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Athleta

The defining characteristic of an entrepreneur is that we can talk ourselves into anything. Luckily, I talked myself into entering a phenomenal market—big, underserved, and growing fast—before knowing anything about it.

— Scott W. Kerslake, President and CEO of Athleta

On the morning of March 26, 2002, Scott Kerslake—president and CEO of Athleta—reflected on the unfamiliar sounds of the city while stuck in a Manhattan traffic jam. In contrast, several employees at the Athleta headquarters in Petaluma, California, were preparing to run in the open preserve near the office or take their dogs for a walk. Kerslake and Joe Teno—Athleta's senior vice president of operations—had come to New York with a single goal: to raise \$3 million–\$4 million in a Series E round of financing from investors who understood and appreciated Athleta's business model and culture. Both Kerslake and Teno were determined to return to California with good news for the company's tightly knit group of employees.

In 1998, Kerslake founded Athleta as a "women's sports company" selling a wide range of women's athletic gear through mail order and online. Since that time, Athleta's revenues had grown more than 150% per year and were projected to reach almost \$26 million in 2002. Now, Athleta anticipated augmenting its multichannel strategy by launching physical retail outlets in 2003. Between 1998 and the end of 2002, Athleta expected to have fulfilled over 400,000 orders, acquired a total of 231,000 customers, and generated over \$55 million in revenue—all with under \$5 million in equity capital. Despite Athleta's historical and present-day undercapitalization, Athleta had survived. Kerslake was convinced the company's success was linked to the enormous dedication of the amateur and professional athletes who made up Athleta's staff. While other companies, such as Lucy.com and FogDog Sports, had closed up shop or scaled back significantly after raising tens of millions of dollars, Athleta had survived the shakeout and was ready to begin the next phase of development.

In June 1998, Kerslake had raised a seed round of capital totaling slightly over \$700,000 from friends and family. Less than six months later, Kerslake turned down offers of up to \$10 million in equity to build an online retail company and instead raised only \$1.2 million—falling short of his target of \$2.2 million—from investors who shared his goal of building a multichannel women's sports company. Kerslake kept a tight rein on Athleta's cash expenditures even after raising another \$3.1

Professors William A. Sahlman and Dean's Fellow Taz Pirmohamed (2001) prepared this case. Certain details have been disguised. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

million between 1999 and 2002. Now, in March 2002, Athleta had less than $330,000 of cash remaining, and Kerslake was eager to close a Series E round. While Kerslake was willing to give shareholders a large stake in the company and even accept potentially onerous financing terms, he wanted to preserve the company's unique culture. Kerslake and Teno had been meeting with venture capital (VC) firms, angel investors, and commercial banks while in New York City. With one eye on his Ironman™ watch and the other eye on the endless Manhattan traffic jam, Kerslake wondered if he would cross the finish line—that is, return to California with $3 million–$4 million in capital and supportive investors in hand.

Founder's Vision

Kerslake had always dreamed about starting his own company. Prior to becoming an entrepreneur, he worked as an investment banker at Salomon Smith Barney and in an operating role at a retail company before joining Sapient Corporation as a management consultant in 1993. There, he played a significant role in starting Sapient Corporation's San Francisco office by helping to manage and grow its team from three to 250 employees in a little over two years. He subsequently served as Sapient's director of marketing and was instrumental in the company's successful initial public offering (see **Exhibit 1** for management biographies). Finally, in 1997, Kerslake decided to start his own company. He explained:

> I have always loved sports and lived a very active life. Sports have been important to my physical and spiritual well-being for as long as I can remember—so the business model is completely rooted in personal passion.
>
> Then, one day, I had a dream—literally speaking—about building a women's sports company. It was only after I conceived of the Athleta brand, product line, and catalog that I did any market research. As it turns out, the statistics on the women's sports industry are phenomenal—an incredible growth rate, a huge participant base, and a group of customers frustrated with the dearth of high-quality women's sportswear sold in traditional retail outlets. So, my dream translated into a great market opportunity—one that far exceeded the opportunity in the men's market. While many people are surprised that a man founded a women's sports company, I developed the Athleta concept from the standpoint of an athlete, not the standpoint of a man.

Women's Sports Apparel Market

In 1999, a total of 21.2 million women and 15.5 million men in the U.S. participated in sports and fitness.[1] Women's participation in sports and fitness had grown rapidly in the past decade; by 1999, women made up nearly 50% of total participants in the most popular sports (see **Table A** for detailed statistics on women's sports participation). In addition, women accounted for 58% of all health club memberships in the United States in 2001.

[1] "Fitness in America," National Sporting Goods Association, 1999.

Table A Women's Sports Participation (1999)

Sport	Women/Total Participants
Running	49%
Cycling	49%
Swimming	55%
Inline Skating	56%
Backpacking	49%
Fitness/Gym	72%

Source: Company documents.

In 2000, women spent $25 billion on sports apparel,[2] while the broader market for women's apparel exceeded $96 billion.[3]

Competition

There were four categories of retailers that sold women's athletic gear (see Exhibit 2 for a detailed list of Athleta's competitors by category):

- Tier 1: Women-specific sports retailers concentrating exclusively on the women's market (e.g., Lady Foot Locker, Title 9)
- Tier 2: Specialty sporting goods retailers concentrating on a particular sport (e.g., running or cycling), carrying mid- to high-end products and offering customers a higher level of expertise (e.g., Fleet Feet, Recreation Equipment Incorporated)
- Tier 3: Big-box retailers carrying very broad and deep product selections for many different sports (e.g., Big 5, SportMart)
- Tier 4: Department stores carrying a narrow range of sports-related products (e.g., Nordstrom, Macy's)

Business Model

Kerslake conceptualized Athleta as a premier women's multichannel sports retailer offering a limited selection of top products across a wide variety of sports and an exceptional level of customer service.

Channel Strategy

Athleta was launched as a multichannel company serving customers through the mail-order and online channels. The company planned to launch retail stores in 2003 after growing its expertise in the women's sporting goods market. In 2001, Athleta derived 70% of total revenue from its direct-mail catalogs and 30% of revenues from the Athleta.com Web site. While many experts were

[2] The Women's Athletic Apparel Market, Packaged Facts, 2001.

