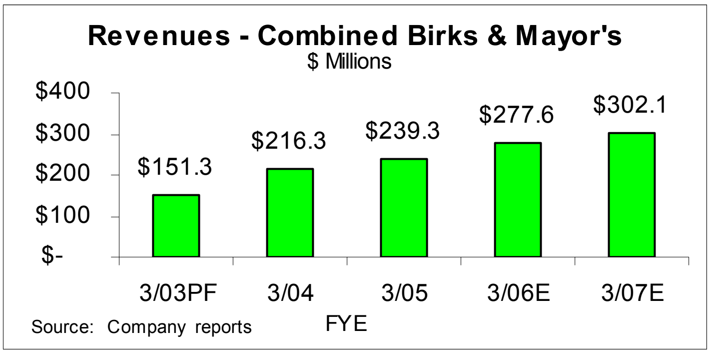
November 1, 2005

IDEX Online Research:
Birks + Mayor's: The Small Fish Swallows The Big Fish

By Ken Gassman

Jewelry industry consolidation continues. By the end of 2005, a new pan-American jewelry chain, Henry Birks & Sons, will exist, born of the merger of Florida-based Mayor's Jewelers and Quebec-based Birks Jewelers. This new retail jeweler will operate about 67 stores and is expected to post over $275 million in sales in the current fiscal year ending March 2006, making it the eighth largest jeweler in North America.



This is clearly the proverbial tale of the small fish – Birks with sales of about $97 million last year – acquiring Mayor's with 2004 sales of about $143 million.

Legal Filings & Sources: Notable Lack of Disclosure

IDEX Online Research culled over a thousand pages of legal filings of both Birks and Mayor's which detail not only historical information for Birks – previously a private company – but also provide projections for by division for the combined companies. In addition, we used our archives for further information. All financials have been converted into U.S. dollars.

Overall, we are disappointed in the lack of disclosure – particularly operational metrics – in the Securities & Exchange Commission documents. While most publicly held jewelers disclose metrics such as the average ticket, sales per store, and conversion rate trends as well as more detail – especially historical trends – of such items as sales by merchandise category, Mayor's/Birks either does not disclose such information or makes only cursory reference to it. Under the increased transparency requirements of Sarbanes-Oxley, we would think that there would be more disclosure rather than less.

The following is an analysis of relevant information, in our opinion.

Company Background

Montreal-based Henry Birks & Sons is a leading Canadian luxury retail jeweler which operates 39 luxury jewelry stores under the "Henry Birks & Sons" brand in all major cities across Canada. Most of Birks' jewelry is 18-karat gold, platinum or sterling silver, usually with precious gemstones, and with significant emphasis on quality craftsmanship and design.

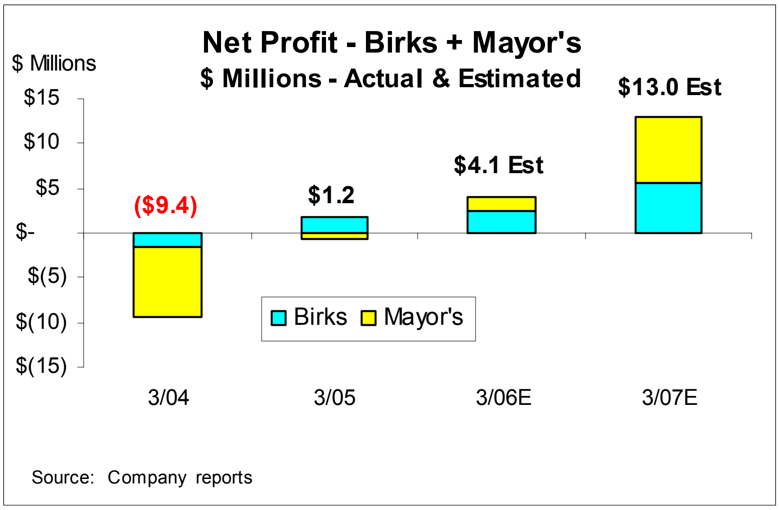
Birks' predecessor was founded in Montreal in 1879 and developed over the years into Canada's premier retailer, designer and manufacturer of fine jewelry, timepieces, sterling and plated silverware and gifts. At its peak, Birks operated over 250 stores. However, in the early 1990s, it encountered difficulties and was forced to close stores and file for bankruptcy. In 1993, Regaluxe Investments, headed by Dr. Lorenzo Rossi di Montelera (of the Martini & Rossi family), acquired Birks. In August 2002, Birks acquired approximately 72% of the voting control in Mayor's for an investment of $15 million. Since then, the operations of Birks and Mayor's have been progressively integrated. Birks is a Canadian corporation. Currently, Birks owns 75.8% of Mayor's.

