BUILD A BEAR WORKSHOP INC
Form 10-K
March 17, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC20549

FORM 10-K

(Mark One)
x Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended January 1, 2011
OR

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

Commission file number: 001-32320

BUILD-A-BEAR WORKSHOP, INC.
(Exact Name of Registrant as Specified in Its Charter)

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

(314) 423-8000
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $0.01 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ¨ Yes x No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. ¨ Yes x No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ¨ Yes ¨ No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) 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. x

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

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨ Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). ¨ Yes x No

There is no non-voting common equity. The aggregate market value of the common stock held by nonaffiliates (based upon the closing price of $6.42 for the shares on the New York Stock Exchange on July 2, 2010) was $108,236,250 as of July 3, 2010.

As of March 15, 2011, there were 19,254,956 issued and outstanding shares of the registrant's common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement for its May 12, 2011 Annual Meeting are incorporated herein by reference.

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FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains certain statements that are, or may be considered to be, "forward-looking statements" for the purpose of federal securities laws, including, but not limited to, statements that reflect our current views with respect to future events and financial performance. We generally identify these statements by words or phrases such as "may," "might," "should," "expect," "plan," "anticipate," "believe," "estimate," "intend," "predict," "future," " "continue," the negative or any derivative of these terms and other comparable terminology. These forward-looking statements, which are subject to risks, uncertainties and assumptions about us, may include, among other things, projections or statements regarding:

- our future financial performance;
- our anticipated operating and growth strategies;
- our future capital expenditures;
- our anticipated rate of store openings;
- our anticipated store opening costs; and
- our franchisees' anticipated rate of international store openings.

These statements are only predictions based on our current expectations and projections about future events. Because these forward-looking statements involve risks and uncertainties, there are important factors that could cause our actual results, level of activity, performance or achievements to differ materially from the results, level of activity, performance or achievements expressed or implied by these forward-looking statements, including those factors discussed under the caption entitled "Risk Factors" as well as other places in this Annual Report on Form 10-K.

We operate in a competitive and rapidly changing environment. New risk factors emerge from time to time and it is not possible for management to predict all the risk factors, nor can it assess the impact of all the risk factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, you should not place undue reliance on forward-looking statements, which speak only as of the date of this Annual Report on Form 10-K, as a prediction of actual results.

You should read this Annual Report on Form 10-K completely and with the understanding that our actual results may be materially different from what we expect. Except as required by law, we undertake no duty to update these forward-looking statements, even though our situation may change in the future. We qualify all of our forward-looking statements by these cautionary statements.

PART I

ITEM 1. BUSINESS

Overview

Build-A-Bear Workshop, Inc., a Delaware corporation, was formed in 1997 and is the leading and only international company providing a "make your own stuffed animal" interactive retail-entertainment experience. As of January 1, 2011, we operated 344 company-owned retail stores in the United States, Canada, the United Kingdom and Ireland, including 290 Build-A-Bear Workshop® stores in the United States and Canada and 54 Build-A-Bear Workshop stores in the United Kingdom and Ireland. In addition, franchisees operated 63 Build-A-Bear Workshop stores in other international locations. Our core concept is based on our guests making, personalizing and customizing their own stuffed animals, and capitalizes on what we believe is the relatively untapped demand for experience-based shopping as well as the widespread appeal of stuffed animals.

We offer an extensive and coordinated selection of merchandise, including over 30 different styles of animals to be stuffed and a wide variety of clothing, shoes and accessories for the stuffed animals as well as other brand appropriate toy and accessory items. Our concept appeals to a broad range of age groups and demographics, including children, teens, parents and grandparents. We believe that our stores, which are primarily located in malls, are destination locations and draw guests from a large geographic reach. Our stores average approximately 2,700 square feet in size and have a highly visual and colorful appearance, including custom-designed fixtures featuring teddy bears and other themes relating to the Build-A-Bear Workshop experience.

We also market our products and build our brand awareness and equity in our countries of operation through national multi-media marketing programs that target our core demographic guests, principally parents and children. The program incorporates consistent messaging across a variety of media, and is designed to increase our brand awareness and store traffic and attract more first-time and repeat guests. In addition, our virtual world Web site, bearville.comTM, promotes brand connection and in-store products and events with branded games, activities and social connectivity features.

Since opening our first store in St. Louis, Missouri in October 1997, we have sold over 90 million stuffed animals. We have grown our store base from 321 stores at the end of fiscal 2007 to 344 as of January 1, 2011.

On February 20, 2007, we announced that our board of directors had authorized a $25 million share repurchase program of our outstanding common stock. On March 10, 2008, we announced that the Board of Directors had authorized an increase in our share repurchase program to up to $50 million. On March 2, 2011, we announced that our share repurchase program had been extended to March 31, 2012. As of March 15, 2011, we had $21.2 million of availability under the program.

Description of Operations

Guests who visit Build-A-Bear Workshop stores enter a teddy bear-themed environment consisting of eight stuffed animal-making stations: Choose Me, Hear Me, Stuff Me, Stitch Me, Fluff Me, Dress Me, Name Me, and Take Me Home®. To attract our target guests, we have designed stores that are open and inviting with an entryway that spans the majority of our storefront and are highly visual with colorful teddy bear themes and displays that create a "theme park" destination in the mall. The duration of a guest's experience can vary greatly depending on his or her preferences. While most guests choose to participate in the full animal-making process and all eight stations, a process which we believe averages 45 minutes to complete, guests can also visit a Build-A-Bear Workshop store and purchase items such as clothing, accessories, our Bear Buck$®and Cub Cash® gift certificates, Bearville Outfitters® game cards or pre-made animals in only a few minutes. We also offer a wide variety of animals and accessories on our e-commerce Web site, buildabear.com®.

We offer an extensive and coordinated selection of merchandise including approximately 30 to 35 varieties of animals to be stuffed, as well as a wide variety of other clothing and accessory items for the animals. Our clothing is inspired by human fashion and includes authentic details such as functional buttons, working pockets, belt loops and zippers and has child-friendly, easy-to-dress details such as an opening for the stuffed animal's tail and adjustable closures to help fit any size animal. We enhance the authentic nature of a number of our products with strategic product licensing relationships with brands that are in demand with our guests such as officially sanctioned NFL®, NBA®, MLB® and FIFA™ team apparel, Skechers® shoes and Justice® clothing. We also tap into pop culture that is relevant to our guests by featuring merchandise such as the Wizards of Waverly Place bear and Alvin and the Chipmunks® stuffed animals.

While our concept is a unique combination of experience and product, we selectively promote seasonal products with special offers and promotions intended to maximize sales at peak traffic periods in the year. We expect to build upon our product and store promotions to drive store visits and conversion of shoppers. We also offer frequent shopper discounts associated with our Stuff Fur Stuff® club loyalty program and strategically use coupons and gift-with-purchase promotions to drive traffic to our stores.

As a retailer whose signature product is a stuffed animal that is typically purchased as a toy or gift, our sales are highest in our fourth quarter which ends on the Saturday nearest December 31 each year, followed by the first quarter. The timing of holidays and school vacations can impact our quarterly results. Historically, for North American stores, seasonality has not been a significant factor in our results of operations as the opening of new stores had mitigated the impact of the relative concentration of sales in the fourth quarter. Our European-based stores have historically been more heavily weighted in the fourth quarter as compared to our North American stores. We cannot ensure that this will continue to be the case.

Growth Strategy

Our growth strategy is to develop and expand the reach of the Build-A-Bear Workshop brand. Product innovation is key to our growth, as well as the full integration of our product, marketing and operations initiatives. We believe the focus on larger, limited edition animal introductions that launch approximately once a month creates a sense of urgency to shop and drives traffic to our stores, increases conversion and improves sales. Additional toy products outside of our core plush animals, yet consistent with our interactive and hands-on experience, will be selectively added to our assortment in order to get incremental purchases as well as add to transactions with make-your-own product to grow transaction value. We will continue to grow online engagement at bearville.com, as well as grow our e-commerce business. We are also exploring new opportunities for Build-A-Bear Workshop products to be sold outside of our current store base. We expect to grow our business by opening additional stores in the United States, Canada, the United Kingdom and Ireland, by the addition of new international stores opened through existing and new franchise agreements, and through the development of third party licensed products that promote Build-A-Bear Workshop as a lifestyle brand and build overall brand awareness.

We have increased our company-owned store locations throughout the United States, Canada and Puerto Rico from 321 at the end of fiscal 2007 to 344 as of January 1, 2011. In April 2006, we acquired Amsbra Limited, our former franchisee in the United Kingdom, as well as The Bear Factory Limited (collectively, the UK Acquisition), a stuffed animal retailer in the United Kingdom whose store locations we subsequently rebranded to the Build-A-Bear Workshop brand. In 2007, we discontinued our franchise agreement in France and opened three company-owned stores there. In 2010, we closed our three stores in France. As of January 1, 2011, we operated 54 stores in the United Kingdom and Ireland all under the Build-A-Bear Workshop brand.

In fiscal 2011, we expect to open two new stores in North America, compared to opening one new store in 2010, and three new stores in Europe, the same as in 2010. We believe there is a market potential for approximately 350 Build-A-Bear Workshop stores in North America and approximately 70 in the United Kingdom and Ireland. In addition, we currently operate Build-A-Bear Workshop stores in non-traditional retail locations including 11 temporary pop-up locations, three Major League Baseball® ballparks, one store located in the Saint Louis Zoo and one store at the St. Louis Science Center. In 2011, we expect locations to open in an airport and a children's hospital. Build-A-Bear Workshop stores are also operated within select Rain Forest Café® and T-Rex Café™ locations under licensing agreements with Landry's® Restaurants.

We lease all of our store locations. The majority of our store leases contain provisions for base rent plus percentage rent based on sales in excess of an agreed upon minimum annual sales level. A number of our leases include a termination provision which applies if we do not meet certain sales levels during a specified period, typically in the third to fourth year and the sixth to seventh year of the lease, at either the landlord's options or ours. Many of our initial leases have expiration dates in the next 18-24 months as well as other more recent leases that have termination or "kick out" options in the same time period. As part of our long-term market planning, we expect to close store locations, relocate other locations and open new locations to reflect changing market conditions and demographic shifts. We also expect to use temporary pop-up store locations with lease terms of twelve to twenty-four months to take opportunistic advantage of excess real estate availability as well as position markets for long term optimization in advance of long term lease decisions. The terms of new leases may have financial increases reflecting current market conditions and if we execute termination rights, we may have expenses and charges associated with those closures. In 2011, we expect to close five to ten stores in North America and one to three store in Europe as well as relocate four existing stores in North America.

We believe that there is continued opportunity to grow our Build-A-Bear Workshop concept and brand outside of North America, the United Kingdom and Ireland primarily through franchise agreements. Our goal is to have franchisees that are well capitalized and bring extensive retail and/or real estate experience. As of January 1, 2011, our franchisees operated 63 Build-A-Bear Workshop stores in twelve foreign countries under master franchise agreements on a country-by-country basis. We expect our franchisees to open approximately five to ten new stores in fiscal 2011, net of closures, under existing and anticipated franchise agreements. We believe there is a market potential for approximately 300 international stores outside North America, the United Kingdom and Ireland, which we expect to be primarily operated through new and existing franchise agreements. Although we expect to continue to open international stores primarily through franchise agreements, we may open additional company-owned stores outside of the United States, Canada, Puerto Rico, the United Kingdom and Ireland, as our international plans adjust to meet a variety of market conditions in additional countries.

We believe there are also growth opportunities to sell Build-A-Bear Workshop products in other retail stores. Over the past 13 years, we have established our store as a place where children can have a hands-on experience, express their creativity and use their imagination. We believe our brand is one that parents value and trust and kids love. We believe that our expertise in product development and the reputation and quality of our brand will drive sales of plush and other branded products in locations other than our own stores. We expect to be able to leverage our extensive guest database to market these new products and build demand for them.

In fiscal 2003, we began testing in certain markets a proprietary collection of Friends 2B Made® make-your-own dolls and related products. In the fiscal 2008 third quarter, we announced plans to close the Friends 2B Made concept. The closure plan affected our nine Friends 2B Made store locations, Friends 2B Made fixtures within approximately 50 Build-A-Bear Workshop stores, and the concept's website. All Friends 2B Made locations were closed by the end of fiscal 2009. Eight of these locations were in or adjacent to a Build-A-Bear Workshop store.

We hold a minority interest in Ridemakerz, LLC (previously Retail Entertainment Concepts, LLC). Ridemakerz® is an early-stage company that has developed a wholesale toy product line and operates interactive retail stores, primarily in selected tourist locations, that allow guests, or customizers, to build and personalize their own model cars. The concept capitalizes on the universal love of cars and a widely popular car culture that crosses ages and demographics, although the primary targets are children and their families. In 2009, Ridemakerz undertook a major restructuring of its operations that included significant store closings. As a result, we reduced the book value of our equity method investment and receivable to zero in 2009. As of January 1, 2011, Ridemakerz operated five stores, including one location in Downtown Disney® District at the Disneyland® Resort in Anaheim, California and one location in Walt Disney World in Orlando, Florida. In 2010, we provided advisory and support services to Ridemakerz in exchange for additional equity.

