
Burlingame, California 94010  
Attn: President

With a copy to:

Bartko, Zenkel, Tarrant & Miller  
Attorneys at Law  
900 Front Street  
Suite 300  
San Francisco, California 94111

Attn: Thomas E. Cooper, Esq.

Lender:

Transamerica Business Credit Corporation  
Two Ravinia Drive, Suite 700  
Atlanta, Georgia 30346  
Attn: Region Credit Manager

except in cases where it is expressly provided herein or by applicable law that such notice, demand to request is not effective until received by the party to whom it is addressed.

8.10. ENTIRE AGREEMENT - AMENDMENT. This Agreement, together with the Term Notes and the other Loan Documents, constitute the entire agreement between the parties hereto with respect to the subject matter hereof and thereof and supersedes any agreement or understanding, oral

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or written, heretofore made in regard thereto. Neither this Agreement, the Term Notes nor any other Loan Document may be changed, waived, discharged, modified or terminated orally, but only by an instrument in writing signed by the party against whom enforcement is sought.

8.11. TIME OF THE ESSENCE. Time is of the essence in this Agreement, the Term Notes and the other Loan Documents.

8.12. INTERPRETATION. No provision of this Agreement or any Loan Document shall be construed against or interpreted to the disadvantage of any party hereto by any court or other governmental or judicial authority by reason of such party having or being deemed to have structured or dictated such provision.

8.13. LENDER NOT A JOINT VENTURER. Neither this Agreement nor any agreements, instruments, documents or transactions contemplated hereby (including the Loan Documents) shall in any respect be interpreted, deemed or construed as making Lender a partner or joint venturer with either Guarantor or Borrower or as creating any similar relationship or entity, and Guarantors and Borrower each agree that they will not make any contrary assertion, contention, claim or counterclaim in any action, suit or other legal proceeding involving Lender and either Guarantor or Borrower.

8.14. JURISDICTION. GUARANTORS AND BORROWER AGREE THAT ANY LEGAL ACTION OR PROCEEDING WITH RESPECT TO THIS AGREEMENT, THE TERM NOTES OR ANY OTHER LOAN DOCUMENT MAY BE BROUGHT IN THE COURTS OF THE STATE OF ILLINOIS OR THE UNITED STATES OF AMERICA FOR THE NORTHERN DISTRICT OF ILLINOIS, CHICAGO DIVISION, ALL AS LENDER MAY ELECT. BY EXECUTION OF THIS AGREEMENT, EACH GUARANTOR AND BORROWER HEREBY SUBMITS TO EACH SUCH JURISDICTION, HEREBY EXPRESSLY WAIVING WHATEVER RIGHTS MAY CORRESPOND TO IT BY REASON OF ITS PRESENT OR FUTURE DOMICILE AND CONSENTS TO SERVICE OF PROCESS BY WRITTEN NOTICE GIVEN IN THE MANNER SPECIFIED FOR THE GIVING OF NOTICES IN SECTION 8.9 ABOVE; PROVIDED, HOWEVER, THAT NOTHING HEREIN SHALL AFFECT THE RIGHT OF LENDER TO COMMENCE LEGAL PROCEEDINGS OR OTHERWISE PROCEED AGAINST EITHER GUARANTOR OR BORROWER IN ANY OTHER JURISDICTION OR TO SERVE PROCESS IN ANY MANNER PERMITTED OR REQUIRED BY LAW. EACH OF LENDER, EACH GUARANTOR AND BORROWER WAIVES ANY RIGHT TO A TRIAL BY JURY IN ANY SUCH PROCEEDING. EACH GUARANTOR AND BORROWER FURTHER AGREES THAT LENDER SHALL NOT BE LIABLE TO IT FOR CONSEQUENTIAL OR SPECIAL DAMAGES ARISING FROM BREACH OF CONTRACT, TORT OR OTHER WRONG OR CLAIM RELATING TO THE ESTABLISHMENT, ADMINISTRATION OR COLLECTION OF ANY OBLIGATIONS OR ANY LOAN DOCUMENT OR ANY ACTION (OR INACTION) BY LENDER THEREUNDER.

8.15. PAYMENT ON NON-BUSINESS DAYS. Whenever any payment to be made hereunder or under the Term Notes shall be stated to be due on a Saturday, Sunday or a public holiday under the

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laws of the State of Georgia or the State of Illinois, such payment may be made

on the next succeeding Business Day, and such extension of time shall in such case be included in the computation of payment of interest hereunder or under the Term Notes.

8.16. WAIVER OF RIGHTS. EXCEPT AS EXPRESSLY PROVIDED IN THIS AGREEMENT, EACH GUARANTOR AND BORROWER HEREBY WAIVES ANY AND ALL RIGHTS, IF ANY, WHICH EITHER GUARANTOR AND BORROWER OTHERWISE HAS OR MAY HAVE UNDER AND BY VIRTUE OF ANY LAW, WITH RESPECT TO THE RIGHT OF EITHER GUARANTOR OR BORROWER TO NOTICE AND TO A JUDICIAL OR ADMINISTRATIVE HEARING PRIOR TO SEIZURE OF ANY COLLATERAL BY LENDER.

8.17. CURE OF DEFAULTS BY LENDER. If, hereafter, either Guarantor or Borrower defaults in the performance of any duty or obligation to Lender hereunder, Lender may, at its option, but without obligation, cure such default and any costs, fees and expenses incurred by Lender in connection therewith including, without limitation, for the purchase of insurance, the payment of taxes and the removal or settlement of liens and claims, shall constitute Obligations, be payable on demand and bear interest until paid at the Default Rate applicable to the Term Note with the then highest contract rate.

8.18. RECITALS. All recitals contained herein are hereby incorporated by reference into this Agreement and made part thereof.

8.19. ATTORNEY-IN-FACT. Each Guarantor and Borrower hereby designates, appoints and empowers Lender irrevocably to act as its attorney-in-fact, at such Guarantor's and Borrower's cost and expense, to do in the name of such Guarantor and Borrower any and all actions which Lender may deem necessary or advisable to carry out the terms hereof, upon the failure, refusal or inability of such Guarantor or Borrower to do so, and each Guarantor and Borrower hereby, jointly and severally, agrees to indemnify and hold Lender harmless from any costs, damages, expenses or liabilities arising against or incurred by Lender in connection therewith.

8.20. SOLE BENEFIT. The rights and benefits set forth in this Agreement and in all the other Loan Documents are for the sole and exclusive benefit of Lender, its Participants (if any), each Guarantor and Borrower and may be relied upon only by them.

8.21. REMEDIES. UNLESS EXPRESSLY PROVIDED TO THE CONTRARY, LENDER MAY ENFORCE ITS RIGHTS UNDER THIS AGREEMENT AND ALL OTHER LOAN DOCUMENTS WITHOUT RESORT TO PRIOR JUDICIAL PROCESS OR JUDICIAL HEARING, AND EACH GUARANTOR AND BORROWER EXPRESSLY WAIVES, RENOUNCES AND KNOWINGLY RELINQUISHES ANY LEGAL RIGHT WHICH MIGHT OTHERWISE REQUIRE LENDER TO ENFORCE ITS RIGHTS BY JUDICIAL PROCESS. IN SO PROVIDING FOR A NON-JUDICIAL REMEDY, EACH GUARANTOR AND BORROWER RECOGNIZES AND CONCEDES THAT SUCH A REMEDY IS CONSISTENT WITH THE USAGE OF THE TRADE, IS RESPONSIVE TO COMMERCIAL NECESSITY AND IS THE RESULT OF BARGAINING AT ARM'S LENGTH. NOTHING IN THIS AGREEMENT IS

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INTENDED TO PREVENT EITHER GUARANTOR, BORROWER OR LENDER FROM RESORTING TO JUDICIAL PROCESS AT ANY PARTY'S OPTION.

8.22. INDEMNITY. Without limiting any provisions of Sections 5.10 or 8.6, Guarantors and Borrower, jointly and severally, agree to save, indemnify and hold harmless Lender from and against any and all debts, liabilities, obligations, damages, costs, expenses or other claims incurred by Lender as a result of its entry into, and performance under, this Agreement or any other Loan Documents, including, without limitation, with respect to the claims of any broker or other intermediary, other than any of the foregoing resulting directly from Lender's gross negligence or willful misconduct.

8.23. ACCEPTANCE. THIS AGREEMENT, TOGETHER WITH THE TERM NOTES AND ALL OTHER LOAN DOCUMENTS, SHALL NOT BECOME EFFECTIVE UNLESS AND UNTIL (I) DULY EXECUTED BY EACH GUARANTOR AND BORROWER, (II) DELIVERED TO LENDER FOR ACCEPTANCE IN CHICAGO, ILLINOIS, (III) ACCEPTED BY LENDER IN CHICAGO, ILLINOIS AND (IV) DULY EXECUTED BY LENDER, AS APPROPRIATE, IN CHICAGO, ILLINOIS. THE DISBURSEMENT OF THE PROCEEDS OF THE TERM LOANS BY LENDER SHALL BE EVIDENCE THAT THE FOREGOING CONDITIONS HAVE BEEN FULFILLED.

9. CONDITIONS PRECEDENT. Unless waived in writing by Lender at or prior to the execution and delivery of this Agreement, the conditions set forth below

shall constitute express conditions precedent to any obligation of Lender hereunder:

(a) NO INJUNCTION; ETC. No action, proceeding, investigation, regulation or legislation shall have been instituted, threatened or proposed before any court, governmental agency or legislative body to enjoin, restrain, or prohibit, or to obtain substantial damages in respect of, or which is related to or arises out of this Agreement, or the consummation of the transactions contemplated hereby, or which Lender determines would make it inadvisable to consummate the transactions contemplated hereby.

(b) NO DEFAULT. Lender shall have determined that no Default Condition or Event of Default shall have occurred and be continuing.

(c) COMPLIANCE WITH LAWS GENERALLY; ENVIRONMENTAL LAW COMPLIANCE. Lender shall be satisfied in all respects that Borrower and Guarantors are in material compliance with all applicable federal, state and local laws and regulations, including particularly, but without limitation, all Environmental Laws.

(d) MATERIAL AGREEMENTS. Lender shall have reviewed all of Borrower's and Guarantors' Material Agreements, and all of the foregoing shall be satisfactory to Lender.

(e) LITIGATION. Lender shall have reviewed all existing litigation, injunctions and proceedings, if any, pending or threatened against Borrower and Guarantors and the results of such review shall be satisfactory to Lender.

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(f) NO MATERIAL ADVERSE CHANGE. Lender shall determine that no Material Adverse Change has occurred. Without limitation of the foregoing, Guarantor One's loss for its third quarter of its fiscal year ending January 31, 1999 shall not exceed \$.03 per share.

(g) DOCUMENTATION. Lender shall have received the following documents, each to be in form and substance satisfactory to Lender and its counsel, and duly executed and delivered by the party or parties thereto:

(1) LOAN DOCUMENTS. This Agreement and all other Loan Documents to be executed and delivered by Borrower and Guarantors hereunder and under the Loan Documents on the Closing Date, to the extent not otherwise specified below;

(2) INSURANCE CERTIFICATES. Receipt by Lender of a certificate from Borrower's insurer (or an authorized agent thereof) respecting all insurance required hereunder, together with copies of all insurance policies evidencing such insurance in each case in form and substance acceptable to Lender.