Mayor's Jewelers operates 28 stores located in Florida and metropolitan Atlanta, Georgia. All of its jewelry products are constructed of 18-karat gold, platinum, or sterling silver, with or without precious gemstones, with significant emphasis on quality craftsmanship and design. Both Birks and Mayor's are known as "guild" jewelers.

Why Merge?

In a filing labeled "confidential" which IDEX Online Research obtained from the Securities & Exchange Commission, management listed 13 reasons for the merger. We believe these 13 reasons can be distilled to two key reasons:

- **Increase operational efficiencies to generate greater profits** – The merged companies – guild jewelers with a strong, loyal customer base – anticipate cross-selling opportunities, development and marketing of more comprehensive product offerings, co-branding, and consistent use of best practices. As the graph below illustrates, the merger should generate a significant increase in profits. If the merger generates profits as expected, the combined companies could post a net profit margin of 4.5%. That's about half of Tiffany's typical net profit, but it is about the same as Zale's net profit.



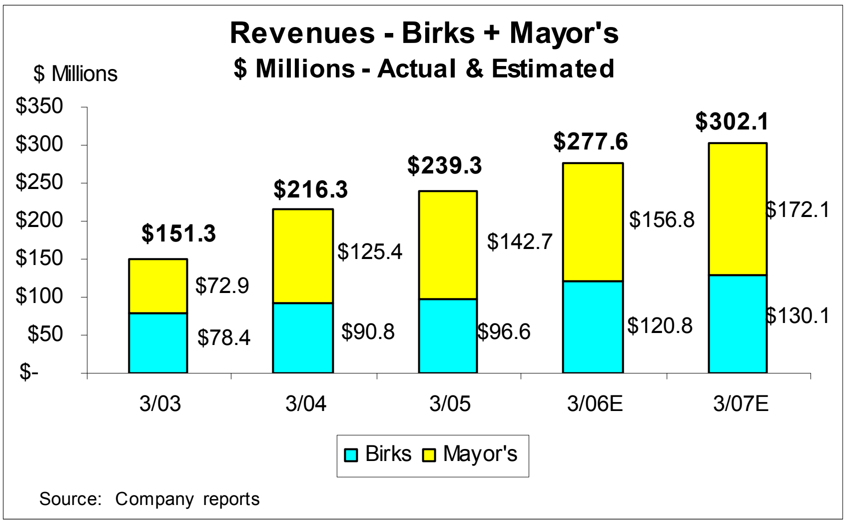
- **Back door way for Birks to become a public company** – In its legal filings, Birks cited this as its first reason for shareholders to support the merger, while citing the elimination of efficiencies as the second reason. We think that shareholders would be more interested in the elimination of inefficiencies to generate profits; hence, we've shown it as the first reason (above).

Birks/Mayor's cited only one "material" negative factor: Mayor's current public shareholders will receive shares of a foreign company. However, shares of the new company will be listed on the American Stock Exchange. Further, GAAP accounting in Canada is similar to GAAP accounting in the U.S.

