

Teavana Holdings, Inc.:

TEA: Acquisition Validates Unique Operating Model

KeyBanc Capital Markets Inc.
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Rating	BUY
Price	\$19.76
12- Mo. Price Target	\$28.00
Dividend	\$0.00
Yield	0.0%
52- Wk. Range	\$14 - \$29
Trading Volume (000)	276
Market Cap. (mm)	\$770.6
Shares Out. (mm)	39.00
Book Value/Share	\$1.38

EPS (Net) Summary

FY Jan	2011A	2012E	2013E
1Q	\$0.09	\$0.10	--
2Q	\$0.03	\$0.04	--
3Q	\$0.02	\$0.03	--
4Q	\$0.32	\$0.42	--
YEAR	\$0.46	\$0.59	\$0.81
Prior	\$0.46	\$0.59	\$0.78
First Call	--	\$0.62E	\$0.79E
P/E	43.0x	33.5x	24.4x

ACTION STATEMENT

While we think Teavana's (TEA-NYSE) acquisition of the Canadian business Teaopia is notable, we believe the most important element of the acquisition is validation of Teavana's business model. The acquisition gives Teavana an important beachhead into the attractive Canadian market (2x the per capita tea consumption as the United States, per company) in 46 high-quality locations. The acquisition will be nominally accretive in FY13, but we think the more important element of the acquisition is the validation of Teavana's unique operating model and culture. The stock remains one of the most differentiated in our coverage universe. Valuation is attractive for long-term growth investors at 33.5x 2012 P/E and 1.1x 2012 PEG, compared to 31.6x P/E and 1.3x PEG for the active and healthy lifestyle peer groups, respectively. We reiterate **BUY** rating and our \$28 price target, which implies a 47.4x P/E based on our 2012 EPS estimate.

• 2013E: \$0.81 from \$0.78

KEY INVESTMENT POINTS

The details. Teavana announced its acquisition of Teaopia, a leading Canadian specialty tea retailer, for \$26.9 million in an all- cash transaction. Teavana will use cash on hand as well as its revolving credit facility to fund the transaction. There will be approximately \$25,000 per store in rebranding costs when stores are moved to Teavana branding. Management notes that the transaction will be neutral to earnings in FY12 and \$0.03- \$0.04 accretive in FY13, excluding transaction costs.

The acquisition should drive long-term earnings growth. Teaopia had approximately CAD \$17 million in sales for its 46 company- owned stores in high-quality mall locations across Canada. Despite a similar product mix, overall mall productivity and loose- leaf tea contribution, Teaopia had sales productivity less than half Teavana (\$435,000 at Teaopia vs. \$913,000 at Teavana). We believe that, over time, Teavana's management team can raise sales productivity levels to Teavana's levels. Should management be successful in achieving this and driving a 25% four- wall contribution margin (similar to Teavana in the United States), the transaction could be (excluding transaction costs and interest expense) up to \$0.16 accretive – see Exhibit 2.

The important takeaway: Teavana has a truly unique store operating model. We find it interesting that a similar – okay, basically a copycat – concept (similar look, store size, mall productivity, loose leaf tea contribution, and even POS) can have a sales productivity less than half of Teavana's. What does this mean to us? We think it shows that Teavana's "specialness" arises not from its store format or product mix. Rather, it stems from its unique, highly consultative store model as well as its unique products. The aforementioned are what give rise to Teavana's \$1,000 per square foot sales productivity, and frankly, despite the best efforts of competitors, are not easily duplicated.

VALUATION

At 33.5x 2012 P/E, 3.5x 2012 EV/Sales and 1.1x 2012 PEG, valuation is reasonable for a high- growth retailer. We think the Company can sustain accelerating earnings growth, particularly given its aggressive new store opening program and strong new store economics. Thus, we think Teavana deserves to trade at a premium to the active and healthy lifestyle peer group average of 31.6x 2012 P/E, 2.2x 2012 EV/Sales and 1.3x 2012 PEG. Additionally, the stock currently trades at a 15.6x 2012 EV/EBITDA compared to 13.1x EV/EBITDA of the peer group. We reiterate our \$28 price target, which implies a 47.4x P/E based on our \$0.59 2012 EPS estimate.

RISKS

Risks that could impede TEA from reaching our price target include, but are not limited to the following: ability to identify suitable locations to open new stores, a change in consumer spending behavior, retention of senior management.

