Serving the best customers in the world for 115 years

The Army & Air Force Exchange Service

Annual Report 2009

www.aafes.com

The AAFES Story: Table of Contents

A U.S. Soldier in Iraq poses with a bag containing his recent AAFES purchase.

Commander's Column

Last year, AAFES accomplished great things serving America's Fighting Heroes

Maj. Gen. Bruce Casella

"We will continually trumpet the value story and relevancy of AAFES as a family, market and combat multiplier—and never take our eyes off our mission and our patrons, the very reasons we exist."

Based in Dallas, AAFES is a global military command with a retail mission carried out by nearly 44,000 military and civilian associates. A board of directors comprised of senior Army and Air Force leaders oversees operations.

In 2009, the AAFES team of nearly 44,000 associates, armed with a clearly defined strategic plan, accomplished many great things as we served America's warfighters and built a strong glide path for the future.

Throughout this Annual Report, you will read about many of these remarkable accomplishments, such as AAFES:

- Boosting earnings to $428.5 million, nearly 14 percent higher than the previous year.
- Recording total sales of nearly $9.8 billion. Without gas figures, our sales rose by $26.3 million from last year.
- Providing dividends of $261.6 million to Morale, Welfare, Recreation and Services programs for troops.
- Continuing the largest capital improvement project in AAFES' 115-year history, investing more than $1.2 billion during the next five years to build new and renovate existing facilities.
- Operating a website, www.aafes.com, with more than 18 million products and 100+ retailers. Read about our unique "Click to Brick" program on Page 3.
- Opening the planet's biggest exchanges—the KMCC BX/PX and Kadena AB, respectively—and breaking ground on Freedom Crossing at Fort Bliss, the world's first village-type lifestyle center on a military installation, to better support our military customers.
- Reducing operating costs by more than $3.7 million through collaborative purchasing arrangements with sister military exchanges.
- Improving our customer satisfaction index to 75, putting us on par with industry leaders.
- Planning for 2010's global rollout of Oracle Retail's auto-replenishment technology, which will centralize and automate purchasing based on merchandise levels.
- Preparing for this year's rollout of a $33 million centralized warehouse management system, which will streamline the way we store and deliver merchandise.

- Providing expeditionary and mission support capabilities to our troops at home, in Afghanistan and Iraq, and other overseas locations.
- Delivering more than $450 million in enterprise productivity.
- Enabling AAFES to remain one of only two global retailers to maintain an AA+ bond rating—the highest in the industry.
- Reaching thousands of military shoppers via Twitter, Facebook, YouTube and the "Salute to Your Service" blog.

AAFES: A financially stable, multi-channel retailer

We remain a financially stable multi-channel retailer operating in more than 30 countries, five U.S. territories, all 50 states and on the World Wide Web, building lifelong emotional connections with our customers one transaction at a time. Wherever the 12.3 million active duty troops, Reservists, National Guard members, military retirees and their families call home, AAFES is there.

In 2009, we operated nearly 3,700 retail stores, including our flagship BXs and PXs, and 1,639 brand-name and AAFES signature-brand restaurants around the

see "Commander's Column," Page 15

Getting the Right Products to the Right People at the Right Places

Like *Women's Wear Daily* put it this past January, we are a $9.8 billion retail giant that operates in every U.S. state and more than 30 countries—and we are striving for even more market share.

In 2009, from Fort Lewis, Wash., to Bagram AB, Afghanistan, 12.3 million active and retired Soldiers, Airmen, National Guard members, Reservists and their families enjoyed more than 3,000 food, entertainment and retail options, and 880,000 products in the stores and 18 million online—from socks and shoes to the most popular electronic gizmos. They got competitive prices—and paid no sales tax.

What's more, no other major retailer serves America's Fighting Heroes in Afghanistan, Iraq and throughout the Middle East, as we literally fulfill our motto, "We go where you go." In 2009, we began drawing down Iraq operations as the Defense Department started withdrawing troops, and we commenced arduous planning to increase services in Afghanistan, as the Global War on Terror shifted geographic focus.

Creating memorable shopping experiences

We could best describe 2009 as a year that presented many challenges, but also many opportunities to boost revenues, streamline operations and create shopping destinations that ensured consumers made AAFES their first choice. While a downturned economy forced many competitors to cut spending, AAFES continued to invest millions of dollars in technology, people and facilities.