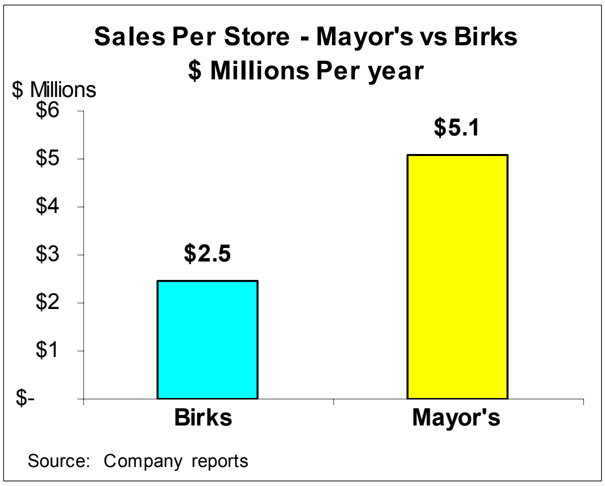
Birks + Mayor's: Making Sense of the Financials

Revenues

The merged companies should be capable of generating revenue growth in excess of 10% annually, with a majority of the growth coming from Mayor's, according to historical financials and company projections. This would place the combined companies' growth rate ahead of the growth rates of most other chain jewelers; further, this is a rate which is at least double our forecasted industry growth (U.S.) for the next several years. The graph below illustrates revenue growth by operating division as well as the combined companies.



As is clear from the graph, there is not a great disparity between total revenues for the Birks division (39 stores) versus the Mayor's division (28 stores). Further, the average size per store is about the same – 4,400 square feet for Mayor's and 4,600 square feet for Birks.



However, a "common denominator" analysis shows an entirely different story. For example, Birks average revenue per store is about $2.5 million; this is less than half of Mayor's sales per store of $5.1 million. Historically, Canadian jewelers' sales productivity per store has lagged U.S. retailers; as a result, Canadian jewelers must charge more for jewelry to generate a higher margin which will help offset lower inventory turn and inefficient store sales productivity. Americans may get a better deal when the buy pharmaceuticals in Canada, but Canadian consumers would do better to buy their jewelry in America.

Further, comparing sales productivity on a per square foot basis, Birks' productivity is less than half of Mayor's. Most jewelers measure sales productivity on the basis of "linear running feet of display" in their stores. Unfortunately, neither Mayor's nor Birks discloses enough information for us to make this comparison and analysis.

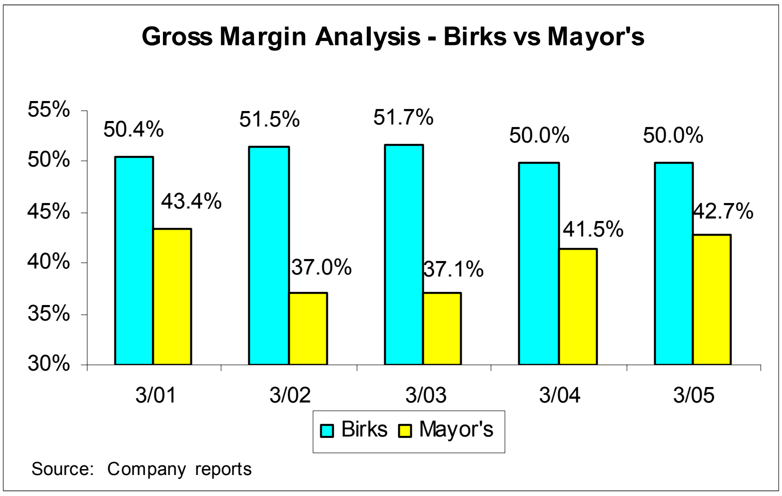
In terms of the average ticket, neither Mayor's nor Birks discloses this basic information. We believe it is probably above $1,000 for Mayor's; it may be less for Birks. In 1999, Mayor's average ticket was $1,189; it should be above this level now.

Management's comments about sales include the following:

- 2004 sales were driven by better economies in both Canada and the U.S.
- Target marketing coupled with improved product offerings helped drive demand.
- SARS and mad cow disease scares hurt demand in the Canadian stores in 2003.
- Mayor's disastrous financials in 2002 (sales of $161 million pro-forma and a loss $84 million) were the result of management turmoil prior to Birks' acquisition of the division in August 2002.
- Currency fluctuations have also had a modest impact on reported results.