Revenue Summary

	2011A	Prior 2011A	2012E	Prior 2012E	2013E	Prior 2013E
1Q	\$34.9	\$34.9	\$45.1	\$45.1	--	--
2Q	\$31.3	\$31.3	\$43.1	\$39.9	--	--
3Q	\$33.4	\$33.4	\$45.3	\$41.9	--	--
4Q	\$68.4	\$68.4	\$93.0	\$86.1	--	--
YEAR	\$168.1	\$168.1	\$226.5	\$213.1	\$286.6	\$269.4

Source: KeyBanc Capital Markets Inc. estimates

MINIMAL COSTS FOR TRANSACTION AND INTEGRATION OF TEAOPIA

Exhibit 1. Similar Concept; Room for Sales Improvement

	Teaopia	Teavana
Store count	46	200
Avg sales per store (thousands)	~\$435	\$913
Mall sales per sq. ft. avg for existing store locations	~\$500	~\$500
Avg size of store (sq. ft.)	~900	920
Occupancy cost \$ per store	~100% of TEA	N/A
Loose-leaf tea as % of revenue	~50%	55%

Source: Company reports.

Exhibit 2. Accretion Analysis

Teaopia Acquisition	
(in millions, except for store and per share data)	
Current Teaopia store count	46
Teaopia average sales per store	\$435,000
Chain revenue (in \$mm of CAD)	\$17.0
Teavana average sales per store	\$913,000
Teaopia productivity	48%
Potential incremental revenue @ Teavana sales productivity	\$42.0
Teavana 4-wall contribution margin	25%
Incremental EBIT	\$10.5
Incremental net income (ex. financing costs, 40% tax rate)	\$6.3
Accretion to EPS	\$0.16

Source: Company reports and KeyBanc Capital Markets Inc.

VALUATION SUMMARY

Exhibit 3. Valuation Summary

Company Name	TKR	Rating	Stock Price	52 Week Price Range	Price Target	2012E P/E on PT	Mkt Cap (\$mm)	EPS		P/E		EV/EBITDA		EV/Sales		PEG	
								2011A	2012E	2011A	2012E	2011A	2012E	2011A	2012E	2011A	2012E
SPECIALTY RETAIL																	
Abercrombie	ANF	BUY	\$46.78	\$40.25 - \$78.25	\$61.00	16.9x	3,963	\$2.30	\$3.60	20.3x	13.0x	6.1x	4.6x	0.8x	0.7x	0.9x	0.6x
Aeropostale	ARO	BUY	\$21.09	\$9.16 - \$26.30	\$25.00	20.7x	1,708	\$0.92	\$1.21	23.0x	17.5x	8.0x	6.4x	0.6x	0.6x	1.5x	1.1x
Buckle	BKE	HOLD	\$45.34	\$33.97 - \$50.00	-	-	2,173	\$3.20	\$3.40	14.2x	13.3x	7.3x	6.9x	1.9x	1.7x	1.1x	1.0x
Chico's	CHS	HOLD	\$15.07	\$9.57 - \$16.50	-	-	2,523	\$0.85	\$0.99	17.8x	15.3x	7.0x	6.2x	1.0x	0.9x	1.1x	0.9x
Ascena Retail	ASNA	BUY	\$21.14	\$12.00 - \$22.62	\$25.00	16.8x	3,247	\$1.28	\$1.48	16.6x	14.2x	6.7x	5.9x	0.9x	0.9x	1.1x	0.9x
Gap Inc	GPS	HOLD	\$26.43	\$15.08 - \$27.00	-	-	12,891	\$1.56	\$1.79	16.9x	14.8x	6.5x	6.4x	0.9x	0.8x	1.7x	1.4x
New York & Company	NWY	HOLD	\$3.65	\$2.25 - \$7.00	-	-	227	(\$0.64)	(\$0.41)	NM	NM	61.8x	11.8x	0.2x	0.2x	NM	NM
Urban Outfitters	URBN	HOLD	\$28.48	\$21.47 - \$33.90	-	-	4,121	\$1.19	\$1.48	24.0x	19.2x	9.8x	8.5x	1.6x	1.4x	1.3x	1.0x
Wet Seal	WTSLS	HOLD	\$3.34	\$3.03 - \$5.23	-	-	303	\$0.19	\$0.18	17.8x	19.0x	3.0x	3.0x	0.2x	0.2x	1.0x	1.1x
Peer Average										18.8x	18.0x	14.0x	7.8x	1.4x	1.2x	1.3x	1.0x
ACTIVE AND HEALTHY LIFESTYLE																	
Lululemon Athletica	LULU	BUY	\$73.40	\$41.18 - \$77.13	\$82.00	51.6x	10,537	\$1.26	\$1.59	58.4x	46.2x	24.6x	19.5x	7.7x	5.8x	1.9x	1.5x
Pacific Sunwear	PSUN	HOLD	\$1.49	\$1.11 - \$4.06	-	-	101	(\$0.77)	(\$0.50)	NM	NM	NM	NM	0.1x	0.1x	NM	NM
Skulcandy	SKUL	BUY	\$17.29	\$11.79 - \$23.40	\$21.00	17.9x	473	\$1.00	\$1.17	17.4x	14.8x	9.9x	7.9x	2.0x	1.6x	0.8x	0.7x
Teavana	TEA	BUY	\$19.76	\$14.28 - \$29.35	\$28.00	47.4x	757	\$0.46	\$0.59	42.7x	33.4x	19.7x	15.6x	4.4x	3.5x	1.3x	1.1x
Under Armour	UA	UW	\$95.08	\$52.62 - \$99.35	\$56.00	24.2x	4,922	\$1.85	\$2.31	51.5x	41.2x	19.1x	15.5x	2.6x	2.1x	2.2x	1.8x
Zumiez	ZUMZ	HOLD	\$34.41	\$15.85 - \$38.79	-	-	1,073	\$1.20	\$1.41	28.7x	24.4x	11.3x	9.6x	1.6x	1.4x	1.4x	1.2x
Peer Average										39.0x	31.6x	16.2x	13.1x	2.8x	2.2x	1.6x	1.3x