Our goal of creating enjoyable shopping experiences is nowhere more apparent than at the world's largest exchanges—the Kaiserslautern Military Community Center (KMCC) BX/PX at Ramstein AB, Germany, and the Kadena AB main store on Okinawa. In addition, we broke ground this past winter on Freedom Crossing at Fort Bliss, Texas, the first Main Street lifestyle center on any military installation in the world.

(To read more about KMCC, Kadena and Freedom Crossing, see Pages 4, 8 and 14.)

Serving Those

In the most aggressive store construction and image upgrade program in AAFES' 115-year history, we also invested $364 million to complete 29 capital improvement projects, including five new main stores, around the world. Nine main stores underwent $31 million in upgrades.

During the past year, we also remodeled more than 60 PowerZone electronics departments to improve product layout and merchandise flow, which led to a 2 percent growth in sales. Now, gadget-minded shoppers can talk with trained associates much easier while interacting with state-of-the-art laptops, GPS units, digital cameras,

We created fun shopping environments for our valued customers, such as this "balloon drop" at Andersen AFB, Guam. They found great prizes in the balloons.

Sales of Martha Stewart products in AAFES stores worldwide topped $5.1 million.

Who Serve

MP3 players, video games and iPods. We're targeting 35 more PowerZones this year for remodeling.

Meanwhile, we opened shop in May for the Rhode Island National Guard, which gave us a history-making presence in all 50 states. Our store serves National Guard members who undergo drills or work at the base and the military retirees and families who live in the area. Sales averaged $35,000 a month.

Our expansion continues well into this year and beyond, with modern, energy-efficient complexes opening in 2010 at Misawa AB, Japan; Randolph AFB, Texas; and Keesler AFB, Miss. The latter store replaces one destroyed by Hurricane Katrina in 2005.

Inside our stores in 2009, we served "the best customers in the world" with merchandise by Liz Claiborne, Nautica, Tag Heuer, Macy's private labels, Estée Lauder, Clinique, Lancôme, Elizabeth Arden, Shiseido, Revlon, Cover Girl, Prada and Victoria's Secret. Our upscale Coach handbag shops feature 35 styles and generate more than $37 million in sales, making Coach one of our top worldwide brands.

In addition, sales of Martha Stewart products in more than 60 stores around the world topped $5.1 million, surpassing our goal of $3.4 million by nearly 50 percent. Our greatest growth opportunities targeted fashion and home décor, with other popular items, including home goods, bed and bath textiles, housewares, casual dinnerware, glassware, cookware and gifts.

Our Sales Directorate enjoyed new growth opportunities in Juniors' daywear, trendy Levi's, Young Men's and Missy's categories, YMI, Jolt, Bubble Gum, TYTE, Bandolino Blu, Adiva, Indigo Joe, among other brands; and added new colors and trends. To maximize our "best brands, best prices" strategy, softlines increased exposure of Izod, Calvin Klein, US Polo and other major brands to add zing and the ability to mix and match clothing that looks great on the sales floors—and on our customers.

Through strategic product placement and innovative marketing techniques, we also targeted key 18- to 28-year-old female shoppers by providing competitive prices on Benefit, Smashbox, Nars, Bare Essentials, Carol's Daughter and other popular cosmetics in our unique beauty bar concept initiative.

On our website—www.aafes.com—that features more than 18 million items, a new product review system allows customers to get as much information as possible about merchandise before ordering. Through our new "Click to Brick" program, which began in 2009, shoppers who buy from among 3,200 products online now enjoy delivery to their local exchanges in the continental United States without shipping charges.

Expanding exclusive labels

What's more, budget-minded consumers enjoyed an expanding selection of AAFES exclusive labels for men's, women's and children's clothing, as well as our Exchange Select products, which are expected to surpass 600 items by year's end. Exchange Select labels offer customers at all military exchanges savings of up to 60 percent and quality comparable to name-brand equivalents. In 2009, our portfolio of all exclusive-label products, including our extensive clothing lines, generated more than $1.2 million in sales.