Gross Margin

Birks' gross margin is higher than Mayor's gross margin. In part this is due to the product mix; in part, this is due to the necessity of achieving a higher margin to offset the lack of sales productivity and slow inventory turns. We believe that both companies are calculating gross margins using similar definitions, but there was not enough disclosure to confirm this.



Several factors have affected the company's historical gross margin.
An increased mix of exclusive merchandise has generated an improved gross margin in recent periods for both Birks and Mayor's. This will be the primary factor fueling the gross margin increase over the next two years, in our opinion.

- Mayor's has successfully implemented new merchandising strategies and marketing programs which have fueled its gross margin improvement. We expect Birks to implement many of these strategies as it attempts to build sales productivity.
- Promotional activities have affected Mayor's gross margin over the past couple of years. The company has liquidated obsolete merchandise at discounted prices to generate "open-to-buy" cash for new merchandise.
- Currency fluctuations have had a modest impact on gross profit levels; as a result, the gross margin has also been affected.

Operating Expenses

As one would expect, Mayor's operates with a lower cost structure than Birks. This is largely because of sales leverage on relatively fixed costs. Factors which affect Birks and Mayor's operating cost ratio include the following:

- A major restructuring at Mayor's has helped bring operating costs in line.
- Solid same-store sales leverage at Mayor's has helped improve the operating cost ratio.
- Weak same-store sales in the Birks division have had a negative impact on the operating cost ratio.
- Management cited health care costs as having a material impact on operating costs. However, this was a positive; management reduced its actuarial-based health care accruals. We hope this doesn't backfire later.
- Expanded marketing efforts have been costly, especially at Mayor's.
- Accounting for certain non-cash financial transactions – warrant value fluctuations related to compensation, for example – have had a material impact on operating costs. Further, the expense associated with restatement of Mayor's financials has been costly.
- Unusual costs associated with Birks' investment in Mayor's and the subsequent expenses associated with the planned merger have hurt the operating cost ratio.
- Currency fluctuations have had a modest impact on operating costs.

Balance Sheet

All stores and other facilities (headquarters and manufacturing operations) are leased. The company owns no significant real estate. The company has a gold hedge in place, but it is unclear how much of its gold purchases are covered by this hedge. It appears that the company does not lease gold. Consignment inventory typically represents 15-20% of total inventories (owned + memo).

Off-Balance Sheet Arrangements

Birks' only off-balance sheet arrangements are letters of credit issued under Mayor's credit facilities primarily to Wells Fargo. These LCs appear to be routine.

Birks + Mayor's: Merging Cultures & Customers

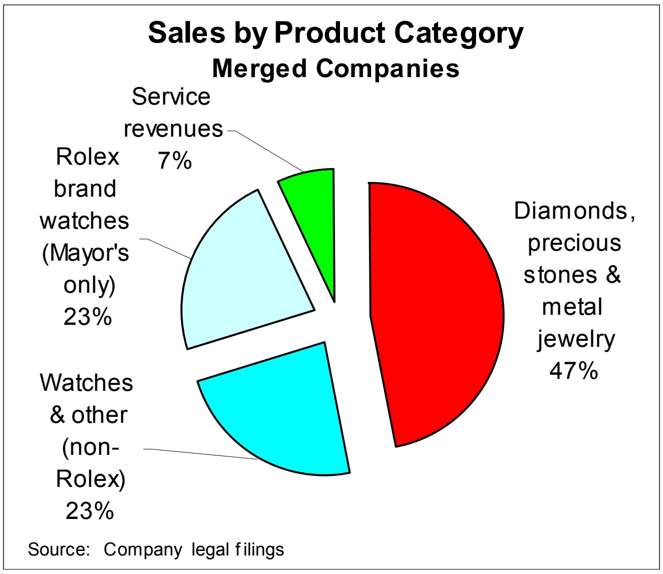
Birks' Corporate Strategy

Birks believes the following are key drivers of its business:

- To execute a merchandising strategy to increase net sales and expand gross margin in existing stores by designing, developing, manufacturing, and marketing higher margin exclusive and unique products.
- To execute a marketing strategy to increase customer awareness of its brands – Mayor's and Birks – and to increase customer traffic and net sales through regional and national advertising.
- To leverage its association with prestige institutions, such as the Royal Ontario Museum.
- To provide outstanding customer service to increase the average ticket and increase the number of shopping trips customers make to its stores.
- To rationalize and integrate the U.S. and Canadian operations by reducing costs and improving operations through best practices.
- To expand distribution through new store openings in existing and new markets.

Products & Merchandising

While disclosures about the company's sales by category are not detailed, the following information is available for the most recent fiscal year.



- Birks' Canadian stores carry a large selection of brand name watches, including its own proprietary watch line as well as watches made by Cartier, Baume & Mercier, Omega, Tag Heuer, Breitling, Jaeger Le Coultre, Gucci, Concorde, Rado, Longines, Mont Blanc, Lockman and Tissot. Birks also carries an exclusive collection of high quality jewelry and watches that it manufactures. Birks emphasizes its own jewelry offerings and particularly its signature designers, Toni Cavelti, Michele della Valle and Esty. Birks also sells designer jewelry by Roberto Coin, Kwiat, Ladyheart, which are exclusive to Birks stores in Canada, and carries a variety of high quality giftware, including writing instruments and giftware made by Mont Blanc.

- Birks' U.S. stores (Mayor's Jewelers) carry a large selection of brand name watches, including Rolex, Cartier, Patek Philippe, Baume & Mercier, Omega, Charriol, Tag Heuer, Breitling, Locman, Corum, Rado, Chopard, Jaeger Le Coultre and Raymond Weil. Designer jewelry offerings in Mayors include jewelry made by David Yurman, Aaron Basha, Charriol, Roberto Coin and DiModolo and a variety of high quality giftware, including writing instruments and giftware made by Correia and Mont Blanc. In addition, Mayor's stores carry Birks brand watches and jewelry products on an exclusive basis in the United States.
- Birks / Mayor's has two primary channels of distribution: the retail sale division, which accounts for 96.6% of sales, and the corporate sales division, which accounts for 3.4% of sales. It also operates secondary distribution channels such as direct marketing and internet sales.

Who Are The Major Suppliers?

Rolex is the company's largest and most important vendor. Rolex revenues represented 38% of Mayor's sales last year. Rolex is known in the industry as a temperamental supplier: keep them happy or you will lose the line. Rolex has tremendous brand recognition and loyalty. It is truly a driver of demand for jewelers who are lucky enough to have it. Rolex is sold only through Mayor's stores; Birks stores do not have access to Rolex. If Rolex terminated Mayor's, it would have a material negative impact on the merged company's sales and profits.

In August, 2002, Birks entered into a diamond inventory supply agreement with Prime Investments to supply Birks with at least 45%, on an annualized cost basis, of its loose diamonds, with certain conditions. Last year, Birks purchased about $4.1 million of diamonds, or 27% of its total diamond purchases, from Prime Investments and related parties. During the prior year, Birks purchased about $1.9 million of diamonds, or 18% of its total diamond purchases, from Prime Investments. In addition, Birks purchased approximately $1.9 million of finished goods from Prime Investments last year. Prime Investments has an ownership position in Birks.

Manufacturing Operations

Birks / Mayor's has manufacturing facilities in Montreal, Vancouver, Rhode Island and Florida. The Montreal facility is the largest of Birks' manufacturing facilities and is involved in all aspects of manufacturing fine jewelry with the exception of the cutting of rough diamonds and other precious stones. Its focus is on manufacturing stone set jewelry. The Rhode Island factory produces silver and gold jewelry as well as stone-set jewelry, while each of the Vancouver and Florida facilities focus on specific types of stone-set jewelry.