[3] "U.S. Apparel Industry in 2000," NPDFashionworld℠, March 2001.

concerned that e-commerce cannibalized other channels, Athleta's management team believed that offering consumers a wide range of choices fostered stronger customer relationships and buying patterns. A study on purchasing behavior found that catalog shoppers who visited a retailer's Web site spent 8% more per order and ordered 11% more frequently from the catalog.[4]

Product

The Athleta product line was sourced from Athleta Essentials—a private-label line of bodywear and technical apparel—and high-quality producers including Patagonia, Adidas, Pearl Izumi, Marmot, Hind, and Sugoi. Kerslake explained the philosophy driving the Athleta private-label line:

> We designed our own line of clothing because our customers were requesting items, colors, and styles that weren't being made. One of the things we heard most often was that it's really tough to find athletic pants in tall and petite sizes. We immediately seized this market opportunity by creating private-label athletic pants in hard-to-find sizes.
>
> There are two models for private-label branding: either sell a knockoff of an existing product at a lower price or develop your own distinctive product. Many retailers will take top-selling products to southern China where they are reverse engineered, manufactured, and then sold at a lower price. We didn't want to compete on price. We wanted to manufacture products that were on par with other high-quality manufacturers. While we could have chased a lot of sales by reverse engineering successful products, we didn't want to compromise the integrity of our brand.

Target Customer

Athleta's initial target customers were women between the ages of 18 and 50 with a college education and average household incomes greater than $80,000. They were also physically active and committed to engaging in regular exercise. They had busy lifestyles and therefore sought alternatives to shopping in traditional retail outlets. Finally, they usually bought high-quality merchandise—even if they had to spend more. Kerslake explained:

> Our customers told us they didn't have the time to dig through a giant bin of sports bras at SportMart and try to guess which bra would work best for them, or worse, have to rely on the advice of the teenage boy likely to be behind the register. They wanted to shop in an environment with a well-organized selection of products and knowledgeable staff that were easily accessible. We listened carefully when they described their lifestyles and their biggest problems—and then built a company that could resolve them.

Brand

The Athleta brand was designed to communicate an understanding of and respect for the importance of sports and athletics in women's lives. As such, the company's catalogs featured fit, healthy, athletic women on its pages. In addition, Athleta sought to educate its customers during the sales process. As such, Athleta's customer service staff were carefully selected and then trained to provide accurate information, give thoughtful advice, and understand the particular needs of women vis-à-vis the fit, performance, and comfort of sportswear. Athleta also employed an unusual practice

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[4] "Channel Surfing: Measuring Multi-Channel Shopping," Bizrate.com/J.C. Williams Group, 2001.

in its sales department—it did not set sales goals around individual items, so sales staff could focus on finding the best product for each customer. The Athleta brand represented a belief in building lasting customer relationships based on integrity and trust.

Culture

Athleta worked hard to create an exceptional culture where the employees embraced the company's five core values. The company values all stemmed from a single premise: the most important values in one's professional life should not differ from those in one's personal life. For example, Athleta employees were encouraged to put their families first even though this occasionally resulted in employees leaving work early to pick up their child or take an animal to the vet. Recognizing the importance of staying healthy, the company had built its headquarters close to an open preserve so that employees could easily go running or cycling during breaks. The employee-friendly culture enabled Athleta to maintain lower-than-average turnover rates and attract top talent in key positions. Finally, the open-concept Athleta office was designed to facilitate open communication and to accommodate employees, pets and, on occasion, children.

Early Company History

After developing the Athleta concept and performing market research on the women's sports apparel industry, Kerslake set out to raise a seed round of financing from friends and family. In June 1998, he raised a total of $769,000 and invested the money in producing the company's first catalog and buying lists of potential customers. Athleta opened for business in June 1998. Kerslake recalled the process of acquiring Athleta's first customers:

> There are three ways to rent names: you can exchange names with a database company if you have a house file with your own customer names; you can pay a large list compiler such as Abacus or Z-24 for names; or you can pay another catalog company with a similar demographic for their names. Initially, we purchased lists from a database company. We were extremely lucky because our first batch of 93,500 catalogs garnered a 2.8% response rate. Normally, acquiring customers through purchased lists is a difficult science—somehow, we managed to send catalogs to the right people. By the end of 1999, our house file included 19,800 names of actual customers—most of whom had become repeat customers.

However, at the end of 1998, nearly all of the seed capital Kerslake had raised was exhausted. Though most of Athleta's investors were ardent believers in the business model, very few could participate in a subsequent round. After reviewing his options, Kerslake decided to raise outside equity: "You can only finance your company in a few ways: you can raise outside equity, you can raise debt, or you can stretch the terms offered by your suppliers. Stretching supplier terms is an extremely bad business strategy, and raising a large amount of debt was too difficult—so we had to raise more equity."

In early 1999, Kerslake approached a large number of venture capital firms to raise an additional $2.2 million in equity. He recalled:

> To begin, there were few venture capital firms focused on consumer commerce. When we walked into their offices and asked for $2.2 million to expand our catalog business, they laughed. They told us that nascent, low-tech consumer companies were unlikely to be funded in 1999. Most venture capitalists were investing in dot-coms, not mail-order businesses. We were offered $10 million if we converted our business model to "Athleta.com." From our

perspective, the venture capitalists were narrowly focused on channel instead of the overall brand or business model. It is the hardest thing in the world to look somebody in the eye and turn down $10 million, especially when you aren't sure you have enough capital to make it to the next quarter.

I know that a lot of companies took the money and then privately decided to do what they wanted with it. It sounds ridiculous to turn down $10 million when you really need it, but I wanted to build a company with integrity. So, we stuck to our guns, retained control of the company, and raised a lot less capital. Looking back, I think we made the right decision because competitors like FogDog burned through tens of millions and then closed their doors.

While Kerslake set out to raise $2.2 million, he closed Athleta's first external round of $1.2 million from angel investors at a premoney valuation of $6.8 million in March 1999. (See **Exhibit 3** for Athleta's historical financial statements.) Armed with additional capital, Kerslake set out to begin manufacturing and selling Athleta private-label sportswear and hiring additional customer service staff. He recalled:

Not having enough capital is really tough. We have always been really, really prudent with money—we watch every single penny. The problem with too little capital is that you have to think about the "here and now." You make cash-oriented decisions as opposed to long-term decisions. We haven't had enough capital to build a company the right way, so we have built it by any means possible. It's been a real challenge.