(3) AUTHORIZED OFFICER CERTIFICATES. Receipt by Lender of certificates from Authorized Officers of Borrower and Guarantors, certifying as to their respective partnership agreements or certificates or articles of incorporation and bylaws, as applicable, and authority to consummate the transactions contemplated hereby;

(4) TERM NOTES. Receipt by Lender of Term Notes in an aggregate principal amount equal to the aggregate principal amount of the Term Loans;

(5) FINANCING STATEMENTS. Copies of all filing receipts or acknowledgments issued by any Governmental Authority to evidence any filing or recordation necessary to perfect the security interests of Lender in all Collateral and evidence in a form acceptable to Lender that such security interests constitute value and perfected first priority security interests in Lender's favor;

(6) APPRAISAL. An appraisal, performed at Borrower's expense, of the Real Estate Collateral, by a nationally recognized independent appraiser selected by Borrower, but acceptable to Lender, using a methodology of appraisal which is acceptable to Lender.

(7) ENVIRONMENTAL ASSESSMENT. As environmental regulatory review for the Real Estate Collateral, prepared at Borrowers' expense, by independent

environmental experts selected by Lender, together with, if Lender shall so request in its sole discretion, based on the results of such environmental regulatory review, "Phase 1" environmental audits and such additional environmental testing as Lender shall so require with respect to the Real Estate Collateral, performed at Borrower's expense by independent environmental experts selected by Lender (which conditions Lender acknowledges have been satisfied);

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(8) SURVEY. A current "as-built" boundary survey for the Real Estate Collateral together with a surveyor's certificate prepared at Borrower's expense from a registered land surveyor;

(9) MORTGAGE. A deed of trust, mortgage, deed to secure debt or other, similar instrument pursuant to which Borrower shall convey to Lender or to a trustee for the benefit of Lender the entirety of its right, title and interest in and to the Real Estate Collateral.

(10) MORTGAGEE'S TITLE INSURANCE POLICIES. A mortgagee's title insurance policy, issued, at Borrower's expense, by a title insurer selected by Borrower, but acceptable to Lender insuring Lender's security interest in the Real Estate Collateral in such amount, and containing only such conditions, limitations and exception as shall be acceptable to Lender;

(11) EVIDENCE OF INSURANCE. Evidence that the Distribution Center is covered by the insurance required under Section 5.6 and in the other Loan Documents and as otherwise may be reasonably required by Lender in connection with the disbursement of the Term Loans; and

(12) OTHER DOCUMENTS. Such other document, instruments, agreements and certificates as Lender shall require.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed and Borrower has caused its seal to be affixed hereto, all as of the day and year first above written.

"LENDER"

TRANSAMERICA BUSINESS CREDIT CORPORATION

By:

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Name: -----  
Title: -----

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"GUARANTOR ONE"

THE GYMBOREE CORPORATION (SEAL)

By: /s/ GARY WHITE

-----  
Name: Gary White  
Title: President

Attest:

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Name:  
Title:

"GUARANTOR TWO"

GYMBOREE MANUFACTURING, INC. (SEAL)

By: /s/ GARY WHITE

-----  
Name: Gary White  
Title: President

Attest:

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Name:  
Title:

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"BORROWER"

GYMBOREE LOGISTICS (SEAL)  
PARTNERSHIP

By: Gymboree Retail Stores, Inc., Partner

By: /s/ GARY WHITE

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Gary White  
Partner

By: The Gymboree Stores, Inc., Partner

By: /s/ GARY WHITE

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Gary White  
President

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EXHIBIT A

Permitted Encumbrances

1. In regard to the Real Estate Collateral, those matters identified as "Permitted Encumbrances" in the Mortgage.
2. Financing Statement No. 9827360784 and 9827360789 filed September 25, 1998 with the Secretary of State of California covering one new 1998 Marathon Horizontal Bailer (S/N 108648), one used Komatsu Model FG25ST-3 Forklift (S/N FG25ST-8) and proceeds of such collateral.

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EXHIBIT B

Subsidiaries

Detail Not Required.

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EXHIBIT C

Litigation

Detail Not Required.

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EXHIBIT D

Financial Test Computations

Detail Not Required.

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THE GYMBOREE CORPORATION  
SUMMARY OF TERMS AND CONDITIONS

MARCH 9, 1999

THIS SUMMARY OF TERMS AND CONDITIONS ("TERM SHEET") INDICATES OUR COMMITMENT TO EXTEND CREDIT AS DESCRIBED IN GENERAL TERMS BELOW ("CREDIT FACILITY"). HOWEVER, IT DOES NOT ATTEMPT TO DESCRIBE ALL OF THE TERMS AND CONDITIONS THAT WOULD PERTAIN TO THE CREDIT FACILITY. INSTEAD, IT IS INTENDED TO OUTLINE BASIC BUSINESS PARAMETERS TO FACILITATE OUR FURTHER DISCUSSIONS.

**BORROWER:** The Gymboree Corporation, and certain subsidiaries ("TGC")

**GUARANTORS:** As required in the existing Agreement.

**LENDER:** Bank of America National Trust and Savings Association (in such capacity, the "Bank").

**PURPOSE:** To finance merchandise importation (through commercial and usance L/Cs), working capital (through funded advances) and rent guarantees (through SBLCs).

**CREDIT FACILITY:** \$100 million revolving Credit Facility with a maturity date of 3/31/2001, with the following quarterly usage limits:

- \$ 68 million through 4/30/99
- \$100 million from 5/1/99 through 7/31/99
- \$ 80 million from 8/1/99 through 12/31/99
- \$ 68 million from 1/1/2000 through 4/30/2000
- \$100 million from 5/1/2000 through 7/31/2000
- \$ 80 million from 8/1/2000 through 3/31/2001

In addition, the following sub-limits will apply:

(A) Commercial L/C sub-limit (with tenors on Commercial L/C's up to 180 days from issuance, drafts payable at sight): difference between the usage limit above, the \$25 million Funded Advance/Usance L/C facility and outstanding Standby Letters of Credit.

(B) \$25 million Funded Advances and Usance Letters of Credit sub-limit (with tenors on Usance Letters of Credit up to 180 days from issuance, with drafts payable at up to 180 days from sight).

(C) \$10 million Standby Letter of Credit sub-limit (with tenors up to one year from issuance).

**REPAYMENT:** Sub-limit (A) & (C): Upon negotiation of documents.  
Sub-limit (B) Funded Advances: Interest monthly with principal due at maturity.  
Sub-limit (B) Usance L/C: At maturity.

**MATURITY/EXPIRATION:** Availability under the Credit Facility through 3/31/2001, with no instruments to mature later than 9/30/2001.

**INTEREST RATES:** Interest rates on the Funded Advance sub-limit (B) of the Credit Facility will be as follows:

- (i) Bank of America's Reference Rate or

(ii) LIBOR plus the applicable margin determined by the attached Variable Pricing Grid.

COMMITMENT FEE: An up front commitment fee of \$50,000 per annum, payable semi-annually in advance. Payable on acceptance of this commitment or 3/12/99, whichever is earlier, and semiannually thereafter.

UNUSED COMMITMENT FEE: A fee of 0.10% per annum, calculated on the unused portion of sub-limit (B) (outstanding Usance Letters of Credit would not reduce the unused portion for purposes of calculating this fee), and payable quarterly in arrears.

OTHER FEES: Commercial L/Cs, Usance L/Cs and SBLCs at pricing agreed to with Bank's trade finance group.  
  
An early Termination fee of 1/16% will be charged on any portion of the Credit Facility canceled by TGC prior to maturity which is not refinanced by the Bank.

ALLOCATIONS: TGC must specify in advance any portion of sub-limit (B) which it will use for usance L/C's. TGC, upon at least five days written notice to the Bank, may request reallocation from any unused allocation of sub-limit (B).

FINANCIAL COVENANTS: TANGIBLE NET WORTH  
-----  
TGC to maintain a minimum tangible worth, measured at each of TGC's fiscal quarter ends as follows:

(in millions)

	1/31/99	4/30/99	7/31/99	10/31/99	1/31/2000
Projected	169	174	173	176	188
COVENANT	166	168	166	168	179

Starting 1/31/2000, TGC to maintain an actual starting Tangible Net Worth (of at least \$183 Million) plus 80% of TGC's consolidated positive quarterly Net Income (which shall not be reduced by any quarterly losses).

Tangible Net Worth defined as the gross book value of TGC's assets (excluding goodwill, patents, trademarks, trade names, organization expense, treasury stock, unamortized debt discount and expense, deferred research and development costs, deferred marketing expenses, and other like intangibles, and monies from subsidiaries, affiliates, officers, directors, or shareholders of TGC but including the aggregate book value of TGC's lease rights up to a maximum aggregate value of \$2.5 million for all such lease rights), less total

liabilities (including but not limited to accrued and deferred income taxes, and excluding liabilities related to redeemable preferred stock) and any reserves against assets, less any proceeds of equity capital raised during the year.

SEASONAL CLEAN DOWN  
TGC to maintain a ratio of cash plus short-term investments, including credit card receivables up to \$5 million, to total letters of credit (commercial, usance

and standby) outstanding plus borrowings under the Funded Advance facility, of at least 0.85:1, for the last two fiscal month-ends of fiscal years 1999 and 2000. In addition the following will apply in the event the ratio is less than 1.00:1:

- o TGC must pay a fee of \$10,000 per reporting period that the ratio is less than 0.90:1 but greater than or equal to 0.85:1.
- o TGC must pay a fee of \$5,000 per reporting period that the ratio is less than 1.00:1 but greater than or equal to 0.90:1.

LIMITATIONS ON CAPITAL EXPENDITURES

TGC shall not incur capital expenditures in excess of \$40 million for the fiscal year 1999, without the prior written consent of the Bank. Additionally, TGC shall not commit to capital expenditures in excess of \$20 million for each of the fiscal years 2000 and 2001, without the prior written consent of the Bank.

TGC shall not enter into any joint venture, merger, acquisition or purchase of a business or its assets during any fiscal year, for consideration over \$5 million, without the Bank's prior consent.

REPORTING COVENANTS:

CPA audited FYE consolidated financial statements

(including 10-K) due within 120 days of FYE, with an unqualified opinion. CPA management letter within 30 days of receipt. TGC prepared consolidating schedules including Balance Sheet, Income Statement and Statement of Cash Flows.

Quarterly TGC prepared consolidated and consolidating financial statements (Balance Sheet, Income Statement and Statement of Cash Flows), 10-Q and Compliance Certificate, due within 45 days of period end.

Monthly TGC prepared consolidated financial statements (Balance Sheet, Income Statement and Statement of Cash Flows), due within 30 days of month-end except for the final month of the fiscal year, which will be due within 60 days of month-end.

Annual TGC prepared projections (Balance Sheet, Income Statement and Statement of Cash Flows) for the upcoming fiscal year within 60 days of FYE; revised projections, including all material adjustments made to the projections, as they occur.

REPRESENTATIONS AND WARRANTIES:

All representations and warranties remain materially unchanged from the existing credit facility

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OTHER TERMS AND CONDITIONS:

A new Amended and Restated Loan Agreement will be documented which will contain language reflecting a Syndicated Credit with the Bank as Agent and permitting assignments under the Agreement. All other terms and conditions remain materially unchanged from the existing credit facility.

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VARIABLE PRICING GRID

If at the end of any fiscal quarter, TGC's Tangible Net Worth (as defined) is equal to or greater than I below, the applicable margin for the following quarter will be 75 BASIS POINTS.