New Stores & Acquisitions

Other than a replacement store which will open this year, the company is largely silent about projected new store openings. We believe that the level of total revenue gains will require new store openings, as management cited in its strategy. However, while most jewelers disclose projected new store openings and signed leases, Birks did not.

Birks says it may pursue strategic acquisitions to enhance its market penetration and increase its revenue base.

Credit Operations

Birks uses credit to drive sales, both to consumers and in its corporate sales division. Both Birks (Canada) and Mayor's have a private label credit card administered by a third party. Birks (Canada) has some recourse exposure, while Mayor's agreement with Wells Fargo is without recourse. In addition, Mayor's also has a private label credit card which is administered internally. The credit staff makes all credit decisions; store personnel are not authorized to grant credit.

In the Mayor's division, proprietary credit sales were 27% of total sales last year. This is below the U.S. industry average of 45-47%. However, luxury jewelers tend to have a lower credit sales ratio.

Birks + Mayor's: Making Sense of the Legalese

Restatement of Financials

- During the financial reporting process associated with Mayor's third fiscal quarter 2004, Mayor's determined that errors had occurred in its accounting treatment of warrants that were issued by Mayor's to Birks in connection with Birks' acquisition of a controlling interest in Mayor's.
- Mayor's also determined that it should reconsider the allocation of the fair value of the equity investment between its preferred stock and the warrants issued to Birks.

- During the past year, Birks' management and its public accounting firm identified two "material weaknesses" in its internal financial reporting controls.
    - Certain automated reporting systems and manual processes were ineffective. The reconciliation of the accounts payable and inventory accounting sub-systems to the general ledger failed to appropriately capture all of the reconciling items.
    - Birks internal control over accounting for certain transactions related to U.S. GAAP were ineffective, due to a lack of accounting personnel with adequate U.S. accounting knowledge and experience. For example, proper inventory valuation is an issue, though it appears to be very minor. Accrued expenses, such as legal costs, do not have adequate documentation, though it appears that all costs were recorded properly. Other examples, which we consider relatively minor, also exist.
    - Birks' internal controls over the estimation of the warranty reserves did not provide an effective process to evaluate those reserves
- The U.S. Securities & Exchange Commission has notified that it is conducting an informal inquiry. No further details are available.

In our opinion, these restatements arose from non-material circumstances. Further, we believe that the SEC inquiry is unlikely related to material issues. However, due to Sarbanes-Oxley, seemingly minor issues have become major issues.

Mayor's Restated Financials

	FYE March 2005	
$ Mil	Reported	Revised
Sales	$ 142.7	$ 142.7
Gross Profit	$ 61.0	$ 61.0
Operating Expenses	$ 55.7	$ 55.8
Net Income	$ 0.8	$ 0.7
Total Assets	$ 102.8	$ 102.8

The table at right illustrates the magnitude of the restated financials. Only operating expenses were affected, and the amount was about $100,000 or less that 0.2% of total revenues. The balance sheet was unchanged, except for a very modest reallocation in the equity account.

Shareholder Information

In the merger, each share of your Mayor's common stock will be converted into the right to receive 0.08695 Class A voting shares of Birks.

- For example, if you own 100 shares of Mayor's common stock, you will receive 8 Birks Class A voting shares plus a cash payment for the fractional shares based on the recent average price of MYR shares.
- The exchange of stock should be tax-free for both U.S. and Canadian shareholders.

Birks will apply for listing of Class A shares on American Stock Exchange.

Upon completion of the merger, Dr. Rossi will beneficially own or control 70.3% of all classes of Birks outstanding voting shares while controlling 95.7% of the voting power associated with such shares. Dr. Rossi, as holder of Class B multiple voting shares, will have the ability to control most actions requiring shareholder approval, including electing the members of Birks' board of directors and the issuance of new equity.