Growing the Company

From the beginning, Kerslake focused on hiring staff that believed in the Athleta business model and shared his passion for sport. He recalled:

Your employees are critical—especially when there is a large gap between what you aspire to do and what you can afford to do. The only way to bridge the gap is through sweat, hard work, and sheer will. We employ athletes who understand the magic of sport—the way going for a run or a bike ride can take you into a completely different realm. Our employees want to help cultivate new and existing athletes. For example, Ellen Krimmel is a former professional athlete who runs our customer service group. She has an enormous will—she would damn near kill herself to help Athleta succeed. There is a downside to such a high level of employee commitment—you don't want your staff to burn out. Every day, I think long and hard about what we need to do in order to attract and retain extraordinary people like Ellen.

Kerslake also described Athleta's teamwork ethic:

Athletes have a profound understanding of what it means to be a team player. Many of our employees are former professional or college athletes who couldn't have succeeded without teamwork. Our employees often say that corporate team-building exercises are "flaky" when compared with the team building inherent in sport. Athleta couldn't have made it this far without employees that espouse a teamwork ethic.

Between 1999 and 2001, Athleta's business model took flight. Despite the paucity of equity capital and the challenges associated with running a retail operation, Athleta developed a loyal customer base. By 2001, Athleta had amassed nearly 152,000 customers and $18.6 million in revenues (see **Table B** for summary of Athleta operating results). Kerslake estimated that 22% of Athleta's orders came from repeat customers. Management claimed that, in 2001, the Athleta catalog generated an average response rate of 6.0%[5] and an average order size of $128,[6] as compared to industry standards of 3.6% and $100, respectively.[7] Kerslake believed that the company's operating results proved the basic business model and demonstrated the company's capacity to succeed in the women's sportswear industry. So, Kerslake decided to raise another round of equity in order to take the company to the next stage of development.

Table B Summary of Athleta Actual and Projected Operating Results

	1999	2000	2001	Est. 2002[a]
Revenue (millions)[b]	$1.7	$9.7	$18.6	$25.9
Customer orders	15,670	81,778	144,375	195,184
Average order size	$104.63	$118.39	$128.61	$132.70
Athleta's house file	19,800	77,500	152,000	231,000

Source: Company.

[a]Estimated for the 12 months ending May 31, 2002.

[b]Revenues represent merchandise sales plus shipping income.

Plans for Growth

In early 2002, Kerslake and his senior management team developed a strategic growth plan for the company (see **Exhibit 4** for Athleta's projected financial statements). They articulated the goals and capital requirements to enable Athleta to become a leading, multichannel women's sports company (see **Table C** for Athleta's detailed financing requirements).

Table C Summary of Athleta Financing Requirements

Area	Purpose of Proceeds	Capital Required (M)
Circulation Growth	Increase annual circulation from 6.5M to 20M in 4 years	$1.50
Working Capital	Improve terms with suppliers/manufacturers	$1.10
Infrastructure	Expand offices and distribution facilities; MIS	$0.28
Merchandising	Private-label product expansion	$0.22
Human Resources	New staff in HR, merchandising, direct marketing	$0.22
General Purpose	Cushion	$0.30
Total		**$3.62**

Source: Company.

[5] Response rate based on total orders/total catalogs mailed in a single fiscal year.

[6] Based on total catalog revenues/total orders in a single fiscal year.

[7] Average industry figures sourced from the DMA State of the Catalog Industry Report, 1999.

1. Increase catalog circulation to acquire a larger base of customers

The catalog business depended heavily upon customer response rates to mailings. In general, it cost Athleta approximately $0.60 to print and mail each catalog. Athleta sought to achieve a 1.8% response rate on prospects[8] and an average order size of $135.00 in order to break even (given 2002 projected margins and fulfillment costs). By 2003, Athleta aimed to grow its catalog circulation from 6.5 million to 20 million. Management believed there were at least 20 million customers in Athleta's target market.

2. Improve supplier terms

Beginning in 2000, Athleta paid its suppliers on an extended basis, forgoing early-payment discounts as large as 8% of cost of goods sold (COGS). While extending supplier payments enabled Athleta to stretch its working capital, the company estimated that it could reduce COGS by 2% through early payment. In addition, the company's suboptimal inventory management resulted in $11.00 for each back order and an annual inventory turnover of four compared with the industry average of five. Athleta required $1.1 million for working capital in order to improve terms with suppliers and reduce inventory management costs.

3. Transfer headquarters and improve management information systems (MIS)

Due to Athleta's rapid growth, it had outgrown its current headquarters and 9,000-square-foot distribution center. Athleta also needed to upgrade its MIS in order to provide more detailed financial reporting for each distribution channel. Athleta required $280,000 for moving expenses and upgrading the company's systems.

4. Expand Athleta's private-label line

Since its inception, Athleta's private-label brand filled a niche in the women's sportswear market. Athleta's private-label line of clothing expanded from 7% of product assortment in 1998 to 28% of product assortment in 2002. In addition, Athleta's private-label line frequently outsold the best products from brands such as Patagonia, Adidas, and Sugoi. Gross margins on Athleta's private-label line were 20% higher than those of its branded manufacturers. Athleta projected that by 2005, 40%–45% of total assortment and 65% of total sales would stem from private-label product sales. Athleta required $220,000 to enhance its private-label business.

5. Team expansion and marketing initiatives

Finally, Athleta intended to hire new staff and invest in new marketing initiatives. To begin, Athleta sought to selectively add to its senior management team. In addition, at least 20 new employees were required in the customer service, distribution, and Web development departments. Athleta also planned to initiate several new marketing programs, including 1) increased editorial coverage/product placement, 2) grass-roots marketing programs and sponsorships, 3) strategic partnerships and comarketing agreements, and 4) co-op advertising. Kerslake estimated that $220,000 was required to grow the Athleta team and to invest in marketing initiatives.

[8] Prospects are defined as new names added to the Athleta mailing list.

Financing Options

When Kerslake and Teno went to New York in late March 2002, Athleta had less than $330,000 in cash remaining. However, several different options emerged during their fund-raising trip to the East Coast.