If at the end of any fiscal quarter, TGC's Tangible Net worth is less than I., but greater than or equal to II. below, the applicable margin for the following quarter will be 87.5 BASIS POINTS.

If at the end of any fiscal quarter, TGC's Tangible Net worth is less than II., but greater than or equal to III. below, the applicable margin for the following quarter will be 100 BASIS POINTS.

Tangible Net Worth as defined in the Summary of Terms and Conditions.  
(in millions of dollars)

QUARTER-ENDED:	I.	II.	III.
04/30/1999	174	171	168
07/31/1999	173	171	166
10/31/1999	176	172	168
01/31/2000	187	183	179
04/30/2000	191	187	Min TNW Cov.
07/31/2000	191	187	Min TNW Cov.
10/31/2000	193	189	Min TNW Cov.
01/31/2001	203	198	Min TNW Cov.

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## COMPUTATION OF INCOME PER SHARE

(In thousands, except per share data)	FISCAL YEAR ENDED		
	January 30, 1999	January 31, 1998	February 2 1997
NET INCOME	\$6,241	\$35,170	\$31,788
Weighted average number of shares of Common Stock outstanding during the period:			
Common Stock	24,164	24,302	25,111
Add incremental shares from assumed exercise of stock options	63	698	559
Weighted average common and common equivalent shares outstanding	24,227	25,000	25,670
BASIC INCOME PER SHARE	\$0.26	\$1.45	\$1.27
DILUTED INCOME PER SHARE	\$0.26	\$1.41	\$1.24

## THE GYMBOREE CORPORATION

## FINANCIAL HIGHLIGHTS

Fiscal year (In thousands, except stores and per share amounts)	1998	1997	1996
<b>OPERATING RESULTS:</b>			
Net sales	\$457,219	\$373,440	\$303,111
Operating income	9,454	53,884	47,593
Net income	6,241	35,170	31,788
Net income as a percentage of sales	1.4%	9.4%	10.5%
Diluted income per share	\$ 0.26	\$ 1.41	\$ 1.24
<b>BALANCE SHEET DATA:</b>			
Working capital	\$ 76,314	\$ 71,590	\$105,190
Total assets	256,705	229,200	216,909
Long term debt	11,460	0	0
Total stockholders' equity	\$168,372	\$157,710	\$161,933
<b>STORES OPEN AT YEAR END:</b>	564	435	354

## TO OUR STOCKHOLDERS:

Looking back over 1998, despite disappointing results, I see several bright spots. Like a child who falls, we stumbled in 1998 and performed below expectations. However, as the child gets up and back in the game, all of us in management and throughout the organization have learned tough lessons and are up and running again.

Our progress in 1998 positioned us well for 1999. Gymboree's net sales grew 22%, to \$457.2 million in 1998 from \$373.4 million in 1997. Our store count increased to 564 from 435, including 18 new stores in Europe and 4 in Canada. We opened our new distribution center in Dixon, California, enabling us to manage product flow efficiently for all our United States stores. Our balance sheet remained strong, and we plan to fund our growth with cash generated by our operations for the foreseeable future. We continued work on our Zutopia launch and our first 10 stores opened in March 1999. We hired or promoted strong managerial leadership. Our products continued to enjoy strong consumer acceptance during the year. Our play programs grew significantly, and we look forward to continued expansion of this core business.

## INVENTORY CHALLENGES

The primary problem experienced during 1998 can be summed up in one word: inventory. Over-optimism and the desire to drive growth by higher inventory purchases proved incorrect. Furthermore, we found certain styles, particularly in boyswear, were not as popular as we had anticipated. These factors adversely affected results because we had to cut prices to

move merchandise out of the way of incoming products. The inevitable outcome was that profits were down, even as gross sales were up.

Typically, we mark down prices when a line has become "broken," meaning only a few sizes of each item are still available. This was not the case during 1998. Instead, even when products were well received and selling at full price, we were forced to cut prices to clear shelves and racks. There is no worse feeling for a merchant than to hang sale tags on merchandise while it is selling through at full price, and we do not intend to see a repeat of this disheartening experience.

The harsh lessons of 1998 led us to improve our inventory management capabilities. In fact, at the end of 1998, our dollar inventory on hand was almost exactly the same as it was at the end of 1997, despite having opened 30% more stores during 1998. Looking forward, we will continue to manage inventories to enable us to capture greater margins on our sales.

#### DISCIPLINED GROWTH

We added 129 new stores in 1998. We plan to open 40 to 50 new stores in 1999, including our new retail concept Zutopia, which is a reduction from our historic growth patterns. Our focus will be on turning new stores into solid contributors as quickly as possible. We will continue to grow our store count until we feel we have covered the areas where there is opportunity to operate profitably.

The Gymboree Gift Center at [www.gymboree.com](http://www.gymboree.com) is an obvious candidate to further expand our channels of distribution and serve electronic commerce customers efficiently and economically. We will also focus new business development resources on investigating the most efficient ways to expand internationally. We are confident that the Gymboree brand holds opportunities not yet tapped.

#### PLAY PROGRAMS A SOLID CONTRIBUTOR

The founding business of Gymboree was play programs for young children. During 1998, we enjoyed the fruits of efforts undertaken in 1997, resulting in strong income growth and expanded numbers of franchise and corporate-owned sites. Income from the play programs increased by 289% in 1998. We have expanded the curriculum and, in 1999, we plan to roll out a fully integrated music program.

#### CLOTHING FOR GENERATION Z

Responding to overwhelming input from parents whose children were outgrowing the Gymboree size range, we are launching our Zutopia line of clothing and accessories, which extends our expertise in design, quality and workmanship to serve the needs of children from six years old to pre-teen. A hip blend of designer, street and alternative

#### THE GYMBOREE CORPORATION

gear, Zutopia products are appropriately styled for these older children. We will include entertaining elements in our Zutopia store, including accessories and toys, decor products, even Internet kiosks to create an environment where youngsters want to spend time. We undertook extensive research with children in our target age range to learn exactly what they want in fashion merchandise. We will shape our merchandise selection and marketing campaigns around what we learned. We believe Zutopia will enable us to serve our loyal Gymboree customers as they grow into young adults.

#### LEADERSHIP TEAM

Leaders with significant industry experience and vision joined our team in critical areas of the company. At the beginning of 1999, our new President, Melanie Cox, assumed responsibility to steer crucial merchandising and product

development efforts. At her side is Lisa Harper, an inspirational head designer who worked with us in the heyday of the early 1990s. We hired Larry Meyer, an experienced Chief Financial Officer in the retail industry. And to ensure the necessary processes are instituted in inventory ordering and allocation, we hired Ed Wong, who has significant experience in vertically integrated, specialty apparel organizations.

Gymboree's three senior team members are Stuart G. Moldaw, Chairman of the Board, Melanie Cox, President, and Gary White, Vice-Chair of the Board and Chief Executive Officer. Together, they have over 90 years experience in retailing to children.

#### LOOKING FORWARD

With a hard year behind us, we are all looking forward to brighter times ahead. We know our shareholders demand nothing less than success from us, and for this reason we have established four business principles which underlie our goals for 1999. They are "Product Innovation", exploring new ways to create and deliver the best products and services to our customers; "Cycle Time", increasing efficiency, improving customer service and reducing costs; "Regular Price Sell Through", minimizing markdowns by delivering products to our stores at the right time in the right amounts; and "Increased Market Share", accelerating customer traffic and the frequency and amount of purchase transactions.

We will continue to use our team approach to set and achieve our goals. We grow by learning from one another and from experience. We look forward to renewed success and improved performance, and we have confidence that we will reward your faith in us in the years ahead.

/S/ GARY WHITE

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GARY WHITE  
Vice-Chair of the Board and Chief Executive Officer  
April 5, 1999

[PICTURE]

THE GYMBOREE CORPORATION

LOOKING BACK, THINKING FORWARD

1998 was an important year for The Gymboree Corporation, a year during which we continued to expand and strengthen our company.

Our goal has always been to be the premier children's clothing company. But in fact we are much more than just a clothing company. We are dedicated to children and to meeting their needs in our play programs and in our stores. We strive to provide them and their parents and caregivers with superior products and exceptional service each time they visit us.

During 1998, we increased the number of products we offered, broadened our distribution channels, and evolved our play programs. Each initiative we undertook was guided by our company's founding values--the celebration of childhood, a commitment to teamwork, and a dedication to building stakeholder value.

BABY YOUR BABY  
GYMBOREE EXPANDS THE LAYETTE LINE

From its introduction, the overwhelming success of our layette line has proven that tiny clothes have great potential. Parents and caregivers want to pamper their new arrivals with products offering the highest quality, ultimate comfort and latest styling. Our layette line fulfills all their desires and continues to be a growing contributor to our bottom line.

To leverage the success of layette, we have expanded the line with special occasion clothing, baby lotions, soaps and shampoos, and exclusive accessories.

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THE GYMBOREE CORPORATION

WWWONDERFUL!  
GYMBOREE OPENS AN ONLINE STORE

Early in 1998, the Gymboree website became fully operational. One year later, [www.gymboree.com](http://www.gymboree.com) is showing strong growth. In the first twelve months, nearly a half million shoppers visited the site and online sales continue to build.

The first items available online were baby gift sets. During the year, we added the entire line of girls' apparel as well as gift certificates for Gymboree merchandise and classes. We also posted an online job listing to help us recruit new team members. This year, the complete layette line will be available online.

Our goal for 1999 is to reach more customers through our website and better serve their needs. To achieve it, we will be expanding the site, increasing our presence on search engines and developing new strategic web partnerships.

SINGING A NEW TUNE:  
GYMBOREE PLAY AND MUSIC

Program enhancements and a beefed up marketing plan helped Gymboree Play Programs grow by leaps and bounds. 1998 was this area's best financial year ever with enrollment and gross revenues both reaching all-time highs.

This year we are adding a music program to the curriculum. In fact, we are changing the name from Gymboree Play Programs to Gymboree Play & Music.

Seventeen different musical styles--from rock 'n roll to classical to reggae--will be explored throughout the year. Preview classes have received rave reviews from parents and children. By fall, both the new music program and traditional Gymboree classes will be offered at nearly all of our 400 worldwide locations.

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[PICTURE]

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[PICTURE]

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#### THE GYMBOREE CORPORATION

#### ZUTOPIA THE NEXT GENERATION

Gymboree has a cool new cousin--Zutopia. Designed to appeal to Generation Z (age six to pre-teen), preppy isn't part of this picture.

Zutopia clothes, shoes and lifestyle accessories are edgy--an inspired blend of designer, street and alternative styling. Developed after in-depth research sessions and focus groups with boys, girls and parents, Zutopia respects kids' attitudes about who they are and who they want to be. It reflects their sense of style and their sense of self.

The new, stand-alone Zutopia retail stores, where the line will be sold exclusively, are an inspired convergence of time, place, attitude. Kids are invited to hang out in the Zu lounge, surf the Internet and play Nintendo at in-store kiosks. To keep Zutopia's styling and strategic positioning fresh, sophisticated and distinctive, completely separate design and merchandising teams head up the brand.

Introducing Zutopia means we will be able to continue our relationship with loyal customers long after they have outgrown Gymboree sizing--and styling. And according to what the kids have told us so far, it's working.

In 1999, 15 to 20 Zutopia stores will open nationwide.

#### BEST FOOT FORWARD: GYMBOREE'S SHOE BUSINESS

In 1998, we began selling shoes as a stand-alone item, not just accessories to our clothing lines. We also added more styles--from dress-up shoes to sneakers

to beach sandals. The result? Shoe sales really stepped up.