We also gave our customers plenty of eating options. In 2009, we expanded our portfolio of name-brand restaurants to a record 41 with the additions of Arby's, Del Taco and Wing Zone and opened or converted 71 new eateries. Our customers now enjoy 1,639 major name-brand and AAFES-signature restaurants wherever Soldiers and Airmen are stationed—or

see, "Right products . . ," Page 12

KMCC and Kadena 'Wow' Customers

Shoppers at Kadena AB on Okinawa, Japan, enjoy the convenience of having their shopping carts ride an escalator with them.

World's largest exchanges offer customers unique, enjoyable shopping destinations

We at AAFES become part of the solution—and America's massive troop movement initiatives are no exception.

As the Defense Department shifts hundreds of thousands of troops to central locations in Europe and the Pacific, AAFES answered the call in 2009 by opening the world's largest and second largest exchanges—the BX/PX at the Kaiserslautern Military Community Center (KMCC) at Ramstein AB, Germany, and the Kadena AB main store on the island of Okinawa, respectively—to our 115-year legacy of serving America's warriors wherever they go.

But those projects were just part of the $1.2 billion we have earmarked during the next five years for new buildings and upgrades to existing stores—the largest capital improvement program in AAFES history. Out of 177 main stores, our construction projects will touch more than half as we strive to establish emotional connections with our valued patrons through attractive, shopper-friendly, state-of-the-art facilities and the best in customer service.

Serving the "Gateway to Europe"

At KMCC, the $170 million, 165,000-square-foot BX/PX—an American-style mall with a European flair—opened in late September as the cornerstone of our efforts to present a complete customer experience in one location to improve the quality of life for the 53,000 Airmen, Soldiers, their Families and 285,000 visitors who pass through Ramstein AB, the "Gateway to Europe."

Located conveniently across from the Air Mobility Command Passenger Terminal, our store is a major anchor in the entire 444,000-square-foot KMCC. A joint partnership between AAFES, Air Force Services, the German government and other organizations, the KMCC expands shopping, restaurant and entertainment options, and increases the number of hotel rooms for service members and their families. For AAFES, the BX/PX is the first one of our stores to be connected to an eight-story, 350-room hotel.

Even a month before KMCC opened officially, our staff in Germany received enthusiastic calls from potential consumers from as far away as Italy and the United Kingdom, proving that the store was creating a buzz across the continent. Since June, when portions of AAFES businesses began opening, customers have spent a whopping $53 million, including $1.2 million on grand opening day, and $19.4 million in December alone. December's sale revenue is 26 percent higher than the five facilities the store replaced.

KMCC is exceeding all expectations across the board and

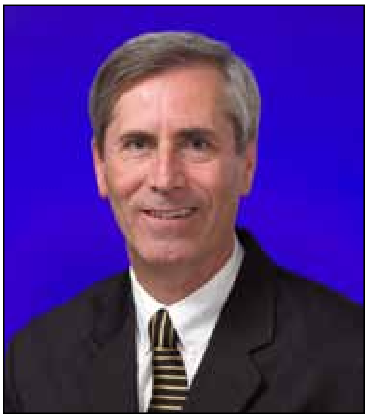
see, "KMCC and Kadena . . . ," Page 14

The Kadena Air Base AAFES BX on the island of Okinawa, Japan, grand opening.

The AAFES BX/PX at the Kaiserslautern Military Community Center (KMCC), Ramstein AB, Germany.

2009: Earnings, Sales, Customer Satisfaction Rise

AAFES: strategically positioned to grow total revenue substantially



By Michael Howard, Chief Operating Officer

By any stretch of the imagination, 2009 certainly brought challenges to the retail industry. Consumer spending and confidence were down. People had to work harder to achieve their strategic goals.

Our associates and customers, though, set us apart from our competitors. No other retailer deploys with the troops like AAFES, no one takes care of military families quite like AAFES, and no other store lives, breathes and sleeps military culture the same as AAFES, a nearly $10 billion enterprise with the motto "We go where you go."

Yes, 2009 was a very challenging year, not only for AAFES, but for the entire retail industry as families continued tightening their spending and retirees—17 percent of our customer base—lost good chunks of their 401(k)s and other retirement plans to downturns in the financial markets.