Venture capital During the first quarter of 2002, the VC market continued a cyclical downturn that had started in early 2001 (see **Exhibit 5** for U.S. venture capital investment trends). In particular, the consumer e-commerce industry was hit hard during the dot-com market crash, which resulted in hundreds of companies declaring bankruptcy because they could not develop a sustainable economic model and/or raise additional capital. As such, VC firms were much more cautious about investing in consumer retail business models and applied even higher discount rates to revenue projections. Though Kerslake was interested in securing a Series E round from a VC firm, he was concerned that Athleta's projected revenues and profits were not high enough to meet the minimum standards set out by most firms. To make matters worse, consumer retail companies had fallen out of favor in the public markets, resulting in sagging valuations (see **Exhibit 6** for specialty retailer comparisons). Therefore, exit options for retailers in the consumer sector were limited to being acquired or merging with another company. Kerslake explained:

> It was really difficult to find a VC firm interested in specialty retail companies—especially one with real expertise in our sector. The firms we approached were very open with us—they told us that they invested in proven concepts, strong management teams, and aggressive growth targets. They also told us to expect a more onerous term sheet that included participation clauses, full-ratchet provisions, and cumulative dividends. The only good news was that deal flow had decreased substantially, so they were willing to move quickly when they found the right portfolio companies.

Angel investors By 2002, there were literally thousands of active angel investors in the U.S., though the crash of 2000–2001 had burned many investors and forced them to reconsider investing in private companies. While in New York, Kerslake and Teno met with a handful of angel investors whose names they had received from existing investors, employees, and VCs. Kerslake had not yet approached other potential angel investors including professional athletes, female celebrities, and owners of women's sports teams. After meeting with a handful of angel investors, Kerslake had several concerns:

> Because of our cash crunch, I was concerned about the time and effort required to raise equity from a group of angels. Given that most angel investors invest between $50,000 and $1 million, we would have to sell our plan to 5 or 10 or even 20 different angels in order to raise $3–$4 million. The upside is that most angel investors really appreciated our concept and business model—they wanted to be "partners" rather than just "investors" in the company.

Commercial banks Another financing option was to negotiate credit lines with one or several different commercial banks in order to finance the company's growing inventory. Based on Athleta's total sales and inventory figures for 2001, Kerslake estimated that the company could raise between $750,000 and $2 million in credit facilities. However, the credit markets had tightened during 2001, and commercial banks were reluctant to open large credit lines with early-stage or higher-risk companies. Kerslake explained:

> Securing credit lines was a last resort for us—mainly because we were unlikely to raise the full amount we required from a commercial bank. While we needed to secure credit lines for Athleta's growing inventory, we also viewed the commercial banks as a viable source of bridge

> financing. Raising a small amount of debt would buy us enough time to raise the Series E from other sources. Unfortunately, commercial banks were very tight-fisted in 2002.

Kerslake was eager to develop a sound financing plan for Athleta. Every day, his company helped hundreds of women find athletic apparel that met their needs. And, Kerslake was convinced that bringing Athleta into physical retail outlets would open up dozens of new opportunities for the company to serve female athletes. Now all he had to do was secure the capital necessary to take Athleta to the next level.

Exhibit 1 Management Biographies

Scott W. Kerslake (37) founded Athleta and serves as President and Chief Executive Officer of the Company. Mr. Kerslake has investment banking experience with Salomon Smith Barney (formerly known as Smith Barney), as well as operating experience in two different industries including retail. Mr. Kerslake was previously a management consultant at Sapient Corporation. He played a significant role in starting Sapient Corporation's San Francisco office by helping grow and manage its team from 3 to 250 employees in a little over two years. He subsequently served as Sapient's Director of Marketing and was instrumental in the company's initial public offering.

Joe Teno (49) serves as Athleta's Senior VP of Operations and brings a wealth of operational experience from the direct marketing and retailing world. Most recently, Mr. Teno ran all operations for Travelsmith, a $130mm direct mail company with 250 employees. Prior to Travelsmith, Mr. Teno spent 13 years at L.L. Bean in a number of senior management positions, including: Director of Total Quality and Human Resources; Director of New Customer Acquisition; and senior manager roles for Corporate Forecasting, Marketing Operations, and Inventory Planning & Liquidations.

Nedis Della Chiesa (34) is Athleta's Controller. Ms. Della Chiesa was formerly the Financial Reporting Manager at Robert Mondavi Corporation, responsible for preparing financial statements, forecasts and SEC reporting. Prior to her work at Robert Mondavi, she was in the audit practice at PricewaterhouseCoopers LLP. Additionally, Ms. Della Chiesa has extensive international experience in finance and accounting and is fluent in German.

Elizabeth Howland (48) is Athleta's Director of Circulation. Ms. Howland has 20 years of experience in catalog circulation, marketing, merchandising and senior management positions. Most recently she served as the Vice President of Client Services at Triplex Direct Marketing, a list supplier to the direct marketing industry. Prior to her work at Triplex, Ms. Howland held various senior positions at Biobottoms including General Manager, Executive Vice President, Director of Marketing and Interim Director of Merchandising. Additionally, Ms. Howland has served as Director of Database Marketing at Gymboree.

Debbie Overton (41) is responsible for Inventory Control and Reporting at Athleta. Ms. Overton has eighteen years of experience in inventory forecasting, planning and purchasing for both catalog and retail. She spent six years with The Sharper Image as Merchandising Control Manager and Store Planning Manager and six years with Biobottoms as Director of Merchandising and Manager of Systems, Reporting and Analysis. Ms. Overton has experience in the operations of high-growth companies and has been a critical member of teams that have grown from $15 million in sales to over $200 million. Prior to joining Athleta, Ms. Overton consulted for a number of mail order companies.

Lara Dittoe (31) is Athleta's product manager and has ten years of experience in the sporting goods industry, including managing 'Fast Lady Sports,' a women-specific running store chain in Seattle. Ms. Dittoe subsequently represented a number of the top cycling and outdoor product manufacturers in the Pacific Northwest.

Kathy Frank (51) is responsible for Athleta's distribution operations. Ms. Frank has over 25 years of experience in fulfillment, distribution and warehouse operations. Ms. Frank spent ten years at Koret of California as Assistant Distribution Manager and ten years as Distribution Manager at Biobottoms. Most recently, Ms. Frank ran the catalog distribution operations at Illuminations, a $100mm direct marketer of home ware products.

Tami Anderson (33) is responsible for marketing and brand development at Athleta. Ms. Anderson has ten years of experience in advertising and public relations and most recently served as Vice-President/Group Manager for the Silicon Valley office of Ketchum where her clients included Levi Strauss, Intuit and Visa. Prior to joining Ketchum, she served as Public Relations Manger for Gryphon Software, a San Diego-based developer/publisher. She began her career in marketing as a broadcast media buyer at Oster & Associates, Inc., where she later founded the public relations department. Ms. Anderson is responsible for developing and executing all internal and external communications for Athleta, including brand building via advertising, public relations and online partnerships.