Today our footwear offers great design and top quality in a range of prices.

Working with experts in children's footwear, we have created both basic and fun shoes that parents and children like. Even more importantly, they fit little feet comfortably.

From a modest beginning, our shoe business has quickly grown into a significant opportunity. And we expect the strong growth to continue. In 1999, Gymboree customers will find more shoes, in more styles, at every Gymboree location.

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#### THE GYMBOREE CORPORATION

#### TEAM GYMBOREE:

WORKING BETTER TOGETHER.

In the same way we look after the well-being and satisfaction of our customers, we take good care of our team. We built our company on a set of shared values: simplicity, creativity, innovation, stakeholder value, teamwork, talent, quality, learning, brand, customer and the celebration of childhood.

All our business decisions are guided by these eleven values. Each year, the individuals or teams who best exemplify our values are presented with the coveted Gympo Award.

[GYMBO AWARD RECIPIENT PICTURE]

#### BALANCING WORK AND LIFE

We provide team members who are new or expectant parents with reserved parking, private space, even pagers to help moms and dads keep in touch during the third trimester.

We organize weekly snack breaks for our team members as well as a popular recess. We believe that celebrating the child in each of us helps keep us in touch with our consumers.

[RESERVED PARKING, GYM MOM-TO-BE PICTURE]

#### CAREER-LONG LEARNING

At Gymboree we value continuous learning. In 1998, we opened the doors of the Gymboree Learning Center.

We currently offer workshops in everything from Time Management to Workplace Diversity, Computer Literacy to Team Leadership. Classes are open to any team member interested in developing new skills and enhancing professional growth and satisfaction.

[LEARNING CENTER PICTURE]

#### GYMCARES

We believe in supporting our communities. Through our GymCares program, we sponsor a local elementary school, donate to child-oriented causes, participate in the U.S. Marine Corps Toys for Tots program and maintain a long-standing commitment to the March of Dimes.

[TOYS FOR TOTS PICTURE]

For two years, Chief Executive Officer Gary White has been the chair of the San Francisco Bay Area March of Dimes "WalkAmerica" fund-raising event. Team members have gathered community support by participating in the walk. In 1998, Gymboree won the Jerry Rice Award after raising over \$1 million for this vital organization.

Every year, we seek ways to match our unique capabilities and the goodwill of our team members to benefit children in need.

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THE GYMBOREE CORPORATION

SELECTED FINANCIAL AND OPERATING DATA

The following selected financial data have been derived from the consolidated financial statements of the Company. The data set forth below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Company's consolidated financial statements and notes thereto.

(In thousands, except operating data and per share amounts)	1998	1997	1996	1995	1994
-----					
INCOME STATEMENT DATA: (1)					
Net sales	\$ 457,219	\$ 373,440	\$ 303,111	\$ 259,381	\$ 188,424
Cost of goods sold, including buying and occupancy expenses	(292,686)	(207,630)	(164,052)	(149,428)	(100,651)
Gross profit	164,533	165,810	139,059	109,953	87,773
Selling, general and administrative expenses	(157,092)	(112,443)	(91,540)	(69,845)	(53,095)
Play programs income, net	2,013	517	74	316	554
Operating income	9,454	53,884	47,593	40,424	35,232
Foreign exchange gains (losses)	187	(837)	0	0	0
Net interest income	265	2,778	3,678	2,823	1,760
Income before income taxes	9,906	55,825	51,271	43,247	36,992
Income taxes	(3,665)	(20,655)	(19,483)	(16,866)	(14,797)
Net income	\$ 6,241	\$ 35,170	\$ 31,788	\$ 26,381	\$ 22,195
Basic income per share	\$ 0.26	\$ 1.45	\$ 1.27	\$ 1.06	\$ 0.91
Diluted income per share	\$ 0.26	\$ 1.41	\$ 1.24	\$ 1.04	\$ 0.88
Basic weighted average shares outstanding	24,164	24,302	25,111	24,862	24,279
Diluted weighted average shares outstanding	24,227	25,000	25,670	25,357	25,265
OPERATING DATA:					
Number of stores at end of period	564	435	354	279	209
Net sales per average gross square foot	\$ 550	\$ 621	\$ 670	\$ 827	\$ 882
Net sales per average store	\$ 915,000	\$ 947,000	\$ 948,000	\$ 1,063,000	\$ 1,050,000
Comparable store net sales increase (decrease) (2)	1%	2%	(6%)	3%	12%
BALANCE SHEET DATA:					
Working capital	\$ 76,314	\$ 71,590	\$ 105,190	\$ 89,417	\$ 73,937
Total assets	256,705	229,200	216,909	160,009	126,083
Long term debt	11,460	0	0	0	0
Stockholders' equity	168,372	157,710	161,933	123,934	92,629
-----					

(1) 1998, 1997, 1996, and 1994 included 52 weeks, while 1995 included 53 weeks.

(2) A store becomes comparable after it is opened for 14 full months. Comparable store net sales in fiscal years 1998 through 1994 were calculated on a 52 week basis.

This annual report contains forward-looking statements reflecting the Company's current expectations and there can be no assurance that the Company's actual future performance will meet such expectations. Factors that could cause future performance to vary from current expectations include, but are not limited to, the factors discussed later under the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section.

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## THE GYMBOREE CORPORATION

### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### GENERAL

The Gymboree Corporation was founded in 1976 as a provider of interactive parent-child play programs and began to franchise this business in 1979. In 1986, the Company opened its first retail store featuring children's apparel and accessories. In fiscal 1999, the Company will open a new retail concept, Zutopia, which targets children ages six to twelve. Through the end of fiscal 1998, the Company had grown to 564 stores, including 525 stores in 50 states in the United States, 15 stores in Canada and 24 stores in Europe.

The Company's net sales for the 52 weeks ended January 30, 1999 increased to \$457.2 million from \$373.4 million in the 52 weeks ended January 31, 1998 and \$303.1 million in the 52 weeks ended February 2, 1997. Net income decreased to \$6.2 million in 1998 from \$35.2 million in 1997 and \$31.8 million in 1996. Comparable store net sales, all based on a 52 week period, increased 1% for 1998, increased 2% for 1997 and decreased 6% for 1996. The Company expects that future increases in net sales and net income will be dependent on the ability to generate sales increases within existing stores, the opening and profitability of new domestic and international stores, and the success of Zutopia.

The Company's year-end is on the Saturday closest to January 31. Fiscal years 1998 and 1997, which both included 52 weeks, ended on January 30, 1999 and January 31, 1998, respectively. Prior to fiscal 1997, the Company's year ended on the Sunday closest to January 31 of each year. Fiscal 1996, which included 52 weeks, ended February 2, 1997. This change did not have a significant effect on the consolidated financial statements of the Company.

#### 1998 COMPARED TO 1997

##### NET SALES

Net sales increased 22% to \$457.2 million for 1998, compared to \$373.4 million for 1997. Sales for the 129 stores opened in 1998 contributed \$49.4 million of the increase in net sales. Stores opened or expanded prior to 1998 but not qualifying as comparable stores, including the 25 stores expanded in 1998, contributed \$31.3 million of the increase in net sales. Increases in comparable store net sales for 1998 contributed \$3.1 million of the increase in net sales. Comparable store net sales increased 1% over 1997. Comparable store sales were adversely affected by the poor consumer acceptance of boys' apparel and an overall decline in the average price per unit of merchandise sold.

##### GROSS PROFIT

Gross profit decreased 1% to \$164.5 million in 1998 from \$165.8 million in 1997. As a percentage of net sales, gross profit decreased to 36.0% in 1998 from 44.4% in 1997. The decrease in gross profit as a percentage of net sales was attributable to a decline in the average price per unit of merchandise sold. Such decline was primarily due to increased average markdowns per store taken to sell excess inventory.

The Company is planning lower average per store inventory levels in fiscal 1999 as compared to fiscal 1998. While the decrease in average per store inventory levels is expected to have a favorable impact on gross profit, this may cause downward pressure on comparable store net sales.

#### SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses ("S,G&A"), which principally consist of non-occupancy store expenses, corporate overhead and distribution expenses, increased as a percentage of net sales to 34.3% in 1998 compared to 30.1% in 1997. The increase in S,G & A, as a percentage of net sales, was primarily attributable to the funding of the Company's international expansion in Europe and Canada, marketing expenses associated with direct mail and other promotional campaigns, start-up expenses for the development of the new retail concept Zutopia, and loss of leverage on store selling expenses caused by lower average store sales. Other increases in S, G&A included distribution costs due to the opening of a new distribution center in Dixon, California, closure of the existing facility located in Hayward, California, and Year 2000 related professional services.

#### PLAY PROGRAMS INCOME

Play Programs income increased 289% to \$2.0 million in 1998, from \$0.5 million in 1997, due primarily to new franchise sales, enrollment growth in both franchised and corporate owned centers and increased play product sales.

#### FOREIGN EXCHANGE GAINS (LOSSES)

Net foreign exchange gains totaled \$187 thousand in 1998 as compared to a loss of \$837 thousand in 1997. The Company entered into forward foreign exchange contracts involving inter-company transactions during fiscal 1998 that resulted in a minimal gain. In the prior year, the Company did not hedge these transactions.

#### NET INTEREST INCOME

Interest income decreased to \$0.8 million in 1998, from \$2.8 million in 1997, due to lower average cash and investment balances. In fiscal 1998 interest expense totaled \$0.5 million, as a result of borrowings, while the prior year's interest expense was immaterial.

#### INCOME TAXES

The Company's effective tax rate for 1998 and 1997 was 37%. See Note 6 to Notes to Consolidated Financial Statements.

#### 1997 COMPARED TO 1996

##### NET SALES

Net sales increased 23% to \$373.4 million for 1997, compared to \$303.1 million for 1996. Sales for the 82 stores opened in 1997 contributed \$40.9 million of the increase in net sales. Stores opened or expanded prior to 1997 but not qualifying as comparable stores, including the 16 stores expanded in 1997, contributed \$24.2 million of the increase in net sales. Increases in comparable store net sales for 1997 contributed \$5.2 million of the increase in net sales. Comparable store net sales increased 2% over 1996.

The increase in comparable store net sales was primarily due to the Company operating with higher store inventory levels throughout 1997 and somewhat higher levels of markdowns compared to 1996.

#### GROSS PROFIT

Gross profit increased 19% to \$165.8 million in 1997 from \$139.1 million in

1996. As a percentage of net sales, gross profit decreased to 44.4% in 1997 from 45.9% in 1996. The decrease in gross profit as a percentage of net sales was attributable to increases in average markdowns per store in 1997 compared to 1996.

#### SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses ("S,G&A"), which principally consist of non-occupancy store expenses, corporate overhead and distribution expenses, remained relatively flat as a percentage of net sales at 30.1% in 1997 compared to 30.2% in 1996. S,G & A, as a percentage of net sales remained flat during fiscal 1997 as compared to 1996 due primarily to increases in comparable store sales and the discontinuation of the Company's catalog business at the end of 1996 largely offset by S,G&A associated with its international store expansions.

#### PLAY PROGRAMS INCOME

Play Programs income increased 599% to \$517 thousand in 1997, from \$74 thousand in 1996, due primarily to new franchise sales, enrollment growth in both franchised and corporate owned centers and increased play product sales.