> "No other retailer deploys with the troops like AAFES, no one takes care of military families quite like AAFES, and no other store lives, breathes and sleeps military culture the same as AAFES."
>
> *—Michael Howard, chief operating officer*

Earnings, customer satisfaction up

Despite economic turmoil in the nation's economy and retail industry, our earnings rose nearly 14 percent to $428.5 million while our total sales hit nearly $9.8 billion. In addition, our Customer Satisfaction Index (CSI) rose three points to 75, which equals several industry leaders. We can trace this earnings growth directly to our successful efforts to make our supply chain operate as smoothly as possible and the millions of dollars we're investing in technology to ensure we get the right products in the right quantities to the right people at the right places so our stores never run out of the hot sellers.

Leveraging major technology

Throughout 2009, our Sales and IT directorates leveraged major technology that provides us with industry-best inventory practices to keep tabs on all products and manage availability at our 177 main stores and 3,475 other retail operations around the world.

Shoppers will now see all of their favorite products in abundant supply on the shelves, which should boost our

Despite economic turmoil in the nation's economy and retail industry, our earnings rose nearly 14 percent to $428.5 million while our total sales hit nearly $9.8 billion. Holiday sales for AAFES in 2009 rose 2 percent to $422.9 million, compared to 1.1 percent for the retail industry.

customer satisfaction even more.

Having this auto-replenishment knowledge will allow our buyers, planners, forecasters and analysts to make the best possible decisions on products and improve our inventory productivity, profit margin and gross profit.

In addition, we implemented in 2009 the Oracle Markdown Optimization module, which created $2.4 million in savings.

In our worldwide distribution centers, our Logistics Directorate is streamlining every facet of how we store merchandise and deliver products. Our global procurement department is executing technology that already is streamlining our corporate purchasing processes and cutting operating costs.

Collaborations equal cost savings

Our purchasing collaborations with other military exchanges and strategic partners have resulted in millions of dollars in cost savings, and our sales promotions with the Defense Commissary Agency are reaping benefits to the bottom lines of both organizations.

Looking to 2010 and beyond, we expect good things. The National Retail Federation forecasts that retail industry sales will rise 2.5 percent this year now that influential economic indicators, such as the housing market and employment, are beginning to show positive signs that could bolster consumer confidence.

Adweek reported this past January that 29 percent of respondents to a Harris Poll said that "because of sales, coupons, promotions and other discounts," they're more likely to consider shopping at discount stores in the next year. That includes 15 percent who said they're "much more likely" to patronize discount stores.

We will continue our diligence at all levels of the organization to strengthen our value proposition to our 12.3 million authorized customers looking to AAFES as their "first choice" to help them stretch their family budgets.

Providing the best

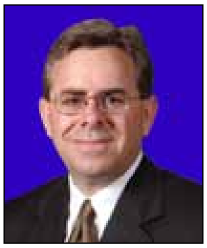
In essence, our many initiatives all tie into providing the best products, prices and services to our customers, while operating as efficiently as possible so we can provide the highest dividends to Morale, Welfare and Recreation programs for the Soldiers and Air Force Services for the Airmen.

As I look forward, I am confident AAFES has all the tools in place to be a value-added benefit to our military communities, just like we have for 115 years.

> "Our many initiatives all tie into providing the best products, prices and services to our customers, while operating as efficiently as possible so we can provide the highest dividends to Morale, Welfare and Recreation programs for the Soldiers and Air Force Services for the Airmen."

The Power of Collaboration

Exciting new lifestyle centers and telecom offerings are on the way



By Dan Metsala, Senior Vice President, Strategic Planning & Partnerships

Last year, when AAFES developed its first five-year Strategic Plan, the organization embraced the concept that forging stronger ties with key business partners was critical to our future success. We believe that collaboration is an essential—perhaps indispensable—route to becoming more innovative, increasing productivity and taking even better care of our customers.