Ellen Krimmel (42) is responsible for Athleta's customer service operations. Ms. Krimmel most recently was a professional cyclist and raced for the Saeco-Timex Women's Cycling Team. Prior to racing professionally, Ms. Krimmel gained extensive experience in all phases of apparel design and product development, including serving as a design consultant to The North Face, and Head Technical Designer for Esprit De Corp. In addition Ms. Krimmel was a designer for apparel maker San Francisco Blue and a Merchandiser for Swatch Watch, USA. Ms. Krimmel still devotes time to cycling and was MVP and Captain of her collegiate soccer team at University of Vermont.

Source: Company.

Exhibit 2 Women's Sportswear Competitive Space

1. Women's Sports Retailers Athleta [C,O] Title 9 Sports [C,O] Lady Footlocker [R]	**2. Specialty Retailers** REI [R,C,O] EMS [R,O] Performance Bike [R,C,O] Road Runner Sports [C,O] Colorado Cyclist [C,O]
3. Big Box Retailers Foot Locker [R] The Sports Authority [R, O] Gart Sports [R] Copeland's [R] Global Sports[O] Hibbett Sports [R] Sport Mart [R] Big 5 [R]	**4. Department Stores** Neiman Marcus [R,C,O] Macy's [R,C,O] Nordstrom [R,C,O] Robinson's-May Co. [R,C,O] R=Offline Retailer O=Online Retailer C=Catalog Retailer

Source: Company documents.

Exhibit 3 Athleta Historical Financials (Income Statement)

ATHLETA CORPORATION
HISTORICAL AND COMMON-SIZE INCOME STATEMENTS

	Fiscal Years Ended May 31,			Fiscal Years Ended May 31,		
	1999	2000	2001	1999	2000	2001
	$000	$000	$000	%	%	%
Merchandise Sales	1,528	8,998	17,214	109.8	116.9	120.0
Shipping Income	106	639	1,342	7.6	8.3	9.4
Total Gross Sales	1,634	9,637	18,556	117.4	125.2	129.4
Returns	242	1,937	4,213	17.4	25.2	29.4
Net Sales	1,392	7,700	14,343	100.0	100.0	100.0
Cost of Goods Sold	770	4,351	8,222	55.3	56.5	57.3
Gross Profit	622	3,348	6,121	44.7	43.5	42.7
Operating Expenses:						
Administration Expense	146	424	698	10.5	5.5	4.9
Employment Expense	462	1,185	2,482	33.2	15.4	17.3
Fulfillment Expense	90	380	1,069	6.5	4.9	7.5
Marketing Expense	736	2,197	4,151	52.9	28.5	28.9
Total Operating Expenses	1,434	4,187	8,399	103.1	54.4	58.6
Operating Income	(812)	(839)	(2,279)	(58.4)	(10.9)	(15.9)
Other Expenses (Income):						
Depreciation & Amort.	31	57	75	2.2	0.7	0.5
Interest Expense	4	17	43	0.3	0.2	0.3
Other Inc/Exp.	(3)	19	(17)	(0.2)	0.2	(0.1)
Total Other Expenses (Income)	31	93	101	2.3	1.2	0.7
Pretax Income	(844)	(932)	(2,380)	(60.6)	(12.1)	(16.6)
Income Taxes Owed (Tax Credit)	(7)	(286)	(489)	(0.5)	(3.7)	(3.4)
Net Income	(837)	(646)	(1,891)	(60.1)	(8.4)	(13.2)

Source: Company documents.

Exhibit 3 (continued) Athleta Historical Financials (Balance Sheet)

ATHLETA CORPORATION
HISTORICAL AND COMMON-SIZE BALANCE SHEETS

	As of May 31,			As of May 31,		
	1999	2000	2001	1999	2000	2001
	$000	$000	$000	% of Gross Sales		
				Gross Sales before Returns		
				1,634	9,637	18,556
ASSETS						
Current Assets:						
Checking/Savings	517	96	132	31.6	1.0	0.7
Accounts Receivable	5	150	233	0.3	1.6	1.3
Inventories	349	1,517	2,476	21.3	15.7	13.3
Prepaid Catalog	244	606	597	14.9	6.3	3.2
Other Current Assets	30	80	46	1.9	0.8	0.2
Total Current Assets	1,145	2,449	3,484	70.1	25.4	18.8
Total Fixed Assets	190	249	444	11.6	2.6	2.4
Other Assets:						
Start Up Costs	30	23	15	1.9	0.2	0.1
Tax Loss Carry Forward	11	297	787	0.7	3.1	4.2
Total Other Assets	41	320	802	2.5	3.3	4.3
Total Assets	1,376	3,018	4,730	84.2	31.3	25.5
LIABILITIES						
Current Liabilities:						
Accounts Payable	334	1,309	2,342	20.4	13.6	12.6
Accrued Expenses	30	148	278	1.8	1.5	1.5
Current Portion of Long-term Debt	-	-	101	-	-	0.5
Conv. Debt	-	878	115	-	9.1	0.6
Reserve for Sales Returns and Allowances	-	220	261	-	2.3	1.4
Other Current Liabilities	9	8	-	0.5	0.1	-
Total Current Liabilities	372	2,562	3,096	22.8	26.6	16.7
Long Term Liabilities:						
Long Term Debt, net of current portion	-	-	37	-	-	0.2
Other Long Term Liabilities	14	7	-	0.9	0.1	-
Total Long Term Liabilities	14	7	37	0.9	0.1	0.2
Total Liabilities	386	2,569	3,133	23.6	26.7	16.9
EQUITY						
Shareholders' Equity:						
Series A	769	769	769	47.1	8.0	4.1
Series B	1,097	1,201	1,988	67.1	12.5	10.7
Series C	-	-	154	-	-	0.8
Series D	-	-	2,095	-	-	11.3
Additional Paid in Capital - Series B Warr.	-	2	0	-	0.0	0.0
Retained Earnings	(877)	(1,523)	(3,414)	(53.7)	(15.8)	(18.4)
Common Stock	-	-	5	-	-	0.0
Total Shareholders' Equity	990	449	1,597	60.6	4.7	8.6
Total Liabilities and Shareholders' Equity	1,376	3,018	4,730	84.2	31.3	25.5

Source: Company documents.