In response to an emerging trend of kids' interaction and play increasingly occurring in the online space, in 2007 we updated our virtual world Web site used primarily by children, bearville.com, and we continue to enhance the site. The site is highly complementary to our store experience and positively enhances our core brand values while offering activity options and features that are tied back to in-store events. We believe that the launch of our virtual world Web site is a critical business strategy to further enhance our brand appeal with children and grow our store sales and that we have a unique competitive advantage over other virtual world sites due to our ability to provide both real world and virtual world experiences. We also believe the virtual world platform enhances our entertainment options. For example, in 2008 we introduced our stuffed animals Holly & Hal Moose® and their storybook. While the book was distributed through our stores and e-commerce websites, the virtual world allowed us to promote the characters and feature animated "webisodes" of the story for children to view throughout the holiday season. In 2009, the webisodes were expanded into a full length holiday TV special that aired on national television in the United States in 2009 and 2010 exposing our brand to millions of viewers.

We also believe that we will be able to generate revenue from the sale of products used exclusively on line in the virtual world space. Our research has shown that approximately one out of every three guests who complete our survey visit bearville.com before visiting our store and that over 40% of all animals registered in our stores by the key bearville.com demographic come online at the site, enhancing value for parents and engagement for kids. In 2008, we introduced virtual world products which are sold online and in our stores and in 2009 we expanded the offerings to include additional game cards as well as monthly and annual subscriptions to the site. Game cards can be used to buy exclusive virtual items, including rides, homes, furniture, clothing and accessories. Online subscriptions provide monthly credits and bonuses to members.

Product Development

Through our in-house design and product development team, we have developed a coordinated, creative and broad merchandise assortment, including a variety of animals, clothing, shoes and accessories. We believe our merchandise is an integral part of our concept and that the proprietary design of many of the products we offer is a critical element of our success, while the authentic and fashionable nature of our products greatly enhances our brand's appeal to our guests. Our product development team regularly monitors current fashion and cultural trends in order to create products that are most appealing to our guests, often reflecting similar styling to the clothes our guests wear themselves. We test our products on an ongoing basis to ensure guest demand supports order quantities. Through our focused vendor relationships, we are able to source our merchandise in a manner that is cost-effective, maximizes our speed to market and facilitates rapid reorder of our best-selling items.

Our stuffed animal skins and clothing are produced from high quality man-made materials or natural fibers such as cotton, and the stuffing is made of a high-grade polyester fiber. We believe all of our products in our stores and online at buildabear.com meet Consumer Product Safety Commission requirements including the Consumer Product Safety Improvement Act (CPSIA) for Children's Products. We also comply with American Society for Testing and Materials

(ASTM), EN71 (European standards) and Canadian specifications for toy safety in all material respects. Our products are tested through independent third-party testing labs for compliance with toy safety standards. We believe we comply with governmental toy safety requirements specific to each country where we have stores. Packaging and labels for each product indicate to our guests the age grading for the product and any special warnings in accordance with guidelines established by the Consumer Product Safety Commission.

Our products have earned the Good Housekeeping Seal of Approval. The Good Housekeeping Seal, introduced in 1909, is earned by products that pass Good Housekeeping Institute review and is one of America's most trusted consumer icons assuring consumers of a quality product. Seal-backed products are covered by Good Housekeeping's two-year money-back warranty.

In order to increase store visits and give guests additional reasons for purchasing at our stores, we expect to expand our product assortment and our leadership in the toy industry by offering additional products to our core plush animals and related items that are consistent with our interactive and hands-on experience, some of which are proprietarily developed and some that come from other toy and accessory companies. We believe the addition of complementary toy and accessory products will allow us to increase our sales and overall profitability.

Marketing

We believe that the strength of the Build-A-Bear Workshop brand is a competitive advantage and an integral part of our business strategy. Our goal is to continue to build brand recognition as a destination that provides affordable, experience-based retail stores that appeal to a broad range of age groups and demographics.

Since February 2004, we have utilized fully integrated marketing programs that include direct marketing, online advertising, and other components as well as national television advertising in the United States. In the fourth quarter of 2010, we expanded our television advertising to the United Kingdom for the first time. Our advertising expenditures were $18.5 million (4.2% of net retail sales) in fiscal 2010, $24.4 million (6.3% of net retail sales) in fiscal 2009 and $33.4 million (7.2% of net retail sales) in fiscal 2008, reflecting the continuation and further refinement of our marketing initiatives.

We employ a variety of different marketing tools and programs to drive traffic to our company-owned stores in North America and Europe and raise overall brand awareness and top of mind recall. We use television advertising that targets both children and adults to reach new guests, and periodically feature specific new product introductions and promotions as a call-to-action to visit our stores for both new and returning guests. We also have used radio, print and online advertising integrating our message across various touch points to maximize our reach to new and existing guests. We leverage the database from our Stuff Fur Stuff club loyalty program of over four million active members in our direct mail and e-mail programs and provide information and e-commerce on our website, buildabear.com. In 2010, we continued to expand our use of social media to better reach our mom target audience. We have also begun utilizing affiliate marketing opportunities in other on-line spaces that share our values and target demographic.

In 2007, we created a virtual world Web site, primarily for kids at bearville.com, with enhanced capabilities, customization options and social connectivity features which we use to promote our brand and raise awareness of in-store products and events.

Our Stuff Fur Stuff club loyalty program was introduced in the United States in 2007 as an update to our previous Buy Stuff Club program and rolled out to Canada in 2008. The program is designed to reward repeat guest visits. The program currently provides one point for each $1 spent, with a $10 discount certificate awarded for every 100 points. The data collected gives us insight into the overall purchasing history of members including visit frequency, items purchased and amounts spent on each visit and cumulatively over time. We continue to leverage this information and improve our direct mail effectiveness and response rates through additional targeting and personalization of communications and offers. We launched a version of the Stuff Fur Stuff program in the United Kingdom in fall of 2008 that does not provide discount certificates but keeps guests informed of new products and offers members special coupons and other seasonal offers.

Licensing and Strategic Relationships

We have developed licensing and strategic relationships with some of the leading retail and cultural organizations in North America and Europe. We believe that our guest base and brand strength make us an attractive partner and our customer research and insight allow us to focus on strategic relationships with other companies that we believe are appealing to our guests. We plan to continue to add strategic relationships with companies that have strong, family-oriented brands and provide us with attractive marketing and merchandising opportunities. These relationships for specific products are generally reflected in contractual arrangements for limited terms that are terminable by either party upon specified notice.

Product and Merchandise Licensing. We have key strategic relationships with select companies, including Disney®, Sanrio®, Skechers, Justice stores, Star Wars, MLB, NBA, NFL, the NHL®, FIFA and World Wildlife Fund US and Canada, in which we feature their brands on products sold in our stores. These strategic relationships allow both parties to generate awareness of their brands. We have also offered selected character and media-oriented products including Sanrio's Hello Kitty, Disney's Wizards of Waverly Place, Fox's Alvin and the Chipmunks, The Squeakquel, Nickelodeon's iCarly as well as the classic movie character, Rudolph the Red-Nosed Reindeer.

Promotional Arrangements. We have also developed promotional arrangements with select organizations. Our arrangements with Major League Baseball teams, including the Chicago Cubs®, St. Louis Cardinals™ and New York Mets® have featured stuffed animal giveaways at each club's ballpark on a day in which our brand is highly promoted within the stadium. In 2009, we partnered with McDonald's® to feature limited edition, collectible mini Build-A-Bear Workshop animals in Happy Meals®. We also have had arrangements featuring product sampling, cross promotions and shared media with companies such as Baskin-Robbins, Wonka Candy, Macy's, FYE and Spirit Halloween stores. In 2010 we partnered with teen celebrity, Victoria Justice, who will be our brand ambassador throughout 2011. The arrangement will also feature Victoria Justice 4 BABW branded merchandise available in our stores.

Third Party Licensing. We have continued a series of licensing arrangements with leading manufacturers to develop a collection of lifestyle Build-A-Bear Workshop branded products including children's furniture, fruit snacks, scrapbooking products, craft kits and bedding. We believe that each of these initiatives has the potential to enhance our brand, raise brand awareness, and drive increased revenues and profitability. We select companies for licensing relationships that we believe are leaders in their respective sectors and that understand and share our strategic vision for offering guests exciting and interactive merchandise. Our relationships with these companies have enabled us to have dedicated product space in other retailers such as Michaels Craft Shops, where we showcase our Build-A-Bear Craftshop® line of craft kits. We have policies and practices in place intended to ensure that the products manufactured under the Build-A-Bear Workshop brand adhere to our quality, value and usability standards. We have entered into or maintained licensing arrangements for our branded products with leading manufacturers including Pulaski Furniture, ConAgra Foods, Colorbok, Ellison Educational and Pem America. Many of our licensed products include a tie-in with our interactive Web site, bearville.com, and a bounce back offer to use in our stores or online.

Industry and Guest Demographics

While Build-A-Bear Workshop offers consumers an interactive and personalized experience, our tangible products are stuffed animals, including our flagship product, the teddy bear, a widely adored icon for over 100 years. According to data published by the Toy Industry Association and The NPD Group, sales of the traditional toy market were $21.9 billion in the United States (excluding video games) in 2010 with plush and doll sales having a combined 20.5% share of the traditional toy market. According to further data provided by The NPD Group, worldwide toy sales topped $83.9 billion dollars in 2009.

Our guests are diverse, spanning broad age ranges and socio-economic categories. Major guest segments include families with children, primarily ages three to twelve, grandparents, aunts and uncles, teen girls who occasionally bring along their boyfriends and child-centric organizations looking for interactive entertainment options such as scouting organizations and schools. Based on information compiled from our guest database for 2010, the average age of the recipient of our stuffed animals at the time of purchase is nine years old and children aged one to fourteen are the recipients of approximately 80% of our stuffed animals.

According to the estimates by the United States Census Bureau, in 2009 there were over 62 million children age 14 and under in the United States. The size of this population group is projected to remain relatively stable over the next decade. Industry sources estimate direct spending by children in the United States at over $50 billion annually and that parents and family members spend an additional $170 billion annually on children. In addition, children influence billions of dollars in other family spending.

Employees and Training

In January 2011, we were recognized by Fortune magazine for the third consecutive year as one of their 100 Best Companies to Work For. We believe that this honor is the result of our commitment to providing a great experience for our diverse team of associates as well as our guests. We have a distinctive culture that we believe encourages contribution and collaboration. We take great pride in our culture and feel it is critical in encouraging creativity, communication, and strong store performance. All store managers receive comprehensive training through our Bear University program, which is designed to promote a friendly and personable environment in our stores and a consistent experience across our stores.

We extensively train our associates on the bear-building process and the guest experience. In fiscal 2010, we hired less than 3% of applicants for store manager positions. We focus on employing and retaining people who are friendly and committed to guest service. Our high employee retention rates contribute to the consistency and quality of the guest experience. Our store teams are evaluated and compensated not only on sales results but also the results from our regular guest satisfaction surveys. Each store has a recognition fund so that exceptional guest service can be immediately recognized and rewarded. We are committed to providing compensation structures that recognize individual accomplishments as well as overall team success.

As of January 1, 2011, we employed approximately 1,200 full-time and 4,300 part-time employees. We divide our store base into four geographic regions, with the United Kingdom and Ireland representing one of those regions. The regions are lead by our Chief Operations and Financial Bear and four Regional Workshop Managing Directors. Bearitory Leaders are responsible for each of our 32 store districts, or bearitories, consisting of on average, 11 stores. Historically, our stores generally have had a full-time Chief Workshop Manager, one full-time Assistant Workshop Manager, and one or two primarily part-time Associate Workshop Managers, in addition to part-time hourly Bear Builder® associates. The number of part-time employees fluctuates depending on our seasonal needs. In addition to the approximately 5,200 employees at our store locations, we employ approximately 200 associates in general administrative functions at our World Bearquarters in St. Louis, Missouri, approximately 100 associates at our Bearhouse distribution center in Groveport, Ohio, and approximately 30 associates in our European Bearquarters in Windsor, England. We are committed to innovation and invention and generally have confidentiality agreements with our employees and consultants. Store managers and Bearquarters associates pass specific profile assessments. None of our employees are represented by a labor union, and we believe our relationship with our employees is good.

International Franchises

In 2003, we began to expand Build-A-Bear Workshop stores outside of the United States, opening company-owned stores in Canada and our first franchised location in the United Kingdom. As of January 1, 2011, there were 63

Build-A-Bear Workshop franchised stores located in the following countries:

Japan	9
South Africa	9
Denmark	9
Australia	9
Germany	8
Thailand	5
Singapore	4
Norway	3
Gulf States(1)	3
Mexico	3
Sweden	1

(1) Gulf States agreement includes Kuwait, Bahrain, Qatar, Oman and the United Arab Emirates.

All stores outside of the U.S., Canada, the United Kingdom and Ireland are currently operated by third party franchisees under separate master franchise agreements covering each country. Master franchise rights are typically granted to a franchisee for an entire country or group of countries for a specified term. The terms of these master franchise agreements vary by country but typically provide that we receive an initial, one-time franchise fee and continuing royalties based on a percentage of the franchisees' stores sales. The terms of these agreements range up to 25 years with a franchisee option to renew for an additional term if certain conditions are met. All franchised stores have similar signage, store layout and merchandise characteristics to our company-owned stores. Our goal is to have well-capitalized franchisees with expertise in retail operations or franchising and real estate in their respective country. We collaborate with our franchisees in the development of their business, marketing and store growth plans. We review all franchisees' orders for merchandise which are made in the same factories that produce products for our company-owned stores and advise our franchisees concerning their operational and business practices in an effort to ensure they are in compliance with our standards. We expect our current franchisees to open approximately five to ten new stores, net of closures, in fiscal 2011 in both existing and new countries.