#### FOREIGN EXCHANGE LOSSES

Foreign exchange losses increased \$837 thousand in 1997 as compared to 1996. Total losses from foreign exchange transactions during 1997 were 0.2% of sales. This increase was primarily attributed to losses incurred from currency fluctuations in inter-company transactions between the Company's U.S. operations and its foreign subsidiaries.

#### NET INTEREST INCOME

Interest income decreased to \$2.8 million in 1997, from \$3.7 million in 1996, due to lower average cash and investment balances resulting from two stock repurchases during 1997.

#### INCOME TAXES

The Company's effective tax rate for 1997 was 37% compared to 38% in 1996 due to implementation of tax planning strategies. See Note 6 of Notes to Consolidated Financial Statements.

#### LIQUIDITY AND CAPITAL RESOURCES

During 1998 the Company satisfied its cash requirements through a combination of cash flow from operations and from permanent financing as compared to 1997 and 1996 when cash requirements were met exclusively from cash flow from operations and available cash balances. Primary uses of cash during 1998 have been to finance the construction of new domestic and international stores. Comparatively, in fiscal 1997 the Company used cash to purchase outstanding common stock and to increase the average store inventory levels. The Company also purchased land and constructed a 300,000 square foot distribution center in Dixon, California in 1997, which was refinanced with debt in 1998.

The combined balances of cash, cash equivalents and investments were \$27.8 million and \$36.5 million at the end of 1998 and 1997, respectively. At January 30, 1999 the Company held no investments. At January 30, 1998, investments included short to medium-term investment grade securities.

Working capital as of January 30, 1999 was \$76.3 million compared to \$71.6 million at January 31, 1998. The increase in working capital was primarily due to a decrease in liabilities. During 1998, the Company generated \$27.5 million of cash from operations, \$18.6 million from the sales of investments, \$12.0 million of proceeds on borrowings, and \$2.5 million from the exercise of stock options. Uses of cash consisted primarily of \$50.7 million for capital expenditures, related largely to the opening of 129 new stores and the expansion of 25 existing stores. During 1997, the Company generated \$37.8 million of cash from operations, \$63.5 million from the sale of investments and \$8.8 million from the exercise of stock options. Uses of cash consisted primarily of \$49.7 million for the repurchase of the Company's common stock and \$49.0 million for capital expenditures, related largely to the opening of 82 new stores, the new Dixon distribution center, the expansion of 16 existing stores and the roll-out of a new point-of-sale system.

As of January 30, 1999, the Company had a bank line of credit that allowed

up to \$100 million in unsecured letters of credit, of which \$11 million can be used for standby letters of credit. As of January 30, 1999, approximately \$67.0 million was available pursuant to such lines. The facility also provided a line of up to \$50 million for foreign exchange contracts. This facility is scheduled to expire May 31, 1999. The Company uses these lines primarily to support letters of credit which fund its foreign sourcing of merchandise inventories. As of January 31, 1998, the Company had a bank line of credit that allowed up to \$100 million in unsecured letters of credit and up to \$10 million in foreign exchange contracts, of which \$61.5 million was available pursuant to such lines.

On March 11, 1999, the Company and its current bank agreed to amend the unsecured credit facility to extend the expiration date to March 31, 2001. The revised terms provide for an overall credit line of \$100 million that may be used for issuance of commercial letters of credit, cash advances up to \$25 million and standby letters of credit up to \$10 million. Included within these terms is a continuation of the foreign exchange facility. The interest rate will be based on the bank's Reference Rate or LIBOR (London Interbank Offered Rate) plus a pre-determined spread. The credit facility contains quarterly and annual financial covenants, which require the Company to maintain minimum tangible net worth and meet certain ratios. Additionally, the facility contains restrictions on capital expenditures.

During fiscal 1998, the Company issued two promissory notes totaling \$12 million both secured by the Company's

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#### THE GYMBOREE CORPORATION

distribution center in Dixon, California. The first note of approximately \$3.1 million bears interest at 7.7%. The second note of approximately \$8.9 million bears interest at 7.9%.

The Company estimates that capital expenditures during 1999 will be between \$30.0 and \$35.0 million, which will primarily be used to open approximately 40 to 50 new domestic and international stores and to expand approximately 25 to 30 existing stores.

The Company anticipates that cash generated from operations, together with its existing cash resources and funds available from its current letters of credit and line of credit facilities, will be sufficient to satisfy its cash needs through at least fiscal 1999.

#### SEASONALITY AND QUARTERLY FLUCTUATIONS

The Company has historically experienced and expects to continue to experience seasonal fluctuations in its retail sales and net income. Historically, a disproportionate amount of the Company's retail sales and a significant portion of its net income have been realized during the months of November and December. In anticipation of increased sales activity during these months, the Company hires a significant number of temporary employees to bolster its store staff. In addition, the Company has experienced periods of increased sales activity in early spring and early fall. If, for any reason, the Company's sales were below seasonal norms during November and December, or during the early spring or early fall, the Company's annual operating results could be materially and adversely affected. Historically, retail sales and net income have been weakest during the second fiscal quarter, and the Company expects this trend to continue. The Company's quarterly results of operations may also fluctuate significantly as a result of a variety of factors, including the timing of new store openings, the costs and increased overhead associated with the opening and future operation of new stores. In addition, the sales contributed by new stores, advertising and marketing expenditures, merchandise mix and timing, and level of markdowns may contribute to fluctuations in operating performance.

#### QUANTITATIVE AND QUALITATIVE DISCLOSURES

The Company enters into forward foreign exchange contracts to hedge certain inter-company loans denominated in foreign currencies (principally Irish punts, British pounds sterling, and Canadian dollars). The term of the forward exchange

contracts is generally less than 90 days. The purpose of the Company's foreign currency hedging activities is to protect the Company from the risk that the eventual dollar net cash inflow resulting from the repayment of certain inter-company loans from the Company's foreign subsidiaries will be adversely affected by changes in exchange rates.

The table below summarizes by major currency the contractual amounts of the Company's forward foreign exchange contracts in U.S. dollars. Foreign currency amounts are translated at rates current at the reported date. The amounts represent the U.S. dollar equivalent to buy or sell foreign currencies.

(In thousands)	Jan. 30, 1999
Canadian dollars	\$11,185
Irish punts	6,308
British pounds sterling	13,985
Total	\$31,478

#### FACTORS THAT MAY AFFECT FUTURE PERFORMANCE

The discussion in this annual report contains certain forward-looking statements, including statements regarding future net sales and net income, future inventory levels, future comparable store net sales, future S,G&A expenses, future interest income, planned capital expenditures, planned store expansions, international expansion and future cash needs. Such forward-looking statements, in particular, and the Company's business and operating results, in general, involve risks and uncertainties. Actual results may differ significantly from the results discussed in the forward-looking statements. Future operating results will depend upon many factors, including general economic conditions, levels of competition, growth in the children's apparel market, financing and working capital needs, the availability of suitable new store locations, the ability to develop new merchandise and the ability to hire and train qualified sales associates, and the ability to successfully identify and respond to emerging children's fashion trends and effectively monitor and control costs. There can be no assurance that the Company will be able to effectively realize its plans for future growth. While the Company also expects that its decreased inventory levels will have a favorable effect on gross profit, there can be no assurance that the Company will have an adequate supply of inventory or will experience increases in gross profit.

The Company's sales and profitability depend upon the continued demand by its customers for its products and services. The Company believes that its future success will depend in large part upon its ability to anticipate, gauge and respond in a timely manner to changing consumer demands and fashion trends and upon the appeal of the Company's products. There can be no assurance that the demand for the Company's apparel or accessories will not decline or that the Company will be able to anticipate, gauge and respond to changes in fashion trends. If demand for the Company's apparel and accessories were to decline or if the Company were to misjudge fashion trends, the Company's business, financial condition and results of operations could be materially and adversely affected.

The Company's future profitability is critically dependent on its ability to achieve and manage potential future growth effectively. There can be no assurance that the Company will be successful in increasing net sales or gross profit in the future or that the rate of period-to-period net sales or gross profit growth, if any, will not decline. If the Company's operations were to continue to grow, of which there can be no assurance, there

could be increasing strain on other resources, and the Company may experience serious operating difficulties, including difficulties in hiring, training, managing an increasing number of employees, difficulties in obtaining sufficient fabric and sourcing capacity to produce its products, problems in upgrading its management information systems and delays in product distribution shipments. There can be no assurance that the Company will be able to manage future growth effectively. Any failure to manage growth effectively could have a material adverse effect on the Company's results of operations and financial condition.

During 1998, the Company expanded its operations in Europe and Canada. As a result, the Company's business is subject to the risks generally associated with doing business abroad, such as foreign governmental regulations, foreign consumer preferences, currency fluctuations, political unrest, disruptions or delays in shipments and changes in economic conditions in countries in which the Company operates its stores. These factors, among others, could influence the Company's ability to sell its products in these international markets. If any such factors were to render the conduct of business in a particular country undesirable or impractical, there could be a material and adverse effect on the Company's results of operations and financial condition.

The matters discussed in this report with respect to the opening of Zutopia, a separate retail concept, are also forward-looking statements that involve risk and uncertainties, including no prior operating history, no prior history of market acceptance, potentially higher expenses without corresponding revenue increases, impact to earnings, ability to obtain new store sites, ability to obtain adequate sources of merchandise, competition from other retailers and uncertainties generally associated with apparel retailing. In addition, the Company has recently hired a highly experienced team to support the production, merchandising and promotion of Zutopia. The Company's limited experience with marketing apparel to this demographic segment could materially and adversely affect its ability to introduce Zutopia successfully or to develop this concept's product line.

The Company is developing a strategy to handle the planned conversion in 2002 of the Irish punt to the Euro.

#### YEAR 2000

Most companies could face a potentially serious information systems problem because many software applications and operational programs written in the past were designed to handle date formats with two-digit years and thus may not properly recognize calendar dates beginning in the Year 2000. This problem could result in computers either outputting incorrect data or shutting down altogether when attempting to process a date such as "01/01/00".

The Company's Year 2000 initiative extends throughout the entire Company and includes all operating functions. Managing this effort on a regular basis is the Company's Year 2000 Project Office, which reports to a member of the Executive Committee. It is through this office that various roles and accountabilities regarding Year 2000 readiness have been established. Each of the Company's business units have been directed to work on Year 2000 projects and assemble teams to identify and implement plans to help mitigate potential problems.

#### STATE OF READINESS

All of the Company's mission critical information technology and non-information technology systems have been inventoried, ranked in terms of risk, and analyzed as to their Year 2000 readiness. The Company has completed an Enterprise Master Plan, Enterprise Test Plan, Configuration Management Plan, and Quality Assurance Plan. A Test Data Center has been constructed and is being used to remediate and test all mission critical systems. The Company's business processes are organized into eighteen groups of applications. The plans call for completing the remediation and testing phase for all groups by the end of the third quarter 1999. The Company currently expects material Year 2000 problems, if any, to be corrected prior to December 1999.

#### COSTS

Based on best estimates, the total cost of the Year 2000 readiness initiative, which covers fiscal years 1998 and 1999, is approximately \$2.0 - \$3.0 million of which \$1.2 million has been expensed for fiscal year 1998. There can be no

assurance that these estimates will not be exceeded. All costs will be paid from the Company's operating funds.