Exhibit 3 (continued) Athleta Historical Financials (Cash Flow Statement)[a]

ATHLETA CORPORATION
HISTORICAL STATEMENTS OF CASH FLOW

	Fiscal Years Ended May 31,		
	1999	2000	2001
	$000	$000	$000
Cash Flow from Operating Activities			
Net Loss	(837)	(646)	(1,891)
Adjustments to Reconcile Net Loss to net cash change from Operating Activities:			
Depreciation and Amortization	38	57	75
Deferred Taxes	(11)	(286)	(490)
Net (Increase) Decrease in Operating Assets:			
Accounts Receivable	(5)	(145)	(83)
Inventories	(316)	(1,168)	(959)
Prepaid Catalog Costs	(108)	(362)	9
Other Current Assets	(24)	(50)	34
Net Increase (Decrease) in Operating Liabilities:	-	-	-
Accounts Payable	237	975	1,033
Accrued Expenses	30	118	180
Reserve for Sales and Returns Allowances	2	218	41
Net Cash Change from Operating Activities	(995)	(1,288)	(2,051)
Cash Flow from Investing Activities			
Purchases of Property, Plant, & Equipment	(50)	(109)	(145)
Disbursements for Org. Costs	(9)	-	-
Net Cash Change from Investing Activities	(59)	(109)	(145)
Cash Flow from Financing Activities			
Proceeds from Debt & Capital Leases	(3)	871	(39)
Proceeds from Issuance of Equity	1,317	105	2,265
Other Cash Flow from Financing Activities	(25)	-	5
Net Cash Change from Financing Activities	1,289	976	2,232
Increase (Decrease) in Cash and Equivalents	236	(421)	36
Cash and Equivalents, Beginning of Year	281	517	96
Cash and Equivalents, End of Year	517	96	132

Source: Company documents.

[a]There is some confusion about reconciling the balance sheet changes and cash flow statement items with respect to financing. The discrepancy may be explained by the conversion of some convertible debt issued in the year ended May 31, 2000 to preferred stock in the following fiscal year.

Exhibit 4 Athleta Financial Projections (Income Statement)

ATHLETA CORPORATION
PROJECTED AND COMMON-SIZE INCOME STATEMENTS

	Projected Fiscal Years Ending May 31,						Projected Fiscal Years Ending May 31,					
	2002	2003	2004	2005	2006	2007	2002	2003	2004	2005	2006	2007
	$000	$000	$000	$000	$000	$000	%	%	%	%	%	%
Merchandise Sales	24,022	29,493	38,342	54,033	89,253	109,588	121.7	120.2	121.3	122.7	122.0	122.0
Shipping Income	1,896	2,419	2,858	4,323	7,140	8,767	9.6	9.9	9.0	9.8	9.8	9.8
Total Sales	25,918	31,912	41,200	58,355	96,393	118,355	131.4	130.0	130.3	132.5	131.7	131.7
Returns	6,188	7,373	9,585	14,319	23,206	28,493	31.4	30.0	30.3	32.5	31.7	31.7
Net Sales	19,731	24,539	31,614	44,036	73,187	89,862	100.0	100.0	100.0	100.0	100.0	100.0
Cost of Goods Sold	10,713	12,371	15,228	20,257	32,202	38,641	54.3	50.4	48.2	46.0	44.0	43.0
Gross Profit	9,018	12,168	16,386	23,780	40,985	51,221	45.7	49.6	51.8	54.0	56.0	57.0
Operating Expenses:												
Administration Expense	767	713	1,012	1,497	2,562	2,696	3.9	2.9	3.2	3.4	3.5	3.0
Employment Expense	3,641	4,181	5,742	8,147	13,174	15,277	18.5	17.0	18.2	18.5	18.0	17.0
Fulfillment Expense	934	1,109	706	1,321	2,196	2,247	4.7	4.5	2.2	3.0	3.0	2.5
Marketing Expense	4,655	5,530	7,223	9,468	15,369	18,422	23.6	22.5	22.8	21.5	21.0	20.5
Total Operating Expenses	9,997	11,532	14,683	20,433	33,300	38,641	50.7	47.0	46.4	46.4	45.5	43.0
Operating Income	(979)	636	1,703	3,347	7,685	12,581	(5.0)	2.6	5.4	7.6	10.5	14.0
Other Expenses (Income):												
Depreciation & Amort.	111	172	264	330	462	814	0.5	0.6	0.7	0.8	0.7	0.6
Interest Expense	-	-	-	32	51	61	0.3	-	-	-	0.1	0.1
Other Inc/Exp.	3	3	3	77	123	196	(0.1)	0.0	0.0	0.0	0.2	0.2
Total Other Expenses (Income)	114	175	267	439	636	1,071	0.7	0.6	0.7	0.8	1.0	0.9
Pretax Income	(1,093)	461	1,436	2,907	7,049	11,510	(16.6)	(5.5)	1.9	5.4	6.6	9.6
Income Taxes Owed (Tax Credit)	(251)	106	396	1,076	2,608	4,259	3.4	1.3	(0.4)	(1.2)	(2.4)	(3.6)
Net Income	(842)	355	1,040	1,832	4,441	7,251	(13.2)	(4.3)	1.4	4.2	4.2	6.1

Source: Company documents.

Exhibit 4 (continued) Athleta Financial Projections (Balance Sheet)