Sourcing and Inventory Management

We do not own or operate any manufacturing facilities. Our animal skins, stuffing, clothing and accessories are produced by factories located primarily in China. We purchased approximately 73% of our inventory in fiscal 2010, approximately 80% in fiscal 2009 and approximately 81% in fiscal 2008 from three long standing vendors. After specifying the details and requirements for our products, our vendors contract orders with multiple manufacturing facilities in China that are approved by us in accordance with our quality control and labor standards. Our supplier factories are compliant with the International Council of Toy Industries (ICTI) CARE certification.

The CARE (Caring, Awareness, Responsible, Ethical) Process is the ICTI program to promote ethical manufacturing, in the form of fair labor treatment, as well as employee health and safety, in the toy industry supply chain worldwide. The program's initial focus is in China, where 70 percent of the world's toy volume is manufactured. In order to obtain this certification, each factory completed a rigorous evaluation performed by an accredited ICTI agent. Our vendors can be used interchangeably as each has a sourcing network for multiple product categories and can expand its factory network as needed. Our relationships with our vendors generally are on a purchase order basis and do not provide a contractual obligation to provide adequate supply or acceptable pricing on a long-term basis.

The average time from the beginning of production to arrival of the products into our stores is approximately 90 to 120 days. Our weekly tracking and reporting tools give us the capability to adjust to shifts in demand. Through an ongoing analysis of selling trends, we regularly update our product assortment by increasing quantities of productive styles and eliminating less productive items. Our distribution centers provide further logistical efficiencies for delivering merchandise to our stores.

Distribution and Logistics

We have a 350,000-square-foot distribution center near Columbus, Ohio which serves a majority of our stores in the United States. We have a third-party distribution center in Toronto, Canada under an agreement that may be terminated with 120-day notice or when no work has been performed for 180 days. In Europe, we contract with a third-party distribution center in Selby, England under an agreement that ends in December 2014. This agreement contains clauses that allow for termination if certain performance criteria are not met. In August 2010, we also engaged a third-party warehouse in southern California to service our West Coast stores. The contract has a one year term and is renewable.

Transportation from the warehouses to the stores is managed by several third-party logistics providers. In the United States and Canada, merchandise is shipped by a variety of distribution methods and the method is alternated depending on the store and seasonal inventory demand. Key delivery methods are direct trucks through third-party pool points, ‘LTL’ (less-than truck load) deliveries, and direct parcel deliveries. Shipments from our third-party distribution centers are scheduled throughout the week in order to smooth workflow and stores that are part of the same shipping route are grouped together to reduce freight costs. All items in our assortment are eligible for distribution, depending on allocation and fulfillment requirements, and we typically distribute merchandise and supplies to each store once a week on a regular schedule, which allows us to consolidate shipments in order to reduce distribution and shipping costs. Back-up supplies, such as Cub Condo® carrying cases and stuffing for the animals, are often stored in limited amounts at local pool points.

Management Information Systems and Technology

Technology is a key component of our business strategy, and we are committed to utilizing technology to enhance our competitive position. Our information and operational systems utilize a broad range of both purchased and internally developed applications which support our guest relationships, marketing, financial, retail operations, real estate, merchandising, e-commerce and inventory management processes. Our employees can securely access these systems over a company-wide network. Sales, daily deposit and guest information are automatically collected from the stores’ point-of-sale terminals and kiosks on a near real time basis. We have developed proprietary software including our party scheduling system and domestic and international versions of our Name Me kiosk, which populates our Find-A-Bear® identification system. Data from these systems are used to support key decisions in all areas of our business, including merchandising, allocation and operations.

We regularly evaluate strategic information technology initiatives focused on competitive differentiation, support of corporate strategy and reinforcement of our internal support systems. Our critical systems are reviewed on a regular basis to evaluate disaster recovery plans and the security of our systems.

Competition

We view the Build-A-Bear Workshop experience as a distinctive combination of entertainment and retail with limited direct competition. Because our signature product is a stuffed animal, we compete with toy retailers, such as Wal-Mart, Toys "R" Us, Target, Kmart and other discount chains. Build-A-Bear Workshop was ranked by Playthings Magazine as the ninth largest toy retailer for retailers with continuing operations, based on 2008 revenues. Since we develop proprietary products, we also compete indirectly with a number of companies that sell stuffed animals in the United States, including, but not limited to, Ty, Fisher Price, Mattel, Ganz, Russ Berrie, Applause, Boyd's, Hasbro, Commonwealth, Gund and Vermont Teddy Bear. Since we sell a product that integrates merchandise and experience, we also view our competition as any company that competes for family time and entertainment dollars, such as movie theaters, amusement parks and arcades, other mall-based entertainment venues and online entertainment. Being a mall-based retailer, we also compete with other mall-based retailers for prime mall locations, including various apparel, footwear and specialty retailers.

We are aware of several small companies that operate "make your own" teddy bear and stuffed animal stores or kiosks in retail locations, but we believe none of those companies offer the breadth and depth of the Build-A-Bear Workshop experience or operate as a national or international retail company.

We also believe that there is an emerging trend within children's play patterns towards internet and online play. According to Emarketer.com, kids aged 8 to 11 reported that they spend between one and two hours online each day. In 2007, 24% of US child and teen Internet users visited virtual worlds. In 2011, an estimated 53% will do so. Therefore, we believe our bearville.com Web site competes with other companies and internet sites that vie for children's attention in the online space including webkinz.com, clubpenguin.com and neopets.com.

Intellectual Property and Trademarks

As of January 1, 2011, we had obtained over 238 U.S. trademark registrations, including Build-A-Bear Workshop for stuffed animals and accessories for the animals, retail store services and other goods and services, 36 issued U.S. patents with expirations ranging from 2013 through 2024 and over 399 copyright registrations. In addition, we have over 27 U.S. trademark applications pending. We also license three patents from third-parties, including a patent for the pre-stitching system used for closing up our stuffed animals after they have been stuffed (U.S. Patent No. 6,109,196). Pursuant to an exclusive patent license agreement with Tonyco, Inc. dated March 12, 2001, we were granted an exclusive license for use of the patent in retail stores similar to ours. While we have the right to sublicense the patent, the licensor has agreed not to grant competing license rights to any of our competitors. In the event that we or the licensor has reason to believe that a third party is infringing upon the patent, the licensor is generally required to bear the expenses required to maintain and defend the patent. The term of the agreement is for the full life of the patent and any improvements thereon. The term will expire in 2019 unless we terminate the agreement, upon notice to the licensor, or in the event that the patent lapses due to the licensor's non-payment of maintenance taxes and fees for the patent. We paid the licensor $760,000 for the license. All payments due under the license have been made and no ongoing payments are required by us.

We believe our copyrights, service marks, trademarks, trade secrets, patents and similar intellectual property are critical to our success, and we intend, directly or indirectly, to maintain and protect these marks and, where applicable, license the intellectual property and the registrations for the intellectual property. We rely on trademark, copyright and other intellectual property law to protect our proprietary rights to the extent available in any relevant jurisdiction. We also depend on trade secret protection through confidentiality and license agreements with our employees, subsidiaries, licensees, licensors and others. We may not have agreements containing adequate protective provisions in every case, and the contractual provisions that are in place may not provide us with adequate protection in all circumstances. Any infringement or misappropriation of our intellectual property rights or breach of our confidentiality or license agreements could result in significant litigation costs, and any failure to adequately protect our proprietary rights could result in our competitors offering similar products, potentially resulting in loss of one or more competitive advantages and decreased revenues. In addition, intellectual property litigation or claims could force us to do one or more of the following: cease selling or using any of our products that incorporate the challenged intellectual property, which would adversely affect our revenue; obtain a license from the holder of the intellectual property right alleged to have been infringed, which license may not be available on reasonable terms, if at all; and redesign or, in the case of trademark claims, rename our products to avoid infringing the intellectual property rights of third parties, which may not be possible and time-consuming if it is possible to do so.

Despite our efforts to protect our intellectual property rights, intellectual property laws afford us only limited protection. A third party could copy or otherwise obtain information from us without authorization. Accordingly, we may not be able to prevent misappropriation of our intellectual property or to deter others from developing similar products or services. Further, monitoring the unauthorized use of our intellectual property is difficult. Litigation has been and may continue to be necessary to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. Litigation of this type could result in substantial costs and diversion of resources, may result in counterclaims or other claims against us and could significantly harm our results of operations. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as do the laws of the United States.

We also conduct business in foreign countries to the extent our merchandise is manufactured or sold outside the United States and we have opened stores outside the United States either directly or indirectly through franchisees. We filed, obtained or plan to file for registration of marks in foreign countries to the degree necessary to protect these marks, although our efforts may not be successful and there may be restrictions on the use of these marks in some jurisdictions.

Segments and Geographic Areas

We conduct our operations through three reportable segments consisting of retail, international franchising, and commercial. The retail segment includes the operating activities of company-owned stores in the United States, Canada, the United Kingdom and Ireland, and other retail operations, including our web-store and non-traditional store locations such as tourist venues, pop-up locations and ballpark stores. The international franchising segment includes the licensing activities of our franchise agreements with locations in Asia, Australia, Africa, the Middle East and Europe, outside of the United Kingdom and Ireland. The commercial segment includes our transactions with other business partners, mainly comprised of licensing our intellectual property, including entertainment properties, for third-party use and wholesale product sales.

Our reportable segments are primarily determined by the types of customers they serve and the types of products and services that they offer. Each reportable segment may operate in many geographic areas. See the financial statements included elsewhere in this Annual Report on Form 10-K for further discussion and financial information related to our segments and the geographic areas in which we operate.

Availability of Information

We make certain filings with the SEC, including our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments and exhibits to those reports, available free of charge in the Investor Relations section of our corporate website, http://ir.buildabear.com, as soon as reasonably practicable after they are filed with the SEC. The filings are also available through the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 or by calling 1-800-SEC-0330. Also, these filings are available on the internet at http://www.sec.gov. Our Annual Reports to shareholders, press releases and recent analyst presentations are also available on our website, free of charge, in the Investor Relations section or by writing to the Investor Relations department at World Bearquarters, 1954 Innerbelt Business Center Dr., St. Louis, MO 63114.

ITEM 1A. RISK FACTORS

We operate in a changing environment that involves numerous known and unknown risks and uncertainties that could materially affect our operations. The risks, uncertainties and other factors set forth below may cause our actual results, performances or achievements to be materially different from those expressed or implied by our forward-looking statements. If any of these risks or events occur, our business, financial condition or results of operations may be adversely affected.

Risks Related to Our Business

A continued decline in general global economic conditions could lead to disproportionately reduced consumer demand for our products, which represent relatively discretionary spending, and have an adverse effect on our liquidity and profitability.

Since purchases of our merchandise are dependent upon discretionary spending by our guests, our financial performance is sensitive to changes in overall economic conditions that affect consumer spending. Consumer spending habits are affected by, among other things, prevailing economic conditions, levels of employment, salaries and wage rates, consumer confidence and consumer perception of economic conditions. A continued slowdown in the United States, Canadian or European economies or uncertainty as to the economic outlook could reduce discretionary spending or cause a shift in consumer discretionary spending to other products. Any of these factors would likely cause us to delay or slow our expansion plans, result in lower net sales and could also result in excess inventories, which could, in turn, lead to increased merchandise markdowns and related costs associated with higher levels of inventory and adversely affect our liquidity and profitability.

A decrease in the customer traffic generated by the shopping malls in which we are located, which we depend upon to attract guests to our stores, could adversely affect our financial condition and profitability.

While we invest heavily in integrated marketing efforts and believe we are more of a destination location than traditional retailers, we rely to a great extent on customer traffic in the malls in which our stores are located. In order to generate guest traffic, we generally attempt to locate our stores in prominent locations within high traffic shopping malls. We rely on the ability of the malls' anchor tenants, generally large department stores, and on the continuing popularity of malls as shopping destinations. We cannot control the development of new shopping malls, the addition or loss of anchors and co-tenants, the availability or cost of appropriate locations within existing or new shopping malls or the desirability, safety or success of shopping malls. In addition, customer mall traffic may be reduced due to a loss of consumer confidence because of the economy, terrorism or war. If we are unable to generate sufficient guest traffic, our sales and results of operations would be harmed. A significant decrease in shopping mall traffic could have a material adverse effect on our financial condition and profitability. For example, the slower economy has caused our sales to decline and led us to slow our growth plans.

If we are unable to generate interest in and demand for our interactive retail experience, including being able to identify and respond to consumer preferences in a timely manner, our financial condition and profitability could be adversely affected.

We believe that our success depends in large part upon our ability to continue to attract guests with our interactive shopping experience and our ability to anticipate, gauge and respond in a timely manner to changing consumer preferences and fashion trends. We cannot assure you that our past success will be sustained or there will continue to be a demand for our "make-your-own stuffed animal" interactive experience, or for our stuffed animals, animal apparel and accessories. A decline in demand for our interactive shopping experience, our animals, animal apparel or accessories, or a misjudgment of consumer preferences or fashion trends, could have a negative impact on our business, financial condition and results of operations. For example, in 2008 we announced plans to close the Friends 2B Made concept. The closure was completed by the end of the fiscal 2009 third quarter with pre-tax charges totaling $3.9 million. In addition, if we miscalculate the market for our merchandise or the purchasing preferences of our guests, we may be required to sell a significant amount of our inventory at discounted prices or even below costs, thereby adversely affecting our financial condition and profitability. For example, in 2007, we wrote-off $1.6 million, net of tax, of inventory, including excess Shrek® merchandise.