RISKS OF YEAR 2000 ISSUES

The area of greatest risk to the Company's business operations is ensuring the readiness of our critical trading partners. We have surveyed all of our critical trading partners to ascertain their Year 2000 readiness. To date, a majority of our trading partners have responded with a formal plan to be Year 2000 compliant. Failure of Year 2000 compliance by our trading partners could result in a delay in the receipt of inventory, potential lost sales, and an inability to operate stores. There can be no assurance that the Year 2000 problem will not have a material adverse effect on the Company's business, operating results or financial condition.

CONTINGENCY PLANS

Contingency plans have been developed for each mission critical application. The contingency plan for trading partners that are not Year 2000 compliant by January 1999 is to obtain alternate suppliers that are Year 2000 compliant. This plan was communicated to our trading partners during the surveying process. As of the beginning of fiscal 1999, the Company has begun implementation of its contingency plan for trading partners that are not Year 2000 compliant. However, there can be no assurance that such contingency plans will remediate all Year 2000 issues which the Company might ultimately encounter.

THE GYMBOREE CORPORATION

CONSOLIDATED BALANCE SHEETS

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(In thousands, except share data)	January 30, 1999	January 31, 1998
=====		
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 27,810	\$ 17,870
Investments	0	18,642
Accounts receivable	7,811	5,184
Merchandise inventories	74,396	75,293
Prepaid expenses and other	8,068	4,467
	-----	-----
Total current assets	118,085	121,456
	-----	-----
PROPERTY AND EQUIPMENT:		
Land	995	810
Building	8,948	8,948
Leasehold improvements	79,832	58,729
Furniture, fixtures, and equipment	91,551	66,819
	-----	-----
	181,326	135,306
Less accumulated depreciation and amortization	(46,886)	(30,934)
	-----	-----
	134,440	104,372
LEASE RIGHTS AND OTHER ASSETS		
	4,180	3,372
	-----	-----
TOTAL ASSETS	\$ 256,705	\$ 229,200
	=====	=====
-----		
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Current portion of long term debt	\$ 540	\$ 0
Accounts payable	21,842	26,046
Accrued liabilities	17,424	15,781
Income taxes payable	1,965	8,039
	-----	-----
Total current liabilities	41,771	49,866
	-----	-----
LONG TERM LIABILITIES:		

Long term debt, net of current portion	11,460	0
Deferred rent and other liabilities	35,102	21,624
	-----	-----
TOTAL LIABILITIES	88,333	71,490
	-----	-----
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Common stock, including excess paid-in capital (\$.001 par value: 100,000,000 shares authorized; 24,240,763 and 24,015,096 shares outstanding at January 30, 1999 and January 31, 1998, respectively)	26,855	23,109
Restricted stock deferred compensation	0	(337)
Retained earnings	141,517	134,938
	-----	-----
Total stockholders' equity	168,372	157,710
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 256,705	\$ 229,200
	=====	=====

See notes to consolidated financial statements

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THE GYMBOREE CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)	Year Ended			As a Percentage of Net Sales for the Year Ended		
	January 30, 1999	January 31, 1998	February 2, 1997	January 30, 1999	January 31, 1998	February 2, 1997
Net sales	\$ 457,219	\$ 373,440	\$ 303,111	100.0%	100.0%	100.0%
Cost of goods sold, including buying and occupancy expenses	(292,686)	(207,630)	(164,052)	(64.0)	(55.6)	(54.1)
Gross profit	164,533	165,810	139,059	36.0	44.4	45.9
Selling, general and administrative expenses	(157,092)	(112,443)	(91,540)	(34.3)	(30.1)	(30.2)
Play program income, net	2,013	517	74	0.4	0.1	0.0
Operating income	9,454	53,884	47,593	2.1	14.4	15.7
Foreign exchange gains (losses)	187	(837)	0	0	(0.2)	0.0
Net interest income	265	2,778	3,678	0.1	0.7	1.2
Income before income taxes	9,906	55,825	51,271	2.2	14.9	16.9
Income taxes	(3,665)	(20,655)	(19,483)	(0.8)	(5.5)	(6.4)
Net income	\$ 6,241	\$ 35,170	\$ 31,788	1.4%	9.4%	10.5%
	=====	=====	=====	=====	=====	=====
Income per share:						
Basic	\$ 0.26	\$ 1.45	\$ 1.27			
Diluted	\$ 0.26	\$ 1.41	\$ 1.24			
Weighted average shares outstanding:						
Basic	24,164	24,302	25,111			
Diluted	24,227	25,000	25,670			

See notes to consolidated financial statements

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THE GYMBOREE CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)	Year Ended		
	January 30, 1999	January 31, 1998	February 2, 1997
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income	\$ 6,241	\$ 35,170	\$ 31,788
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	18,776	13,549	8,899
Non-cash compensation expenses	0	416	386
Loss on disposal of property and equipment	1,794	1,510	980
Provision for deferred income taxes	214	2,136	1,200
Tax benefit from exercise of stock options	1,596	1,217	1,167
Change in assets and liabilities:			
Accounts receivable	(2,627)	(848)	(1,468)
Merchandise inventories	1,263	(26,346)	(11,327)
Prepaid expenses and other assets	(2,894)	(1,176)	(1,338)
Accounts payable	(4,204)	4,097	12,292
Accrued liabilities	2,936	1,554	1,089
Income taxes payable	(6,074)	1,408	387
Other liabilities	10,456	5,067	5,085
Net cash provided by operating activities	27,477	37,754	49,140
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Capital expenditures	(50,662)	(48,964)	(37,059)
Proceeds from sales of assets	24	117	0
Sales of investments	18,614	63,526	(17,649)
Acquisition of lease rights	0	(1,788)	0
Net cash provided by (used in) investing activities	(32,024)	12,891	(54,708)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Issuance of stock	2,487	8,844	4,840
Repurchase of common stock	0	(49,646)	0
Proceeds from borrowings	12,000	0	0
Net cash provided by (used in) financing activities	14,487	(40,802)	4,840
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	9,940	9,843	(728)
<b>CASH AND CASH EQUIVALENTS:</b>			
Beginning of year	17,870	8,027	8,755
End of year	\$ 27,810	\$ 17,870	\$ 8,027
<b>OTHER CASH FLOW INFORMATION:</b>			
Cash paid during the year for income taxes	\$ 3,561	\$ 16,298	\$ 16,822
Cash paid during the year for interest	\$ 537	\$ 19	\$ 9

See notes to consolidated financial statements

THE GYMBOREE CORPORATION

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Common Stock and Excess Paid-in Capital	Restricted Stock
--	---------------------

(In thousands)	Shares	Amount	Deferred Compensation	Retained Earnings	Total
BALANCE AT FEBRUARY 4, 1996	24,992,276	\$ 56,687	\$ (1,139)	\$ 68,386	\$ 123,934
Issuance of common stock under stock option plans	331,784	4,840			4,840
Tax benefit from exercise of stock options		1,167			1,167
Amortization of restricted stock			386		386
Net income				31,788	
Other comprehensive income				(182)	
Comprehensive income				31,606	31,606
BALANCE AT FEBRUARY 2, 1997	25,324,060	62,694	(753)	99,992	161,933
Issuance of common stock under stock option plans	613,036	8,844			8,844
Stock repurchase	(1,922,000)	(49,646)			(49,646)
Tax benefit from exercise of stock options		1,217			1,217
Amortization of restricted stock			416		416
Net income				35,170	
Other comprehensive income				(224)	
Comprehensive income				34,946	34,946
BALANCE AT JANUARY 31, 1998	24,015,096	23,109	(337)	134,938	157,710
Issuance of common stock under stock option plans	225,667	2,487			2,487
Tax benefit from exercise of stock options		1,596			1,596
Cancellation of restricted stock		(337)	337		0
Net income				6,241	
Other comprehensive income				338	
Comprehensive income				6,579	6,579
BALANCE AT JANUARY 30, 1999	24,240,763	\$ 26,855	\$ 0	\$ 141,517	\$ 168,372

See notes to consolidated financial statements

THE GYMBOREE CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The consolidated financial statements include The Gymboree Corporation and its wholly owned subsidiaries (the "Company"). All significant inter-company balances and transactions have been eliminated.

NATURE OF THE BUSINESS

The Company is a leading provider of apparel, accessories, and play programs for children ages newborn to preteen. The Company operates as one reportable segment. As of January 30, 1999, January 31, 1998, and February 2, 1997, the Company had 564, 435 and 354 retail stores, respectively. The Company also offers directed parent-child developmental play programs at approximately 380 franchised locations and 18 Company-operated locations.

FISCAL YEAR

The Company's year-end is on the Saturday closest to January 31. Fiscal years 1998 and 1997, which both included 52 weeks, ended on January 30, 1999 and

January 31, 1998, respectively. Prior to fiscal 1997, the Company's year ended on the Sunday closest to January 31 of each year. Fiscal 1996, which included 52 weeks, ended February 2, 1997. This change did not have a significant effect on the consolidated financial statements of the Company.

#### USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles 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 amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### CASH AND CASH EQUIVALENTS

Cash equivalents consist of highly liquid investment instruments with a maturity of three months or less, at date of purchase.

#### INVESTMENTS

As of January 30, 1999, there were no investments. For the year ended January 31, 1998, the Company's investments, consisting primarily of municipal bonds, were classified as available-for-sale and were recorded at fair market value. Fair market value is based upon quoted market prices on the last day of the year. Unrealized gains and losses are included in other comprehensive income. As of January 31, 1998, the fair market value of investments of \$18.6 million approximated the amortized cost.

#### ESTIMATED FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying value of cash and cash equivalents, accounts receivable, accounts payable, and debt approximates their estimated fair value.

#### MERCHANDISE INVENTORIES

Merchandise inventories are recorded under the retail method of accounting and are stated at the lower of cost or market.

#### PROPERTY AND EQUIPMENT

Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from approximately 3 to 10 years. Leasehold improvements are amortized over the lesser of the lease term which range from 10 to 25 years, or the estimated useful lives of the improvements. Internally developed and purchased computer software is recorded at cost and is amortized using the straight-line method based on an estimated useful life of 5 years.

#### INCOME TAXES

The Company computes income taxes using the asset and liability method. Deferred income taxes are provided for the temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities.

#### LEASE RIGHTS

Lease rights are recorded at cost and are amortized over 10 years or the life of the lease.

#### DEFERRED RENT

Many of the Company's operating leases contain predetermined fixed increases of the minimum rental rate during the initial lease term. For these leases, the Company recognizes the related rental expense on a straight-line basis and records the difference between the amount charged to expense and the rent paid as deferred rent.

#### CONSTRUCTION ALLOWANCE

As part of its lease agreements, the Company receives construction allowances from landlords. These allowances offset the capital expenditures associated with the expansion or construction of stores. The construction allowances have been deferred and are amortized on a straight-line basis over the life of the lease as a reduction of rent expense. Construction allowances of \$10.5 million and

\$4.6 million were granted in fiscal years 1998 and 1997, respectively.

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#### THE GYMBOREE CORPORATION

##### FOREIGN CURRENCIES

Assets and liabilities of foreign subsidiaries are translated to U.S. dollars at the exchange rates effective on the balance sheet date. Translation adjustments resulting from this process are recorded as other comprehensive income. Revenues, costs of sales, expenses and other income are translated at average rates of exchange prevailing during the year.

In fiscal 1998 the Company entered into forward foreign exchange contracts to reduce exposure to foreign currency exchange risk related to its inter-company loans, which are denominated in foreign currencies. The net gains and losses between the forward foreign exchange contracts and inter-company loans are included in net income.