Source: Company reports, FactSet and KeyBanc Capital Markets Inc. estimates as of April 2012.

ASNA FY ends in July. EPS estimates represent calendar year estimates.

RISKS

The primary risks to our ratings and price targets continue to center around macroeconomic risk, particularly on the downside. Risks that could impede a stock from reaching our upside price target include, but are not limited to: deterioration in the consumer spending environment, a slowdown in comparable store sales growth, and the fashion risk associated with being in a seasonal, cyclical and trend focused sector. Risks that could impede a stock from reaching our downside price target, include but are not limited to: a significant positive improvement in the overall economy, which would subsequently impact consumer buying behavior.

Risks specific to TEA that could impede the stock from reaching our UPSIDE price target include but are not limited to the following: ability to identify suitable locations to open new stores, a change in consumer spending behavior, retention of senior management.

Exhibit 4. Income Statement

(\$ in millions except per share data)

	2008	2009	2010	2011					2012E				2013E	
	Year	Year	Year	1Q	2Q	3Q	4Q	Year	1Q	2Q	3Q	4Q	Year	Year
Revenues	63.9	90.3	124.7	34.9	31.3	33.4	68.4	168.1	45.1	43.1	45.3	93.0	226.5	286.6
Cost of goods sold	27.2	36.4	46.3	12.5	12.2	12.7	23.5	60.9	16.5	16.9	17.3	32.3	83.0	100.4
Gross profit	36.7	53.8	78.4	22.5	19.1	20.7	44.9	107.2	28.7	26.2	28.0	60.7	143.5	186.1
Selling, general & administrative expense	29.2	38.1	50.6	14.8	15.4	17.5	22.0	69.7	19.7	21.7	23.8	30.2	95.5	120.7
Depreciation and amortization expense	2.7	3.5	4.4	1.3	1.4	1.6	1.7	5.9	1.7	2.0	2.1	2.3	8.1	10.9
Operating income	4.8	12.2	23.5	6.5	2.3	1.6	21.2	31.6	7.2	2.5	2.0	28.1	39.9	54.6
Interest expense, net	2.1	2.4	2.6	0.7	0.7	0.1	0.1	1.7	0.1	0.1	0.1	0.1	0.5	0.5
Earnings before income taxes	2.7	9.8	20.9	5.8	1.6	1.5	21.1	29.9	7.1	2.4	1.9	28.0	39.4	54.1
Income tax expense	1.5	4.5	8.9	2.4	0.6	0.6	8.6	12.2	3.0	0.8	0.7	11.4	16.0	21.9
Net earnings	1.2	5.3	12.0	3.3	1.0	0.9	12.5	17.8	4.1	1.6	1.2	16.6	23.4	32.2
Weighted average shares outstanding - diluted	37.1	37.3	37.7	37.7	37.8	39.0	39.1	38.4	39.1	39.3	39.5	39.7	39.4	39.7
Earnings per share - diluted	\$0.03	\$0.14	\$0.32	\$0.09	\$0.03	\$0.02	\$0.32	\$0.46	\$0.10	\$0.04	\$0.03	\$0.42	\$0.59	\$0.81
EBITDA	7.4	15.7	27.9	7.7	3.8	3.2	22.9	37.5	8.9	4.5	4.2	30.4	48.0	65.4