Our future growth and profitability could be adversely affected if our marketing and online initiatives are not effective in generating sufficient levels of brand awareness and guest traffic.

We continue to update and evaluate our marketing initiatives, focusing on brand awareness, new product news, timely promotions and rapidly changing consumer preferences. We may not be able to successfully engage children in our virtual world website, bearville.com, and achieve high enough traffic levels nor be able to leverage the site to drive traffic to our stores. Our future growth and profitability will depend in large part upon the effectiveness and efficiency of our marketing programs and future marketing efforts that we undertake, including our ability to:

- create greater awareness of our brand, interactive shopping experience and products;
- identify the most effective and efficient level of spending in each market;
- determine the appropriate creative message and media mix for marketing expenditures;
- effectively manage marketing costs (including creative and media) in order to maintain acceptable operating margins and return on marketing investment;
- select the right geographic areas in which to market;
- convert consumer awareness into actual store visits and product purchases; and
- reach a level of engagement on the virtual world website with large numbers of unique visitors with frequent visitation that drives visits to our retail stores resulting in purchases.

Our planned marketing expenditures may not result in increased total or comparable store sales or generate sufficient levels of product and brand awareness. We may not be able to manage our marketing expenditures on a cost-effective basis.

If we are not able to increase our comparable store sales trends, our results of operations and financial condition could be adversely affected.

Our comparable store sales for 2010 declined 2.0% following a 13.4% decline in fiscal 2009, a 14.0% decline in fiscal 2008, a 9.9% decline in fiscal 2007 and a 6.5% decline in fiscal 2006. We believe that global economic conditions continued to impact our comparable store sales in 2010. We believe that the decrease in fiscal 2009 was primarily attributable to the continued economic recession and dramatic decrease in consumer sentiment and the decline in North American shopping mall traffic. We believe that the decrease in 2008 was primarily attributable to the economic recession and decrease in consumer disposable income, a continued decline in shopping mall customer traffic and changes in media strategies, online entertainment, children's media consumption and play patterns. We believe that the decrease in 2007 was primarily attributable to a decline in shopping mall customer traffic and consumer spending on discretionary products, changes in media strategies, online entertainment, children's media consumption and play patterns, competitive plush animal products and lower than expected customer purchases of select licensed movie products introduced in the fiscal 2007 second quarter. We believe that the decrease in 2006 was primarily the result of changing customer preferences, a decline in customer traffic, and the more difficult macro-economic conditions generally impacting consumer confidence and spending patterns. We believe the principal factors that will affect comparable store results include the following:

- the continuing appeal of our concept;
- the effectiveness of our marketing efforts to attract new and repeat guests;
- consumer confidence and general economic conditions;
- our ability to anticipate and to respond, in a timely manner, to consumer trends;
- the continued introduction and expansion of our merchandise offerings;
- the impact of new stores that we open in existing markets;
- mall traffic;
- competition for product offerings including in the online space;
- the timing and frequency of national media appearances and other public relations events; and
- weather conditions.

As a result of these and other factors, we may not be able to generate or achieve comparable stores sales growth in the future. If we are unable to do so, our results of operations could be significantly harmed and we may be required to record significant impairment charges.

If we are unable to renew, renegotiate or replace our store leases or enter into leases for new stores on favorable terms, or if we violate any of the terms of our current leases, our growth and profitability could be harmed.

We lease all of our store locations. The majority of our store leases contain provisions for base rent plus percentage rent based on sales in excess of an agreed upon minimum annual sales level. A number of our leases include a termination provision which applies if we do not meet certain sales levels during a specified period, typically in the third to fourth year and the sixth to seventh year of the lease, which may be at either the landlord's options or ours. Furthermore, some of our leases contain various restrictions relating to change of control of our company. Our leases also subject us to risks relating to compliance with changing mall rules and the exercise of discretion by our landlords on various matters within the malls. In addition, the lease for our store in the Downtown Disney® District at the Disneyland® Resort in Anaheim, California provides that the landlord may terminate the lease at any time, subject to the payment of an early termination fee. As a result, we cannot assure you that the landlord will not exercise its right to terminate this lease.

In addition, most of our leases will expire within the next ten years and many of our initial leases are near completion and do not contain options to renew. We may not be offered a lease renewal by our landlord, may not be able to renew leases under favorable economic terms or maintain our existing store location thereby requiring additional capital expenditure to move the store location within the mall. Those locations may be in parts of the mall that have less traffic or be positioned further from our desired co-tenants and our ongoing sales and profitability results may be negatively affected. The terms of new leases may not be as favorable, increasing store expenses and impacting overall profitability. If we execute termination rights, we may have expenses and charges associated with those closures which could negatively impact our profitability.

Our growth strategy requires us to operate a significant number of stores in the United States, Canada, the United Kingdom and Ireland each year as well as open new store locations in these countries. If we are not able to operate these stores or to effectively manage the growth of additional stores, it could adversely affect our ability to grow and could significantly harm our profitability.

Our growth will largely depend on our ability to operate our stores successfully in the United States, Canada, the United Kingdom and Ireland as well as open additional stores in those countries. We opened 25, 50, and 35 stores in fiscal 2008, 2007 and 2006, respectively. We slowed new store growth considerably in 2009, opening one store, and in 2010 opening four stores, exclusive of temporary, pop-up locations. We plan to continue this slower expansion in 2011. Our ability to identify and open new stores in future years in desirable locations and operate such new stores profitably is a key factor in our ability to grow successfully. We cannot assure you as to when or whether desirable locations will become available, the number of Build-A-Bear Workshop stores that we can or will ultimately open, or whether any such new stores can be profitably operated. We have not always succeeded in identifying desirable locations or in operating our stores successfully in those locations. For example, in 2010, we closed five locations. Prior to 2010, we had closed four stores since our inception (excluding four stores that we closed in connection with our 2006 acquisition of Amsbra and The Bear Factory). We may decide to close other stores in the future. In addition, our ability to open new stores and manage our growth will be limited to some extent by market saturation of our stores. Our ability to open new stores and to manage our growth also depends on our ability to:

- negotiate acceptable lease terms, including desired tenant improvement allowances;
- finance the preopening costs, capital expenditures and working capital requirements of the stores;
- manage inventory to meet the needs of new and existing stores on a timely basis;
- hire, train and retain qualified store personnel;
- develop cooperative relationships with our landlords; and
- successfully integrate new stores into our existing operations.

In July 2005, we opened our flagship store in New York City. This store is much larger than our typical mall-based stores and, as such, we may be unable to generate revenues from this store at a level that justifies keeping the store open. Closing this store could not only have an adverse impact on our profitability, as the costs of opening this store were much larger than those for a typical store, but, as our flagship store, it could also have an adverse impact on the Build-A-Bear Workshop brand and consumer perception of our brand.

Increased demands on our operational, managerial and administrative resources as a result of our growth strategy could cause us to operate our business less effectively, which in turn could cause deterioration in our profitability.

Our merchandise is manufactured by foreign manufacturers and we transact business in various foreign countries; therefore the availability and costs of our products, as well as our product pricing, may be negatively affected by risks associated with international manufacturing and trade and foreign currency fluctuations.

We purchase our merchandise from domestic vendors who contract with manufacturers in foreign countries, primarily in China. Any event causing a disruption of imports, including the imposition of import restrictions or labor strikes or lock-outs, could adversely affect our business. For example, in fiscal 2002, we experienced disruption to our import of merchandise as well as increased shipping costs associated with a dock-worker labor dispute. The flow of merchandise from our vendors could also be adversely affected by financial or political instability in any of the countries in which the goods we purchase are manufactured, especially China, if the instability affects the production or export of merchandise from those countries. Trade restrictions in the form of tariffs or quotas, or both, applicable to the products we sell as well as increases in raw material and labor costs could also affect the importation of those products and could increase the cost and reduce the supply of products available to us. In addition, decreases in the value of the U.S. dollar against foreign currencies, particularly the Chinese renminbi, could increase the cost of products we purchase from overseas vendors. The pricing of our products in our stores may also be affected by changes in foreign currency rates and require us to make adjustments which would impact our revenue and profit in various markets.

We rely on a few vendors to supply substantially all of our merchandise, and significant price increases or any disruption in their ability to deliver merchandise could harm our ability to source products and supply inventory to our stores.

We do not own or operate any manufacturing facilities. We purchased approximately 73% of our merchandise in fiscal 2010, approximately 80% in fiscal 2009 and approximately 81% in fiscal 2008, from three vendors. Our 2010 purchases included a significant purchase of non-proprietary toy products that were incremental to our traditional purchasing. Excluding these purchases, we purchased approximately 80% of our merchandise from three vendors. These vendors in turn contract for our orders with multiple manufacturing facilities located primarily in China for the production of merchandise. Our relationships with our vendors generally are on a purchase order basis and do not provide a contractual obligation to provide adequate supply or acceptable pricing on a long-term basis. Our vendors could discontinue sourcing merchandise for us at any time. If any of our significant vendors were to discontinue their relationship with us, or if the factories with which they contract were to suffer a disruption in their production, we may be unable to replace the vendors in a timely manner, which could result in short-term disruption to our inventory flow as we transition our orders to new vendors or factories which could, in turn, disrupt our store operations and have an adverse effect on our business, financial condition and results of operations. Additionally, in the event of a significant price increase from these suppliers, we may not be able to find alternative sources of supply in a timely manner or raise prices to offset the increases, which could have an adverse effect on our business, financial condition and results of operations.

Our profitability could be adversely affected by high petroleum products prices.

The profitability of our business depends to a certain degree upon the price of petroleum products, both as a component of the transportation costs for delivery of inventory from our vendors to our stores and as a raw material used in the production of our animal skins and stuffing. For example, our results in fiscal 2008 and 2007 were impacted by significant increases in fuel surcharges due to higher petroleum products prices. We are unable to predict what the price of crude oil and the resulting petroleum products will be in the future. We may be unable to pass along to our customers the increased costs that would result from higher petroleum prices. Therefore, any such increase could have an adverse impact on our business and profitability.

If we are not able to franchise new stores outside of the United States, Canada, the United Kingdom and Ireland, if we are unable to effectively manage our international franchises or if the laws relating to our international franchises change, our growth and profitability could be adversely affected and we could be exposed to additional liability.

In 2003, we began to expand the Build-A-Bear Workshop brand outside of the United States, opening Company-owned stores in Canada and our first franchised location in the United Kingdom. We have continued to expand outside of our company-owned regions through franchising in a number of countries.As of January 1, 2011, there were 63 Build-A-Bear Workshop franchised stores located outside of the United States, Canada, the United Kingdomand Ireland. We cannot assure you that our franchisees will be successful in identifying and securing desirable locations or in operating their stores. International markets frequently have different demographic characteristics, competitive conditions, consumer tastes and discretionary spending patterns than our existing North American and European markets, which may cause these stores to be less successful than those in our existing markets. Additionally, our franchisees may experience merchandising and distribution expenses and challenges that are different from those we currently encounter in our existing markets. The operations and results of our franchisees could be negatively impacted by the economic or political factors in the countries in which they operate or foreign currency fluctuations. These challenges, as well as others, could have a material adverse effect on our business, financial condition and results of operations.

The success of our franchising strategy will depend upon our ability to attract and maintain qualified franchisees with sufficient financial resources to develop and grow the franchise operation and upon the ability of those franchisees to successfully develop and operate their franchised stores. Franchisees may not operate stores in a manner consistent with our standards and requirements, may not hire and train qualified managers and other store personnel and may not operate their stores profitably. As a result, our franchising strategy may not be profitable to us. Moreover, our brand image and reputation may suffer. When franchisees perform below expectations we may transfer those agreements to other parties or discontinue the franchise agreement. Furthermore, even if our international franchising strategy is successful, the interests of franchisees might sometimes conflict with our interests. For example, whereas franchisees are concerned with their individual business strategies and objectives, we are responsible for ensuring the success of the Build-A-Bear Workshop brand and all of our stores.

The laws of the various foreign countries in which our franchisees operate govern our relationships with our franchisees. These laws, and any new laws that may be enacted, may detrimentally affect the rights and obligations between us and our franchisees and could expose us to additional liability.

We may not be able to operate our European company-owned stores in the United Kingdom and Ireland profitably.

In April 2006, we acquired The Bear Factory Limited, a stuffed animal retailer in the United Kingdom owned by The Hamleys Group Limited, and Amsbra Limited, our former United Kingdom franchisee. Both The Bear Factory and Amsbra had losses in 2006, 2005 and prior fiscal years. Although we have realized benefits from these operations as part of our larger company, we may be unable to continue to do so on a consistent basis. In particular, we face business, regulatory and cultural differences from our domestic business, such as economic conditions,changes in foreign government policies and regulations and potential restrictions and costs to convert and repatriate currency, as well as other risks that we may not anticipate. We also face difficulties realizing benefits because we have less brand awareness than in the U.S., face higher labor and rent costs, and have different holiday schedules. In 2007, we terminated our French franchise agreement and opened three company-owned stores in France. We were unable to operate the stores in France profitably and in 2010, we closed all three of our company-owned stores in France.