As of January 30, 1999, the Company had forward foreign contracts of \$11.2 million, \$6.3 million and \$14.0 million to hedge Canadian dollars, Irish punts and British pound sterling, respectively. The amounts represent the U.S. dollar equivalent to buy or sell foreign currencies.

##### STORE PRE-OPENING COSTS

Store pre-opening costs are expensed as incurred.

##### PLAY PROGRAMS REVENUE RECOGNITION

Initial franchise fees for all sites sold in a territory are recognized as revenue when the franchisee has paid the initial franchise fee, has received government approval in the case of international franchises, and has completed the training program. At that time, the Company has provided substantially all of the initial services required by the franchise agreement.

##### STOCK-BASED COMPENSATION

The Company accounts for stock-based awards to employees using the intrinsic value method in accordance with Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees."

##### RECLASSIFICATIONS

Certain amounts for prior years have been reclassified to conform to the 1998 presentation.

##### INCOME PER SHARE

Basic income per share is computed as net income divided by the weighted average number of common shares outstanding for the period. Diluted income per share reflects the potential dilution that could occur from common shares issuable through stock options and restricted stock and is computed by dividing net income by the weighted average number of common shares outstanding for the period plus the dilutive effect of outstanding stock options and restricted stock.

##### NEW ACCOUNTING STANDARDS

The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 130, "Reporting Comprehensive Income," during fiscal 1998. SFAS No. 130 requires the presentation, by major components and as a single total, the change in the Company's net assets during a period from non-owner sources. As other comprehensive income is immaterial for all periods, such amount is included in retained earnings. Additionally, the Company is required to adopt SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activity," during fiscal 1999. The adoption of this statement will not have a significant effect on the

consolidated financial statements of the Company.

## 2 LEASES

The Company leases its store locations, corporate headquarters, foreign distribution centers and certain fixtures and equipment under operating leases. The leases expire at various dates through the year 2023. Store leases typically provide for payment by the Company of operating expenses, real estate taxes and additional rent based on a percentage of sales if a specified sales target is exceeded. Furthermore, a majority of the leases allow the Company to vacate after a stipulated period.

Future minimum lease payments under operating leases at January 30, 1999 are as follows:

=====  
(In thousands)  
=====  
Year:

1999	\$ 35,612
2000	35,292
2001	35,127
2002	34,479
2003	33,728
Later years	142,139
	-----
Total minimum lease commitments	\$316,377

=====

Rent expense for all operating leases was \$46.7 million, \$36.9 million and \$29.1 million, in 1998, 1997 and 1996 respectively, which includes percentage rent expense and other lease required expenses of \$15.4 million, \$12.7 million and \$10.9 million for 1998, 1997 and 1996, respectively.

## THE GYMBOREE CORPORATION

## 3 LINES OF CREDIT

As of January 30, 1999, the Company had a bank line of credit that allowed up to \$100 million in unsecured letters of credit, of which \$11 million can be used for standby letters of credit. As of January 30, 1999, approximately \$67.0 million was available pursuant to such lines. The facility also provided a line of up to \$50 million for foreign exchange contracts. The facility is scheduled to expire May 31, 1999. The Company uses these lines primarily to support letters of credit which fund its foreign sourcing of merchandise inventories. As of January 31, 1998, the Company had a bank line of credit that allowed up to \$100 million in unsecured letters of credit and up to \$10 million in foreign exchange contracts, of which \$61.5 million was available pursuant to such lines.

On March 11, 1999, the Company and its current bank agreed to amend the unsecured credit facility to extend the expiration date to March 31, 2001. The revised terms provide for an overall credit line of \$100 million that may be used for issuance of commercial letters of credit, cash advances up to \$25 million and standby letters of credit up to \$10 million. Included within these terms is a continuation of the foreign exchange facility. The interest rate will be based on the bank's Reference Rate or LIBOR (London Interbank Offered Rate) plus a pre-determined spread.

The credit facility contains quarterly and annual financial covenants, which require the Company to maintain minimum tangible net worth and meet certain ratios. Additionally, the facility contains restrictions on capital

expenditures.

#### 4 ACCRUED LIABILITIES

Accrued liabilities consist of the following:

(In thousands)	Jan. 30, 1999	Jan. 31, 1998
Employee compensation	\$ 5,623	\$ 6,293
Store operating expenses and other	4,538	1,925
Store credits and gift certificates	3,103	3,223
Sales taxes	1,838	881
Percentage rent	1,211	1,057
Deferred taxes	1,111	2,402
Total	\$17,424	\$15,781

#### 5 LONG TERM DEBT

During fiscal 1998, the Company issued two promissory notes totaling \$12 million both secured by the Company's distribution center in Dixon, California. The first note of approximately \$3.1 million bears interest at 7.7%. The second note of approximately \$8.9 million bears interest at 7.9%.

Aggregate principal payments required under the two notes are as follows:

(In thousands)	
Year:	
1999	\$ 540
2000	583
2001	630
2002	681
2003	733
Later years	8,833
Total	\$12,000

#### 6 INCOME TAXES

The provision for income taxes consists of the following:

(In thousands)	1998	1997	1996
Current:			
Federal	\$ 3,073	\$14,996	\$15,100
State taxes	148	3,523	3,183
Foreign	230	0	0

Total current	3,451	18,519	18,283
	-----	-----	-----
Deferred:			
Federal	62	1,796	960
State	152	340	240
	-----	-----	-----
Total deferred	214	2,136	1,200
	-----	-----	-----
Total provision	\$ 3,665	\$20,655	\$19,483

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THE GYMBOREE CORPORATION

A reconciliation of the statutory federal income tax rate with the Company's effective income tax rate is as follows:

	1998	1997	1996
Statutory federal rate	35%	35%	35%
State income taxes, net of income tax benefit	4	4	4
Tax exempt interest	0	(1)	(1)
Other	(2)	(1)	0
	---	---	---
Effective tax rate	37%	37%	38%

Deferred income taxes reflect the impact of "temporary differences" between amounts of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws. Temporary differences and carry-forwards, which give rise to deferred tax assets and liabilities, are as follows:

(In thousands)	Jan. 30, 1999	Jan. 31, 1998
Deferred tax assets:		
Uniform capitalization costs	\$ 1,292	\$ 1,399
Accrued reserves	1,267	672
State taxes	187	481
Deferred foreign assets	31	0
Deferred rent	3,132	1,654
Other	3,095	58
	-----	-----
	9,004	4,264
	-----	-----
Deferred tax liability:		
Deferred foreign liability	(5)	0
Prepaid expenses	(1,109)	(510)
Fixed asset basis differences	(10,067)	(5,717)
	-----	-----

	(11,181)	(6,227)
	-----	-----
Net deferred tax liabilities	\$ (2,177)	\$ (1,963)

7 STOCK PLANS

STOCK OPTION PLANS

The Company's 1983 Incentive Stock Option Plan (the "1983 Plan") and 1993 Stock Option Plan (the "1993 Plan") provide for grants to team members of incentive stock options within the meaning of Section 422 of the Internal Revenue Code and for grants of non-statutory stock options and stock purchase rights to team members, consultants and non-employee directors of the Company. The Company has reserved a total of 3,600,000 shares of common stock for issuance under the 1983 Plan and 6,025,000 shares of common stock for issuance under the 1993 Plan, taking into consideration the additional 2,000,000 shares approved subsequent to year-end. Options granted pursuant to the plans have been granted at exercise prices equal to the fair market value of the Company's common stock on the date of grant. The options have a term of either five or ten years and generally vest over a four year period. No further options may be granted under the 1983 Plan. There were 70,095 and 743,589 shares available for the grant of options under the 1993 Plan at January 30, 1999 and January 31, 1998, respectively.

At a special meeting of shareholders on February 8, 1999, the Company's 1993 Stock Option Plan as Amended and Restated was approved. The changes to the plan include:

- (a) increased the aggregate number of shares of common stock authorized for issuance under the Plan by 2,000,000 shares raising the number of shares reserved under the plan since its inception to 6,025,000;
- (b) imposed annual limits on the number of shares subject to stock option grants, so as to qualify the compensation associated with such grants as "performance-based" compensation within the meaning of Section 162(m) of the Internal Revenue Code;
- (c) imposed an annual maximum limit of 200,000 shares that may be issued pursuant to Stock Purchase Rights;
- (d) imposed a minimum 3 year vesting schedule for all Stock Purchase Rights;
- (e) removed language from the 1993 Plan that contemplated option re-pricings and exchanges.

THE GYMBOREE CORPORATION

The following summarizes all stock option transactions for the three years ended January 30, 1999:

(Shares in thousands)	Shares Outstanding	Weighted Average Price Per Share
-----		
Balance, February 4, 1996	1,768	\$ 17.50
Options granted	704	24.37
Options exercised	(294)	14.48
Options canceled	(252)	23.92

Balance, February 2, 1997	1,926	19.51
Options granted	1,299	24.55
Options exercised	(577)	13.67
Options canceled	(323)	24.42
Balance, January 31, 1998	2,325	22.11
Options granted	1,610	17.52
Options exercised	(131)	13.25
Options canceled	(938)	21.60
Balance, January 30, 1999	2,866	\$ 20.16

The following table summarizes information about stock options outstanding at January 30, 1999 (shares in thousands):

Options Outstanding				Options Exercisable (Vested)	
Range of Exercisable Prices	Number of Shares	Weighted Average Remaining Life (in years)	Weighted Average Exercise Price	Number Exercisable at 1/30/99	Weighted Average Exercise Price
\$0.17 to \$ 8.25	571	9.7	\$ 7.03	28	\$ 3.51
8.38 to 20.81	521	7.6	16.03	240	19.59
21.25 to 24.00	537	7.5	23.62	312	23.48
24.13 to 25.38	493	8.6	25.20	160	25.11
25.44 to 27.06	638	8.6	26.90	201	26.81
27.13 to 36.63	106	7.2	29.74	63	30.26
\$0.17 to \$ 36.63	2,866		\$ 20.16	1,004	\$ 23.36

#### 1993 EMPLOYEE STOCK PURCHASE PLAN

The Company has reserved a total of 600,000 shares of common stock for issuance under the 1993 Employee Stock Purchase Plan (the "Purchase Plan"). The price at which stock is purchased under the Purchase Plan is equal to 85% of the fair market value of the common stock on the first day of the applicable offering period or the last day of the applicable purchase period, whichever is lower. Unless terminated earlier, the Purchase Plan will terminate in 2013. There were 94,232 and 35,797 shares issued under the Purchase Plan in fiscal 1998 and 1997, respectively.

#### RESTRICTED STOCK

In 1994, the Company granted 100,000 shares of its common stock to its former President and Chief Executive Officer at an aggregate purchase price of \$50.00. The aggregate fair market value of the shares, as measured by the stock price on the vesting commencement date, totaled \$1,937,500. The shares, which were issued pursuant to the 1993 Plan, were subject to a repurchase option that originally lapsed over a period of 60 months. The difference between the purchase price and the aggregate fair market value was being amortized over this 60-month period and was recognized as compensation expense totaling \$416,000 in 1997 and \$386,000 in 1996. Upon the resignation of this individual in fiscal 1997, the purchase option was cancelled and no compensation expense was recognized in fiscal 1998.