ATHLETA CORPORATION
PROJECTED AND COMMON-SIZE BALANCE SHEETS

	Projected Fiscal Years Ended May 31,						Projected Fiscal Years Ended May 31,					
	2002	2003	2004	2005	2006	2007	2002	2003	2004	2005	2006	2007
	$000	$000	$000	$000	$000	$000	% of Gross Sales					
							Gross Sales Before Returns					
ASSETS							25,918	31,912	41,200	58,355	96,393	118,355
Current Assets:												
Checking/Savings	1,756	2,176	2,342	5,095	6,855	12,141	6.8	6.8	5.7	8.7	7.1	10.3
Accounts Receivable	336	413	537	732	1,210	1,485	1.3	1.3	1.3	1.3	1.3	1.3
Inventories	3,589	4,031	4,141	6,100	9,697	11,636	13.8	12.6	10.1	10.5	10.1	9.8
Prepaid Catalog	885	1,175	1,534	1,471	2,338	2,805	3.4	3.7	3.7	2.5	2.4	2.4
Other Current Assets	62	61	88	114	181	218	0.2	0.2	0.2	0.2	0.2	0.2
Total Current Assets	6,628	7,855	8,641	13,512	20,281	28,285	25.6	24.6	21.0	23.2	21.0	23.9
Total Fixed Assets	478	980	1,320	1,320	1,518	2,464	1.8	3.1	3.2	2.3	1.6	2.1
Other Assets:												
Start Up Costs	-	-	-	-	-	-	-	-	-	-	-	-
Tax Loss Carry Forward	1,038	932	536	-	-	-	4.0	2.9	1.3	-	-	-
Total Other Assets	1,038	932	536	-	-	-	4.0	2.9	1.3	-	-	-
Total Assets	8,144	9,767	10,497	14,832	21,799	30,749	31.4	30.6	25.5	25.4	22.6	26.0
LIABILITIES												
Current Liabilities:												
Accounts Payable	2,927	3,149	3,308	4,897	6,271	7,389	11.3	9.9	8.0	8.4	6.5	6.2
Accrued Expenses	235	251	364	684	1,088	1,306	0.9	0.8	0.9	1.2	1.1	1.1
Line of Credit	-	990	440	770	1,210	1,375	-	3.1	1.1	1.3	1.3	1.2
Reserve for Sales Returns and Allowances	261	330	330	539	825	990	1.0	1.0	0.8	0.9	0.9	0.8
Other Current Liabilities	114	86	55	110	132	165	0.4	0.3	0.1	0.2	0.1	0.1
Total Current Liabilities	3,538	4,806	4,497	7,000	9,526	11,225	13.7	15.1	10.9	12.0	9.9	9.5
Long Term Liabilities:												
Long Term Debt, net of current portion	-	-	-	-	-	-	-	-	-	-	-	-
Other Long Term Liabilities	-	-	-	-	-	-	-	-	-	-	-	-
Total Long Term Liabilities	-	-	-	-	-	-	-	-	-	-	-	-
Total Liabilities	3,538	4,806	4,497	7,000	9,526	11,225	13.7	15.1	10.9	12.0	9.9	9.5
EQUITY												
Shareholders' Equity:												
Series A	769	769	769	769	769	769	3.0	2.4	1.9	1.3	0.8	0.6
Series B	1,988	1,988	1,988	1,988	1,988	1,988	7.7	6.2	4.8	3.4	2.1	1.7
Series C	154	154	154	154	154	154	0.6	0.5	0.4	0.3	0.2	0.1
Series D	2,095	2,095	2,095	2,095	2,095	2,095	8.1	6.6	5.1	3.6	2.2	1.8
Series E	3,850	3,850	3,850	3,850	3,850	3,850	14.9	12.1	9.3	6.6	4.0	3.3
Add. Paid in Capital - Series B Warr.	0	0	0	0	0	0	0.0	0.0	0.0	0.0	0.0	0.0
Retained Earnings	(4,256)	(3,901)	(2,862)	(1,030)	3,411	10,662	(16.4)	(12.2)	(6.9)	(1.8)	3.5	9.0
Common Stock	5	5	5	5	5	5	0.0	0.0	0.0	0.0	0.0	0.0
Total Shareholders' Equity	4,606	4,961	6,000	7,832	12,273	19,524	17.8	15.5	14.6	13.4	12.7	16.5
Total Liab. and Shareholders' Equity	8,144	9,767	10,497	14,832	21,799	30,749	31.4	30.6	25.5	25.4	22.6	26.0

Source: Company documents.

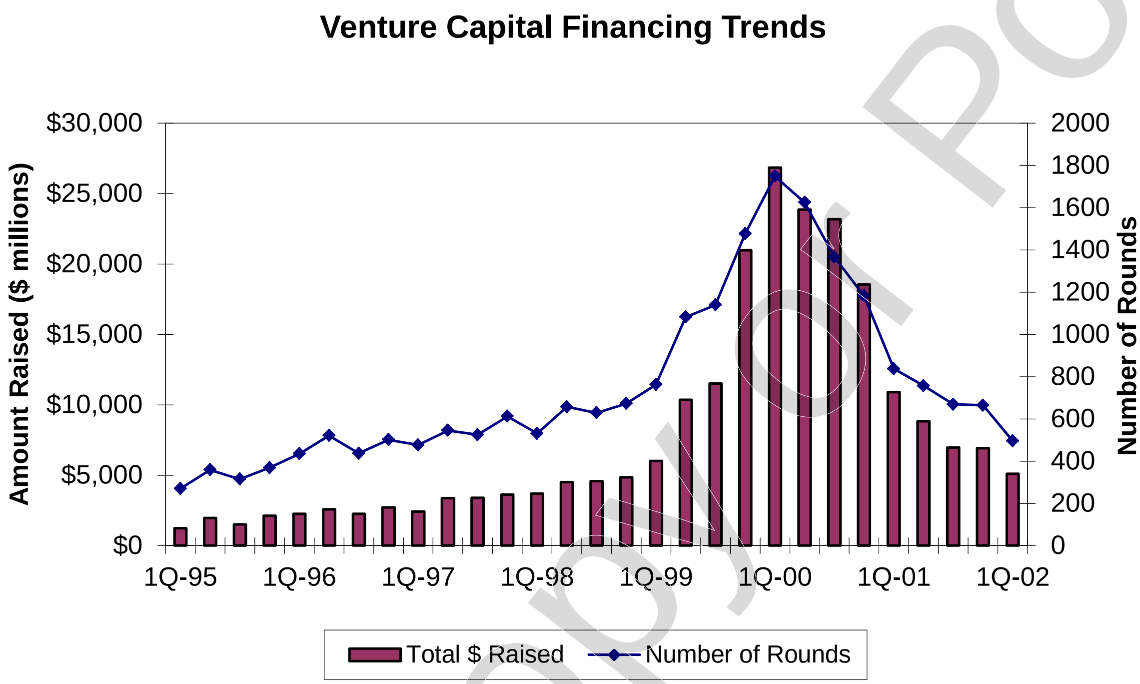
Exhibit 4 (continued) Athleta Financial Projections (Cash Flow Statement)