Our leases in the United Kingdom and Ireland also typically contain provisions requiring rent reviews every five years in which the base rent that we pay is adjusted to current market rates. These rent reviews require that base rents cannot be reduced if market conditions have deteriorated but can be changed “upwards only”. We may be required to pay base rents that are significantly higher than we have forecast. For example, past rent reviews have resulted in increases as high as 40% in select locations within the United Kingdom. As a result of these and other factors, we may not be able to operate our European store locations profitably. If we are unable to do so, our results of operations and financial condition could be harmed and we may be required to record significant additional impairment charges.

We may suffer negative publicity or be sued if the manufacturers of our merchandise ship any products that do not meet current safety standards or production requirements or if our products are recalled or cause injuries.

Although we require our manufacturers to meet our product specifications and safety standards and submit our products for testing, we cannot control the materials used by our manufacturers. If one of these manufacturers ships merchandise that does not meet our required standards, we could in turn experience negative publicity or be sued.

Many of our products are used by small children and infants who may be injured from usage if age grading or warnings are not followed. We may decide or be required to recall products or be subject to claims or lawsuits resulting from injuries. For example, in 2009 we voluntarily recalled a product due to a possible safety issue, for which a vendor reimbursed us for certain related expenses. Negative publicity in the event of any recall or if any children are injured from our products could have a material adverse effect on sales of our products and our business, and related recalls or lawsuits with respect to such injuries could have a material adverse effect on our financial position. Although we currently have liability insurance, we cannot assure you that it would cover product recalls, and we face the risk that claims or liabilities will exceed our insurance coverage. Furthermore, we may not be able to maintain adequate liability insurance in the future.

Portions of our business are subject to privacy and security risks. If we improperly obtain, or are unable to protect, information from our guests, in violation of privacy or security laws or expectations, we could be subject to liability and damage to our reputation.

Our website, bearville.com, features children's games and in world e-mail and chat system. In addition, our e-commerce site, buildabear.com, features e-cards and printable party invitations and thank-you notes and provides an opportunity for children under the age of 13 to sign up, with the consent of their parent or guardian, to receive our online newsletter. We currently obtain and retain personal information about our website users, store shoppers and Stuff Fur Stuff loyalty program members. In addition, we obtain personal information about our guests as part of their registration in our Find-A-Bear identification system. Federal, state and foreign governments have enacted or may enact laws or regulations regarding the collection and use of personal information, with particular emphasis on the collection of information regarding minors. Such regulations include or may include requirements that companies establish procedures to:

- give adequate notice regarding information collection and disclosure practices;
- allow consumers to have personal information deleted from a company's database;
- provide consumers with access to their personal information and the ability to rectify inaccurate information;
- obtain express parental consent prior to collecting and using personal information from children; and
- comply with the Federal Children's Online Privacy Protection Act.

Such regulation may also include enforcement and redress provisions. While we have implemented programs and procedures designed to protect the privacy of people, including children, from whom we collect information, and our websites are designed to be fully compliant with the Federal Children's Online Privacy Protection Act, there can be no assurance that such programs will conform to all applicable laws or regulations. If we fail to fully comply, we may be subjected to liability and damage to our reputation.

We have a stringent, comprehensive privacy policy covering the information we collect from our guests and have established security features to protect our guest database and website. However, our security measures may not prevent security breaches. We may need to expend significant resources to protect against security breaches or to address problems caused by breaches. If unauthorized third parties were able to penetrate our network security and gain access to, or otherwise misappropriate, our guests' personal information, it could harm our reputation and, therefore, our business and we could be subject to liability. Such liability could include claims for misuse of personal information or unauthorized use of credit cards. These claims could result in litigation, our involvement in which, regardless of the outcome, could require us to expend significant financial resources. In addition, because our guest database primarily includes personal information of young children and young children frequently interact with our website, we are potentially vulnerable to charges from parents, children's organizations, governmental entities, and the media of engaging in inappropriate collection, distribution or other use of data collected from children. Such charges could adversely impact guest relationships and ultimately cause a decrease in net sales and also expose us to litigation and possible liability.

Our virtual world Web site, primarily for children, bearville.com, allows social interaction between users. While we have security features and chat monitoring, our security measures may not protect users' identities and our online safety measures may be questioned which may result in negative publicity or a decrease in visitors to our site. If site users act inappropriately or seek unauthorized contact with other users of the site, it could harm our reputation and, therefore, our business and we could be subject to liability. Internet privacy is a rapidly changing area and we may be subject to future requirements and legislation that are costly to implement and negatively impact our results.

We may suffer negative publicity or be sued if the manufacturers of our merchandise violate labor laws or engage in practices that our guests believe are unethical.

We rely on our sourcing personnel to select manufacturers with legal and ethical labor practices, but we cannot control the business and labor practices of our manufacturers. If one of these manufacturers violates labor laws or other applicable regulations or is accused of violating these laws and regulations, or if such a manufacturer engages in labor or other practices that diverge from those typically acceptable in the United States, we could in turn experience negative publicity or be sued.

We may suffer negative publicity or a decrease insales or profitability if the non-proprietary toy products we sell in our stores do not meet our quality standards or fails to achieve our sales expectations.

We expect to expand our product assortment to include interactive toy products manufactured by other toy companies. If sales of such products do not meet our expectations or are impacted by competitors’ pricing, we may have to take markdowns or employ other strategies to liquidate the product. If other toy companies do not meet quality standards or violate any manufacturing or labor laws, we suffer negative publicity and not realize our sales plans.

We may not be able to operate successfully if we lose key personnel, are unable to hire qualified additional personnel, or experience turnover of our management team.

The success of our business depends upon our senior management closely supervising all aspects of our business, in particular the operation of our stores and the design, procurement and allocation of our merchandise. Also, because guest service is a defining feature of the Build-A-Bear Workshop corporate culture, we must be able to hire and train qualified managers and Bear Builder associates to succeed. The loss of certain key employees, in particular Maxine Clark, our founder and Chief Executive Bear, as well as other members of our senior management, our inability to attract and retain other qualified key employees or a labor shortage that reduces the pool of qualified store associates could have a material adverse effect on our business, financial condition and results of operations. We generally do not maintain key person insurance with respect to our executives, management or other personnel, except for limited coverage of Ms. Clark, which we do not believe would be sufficient to completely protect us against losses we may suffer if her services were to become unavailable to us in the future.

We rely on a company-owned distribution center to service the majority of our stores in North America, and our third-party distribution center providers used in the western United States, Canada and Europe may perform poorly.

The efficient operation of our stores is dependent on our ability to distribute merchandise to locations throughout the United States, Canada and Europe in a timely manner. We have a 350,000-square-foot distribution center in Groveport, Ohio. We rely on this company-owned distribution center to receive, store and distribute merchandise for the majority of our North America stores. We rely on third parties to manage all of the warehousing and distribution aspects of our business on the West Coast of the United States, in Europe and a portion of our operations in Canada. Any significant interruption in the operation of the distribution centers due to natural disasters and severe weather, as well as events such as fire, accidents, power outages, system failures or other unforeseen causes could damage a significant portion of our inventory. These factors may also impair our ability to adequately stock our stores and could increase our costs associated with our supply chain.

Our market share may be adversely impacted at any time by a significant number of competitors.

We operate in a highly competitive environment characterized by low barriers to entry. We compete against a diverse group of competitors. Because we are mall-based, we see our competition as those mall-based retailers that compete for prime mall locations, including various apparel, footwear and specialty retailers. As a retailer whose signature product is a stuffed animal that is typically purchased as a toy or gift, we also compete with toy retailers, such as Wal-Mart, Toys “R” Us, Target, Kmart and other discount chains, as well as with a number of manufacturers that sell plush toys in the United States and Canada, including, but not limited to, Ty, Fisher Price, Mattel, Ganz, Russ Berrie, Applause, Boyds, Hasbro, Commonwealth, Gund and Vermont Teddy Bear. Since we offer our guests an experience as well as merchandise, we also view our competition as any company that competes for our guests’ time and entertainment dollars, such as movie theaters, restaurants, amusement parks and arcades. In addition, there are several small companies that operate “make your own” teddy bear and stuffed animal experiences in retail stores and kiosks. Although we believe that currently none of these companies offers the breadth and depth of the Build-A-Bear Workshop products and experience, we cannot assure you that they will not compete directly with us in the future.

Many of our competitors have longer operating histories, significantly greater financial, marketing and other resources, and greater name recognition. We cannot assure you that we will be able to compete successfully with them in the future, particularly in geographic locations that represent new markets for us. If we fail to compete successfully, our market share and results of operations could be materially and adversely affected.

We also believe that there is an emerging trend within children’s play patterns towards electronic toys, internet and online play. According to Emarketer.com, kids aged 8 to 11 reported that they spend between one and two hours online each day. In 2007, 24% of US child and teen Internet users will visit virtual worlds. By 2011, an estimated 53% will do so. Therefore, we believe our Web site, bearville.com, competes with other companies and internet sites that vie for children's attention in the online space including webkinz.com, clubpenguin.com and neopets.com. A growing number of traditional children's toy and entertainment companies have also developed their own virtual world online play sites including Barbie.com® and McWorld. We cannot assure you that children's preferences for our products will remain strong or that our on line Web site for children, bearville.com, will be successful in attracting children to our brand. If children decide to engage with other products or Web sites, our sales will be negatively impacted and our results will be materially impacted.

We may fail to renew, register or otherwise protect our trademarks or other intellectual property and may be sued by third parties for infringement or, misappropriation of their proprietary rights, which could be costly, distract our management and personnel and which could result in the diminution in value of our trademarks and other important intellectual property.

Other parties have asserted in the past, and may assert in the future, trademark, patent, copyright or other intellectual property rights that are important to our business. We cannot assure you that others will not seek to block the use of or seek monetary damages or other remedies for the prior use of our brand names or other intellectual property or the sale of our products or services as a violation of their trademark, patent or other proprietary rights. Defending any claims, even claims without merit, could be time-consuming, result in costly settlements, litigation or restrictions on our business and damage our reputation.

In addition, there may be prior registrations or use of intellectual property in the U.S. or foreign countries for similar or competing marks or other proprietary rights of which we are not aware. In all such countries it may be possible for any third party owner of a national trademark registration or other proprietary right to enjoin or limit our expansion into those countries or to seek damages for our use of such intellectual property in such countries. In the event a claim against us were successful and we could not obtain a license to the relevant intellectual property or redesign or rename our products or operations to avoid infringement, our business, financial condition or results of operations could be harmed. Securing registrations does not fully insulate us against intellectual property claims, as another party may have rights superior to our registration or our registration may be vulnerable to attack on various grounds.

Poor global economic conditions could have a material adverse effect on our liquidity and capital resources.

In 2008 and 2009, the general economic and capital market conditions in the United States and other parts of the world deteriorated significantly. These conditions adversely affected borrowers' access to capital and increased the cost of capital. Although we believe that our capital structure and credit facilities will provide sufficient liquidity, there can be no assurance that our liquidity will not be affected by changes in the capital markets or that our capital resources will at all times be sufficient to satisfy our liquidity needs. Capital market conditions may affect the renewal or replacement of our credit agreement, which was originally entered into in 2000 and has been extended annually since then and currently expires December 31, 2012.

Risks Related to Owning Our Common Stock

Fluctuations in our quarterly results of operations could cause the price of our common stock to substantially decline.

Retailers generally are subject to fluctuations in quarterly results. Our operating results for one period may not be indicative of results for other periods, and may fluctuate significantly due to a variety of factors, including:

- the profitability of our stores;
- increases or decreases in comparable store sales;
- changes in general economic conditions and consumer spending patterns;
- seasonal shopping patterns, including whether the Easter holiday occurs in the first or second quarter and other vacation schedules;
- the effectiveness of our inventory management;
- the timing and frequency of our marketing initiatives;
- changes in consumer preferences;
- the continued introduction and expansion of merchandise offerings;
- actions of competitors or mall anchors and co-tenants;
- weather conditions;
- the timing of new store openings and related expenses; and
- the timing and frequency of national media appearances and other public relations events.

If our future quarterly results fluctuate significantly or fail to meet the expectations of the investment community, then the market price of our common stock could decline substantially.

Fluctuations in our operating results could reduce our cash flow and we may be unable to repurchase shares at all or at the times or in the amounts we desire or the results of the share repurchase program may not be as beneficial as we would like.

Our Board of Directors has implemented a $50 million share repurchase program. The program does not require the Company to repurchase any specific number of shares of our common stock, and may be modified, suspended or terminated at any time without prior notice. Shares repurchased under the program will be subsequently retired. If our cash flow decreases as a result of decreased sales, increased expenses or capital expenditures or other uses of cash, we may not be able to repurchase shares of our common stock at all or at times or in the amounts we desire. As a result, the results of the share repurchase program may not be as beneficial as we would like.

Our certificate of incorporation and bylaws and Delaware law contain provisions that may prevent or frustrate attempts to replace or remove our current management by our stockholders, even if such replacement or removal may be in our stockholders' best interests.