Comparable store sales	3.0%	6.9%	8.7%	6.0%	6.9%	6.0%	4.4%	5.5%	4.0%	5.0%	5.0%	6.5%	5.4%	5.4%
Y/Y Inventory Growth			45.7%					51.7%					67.9%	18.2%
Margin analysis														
Cost of goods sold/revenue	42.6%	40.4%	37.1%	35.6%	38.9%	38.1%	34.4%	36.2%	36.5%	39.2%	38.2%	34.8%	36.7%	35.0%
Y/Y change in bps	27	(222)	(326)	(325)	(223)	(323)	202	(88)	85	30	10	40	42	(160)
Gross margin	57.4%	59.6%	62.9%	64.4%	61.1%	61.9%	65.6%	63.8%	63.5%	60.8%	61.8%	65.2%	63.3%	65.0%
Y/Y change in bps	(27)	222	326	325	223	323	(202)	88	(85)	(30)	(10)	(40)	(42)	160
Selling, general & administrative expense/sal	45.8%	42.3%	40.6%	42.2%	49.1%	52.4%	32.2%	41.5%	43.7%	50.3%	52.6%	32.5%	42.2%	42.1%
Y/Y change in bps	(131)	(353)	(170)	34	204	341	(67)	90	150	125	20	30	70	(3)
Depreciation and amortization expense/sales	4.2%	3.9%	3.5%	3.6%	4.6%	4.6%	2.4%	3.5%	3.7%	4.6%	4.7%	2.5%	3.6%	3.8%
Y/Y change in bps	(11)	(3)	(37)	(13)	(5)	16	6	3	10	5	5	5	6	20
Operating margin	7.5%	13.5%	18.8%	18.5%	7.4%	4.8%	31.0%	18.8%	16.0%	5.8%	4.5%	30.2%	17.6%	19.0%
Y/Y change in bps	115	606	533	304	24	(34)	(141)	(5)	(245)	(160)	(35)	(75)	(118)	144
EBITDA margin	11.6%	17.4%	22.3%	22.1%	12.0%	9.5%	33.4%	22.3%	19.8%	10.5%	9.2%	32.7%	21.2%	22.8%
Y/Y change in bps	575	496	291	19	(18)	(135)	(2)	(235)	(155)	(30)	(70)	(112)	(112)	164
Effective tax rate	55.7%	45.8%	42.6%	42.4%	35.2%	37.2%	40.8%	40.6%	42.4%	35.2%	37.2%	40.8%	40.6%	40.5%
Y/Y change in bps	(1,706)	(986)	(320)	(20)	(746)	(548)	(177)	(196)	0	0	0	0	(6)	(4)
Y/Y growth														
Revenues	35.3%	41.3%	38.2%	35.6%	36.3%	35.1%	33.6%	34.8%	29.2%	37.6%	35.4%	35.9%	34.8%	26.5%
Cost of goods sold	36.2%	34.0%	27.0%	24.2%	28.9%	24.5%	42.0%	31.6%	32.3%	38.7%	35.8%	37.5%	36.3%	21.0%
Gross profit	34.7%	46.8%	45.7%	42.8%	41.4%	42.5%	29.6%	36.7%	27.5%	37.0%	35.2%	35.1%	33.9%	29.7%
Selling, general & administrative expense	31.5%	30.4%	32.6%	36.6%	42.2%	44.5%	30.9%	37.8%	33.8%	41.1%	36.0%	37.2%	37.0%	26.4%
Depreciation and amortization expense	31.8%	30.9%	25.0%	30.9%	34.7%	40.0%	37.2%	35.9%	32.8%	39.1%	36.9%	38.7%	37.1%	33.7%
Operating income	59.9%	156.2%	92.6%	62.3%	40.7%	26.1%	27.8%	34.5%	12.1%	8.1%	25.6%	32.6%	26.3%	36.8%
Net earnings	216.7%	342.0%	126.9%	72.4%	78.1%	175.3%	36.2%	48.0%	23.4%	51.0%	27.8%	32.8%	31.8%	37.4%
EPS	213.7%	339.3%	124.4%	71.3%	77.2%	165.9%	31.7%	45.3%	19.1%	45.2%	26.1%	30.7%	28.6%	36.3%
EBITDA		111.2%	77.6%	56.1%	38.4%	32.6%	28.4%	34.7%	15.5%	19.8%	31.2%	33.1%	28.0%	36.3%

Source: Company reports, FactSet and KeyBanc Capital Markets Inc. estimates as of April 2012.