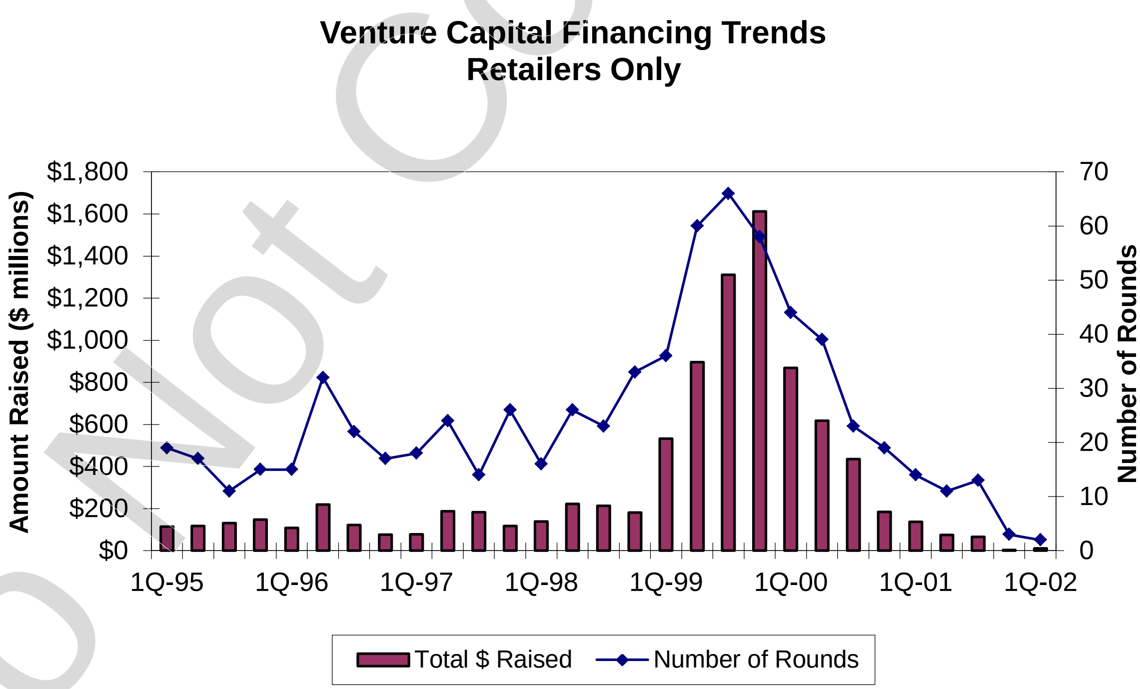
ATHLETA CORPORATION
PROJECTED STATEMENTS OF CASH FLOW

	Projected Fiscal Years Ending May 31,					
	2002	2003	2004	2005	2006	2007
	$000	$000	$000	$000	$000	$000
Cash Flow from Operating Activities						
Net Income (Loss)	(842)	355	1,040	1,832	4,441	7,251
Adjustments to Reconcile Net Income to Change From Operating Activities:						
Depreciation and Amortization	111	172	264	330	462	814
Deferred Taxes	(251)	106	396	536	-	-
Net (Increase) Decrease in Operating Assets:						
Accounts Receivable	(103)	(77)	(124)	(196)	(477)	(276)
Inventories	(1,113)	(442)	(110)	(1,959)	(3,597)	(1,939)
Prepaid Catalog Costs	(288)	(290)	(359)	63	(867)	(467)
Other Current Assets	(0)	1	(27)	(26)	(67)	(36)
Net Increase (Decrease) in Operating Liabilities:						
Accounts Payable	585	221	159	1,589	1,374	1,118
Accrued Expenses	(42)	15	113	320	404	218
Reserve for Sales and Returns Allowances	-	69	-	209	286	165
Other Liabilities	(0)	(28)	(31)	55	22	33
Net Cash Change from Operating Activities	(1,944)	103	1,320	2,754	1,979	6,881
Cash Flow from Investing Activities						
Purchases of Property, Plant, & Equipment	(145)	(673)	(604)	(330)	(660)	(1,760)
Cash Flow from Financing Activities						
Proceeds from Debt & Capital Leases	(136)	-	(990)	330	440	165
Proceeds from Issuance of Equity	3,850	-	-	-	-	-
Other Cash Flow from Financing Activities	-	990	440	-	-	-
Net Cash Change from Financing Activities	3,714	990	(550)	330	440	165
Increase (Decrease) in Cash and Equivalents	1,624	420	166	2,754	1,759	5,286
Cash and Equivalents, Beginning of Year	132	1,756	2,176	2,342	5,095	6,855
Cash and Equivalents, End of Year	1,756	2,176	2,342	5,095	6,855	12,141

Source: Company documents.

Exhibit 5 Venture Capital Investments: Overall and in Consumer Retail Sector (1995–2002)





Source: Adapted from Venture One, Equity Financings for Venture-Backed Companies, by Industry Group (1995–1Q 2002). Available at www.ventureone.com.

Exhibit 6 Specialty Retail Comparisons

	Share Price April 4, 2002	Market Capitalization	Five-Year Growth Rate	EPS Multiple 2001	EPS Multiple 2002E	EPS Multiple 2003E	EBITDA Multiple 2001	EBITDA Multiple 2002E
Specialty Retailers								
Abercrombie	$30.14	3,059	20%	$1.65	15.9	13.4	9.1	7.8
Ann Taylor	$41.90	1,324	20%	$1.34	20.7	17.8	10.8	9.4
Children's Place	$33.20	901	25%	$1.73	15.4	12.3	8.2	6.6
Gap	$14.92	12,900	15%	$0.14	33.4	19.8	12.0	7.4
Gucci	$92.16	9,360	11%	$2.60	36.1	27.3	14.2	14.0
Gymboree	$14.55	437	12%	$0.16	27.2	21.3	12.1	8.4
Limited	$16.99	7,396	18%	$0.88	18.5	15.8	6.5	6.8
Oakley	$17.15	1,188	20%	$0.72	21.9	18.5	12.8	10.8
Pacific Sunwear	$24.26	804	25%	$0.91	21.4	17.3	10.7	8.5
Talbots	$34.05	2,104	15%	$2.00	14.9	12.9	8.7	7.8
Tiffany	$35.24	5,275	18%	$1.17	27.8	23.5	15.4	14.0
Too, Inc	$28.50	921	20%	$1.23	19.4	16.3	10.6	9.1
Vans	$11.79	216	20%	$0.94	23.4	14.7	4.7	7.4
Zales	$40.08	1,411	15%	$2.76	12.3	11.3	6.0	5.7
Athletic Footwear Retailers								
Finish Line	$18.10	448	10%	$0.70	20.4	17.8	9.5	7.6
Foot Locker	$15.88	2,392	14%	$0.98	14.0	12.3	6.4	5.8
Footstar	$30.59	633	14%	$2.26	11.1	9.7	5.4	4.7
The Sports Authority	$11.42	383	N/M	$0.32	19.0	16.3	8.5	7.5

Source: Adapted from Merrill Lynch (Specialty Retail Scoreboard, April 2002).