Our basic corporate documents and Delaware law contain provisions that might enable our management to resist a takeover. These provisions:

- restrict various types of business combinations with significant stockholders;
- provide for a classified board of directors;
- limit the right of stockholders to remove directors or change the size of the board of directors;
- limit the right of stockholders to fill vacancies on the board of directors;
- limit the right of stockholders to act by written consent and to call a special meeting of stockholders or propose other actions;
- require a higher percentage of stockholders than would otherwise be required to amend, alter, change or repeal our bylaws and certain provisions of our certificate of incorporation; and
- authorize the issuance of preferred stock with any voting rights, dividend rights, conversion privileges, redemption rights and liquidation rights and other rights, preferences, privileges, powers, qualifications, limitations or restrictions as may be specified by our board of directors.

These provisions may:

- discourage, delay or prevent a change in the control of our company or a change in our management, even if such change may be in the best interests of our stockholders;
- adversely affect the voting power of holders of common stock; and
- limit the price that investors might be willing to pay in the future for shares of our common stock.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

Stores

As of January 1, 2011, we operated 290 retail stores located primarily in major malls throughout the United States, Canada and Puerto Rico, 52 stores located in the United Kingdom and two stores in Ireland. Our North American mall-based stores generally range in size from 2,000 to 4,000 gross square feet and average approximately 2,800 square feet, while our tourist location stores currently range up to 7,000 square feet and our flagship store in New York City is approximately 20,000 square feet. Our stores are highly visual and colorful featuring a teddy bear theme and larger than life details including a "sentry bear" at the front entry, custom-designed fixtures as well as a customized Build-A-Bear Workshop tile logo in our entryway. Our stores are designed to be open and inviting so that guests can fully immerse in the shopping experience and actively participate in the creation and customization of their purchase. Our typical store features one or two stuffing machines, three to five Name Me computer stations and numerous displays of fully-dressed stuffed animals throughout the store. We select malls and make site selections within the mall based upon demographic analysis, market research, site visits and mall dynamics as well as a proprietary forecasting model that projects a potential location's first year sales. We have identified additional target sites that meet our criteria for new stores in new and existing markets. We seek to locate our mall-based stores in areas with maximum customer traffic, often near to or in the center of the mall, as well as offering adjacencies to other children, teen and family retailers. After we approve a site, it typically takes approximately 26 weeks to finalize the lease, design the layout, build out the site, hire and train associates, and stock the store for opening.

We lease all of our store locations. Due to our attraction as a family-oriented entertainment destination concept, we have received numerous requests from mall owners and developers to locate a Build-A-Bear Workshop store in their malls. We believe that we generally have negotiated favorable lease terms including provisions providing for exclusivity of operation of our concept in the mall. Our stores are located in a variety of shopping center types. As of January 1, 2011, the distribution of our stores is as follows:

Super regional center	200
Regional center	108
Open air lifestyle center	17
Outlet center (1)	8
Other (theme, NYC, concession)	11
Total company-owned stores	344
Temporary pop-up locations	11
Other (ballparks, zoo)	4
Total company-owned retail locations	359

(1) Build-A-Bear Workshop stores in outlet centers are not merchandised with outlet merchandise.

Most of our leases have an initial term of ten years and do not have renewal options or clauses although our leases in the United Kingdom are typically covered by laws and regulations that give us priority rights of renewal. A number of our leases provide a lease termination or "kick out" option, which may be mutual, allowing either party to exercise the option in a pre-determined year or years, typically the third or fourth year and sixth or seventh year of the lease, if we do not meet certain agreed upon minimum sales levels. In addition, our leases typically require us to pay personal property taxes, our pro rata share of real property taxes of the shopping mall, our own utilities, repairs and maintenance in our store, a pro rata share of the malls' common area maintenance and, in some instances, merchant association fees and media fund contributions. Most of our leases in North America also require the payment of a fixed minimum rent as well as percentage rent based on sales in excess of agreed upon minimum annual sales levels. Our leases in the United Kingdom and Ireland typically have rent reviews every five years in which the base rental rate is adjusted to current market rates if they are higher than the original rent agreed.

Following is a list of our 344 company-owned stores in the United States, Canada, the United Kingdom and Ireland as of January 1, 2011:

State	Number of Stores
Alabama	5
Alaska	1
Arizona	5
Arkansas	3
California	26
Colorado	6
Connecticut	5
Delaware	1
Florida	20
Georgia	8
Idaho	1
Illinois	9
Indiana	7
Iowa	3
Kansas	2
Kentucky	3
Louisiana	5
Maine	2
Maryland	5
Massachusetts	9
Michigan	5
Minnesota	2
Mississippi	1
Missouri	7
Montana	1
Nebraska	1
Nevada	3
New Hampshire	2
New Jersey	12
New Mexico	1
New York	13
North Carolina	9
Ohio	10
Oklahoma	2
Oregon	3
Pennsylvania	11
Puerto Rico	1
Rhode Island	1
South Carolina	3
Tennessee	5
Texas	24
Utah	3
Virginia	10
Washington	6

West Virginia	1
Wisconsin	5

20

Canadian Province	Number of Stores
Alberta	3
British Columbia	3
Manitoba	1
Nova Scotia	1
Ontario	10
Quebec	3
Saskatchewan	1
United Kingdom	
England	44
Scotland	6
Wales	1
Northern Ireland	1
Ireland	2

Non-Store Properties

In addition to leasing all of our store locations, we lease approximately 59,000 square feet for our corporate headquarters, or World Bearquarters, in St. Louis, Missouri. Our World Bearquarters houses our corporate staff, our call center and our on-site training facilities. The lease was amended, effective January 1, 2008 with a five-year term, and may be extended for two additional five-year terms. In September 2006, we completed construction of a company-owned warehouse and distribution center, or Bearhouse, in Groveport, Ohio. The facility is approximately 350,000 square feet. In 2007, our web fulfillment site moved to the Bearhouse.

In the United Kingdom, we lease approximately 2,000 square feet for our regional headquarters in Windsor, England. The lease commenced in August 2003. The lease can be terminated at any time by either party giving notice of termination six months prior to cancellation.

ITEM 3. LEGAL PROCEEDINGS

From time to time we are involved in ordinary routine litigation typical for companies engaged in our line of business. We are involved in several court actions seeking to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. As of the date of this Annual Report on Form 10-K, we are not involved in any pending legal proceedings that we believe would be likely, individually or in the aggregate, to have a material adverse effect on our financial condition or results of operations.

ITEM 4. RESERVED

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is listed on the New York Stock Exchange (NYSE) under the symbol "BBW." Our common stock commenced trading on the NYSE on October 28, 2004. The following table sets forth the high and low sale prices of our common stock for the periods indicated.

	Fiscal 2010		Fiscal 2009	
	High	Low	High	Low
First Quarter	$ 7.43	$ 4.50	$ 6.65	$ 3.34
Second Quarter	$ 9.76	$ 6.37	$ 7.27	$ 4.05
Third Quarter	$ 7.45	$ 4.85	$ 5.62	$ 4.12
Fourth Quarter	$ 9.24	$ 5.54	$ 6.78	$ 4.45

As of March 15, 2011, the number of holders of record of the Company's common stock totaled approximately 2,739.

PERFORMANCE GRAPH

The following performance graph compares the 50-month cumulative total stockholder return of our common stock, with the cumulative total return on the Russell 2000® Index and an SEC-defined peer group of companies identified as SIC Code 5600-5699 (the "Peer Group"). The Peer Group consists of companies whose primary business is the operation of apparel and accessory retail stores. Build-A-Bear Workshop is not strictly a merchandise retailer and there is a strong interactive, entertainment component to our business which differentiates it from retailers in the Peer Group. However, in the absence of any other readily identifiable peer group, we believe the use of the Peer Group is appropriate.

The performance graph starts on January 1, 2006 and ends on December 31, 2010, the last trading day prior to January 1, 2011, the end of our fiscal 2010. The graph assumes that $100 was invested on January 1, 2006 in each of our common stock, the Russell 2000 Index and the Peer Group, and that all dividends were reinvested.

These indices are included only for comparative purposes as required by Securities and Exchange Commission rules and do not necessarily reflect management's opinion that such indices are an appropriate measure of the relative performance of the common stock. They are not intended to forecast the possible future performance of our common stock.

ISSUER PURCHASES OF EQUITY SECURITIES

Period	(a) Total Number of Shares (or Units) Purchased (1)	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (2)	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs (2)
Oct. 3, 2010 – Oct. 30, 2010	764	$6.34	-	$ 23,714,009
Oct. 31, 2010 – Nov. 27, 2010	-	$-	-	$ 23,714,009
Nov. 28 2010 – Jan. 1, 2011	109	$7.45	-	$ 23,714,009
Total	873	$6.47	-	$ 23,714,009

(1) Includes shares of our common stock delivered to us in satisfaction of the tax withholding obligation of holders of restricted shares which vested during the quarter. Our equity incentive plans provide that the value of shares delivered to us to pay the withheld to cover tax obligations is calculated as the closing trading price of our common stock on the date the relevant transaction occurs.

(2) On March 2, 2011, we announced the further extension of our $50 million share repurchase program of our outstanding common stock until March 31, 2012. The program was authorized by our board of directors. Purchases may be made in the open market or in privately negotiated transactions, with the level and timing of activity depending on market conditions, applicable regulatory requirements, and other factors. Purchase activity may be increased, decreased or discontinued at any time without notice. Shares purchased under the program are subsequently retired. As of March 15, 2011, we had $21.2 million of availability under the program.

Recent Sales of Unregistered Securities

There were no sales of unregistered securities during the fourth quarter of fiscal 2010.

Dividend Policy

We anticipate that we will retain any future earnings to support operations, to finance the growth and development of our business and to repurchase shares of our common stock from time to time and we do not expect, at this time, to pay cash dividends in the future. Any future determination relating to our dividend policy will be made at the discretion of our board of directors and will depend on a number of factors, including future earnings, capital requirements, financial conditions, future prospects and other factors that the board of directors may deem relevant. Additionally, under our credit agreement, we are prohibited from declaring dividends without the prior consent of our lender, subject to certain exceptions, as described in “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources.”

ITEM 6. SELECTED FINANCIAL DATA

Throughout this Annual Report on Form 10-K, we refer to our fiscal years ended January 1, 2011, January 2, 2010, January 3, 2009, December 29, 2007 and December 30, 2006, as fiscal years 2010, 2009, 2008, 2007 and 2006, respectively. Our fiscal year consists of 52 or 53 weeks, and ends on the Saturday nearest December 31 in each year. Fiscal years 2010, 2009, 2007 and 2006 included 52 weeks and fiscal year 2008 included 53 weeks. All of our fiscal quarters presented in this Annual Report on Form 10-K included 13 weeks, with the exception of the fourth quarter of fiscal 2008 which included 14 weeks. When we refer to our fiscal quarters, or any three month period ending as of a specified date, we are referring to the 13-week or 14-week period prior to that date.

The following table sets forth, for the periods and dates indicated, our selected consolidated financial and operating data. The balance sheet data as of January 1, 2011 and January 2, 2010 and the statement of operations and other financial data for our fiscal years ended January 1, 2011, January 2, 2010 and January 3, 2009 are derived from our audited financial statements included elsewhere in this Annual Report on Form 10-K. The balance sheet data as of January 3, 2009, December 29, 2007 and December 30, 2006, and the statement of income and other financial data for our fiscal years ended December 29, 2007 and December 30, 2006 are derived from our audited consolidated financial statements that are not included in this Annual Report on Form 10-K. You should read our selected consolidated financial and operating data in conjunction with our consolidated financial statements and related notes and with "Management's Discussion and Analysis of Financial Condition and Results of Operations" appearing elsewhere in this Annual Report on Form 10-K.

	Fiscal Year				
	2010	2009	2008	2007	2006
	(Dollars in thousands, except share, per share, per store and per gross square foot data)				
Statement of income data:					
Total revenues	$401,452	$395,906	$468,316	$475,360	$437,462
Costs and expenses:					
Cost of merchandise sold	239,556	247,511	270,918	260,077	227,899
Selling, general and administrative	163,910	161,692	185,608	177,375	158,712
Store preopening	708	90	2,410	4,416	3,958
Store closing	-	981	2,952	-	-
Losses from investment in affiliate	-	9,615	-	-	-
Interest expense (income), net	(250)	(143)	(799)	(1,531)	(1,530)
Total costs and expenses	403,924	419,746	461,089	440,337	389,039
Income (loss) before income taxes	(2,472)	(23,840)	7,227	35,023	48,423
Income tax expense (benefit)	(2,576)	(11,367)	2,663	12,514	18,933
Net income (loss)	$104	$(12,473)	$4,564	$22,509	$29,490
Earnings (loss) per common share:					
Basic	$0.01	$(0.66)	$0.24	$1.11	$1.46
Diluted	$0.01	$(0.66)	$0.24	$1.10	$1.44
Shares used in computing common per share amounts:					
Basic	18,601,465	18,874,352	19,153,123	20,256,847	20,169,814
Diluted	19,034,048	18,874,352	19,224,273	20,448,793	20,468,256

	Fiscal Year 2010	2009	2008	2007	2006
	(Dollars in thousands, except share, per share, per store and per gross square foot data)				
Other financial data:					
Retail gross margin ($) (1)	$155,128	$142,572	$190,500	$209,090	$205,063
Retail gross margin (%) (1)	40.1 %	36.7 %	41.3 %	44.7 %	47.4 %
Capital expenditures, net (2)	$14,649	$8,148	$23,215	$37,235	$54,036
Depreciation and amortization	26,976	28,487	28,883	26,292	22,394
Cash flow data:					
Cash flows provided by operating activities	$22,021	$23,990	$23,615	$56,374	$53,035
Cash flows used in investing activities	(13,766)	(8,898)	(26,629)	(40,938)	(93,772)
Cash flows provided by (used in) financing activities	(7,216)	-	(14,024)	(3,052)	3,537
Store data (3):					
Number of stores at end of period					
North America	290	291	292	272	233
Europe	54	54	54	49	38
Total stores	344	345	346	321	271
Square footage at end of period					
North America	841,600	846,373	856,504	810,208	712,299
Europe (4)	77,870	77,520	77,520	70,577	56,701
Total square footage	919,470	923,893	934,024	880,785	769,000
Average net retail sales per store (5) (6)	$1,030	$1,044	$1,329	$1,576	$1,761
Net retail sales per gross square foot - North America (6) (7)	$356	$358	$445	$516	$573
Consolidated comparable store sales change (%) (8)	(2.0)%	(13.4)%	(14.0)%	(9.9)%	(6.5)%
Balance sheet data:					
Cash and cash equivalents	$58,755	$60,399	$47,000	$66,261	$53,109
Working capital	51,671	53,865	38,880	40,090	28,731
Total assets	275,794	284,273	300,152	339,531	305,170
Total stockholders' equity	157,713	164,780	167,725	193,608	170,443

(1) Retail gross margin represents net retail sales less cost of retail merchandise sold, which excludes cost of wholesale merchandise sold. Retail gross margin percentage represents retail gross margin divided by net retail sales.