KeyBanc Capital Markets Inc. Disclosures and Certifications

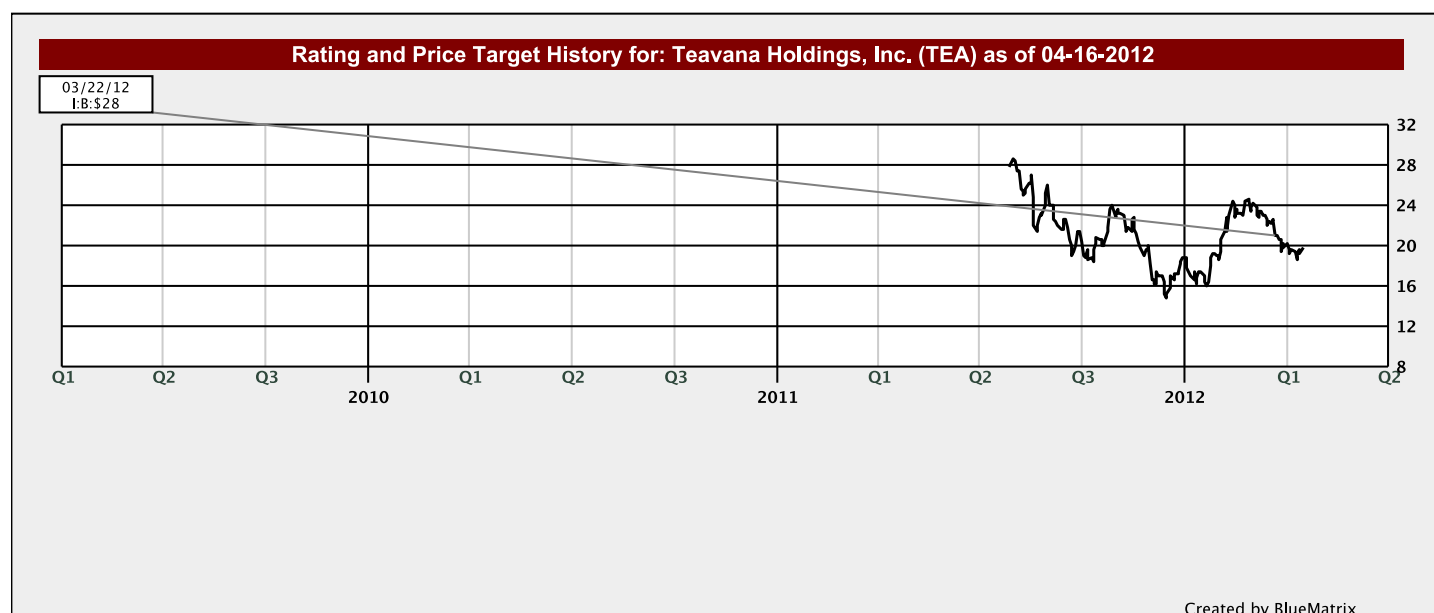
Teavana Holdings, Inc. - TEA

We expect to receive or intend to seek compensation for investment banking services from Teavana Holdings, Inc. within the next three months.

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Three- Year Rating and Price Target History



Rating Disclosures

Distribution of Ratings/IB Services Firmwide and by Sector									
KeyBanc Capital Markets					CONSUMER				
Rating	Count	Percent	IB Serv/Past 12 Mos.		Rating	Count	Percent	IB Serv/Past 12 Mos.	
			Count	Percent				Count	Percent
BUY [BUY]	225	44.38	47	20.89	BUY [BUY]	55	47.01	6	10.91
HOLD [HOLD]	270	53.25	49	18.15	HOLD [HOLD]	60	51.28	2	3.33
SELL [UND]	12	2.37	4	33.33	SELL [UND]	2	1.71	0	0.00

Rating System

BUY - The security is expected to outperform the market over the next six to 12 months; investors should consider adding the security to their holdings opportunistically, subject to their overall diversification requirements.

HOLD - The security is expected to perform in line with general market indices over the next six to 12 months; no buy or sell action is recommended at this time.

UNDERWEIGHT - The security is expected to underperform the market over the next six to 12 months; investors should reduce their holdings opportunistically.

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