Chronology: Mayor's Jewelers

In 1910, Samuel Mayor Getz opened his first jewelry store – called Mayor's Jewelers – in Cincinnati, Ohio. In 1937, Getz moved south and opened the first Florida Mayor's store in the heart of downtown Miami. Sam Getz's son, Irving, who joined the company in 1946, is credited with providing the vision for growth. In 1947, Irving Getz took control of the company. Irving's son, Samuel A. Getz, joined the company full time in 1980.

In 1994, Mayor's merged with Maier & Berkele, a five-store luxury jewelry chain in Atlanta. Maier & Berkele had been founded in the late 1800s. In 2001, the Maier & Berkele stores changed their name to Mayor's.

In the decade of the 1990s, Mayor's tried to float a public equity offering twice, but was unsuccessful both times. Sam Getz, grandson of the founder, was running the company when it was acquired by Jan Bell Marketing in July 1998. At that time, Mayor's operated 24 stores generating $142.2 million in sales, or $5.925 million per store. Sam Getz was still associated with the company, though Isaac Arguetty, Jan Bell's chairman, became chairman of the merged companies.

Jan Bell Takes Over

Jan Bell bought Mayors' because Jan Bell's leased department arrangement with Sam's Club (Wal-Mart) was ending at the end of January 2001. Sam's notified Jan Bell in April 1999 that its leased department arrangement would not be extended beyond February 1, 2001.

In a "road show" for investors in 1999, Jan Bell management made a presentation in which they repeated the phrase, both verbally and in slides, that "the devil is in the details." Clearly, the devil was actually there, because the Jan Bell management team never could bridge the cultural gap between operating a high-volume, low-margin business with an average price point of $80 versus a high-end guild jeweler with an average ticket of almost $1,200. Further, the Jan Bell team tried to double the size of Mayor's by opening many new stores over just a couple of years, with disastrous results.

Mayor's sales mix in 1999 consisted of the following: watches 44% (includes Rolex 30%); diamonds basic 22%; jewelry 25%; other 9%. Diamonds were important: diamond jewelry and diamond jewelry with gemstones were 39%

of sales. Its average ticket was a $1,189. In 1999, Mayor's bought over $7 million in estate jewelry for resale or remanufacture.

A New Millennium; A New Saga

At the dawn of the new millennium, Mayor's was struggling: it was financially stressed.

In 2001, Mayor's Jewelers tried to raise its profile with both the public and the trade, even while financials were stressed. In a major PR effort, the company paid for a slick multi-page free-standing insert to Women's Wear Daily. Mayor's executives gushed about the company's future. Al Rahm, then-president of Mayor's stores, said that 38 Mayor's sales people had sales of over $1 million in 2000. Two associates had sales over $2 million. The company paid supermodels such as Christy Turlington, Nicolas Malleville, and Bridget Hall to model its jewelry. Finally, in a nod to Wall Street, the company touted its website, Mayors.com, as a place for "internet fanatics to browse the global jewelry market."

In April 2001, the company said it was pursuing strategic alternatives to enhance shareholder value, including the possible sale of Mayor's to another entity, a merger, or a consolidation. Essentially, Mayor's was seeking an equity partner.

During the Basel Fair in 2001, rumors circulated that luxury goods conglomerate LVMH Moet Hennessy Louis Vuitton, of Paris, was planning to buy Mayor's. The company denied the rumors.

In 2001, outsiders began to become involved in Mayor's. In January, 2001, a group led by Eliahu Ben-Shmuel, an Israeli citizen living in Florida, raised his ownership of Mayor's shares to nearly 10%. Ben-Shmuel never publicly stated his intentions. Mayor's current registration statement still lists Ben-Schmuel as a 5%+ shareholder, based on documents filed in 2001. In February 2001, a dissident shareholder, Philip Goldstein, nominated himself and two others to the board of Mayor's. Goldstein was pushing for the sale of Mayor's.

Family Era Ends

In March 2001, Sam Getz resigned from the company.