(2) Capital expenditures, net consist of leasehold improvements, furniture and fixtures, land, buildings, computer equipment and software purchases, as well as trademarks, intellectual property, key money deposits and deferred leasing fees.

(3) Excludes our webstore and pop-up, seasonal and event-based locations.

(4) Square footage for stores located in Europe is estimated selling square footage and includes stores in the United Kingdom, Ireland and France.

(5) Average net retail sales per store represents net retail sales from stores open throughout the entire period in North America divided by the total number of such stores.

(6) When we refer to average net retail sales per store and net retail sales per gross square foot for any period, we include in those calculations only those stores that have been open for that entire period in North America. European stores are not included.

(7) Net retail sales per gross square foot represents net retail sales from stores open throughout the entire period in North America divided by the total gross square footage of such stores. European stores are not included.

(8) Comparable store sales percentage changes are based on net retail sales and stores are considered comparable beginning in their thirteenth full month of operation. Fiscal 2008 first quarter was the first quarter that our European operations met the criteria for inclusion in our comparable store calculation. As such, fiscal 2008 is the first period to include comparable store sales change for Europe in the consolidated comparable store sales change.

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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from the results discussed in the forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in "Risk Factors" and elsewhere in this Annual Report on Form 10-K. The following section is qualified in its entirety by the more detailed information, including our financial statements and the notes thereto, which appears elsewhere in this Annual Report on Form 10-K.

Overview

We are the leading, and only international, company providing a "make your own stuffed animal" interactive entertainment experience under the Build-A-Bear Workshop brand, in which our guests stuff, fluff, dress, accessorize and name their own teddy bears and other stuffed animals. Our concept, which we developed for mall-based retailing, capitalizes on what we believe is the relatively untapped demand for experience-based shopping as well as the widespread appeal of stuffed animals. The Build-A-Bear Workshop experience appeals to a broad range of age groups and demographics, including children, teens, their parents and grandparents. As of January 1, 2011, we operated 290 stores in the United States, Canada and Puerto Rico, 52 stores in the United Kingdom and two stores in Ireland, and had 63 franchised stores operating in international locations under the Build-A-Bear Workshop brand. In addition to our stores, we sell our products on our e-commerce Web site, buildabear.com and market our products and build our brand through our "virtual world" Web site, bearville.com, which complements our interactive shopping experience and positively enhances our core brand value. We also operate non-traditional store locations in Major League Baseball ballparks, 11 temporary pop-up locations, one location in a zoo and one location in a science center.

On April 2, 2006, we acquired all of the outstanding shares of The Bear Factory Limited, a stuffed animal retailer in the United Kingdom, and Amsbra Limited, our former United Kingdom franchisee. The results of the acquisitions' operations have been included in the consolidated financial statements since that date. We are currently operating 36 of the acquired stores, having permanently closed four locations during transition. Since 2006, our European operations have grown to 54 stores. We have improved sales performance and adopted internal best practices in the areas of merchandising, marketing, purchasing and store operations, across the acquired store base that resulted in improved sales and earnings from the acquisition.

We operate in three segments that share the same infrastructure, including management, systems, merchandising and marketing, and generate revenues as follows:

- Company-owned retail stores located in the United States, Canada, Puerto Rico, the United Kingdom and Ireland, a webstore and seasonal, event-based locations;
- International stores operated under franchise agreements; and
- Transactions with other business partners, mainly comprised of licensing our intellectual property, including entertainment properties, for third-party use and wholesale product sales.

Selected financial data attributable to each segment for fiscal 2010, 2009 and 2008, are set forth in Note 19 to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K.

For a discussion of the key trends and uncertainties that have affected our revenues, income and liquidity, see the "— Revenues," "— Costs and Expenses" and "— Expansion and Growth Potential" subsections of this Overview.

We believe that we have developed an appealing retail store concept that, for North American stores open for the entire year, averaged $1.0 million in fiscal 2010 and fiscal 2009 and $1.3 million in fiscal 2008 in net retail sales per store. For a discussion of the changes in comparable store sales in fiscal years 2010, 2009 and 2008, see "— Revenues" below. Store contribution, which consists of income (loss) before income tax expense (benefit); interest; store depreciation, amortization and impairment; store preopening expense; store closing expense; losses from investment in affiliate and general and administrative expense, excluding franchise fees, income from commercial activities and contribution from our webstore, pop-ups and seasonal event-based locations, as a percentage of net retail sales, excluding revenue from our webstore, pop-ups and seasonal and event-based locations, was 15.3% for fiscal 2010,12.4% for fiscal 2009 and 16.0% for fiscal 2008. Total company net income as a percentage of total revenues was 0.0% for fiscal 2010 and 1.0% for fiscal 2008. Total company net loss as a percentage of total revenues was 3.2% for fiscal 2009. See "— Non-GAAP Financial Measures" for a reconciliation of store contribution to net income. Net income increased in 2010 due to stable store sales trends, continued cost reductions, improvements in margin and leverage of fixed costs. Additionally, certain non-cash charges included in 2009 did not recur, or were significantly lower in 2010. Net income declined in 2009 and 2008 due primarily to the decrease in comparable store sales and in 2009 due to the impact of certain non-cash charges. In 2009 and 2008, merchandise margin improvement was more than offset by fixed occupancy cost deleverage due primarily to the decrease in comparable store sales.

In 2008, 2009 and 2010, our results reflect the challenging retail environment – economic recession, declining mall traffic, and slowing consumer spending – factors impacting many retailers and particularly our company given the discretionary nature of our products and our experience. In 2010, our store contribution increased, primarily due to a significant decrease in store asset impairment charges as compared to 2009 as well as improvements in margin and leverage of fixed store costs. In 2009 and 2008, our total store contribution declined, primarily due to 13.4% and 14.0% decreases in comparable store sales, respectively. This decrease in total store contribution was partially offset by approximately $25 million in cost reductions in North America in 2009.

Our 2011 plan balances our long term business goals while recognizing the continuing challenges of the retail environment. While we believe our market potential in North America remains more than 350 stores, we will open two new stores in North America in 2011, compared to one in 2010, excluding temporary pop-up locations. In the United Kingdom and Ireland, we believe our market potential is approximately 70 locations and we plan to open three new stores in 2011, the same as in 2010. This slower pace of new store growth allows us to focus on our business and align all operations around our goals of new guest acquisition and guest retention aimed at improving our comparable stores sales performance, while also building our long term brand value. Our growth strategy is to develop and expand the reach of the Build-A-Bear Workshop brand through product innovation and the full integration of product, marketing and operations to create a sense of urgency to shop, thereby increasing store traffic, increasing conversion and improving sales. We will continue to look for opportunities to add other toy products outside of our core plush animals, yet consistent with our interactive and hands-on experience when we see an opportunity to drive incremental purchases. We plan to continue to improve our online and e-commerce business, as well as grow our virtual world engagement through bearville.com. We intend to refine our marketing programs balancing communication with new and existing guests and place emphasis on our product newness and collectibility, a fundamental strength of our brand. In 2009, we implemented cost reduction initiatives that resulted in approximately $25 million in pre-tax savings. We were able to maintain these savings in 2010. We ended fiscal 2010 with no borrowings under our bank loan agreement and with $59 million in cash and cash equivalents after investing $15 million in capital projects and $7 million in share repurchases. Our 2010 comparable store sales trend reflected a significant improvement over 2009, and we believe that our business strategies, strong store contribution model, strong cash flow and flexible capital structure will deliver long term sales and earnings growth.

Following is a description and discussion of the major components of our statement of operations:

Revenues

Net retail sales: Net retail sales are revenues from retail sales (including our webstore and other non-store locations), are net of discounts, exclude sales tax, include shipping and handling costs billed to customers, and are recognized at the time of sale. Revenues from gift cards are recognized at the time of redemption. Our guests use cash, checks, gift cards and third party credit cards to make purchases. We classify stores as new or comparable stores and do not include our webstore or seasonal, event-based locations in our store count or in our comparable store calculations. Stores enter the comparable store calculation in their thirteenth full month of operation and as such, European stores were not included for 2007. If a store relocation or remodel results in a significant change in square footage, the net retail sales for that location are excluded from comparable store sales calculations until the thirteenth full month of operation after the date of the change. In the fiscal 2008 third quarter, we announced plans to close the Friends 2B Made concept. By the end of fiscal 2009, all Friends 2B Made locations were closed. All but one of these locations were inside or adjacent to a Build-A-Bear Workshop store and shared common store management, employees and infrastructure. Other than one stand-alone store in Ontario, California, these locations were considered expansions of the existing Build-A-Bear Workshop store and were not considered an addition to our total store count. The net retail sales of these expanded Build-A-Bear Workshop stores were excluded from comparable store sales calculations until the thirteenth full month of operation after the date of the expansion as well as after the subsequent closure.

We have a loyalty program with a frequent shopper reward feature in North America, the Stuff Fur Stuff club, whereby guests enroll in the program and receive one point for every dollar or partial dollar spent and after reaching 100 points receive a $10 discount on a future purchase. On a quarterly basis, an estimate of the obligation related to the program, based on actual points and certificates outstanding and historical point conversion and certificate redemption pattern, is recorded as an adjustment to deferred revenue and net retail sales. At the time of redemption of the $10 discount, the deferred revenue obligation is reduced, and a corresponding amount is recognized in net retail sales. As the reward certificates can be earned or redeemed at any of our store locations, we account for changes in the deferred revenue account at the total company level only. Therefore, when we refer to net retail sales by location, such as comparable stores or new stores, these amounts do not include any changes in the deferred revenue amount. See “Critical Accounting Estimates” for additional details on the accounting for the deferred revenue program.

We use net retail sales per gross square foot and comparable store sales as performance measures for our business. The following table details net retail sales per gross square foot by age of store for the periods presented:

	Fiscal 2010	Fiscal 2009	Fiscal 2008
Net retail sales per gross square foot - North America (1) (2)			
Store Age > 5 years (194, 164 and 145 stores, respectively)	$370	$372	$448
Store Age 3-5 years (71, 62 and 54 stores respectively)	$321	$341	$455
Store Age <3 years (21, 59 and 73 stores, respectively)	$317	$333	$432
All comparable stores	$356	$358	$445

(1) Net retail sales per gross square foot represents net retail sales from North American stores open throughout the entire period divided by the total gross square footage of such stores. Calculated on an annual basis only.
(2) Excludes our webstore, pop-up and seasonal and event-based locations.

The percentage increase (or decrease) in comparable store sales for the periods presented below is as follows:

	Fiscal 2010	Fiscal 2009	Fiscal 2008
Comparable store sales change - North America (%) (1) (2)			
Store Age > 5 years (194, 164 and 145 stores, respectively)	(0.4)%	(15.1)%	(16.0)%
Store Age 3-5 years (71, 62 and 54 stores respectively)	(3.3)%	(17.7)%	(16.0)%
Store Age <3 years (21, 59 and 73 stores, respectively)	(3.8)%	(22.2)%	(20.2)%
Total comparable store sales change	(1.2)%	(16.7)%	(16.8)%
Comparable store sales change - Europe (%) (1) (2)	(5.5)%	5.0 %	7.7 %
Comparable store sales change - Consolidated (%) (1) (2)	(2.0)%	(13.4)%	(14.0)%

(1) Comparable store sales percentage changes are based on net retail sales and stores are considered comparable beginning in their thirteenth full month of operation.
(2) Excludes our webstore, pop-up and seasonal and event-based locations.

Our older stores consistently perform the best on both a sales per square foot and a comparable store sales basis.

Fiscal 2010 consolidated comparable store sales decreased by 2.0%, including a 5.5% decrease in Europe and a 1.2% decrease in North America (full year comparable store sales are compared to the 52 week period ended Jan. 2, 2010). We believe the decline in consolidated comparable store sales was attributed primarily to the following factors:

- the continuing impact of the economic recession and resulting pullback in consumer spending impacted our comparable store sales particularly in Europe. While these factors impact many retailers, we believe that they impact our comparable store sales particularly given the discretionary nature of our products and our experience.