#### ADDITIONAL STOCK PLAN INFORMATION

The Company applies APB Opinion No. 25 and related interpretations in accounting for its three stock-based compensation plans, described above. Accordingly, no compensation expense has been recognized for its stock option plans and its employee stock purchase plan. Compensation expense has been charged against income for its restricted stock plan. Had compensation expense for the Company's stock option plans and the Purchase Plan been determined based on the fair value at the grant dates for awards under these plans, consistent with the method of SFAS No.123, "Accounting for Stock-Based Compensation," the Company's net income and income per share would have been reduced to the pro forma amounts indicated below:

THE GYMBOREE CORPORATION

		Year Ended		
		January 30, 1999	January 31, 1998	February 2, 1997
(In thousands, except per share data)				
Net income	As reported	\$6,241	\$35,170	\$31,788
	Pro forma	1,805	32,210	29,317
Basic income				
per share	As reported	\$ 0.26	\$ 1.45	\$ 1.27
	Pro forma	0.07	1.33	1.17
Diluted income				
per share	As reported	\$ 0.26	\$ 1.41	\$ 1.24
	Pro forma	0.07	1.29	1.14

The weighted average fair value of options granted during 1998, 1997 and 1996 were \$8.53, \$10.29, and \$8.67, respectively. The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted-average assumptions:

	Year Ended		
	January 30, 1999	January 31, 1998	February 2, 1997
Expected dividend rate	0.0%	0.0%	0.0%
Expected volatility	70.9%	54.4%	55.0%
Risk-free interest rate	5.1%	6.0%	6.0%
Expected lives (yrs.)	3.0	3.0	3.0

8 401(K) PLAN

The Company maintains a voluntary defined contribution 401(k) profit sharing plan (the "Plan") covering all team members who have met certain service and eligibility requirements. Employees may elect to contribute up to 20% of their compensation to the Plan, not to exceed the dollar limit set by law. The Company matches \$0.50 to the Plan for each \$1.00 contributed by a team member, up to a maximum Company contribution of \$500 per team member per year. The Company's matching contributions to the Plan were \$170,000, \$176,000, and \$133,000 in 1998, 1997, and 1996, respectively.

9 STOCKHOLDER RIGHTS PLAN

In March 1997, the Company adopted a Stockholder Rights Plan (the "Plan"). The Plan entails a dividend of one right for each outstanding share of the Company's common stock. The rights are represented by and traded with the Company's common stock. There are no separate certificates or markets for the rights.

The rights do not become exercisable or trade separately from the common stock unless 17.5% or more of the common stock of the Company has been acquired, or after a tender or exchange offer is made for 17.5% or greater ownership of the Company's common stock. Should the rights become exercisable, each right will entitle the holder thereof to buy 1/1,000th of a share of the Company's Series A Preferred Stock at an exercise price of \$125. Each 1/1,000th of a share of the new Series A Preferred Stock will essentially be the economic equivalent of one share of common stock.

Under certain circumstances, the rights "flip-in" and become rights to buy the Company's common stock at a 50% discount. Under certain other circumstances, the rights "flip-over" and become rights to buy an acquirer's common stock at a 50% discount.

The rights may be redeemed by the Company for \$0.01 per right at any time on or prior to the fifth day (or a later date as determined by the Board of Directors) following the first public announcement by the Company of the acquisition of beneficial ownership of 17.5% of the Company's common stock.

THE GYMBOREE CORPORATION

10 STOCK REPURCHASE

In fiscal 1997, common stock repurchase programs were authorized by the Board of Directors whereby the Company could buy back up to \$60 million of its common stock. During fiscal 1997, 1,922,000 shares were repurchased by the Company for an aggregate amount of \$49,646,000. During fiscal 1998, there were no shares repurchased by the Company.

11 QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

The quarterly financial information presented below reflects all adjustments which, in the opinion of the Company's management, are of a normal and recurring nature necessary to present fairly the results of operations for the periods presented.

(In thousands, except per share amounts and store data)	1998 Quarter Ended			
	May 2, 1998	Aug. 1, 1998	Oct. 31, 1998	Jan. 30, 1999
Net sales	\$ 103,106	\$ 99,789	\$ 113,991	\$ 140,333
Gross profit	41,479	33,334	41,094	48,626

Operating income	6,084	(1,345)	(430)	5,145
Net income	4,148	(831)	(273)	3,197
Basic income per share	\$ 0.17	\$ (0.03)	\$ (0.01)	\$ 0.13
Diluted income per share	\$ 0.17	\$ (0.03)	\$ (0.01)	\$ 0.13
Stores at end of period	464	495	548	564

1997 Quarter Ended

	May 3, 1997	Aug. 2, 1997	Nov. 1, 1997	Jan. 31, 1998
Net sales	\$ 85,240	\$ 71,684	\$ 101,120	\$ 115,396
Gross profit	38,946	30,452	45,859	50,553
Operating income	12,640	6,544	16,893	17,807
Net income	8,599	4,578	10,865	11,128
Basic income per share	\$ 0.34	\$ 0.19	\$ 0.44	\$ 0.46
Diluted income per share	\$ 0.34	\$ 0.19	\$ 0.44	\$ 0.46
Stores at end of period	380	401	427	435

THE GYMBOREE CORPORATION

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders of  
The Gymboree Corporation:

We have audited the accompanying consolidated balance sheets of The Gymboree Corporation and subsidiaries (the "Company") as of January 30, 1999 and January 31, 1998, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three fiscal years in the period ended January 30, 1999. 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 generally accepted auditing standards. 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, such consolidated financial statements present fairly, in all material respects, the financial position of The Gymboree Corporation and subsidiaries as of January 30, 1999 and January 31, 1998, and the results of their operations and their cash flows for each of the three fiscal years in the period ended January 30, 1999 in conformity with generally accepted accounting principles.

/s/ Deloitte & Touche LLP

San Francisco, California

February 24, 1999

(March 11, 1999 as to the second paragraph of Note 3)

## THE GYMBOREE CORPORATION

## BOARD OF DIRECTORS

Walter F. Loeb  
Director

Stuart G. Moldaw  
Chairman of the Board

Barbara L. Rambo  
Director

Deborah A. Sorondo  
Director

William U. Westerfield  
Director

Carole J. Whitacre  
Director

Gary White  
Vice-Chair and  
Chief Executive Officer

## OFFICERS

Melanie B. Cox  
President

Edward A. Loseman  
Senior Vice President,  
Sourcing and Logistics

Lawrence H. Meyer  
Senior Vice President and  
Chief Financial Officer

Kenneth F. Meyers  
Senior Vice President,  
Human Resources

Stuart G. Moldaw  
Chairman of the Board

Gary White  
Vice-Chair and  
Chief Executive Officer

## SECRETARY

Jeffrey D. Saper  
Wilson, Sonsini,  
Goodrich & Rosati

## VICE PRESIDENTS

Theresa R. Backes  
Vice President,  
Store Operations

Della G. Berger  
Vice President,  
Compensation & Benefits

Robert B. Campbell  
President,  
Play Programs

JoAnn H. Davis  
Vice President,  
Real Estate, Construction  
and Store Planning

John F. Estill  
Vice President &  
Managing Director  
UK/Ireland Stores

Lisa A. Fitzgerald  
Vice President and  
Divisional Merchandise  
Manager-Girls and Layette

Keith L. Harband  
Vice President, Marketing

Lisa G. Harper  
Vice President, Design

Carver L. Johnson  
Vice President and  
Chief Information Officer

Maura B. Kabureck  
Vice President,  
North American Stores

Patricia F. Kampmann  
Vice President and  
Divisional Merchandise  
Manager-Boys, Accessories  
and Play Products

Susan G. Neal  
Vice President,  
Business Development

F. Mario Petrocco  
Vice President & Treasurer

Rick A. Planos  
Vice President, Stores-Zutopia

George A. Rodriguez  
Vice President, Production

Sheree A. Waterson  
Vice President,  
Merchandising-Zutopia

Laura A. Wilkin  
Vice President, Logistics

Edward Wong  
Vice President, Planning & Allocation

#### CORPORATE INFORMATION

##### HEADQUARTERS

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1.800.558.9885

PLAY PROGRAMS

1.800.520.PLAY

WEBSITE

[www.gymboree.com](http://www.gymboree.com)

STOCKHOLDERS INFORMATION

ANNUAL MEETING

Stockholders are invited to attend our annual meeting at 9 a.m. on Wednesday, May 26, 1999 at the San Francisco Airport Marriott Hotel, 1800 Old Bayshore Highway, Burlingame, California.

COMMON STOCK TRADING

Common stock for The Gymboree Corporation is traded under the symbol GYMB on the Nasdaq National Market System.

	FISCAL 1998	
	HIGH	LOW
1st Qtr	27.375	18.250
2nd Qtr	19.031	12.000
3rd Qtr	10.500	4.063
4th Qtr	8.500	4.875

As of April 5, 1999, there were approximately 764 stockholders of record, excluding stockholders whose stock is held in the nominee or street name by brokers.

INDEPENDENT AUDITORS

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San Francisco, CA 94105  
Telephone: 415.247.4000

GENERAL COUNSEL

Wilson, Sonsini,  
Goodrich & Rosati  
650 Page Mill Road

Palo Alto, CA 94304  
Telephone: 650.493.9300

REGISTRAR AND TRANSFER AGENT

Inquiries from our stockholders regarding address changes and lost certificates should be directed to:  
Bank Boston, NP  
c/o Equiserve  
P.O. Box 8040  
Boston, MA 02266  
Telephone: 1.800.733.5001

INVESTOR RELATIONS

Copies of The Gymboree Corporation's 1998 Annual Report, Form 10-K and Form 10-Q are available by writing to:  
The Gymboree Corporation  
Investor Relations  
700 Airport Boulevard  
Burlingame, CA 94010  
Fax Requests: 650.696.7502

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## SUBSIDIARIES OF THE REGISTRANT

Gymboree Manufacturing, Inc., a California corporation.  
Gym-mark, Inc., a California corporation.  
The Gymboree Stores, Inc., a California corporation.  
Gymboree Retail Stores, Inc., a California corporation.  
Gymboree Logistics Partnership, a California General partnership, wholly owned by The Gymboree Stores, Inc. and Gymboree Retail Stores, Inc.  
Gymboree Play Program, Inc., a California corporation.  
Gymboree Operations, Inc., a California corporation.  
Gymboree, Inc., a Canadian and Delaware corporation.  
Gymboree Japan K.K., a Japanese corporation.  
Gymboree Industries Holdings Ltd., a Republic of Ireland Limited Company.  
Gymboree Hong Kong Ltd., a Hong Kong Limited Company, wholly owned by Gymboree Industries Holdings Ltd.  
Gymboree Industries Ltd., a Republic of Ireland Limited Company, wholly owned by Gymboree Industries Holdings Ltd.  
Gymboree Ireland Leasing Ltd., a Republic of Ireland Limited Company.  
Gymboree of Ireland, Ltd., a Republic of Ireland Limited Company.  
Gymboree U.K. Leasing Ltd., a United Kingdom Limited Company.  
Gymboree U.K. Ltd., a United Kingdom Limited Company.

## INDEPENDENT AUDITORS' CONSENT

We consent to the incorporation by reference in Registration Statement Nos. 33-60310, 33-90452, 33-94594 and 333-10811 of The Gymboree Corporation and subsidiaries all on Forms S-8 of our report dated February 24, 1999 (March 11, 1999 as to the second paragraph of Note 3), incorporated by reference in this Annual Report on Form 10-K of The Gymboree Corporation and subsidiaries for the fiscal year ended January 30, 1999.

March 26, 1999

<ARTICLE> 5

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