In March 2002, Isaac Arguetty stepped down as chairmen of Mayor's, apparently due to continuing financial problems. Arguetty was listed as the "company's founder" in a news release. Technically, he founded Jan Bell, not Mayor's Jewelers. But by that time, Jan Bell had changed its name to Mayor's.

In March 2002, the Steinmetz Group and its subsidiary, Diamond.com, apparently offered $20 million in cash and $20 million in diamonds in March 2002, but the offer was contingent on Rolex continuing to supply products. Rolex had temporarily suspended shipments to Mayor's during the Spring of that year, so the offer was rejected by Mayor's.

In an effort to rein in expenses while it was seeking a capital infusion, Mayor's announced a major restructuring plan in May 2002 which called for the closing of 13 stores. At its peak, Mayor's operated 41 stores, many in locations beyond its core Florida and Georgia markets, where its name was unknown.

In July 2002, the Steinmetz Group and its subsidiary, Diamond.com, apparently offered some $20 million in cash and $10 million in diamonds to Mayor's executives. The offer was allegedly in return for control of the company and five seats on Mayor's nine-member board. Diamond.com sold jewelry over the internet and was run by the founder of the company that bought Mayor's in 1998.

While Steinmetz and Mayor's were talking, another rescue mission was led by Henry Birks & Sons Holdings, a Montreal-based operation with jewelry stores across Canada. In May 2002, Mayor's had tentatively agreed to let Birks acquire a majority stake for $11.5 million cash, but postponed the deal while pursuing an offer for an undisclosed amount from a third suitor, New York-based Steel Partners II LP, an investment group controlled by Warren Lichtenstein.

On June 24, 2002, Mayor's announced that its preliminary agreement with Birks had expired, but failed to mention Steel Partners.

After all of this dickering, Henry Birks announced on July 31, 2002, that it had executed a definitive agreement with Mayor's for a $15 million investment. This investment gave Birks a 72% equity ownership of Mayor's. By August, 2002, Birks had accepted the resignation of five members of Mayor's board of directors; further, Mayor's CEO also stepped down. Birks put four of its team on the board of directors and installed its CFO as acting CFO of Mayor's.

In a press release dated October 9, 2002, Mayor's announced management changes which essentially sent most Jan Bell personnel packing and swept in Birks' management group.

In July 2004, Birks notified Mayor's that it wished to pursue a formal business combination. Thus, the process of the merger began.

After the companies were well into the merger process, management of Mayor's was notified in September 2004 that a competitor of Mayor's was possibly interested in acquiring the company. However, the controlling shareholders of Birks and Mayor's said they were not interested in selling their shares. In October, Mayor's received another indication of interest from the potential acquiror. As a result of this second inquiry, Mayor's management indicated that a transaction with anyone other than Birks would be futile, since Birks shareholders were unwilling to sell.

Corporate Background

Birks' corporate headquarters are located at 1240 Square Phillips, Montreal, Quebec, Canada H3B 3H4. Birks' telephone number is (514) 397-2511. Mayor's is a Delaware corporation. Its corporate headquarters are located at 14051 N.W. 14th Street, Suite 200, Sunrise, Florida 33323. Mayor's telephone number is (954) 846-8000.

The companies are in registration with the U.S. Securities & Exchange Commission. The facts presented in our analysis are not guaranteed, and our analysis may change. Neither Mayor's nor Birks' management could comment on our article, since the company is in registration. The author owns one hundred (100) shares of MYR.

About IDEX Online Research

IDEX Online Research is a division of IDEX Online (www.idexonline.com) which produces real-time transparent, unbiased pricing information for the global diamond and jewelry industry. IDEX Online Research provides exclusive, in-depth analysis of the global diamond and jewelry trade, industry research, retail and consumer analysis, as well as trend forecasts and financial breakdowns.

IDEX Online Research is headed by leading industry analyst Ken Gassman. For over 20 years, Ken has been a leading retail and consumer analyst on Wall Street, covering the global diamond and jewelry trade, working with major national U.S. retailers including Wal-Mart and Home Depot as well as jewelers such as Zale Corporation, Signet Group, Movado, and others.