- We believe that our product selection and improved integration of product marketing and store operations positively impacted our North American comparable store sales trend in 2010 by improving our average transaction value.

Fiscal 2009 consolidated comparable store sales decreased by 13.4%, including a 5.0% increase in Europe and a 16.7% decline in North America (full year comparable store sales are compared to the 52 week period ended Jan. 3, 2009). We believe the decline in consolidated comparable store sales was attributed primarily to the following factors:

- the economic recession and dramatic decrease in consumer sentiment resulted in a pullback in consumer spending and impacted our comparable store sales; and
- the slowdown in North America shopping mall customer traffic during fiscal 2009 compared to fiscal 2008 impacted the number of new and returning guests visiting our stores and therefore our comparable store sales. The comparable store sales decline included both a decrease in the number of transactions and a decrease in the average transaction value.

Commercial revenue: Commercial revenue, formerly referred to as licensing revenue, includes the company's transactions with other businesses, mainly through wholesale and licensing transactions. Revenue from licensing activities is generally based on a percentage of sales made by licensees to third parties and is recognized at the time the product is shipped by the licensee or at the point of sale. We have entered into a number of licensing arrangements whereby third parties manufacture and sell to other retailers merchandise carrying the Build-A-Bear Workshop trademark. Historically, revenue from wholesale product sales included revenue from merchandise sold at stores operated by Landry's restaurants. In 2010, it also includes two transactions totaling $6.4 million with no associated gross margin.

Franchise fees: We receive an initial, one-time franchise fee for each master franchise agreement which is amortized to revenue over the life of the respective franchise agreements, which extend for periods up to 25 years. Master franchise rights are typically granted to a franchisee for an entire country or countries. Continuing franchise fees are based on a percentage of sales made by the franchisees' stores and are recognized as revenue at the time of those sales.

As of January 1, 2011, we had 63 stores, including 10 opened and 12 closed in fiscal 2010, operating under franchise arrangements in the following countries:

Japan	9
South Africa	9
Denmark	9
Australia	9
Germany	8
Thailand	5
Singapore	4
Norway	3
Gulf States(1)	3
Mexico	3
Sweden	1

(1) Gulf States agreement includes Kuwait, Bahrain, Qatar, Oman and the United Arab Emirates

Costs and Expenses

Cost of merchandise sold and retail gross margin: Cost of merchandise sold includes the cost of the merchandise, including royalties paid to licensors of third party branded merchandise; store occupancy cost, including store depreciation and store asset impairment charges; cost of warehousing and distribution; packaging; stuffing; damages and shortages; and shipping and handling costs incurred in shipment to customers. Retail gross margin is defined as net retail sales less the cost of retail merchandise sold, which excludes cost of wholesale merchandise sold.

Selling, general and administrative expense: These expenses include store payroll and benefits, advertising, credit card fees, and store supplies, as well as central office general and administrative expenses, including costs for virtual world maintenance, management payroll, benefits, stock-based compensation, travel, information systems, accounting, insurance, normal store closings, legal and public relations. These expenses also include depreciation and amortization of central office leasehold improvements, furniture, fixtures and equipment as well as the amortization of intellectual property costs.

Central office general and administrative expenses grew over time in order to support the increased number of stores in operation. In 2009, we achieved $22 million in savings in selling, general and administrative expenses including marketing, central office payroll and outside services. Advertising increased significantly with the introduction in fiscal 2004 of our national television and online advertising campaign. We decreased the level of advertising expense as a percentage of net retail sales in fiscal 2010 as compared to fiscal 2009 which was a decrease from fiscal 2008. We anticipate 2011 advertising expense to be consistent with 2010. Other store expenses such as credit card fees and supplies historically have increased or decreased proportionately with net retail sales.

We have share-based compensation plans covering the majority of our management groups and our Board of Directors. We account for share-based payments utilizing the fair value recognition provisions of Accounting Standards Codification (ASC) Section 718 – Stock Compensation. We recognize compensation cost for equity awards on a straight-line basis over the requisite service period for the entire award. In 2010, we recorded stock based compensation of approximately $4.8 million ($2.9 million net of tax). In 2009, we recorded stock-based compensation of approximately $4.3 million ($2.6 million net of taxes). In 2008, we recorded stock based compensation of $3.6 million ($2.2. million net of tax).

Store preopening: Preopening costs are expensed as incurred and include store set-up, certain labor and hiring costs, and rental charges incurred prior to a store's opening.

Store closing: Store closing costs include costs associated with the closure of our Friends 2B Made concept including, but not limited to, long-lived asset impairment, lease termination and other costs.

Losses from investment in affiliate. Equity losses from investment in affiliate are the result of the allocation of losses related to our investment in Ridemakerz, LLC. Ridemakerz, an early-stage company still in its start-up phase, has incurred substantial losses including charges resulting from a major restructuring of its operations that included store closings. Under the agreements in place in 2009, we were the sole member of an equity class that is allocated losses only following the allocation of losses to all other common and preferred equity holders to the extent of their capital contributions. All of the priority equity members' capital was reduced to zero in the fiscal 2009 second quarter. We continued to provide services to Ridemakerz in exchange for equity in 2010. The book value of our investment was $-0- at January 1, 2011 and January 2, 2010. These services will be significantly reduced in 2011.

Expansion and Growth Potential

Company-owned stores:

The number of Build-A-Bear Workshop stores in the United States, Canada, Puerto Rico, the United Kingdom, Ireland and France for the last three fiscal years can be summarized as follows:

	Fiscal 2010	Fiscal 2009	Fiscal 2008
Beginning of period	345	346	321
Opened	4	1	25
Closed	(5)	(2)	—
End of period	344	345	346

On April 2, 2006 we acquired all of the outstanding shares of The Bear Factory Limited, a stuffed animal retailer in the United Kingdom and Ireland, and Amsbra Limited, our former United Kingdom franchisee. We are currently operating 36 of the acquired stores, having permanently closed four locations during transition. We currently operate 52 stores in the United Kingdom and two stores in Ireland. In 2010, we closed our three stores in France.

The Friends 2B Made stores are not included in the number of store openings in fiscal 2009 or 2008 as noted above but rather are considered expansions of Build-A-Bear Workshop stores. In the fiscal 2008 third quarter, we announced plans to close the Friends 2B Made concept; concept closure was completed in the fiscal 2009 third quarter.

In fiscal 2010, we opened one Build-A-Bear Workshop store in North America, two in the United Kingdom and one in Ireland. In fiscal 2011, we anticipate opening two Build-A-Bear Workshop stores in North America and three in the United Kingdom. We believe there is a market potential for at least 350 Build-A-Bear Workshop stores in the United States, Puerto Rico and Canada and 70 stores in the United Kingdom and Ireland.

Non-store Locations:

In 2004 we began offering merchandise in seasonal, event-based locations such as Major League Baseball ballparks. We expect to expand our future presence at select seasonal and non-traditional locations contingent on their availability. As of January 1, 2011, we had a total of three ballpark locations. We opened our first store in a zoo during fiscal 2006 and our first store in a science center during fiscal 2007. In 2010, we opened our first pop-up stores. Pop-up stores are temporary locations that generally have lease terms of six to eighteen months and are excluded from our store count. These locations are intended to capitalize on short-term opportunities in specific locations. As of January 1, 2011, 11 pop-up stores were open.

Commercial Revenue:

In fiscal 2004, we began entering into license agreements pursuant to which we receive royalties on Build-A-Bear Workshop brand products. These agreements generated revenue of $2.8 million in 2010, $2.5 million in 2009 and $2.7 million in 2008. In addition to our normal wholesale business, in 2010, we had two wholesale transactions totaling $6.4 million with no gross margin. We anticipate entering into additional license and wholesale agreements in the future.

International Franchise Revenue:

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

	Fiscal 2010	Fiscal 2009	Fiscal 2008
Beginning of period	65	62	53
Opened	10	10	16
Closed	(12)	(7)	(7)
End of period	63	65	62

As of January 1, 2011, we had 12 master franchise agreements, which typically grant franchise rights for a particular country or group of countries, covering an aggregate of 16 countries. In the ordinary course of business, we anticipate signing additional master franchise agreements in the future and terminating other such agreements. We expect our current and future franchisees to open five to ten stores in fiscal 2011, net of closures. We believe there is a market potential for approximately 300 international stores outside of the United States, Canada, the United Kingdom and Ireland, which we expect to be operated primarily by new and existing franchisees.

Results of Operations

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

	Fiscal 2010	Fiscal 2009	Fiscal 2008
Revenues:			
Net retail sales	96.4 %	98.1 %	98.4 %
Commercial revenues	2.8	1.0	0.7
Franchise fees	0.8	0.8	0.9
Total revenues	100.0	100.0	100.0
Costs and expenses:			
Cost of merchandise sold (1)	60.1	63.1	58.4
Selling, general, and administrative	40.8	40.8	39.6
Store preopening	0.2	0.0	0.5
Store closing	-	0.2	0.6
Losses from investment in affiliate	-	2.4	-
Interest expense (income), net	(0.1)	(0.0)	(0.2)
Total costs and expenses	100.6	106.0	98.5
Income (loss) before income taxes	(0.6)	(6.0)	1.5
Income tax expense (benefit)	(0.6)	(2.9)	0.6
Net income (loss)	0.0	(3.2)	1.0
Retail gross margin (%) (2)	40.1 %	36.7 %	41.3 %

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

(2) Retail gross margin represents net retail sales less cost of retail merchandise sold, which excludes cost of wholesale merchandise sold. Retail gross margin was $155.1 million, $142.6 million and $190.5 million in 2010, 2009 and 2008, respectively. Retail gross margin percentage represents retail gross margin divided by net retail sales.

Fiscal Year Ended January 1, 2011 (52 weeks) Compared to Fiscal Year Ended January 2, 2010 (52 weeks)

Total revenues. Net retail sales decreased to $387.2 million for fiscal 2010 from $388.6 million for fiscal 2009, a decrease of $1.4 million, or 0.4%. Comparable store sales decreased $7.2 million in fiscal 2010, or 2.0% and sales from non-comparable locations decreased $2.1 million. Partially offsetting these decreases is an increase of $4.3 million related to the revenue deferral under our customer loyalty program. This year-end adjustment represented a refinement in the calculation used to estimate the liability that also took into account the change in member's redemption patterns experienced in 2010. This increase was partially offset by $1.9 million of revenue deferred throughout the year as estimated under the previous approach. Increases in net retail sales resulted from sales in new stores and increases in sales over the Internet of $2.4 million and $1.2 million, respectively. Other increases totaling $1.9 million came from sales at non-store locations which includes pop-up locations, other retail revenues and the impact of foreign currency exchange rates.

Commercial revenue, formerly referred to as licensing revenue, was $11.2 million in fiscal 2010 compared to $4.0 million in fiscal 2009. This increase was primarily due to $6.4 million in non-recurring wholesale transactions. Excluding these transactions, commercial revenues increased $0.8 million reflecting the introductionof Build-A-Bear Craftshop kits. Revenue from international franchise fees decreased to $3.0 million for fiscal 2010 from $3.4 million for fiscal 2009, a decrease of $0.4 million. This decrease was primarily due to continuing adverse global economic conditions.

Gross margin. Total gross margin, calculated as net retail sales and commercial revenues less cost of merchandise sold, increased to $158.9 million for fiscal 2010 from $145.0 million for fiscal 2009, an increase of $13.8 million, or 9.5%. Retail gross margin increased to $155.1 million in fiscal 2010 from $142.6 million in fiscal 2009, and increase of $12.6 million or 8.8%. As a percentage of net retail sales, retail gross margin increased to 40.1% for fiscal 2010 from 36.7% for fiscal 2009, an increase of 340 basis points as a percentage of net retail sales (bps). This improvement in margin was primarily attributable to a 110 basis point improvement resulting from the significant reduction in asset impairment charges in 2010 as compared 2009. Additionally, we achieved 100 basis points of improved leverage on fixed occupancy costs and a 70 basis point improvement in merchandise margin along with other improvements in distribution and purchasing.

Selling, general and administrative. Selling, general and administrative expenses were $163.9 million for fiscal 2010 as compared to $161.7 million for fiscal 2009, an increase of $2.2 million, or 1.4%. As a percentage of total revenues, selling, general and administrative expenses were 40.8% for fiscal 2010, the same as in 2009. The dollar increase was primarily attributable to $1.6 million in charges related to the closure of our stores in France and increases in corporate payroll costs primarily related to a bonus. These increases were partially offset by marketing savings and improved leverage on store salaries and other fixed overhead costs.

Store preopening. Store preopening expense was $0.7 million for fiscal 2010 as compared to $0.1 million for fiscal 2009. The increase was primarily due to opening four stores in fiscal 2010 as compared to one in 2009. These amounts include preopening rent expense of $0.1 million for 2010 and $9,000 for fiscal 2009. Preopening expenses include expenses for stores that have opened including temporary popup locations, as well as some expenses incurred for stores that will be opened at a later date.

Store closing. Store closing expenses of $1.0 million for fiscal 2009 related to the closure of the Friends 2B Made concept and consisted primarily of lease termination charges, inventory write-offs and construction costs incurred to reformat locations for return to the landlord.