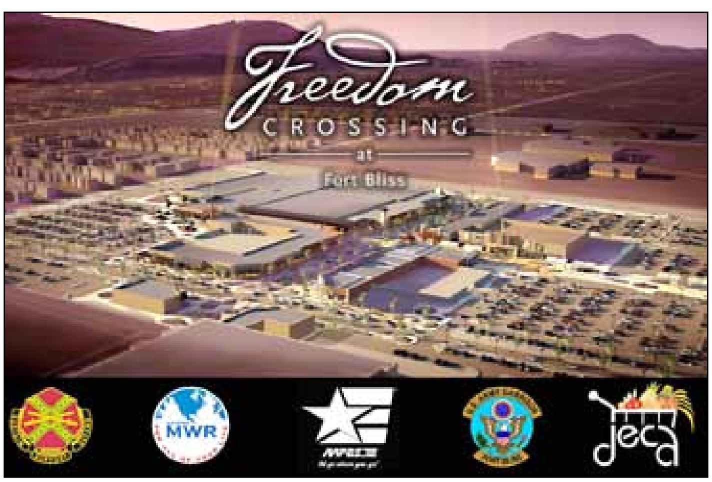
AAFES' belief is embedded in one of our five corporate strategic goals: "Be the premier collaborative partner with federal and commercial entities."

Leveraging diverse resources, skills

AAFES made significant strides toward this goal of being the premier collaborative partner during 2009, particularly in the area of cost savings. Teaming with other military exchanges on consolidated purchases and distribution has already saved millions of dollars in unnecessary expense.

Collaboration leverages diverse resources and skills of two or more organizations toward achievement of a common goal. The Strategic Planning & Partnerships Directorate has oversight of two of these initiatives, both focused on teaming with others to improve the customer experience and new business growth.

In 2009, construction began on the Freedom Crossing Lifestyle Center at Fort Bliss, Texas, which is set to open its major phase in November 2010. While the concept of creating a physical center to serve as a community gathering point is a proven strategy in the commercial world, Fort Bliss is the first such development on a military installation. Anchored by an AAFES exchange and Defense Commissary Agency (DeCA), Freedom Crossing will feature name-brand retail, casual dining and entertainment options.



Freedom Crossing's success reflects expansive collaboration with diverse audiences, such as the Department of Defense; U.S. Army installation officials; the Family and Morale, Welfare and Recreation Command (FMWRC); DeCA; Congress and local governments. The partnerships also include private-sector chambers of commerce, retail developers, investment bankers and an array of retailers.

Although still in its infancy, the lifestyle center concept will create a new paradigm in customer experience during the next few years as Freedom Crossing matures and other opportunities for lifestyle centers are explored at Fort Sam Houston, Texas, and Joint Base Lewis/McChord, Wash. Lessons learned will also be applied to the next generation shopping centers that will have much broader application.

Emerging partnership, new offerings

Equally significant are emerging strategies with retail offerings of wireless and bundled services and the telecom partnership with FMWRC. These initiatives will change the way cell phone, Internet, TV and telephone services are provided on military installations worldwide.

The telecom partnership with FMWRC and the Army Recreation Machine Program will include an integrated joint business strategy to eliminate internal competition; apply best business practices to provide the best value to AAFES and FMWR customers; and centralize management and oversight of personal information services with AAFES as the primary proponent. This will allow for development and expansion of Internet service in the barracks. To assist with managing this program, FMWRC has provided a business manager and contracting officer to AAFES for day-to-day operations and strategic planning of our telecom programs.

The new partnership brings a global strategy that eliminates duplication of efforts, provides the latest products and services, and brings a consistent offering of service and quality.

Telecom: dynamic business

Telecom is a very dynamic business—and our customers' needs and wants also continue to change. To keep pace, AAFES and Deloitte Consulting have developed business models for wireless service and home services for telephone, Internet and TV that will launch later this year.

There's great excitement as AAFES prepares to deliver these offerings geared specifically to the needs of our customers, featuring established brands, more choices, greater convenience with competitive prices and military discounts. Stay tuned.

The AAFES Story by the Numbers

$9.8 billion — Amount of sales generated by AAFES' worldwide operations.

$2.4 billion — Estimated total dividends contributed by AAFES from its revenues to military Morale, Welfare and Recreation programs during the past 10 years.

12.3 million — Number of active duty troops, Reserves, National Guard members, retirees and family members served by AAFES.

177 and **3,475** — Number of AAFES main stores and other retail operations, respectively, around the world.

1,096 and **543** — Number of brand-name and AAFES signature-brand restaurants, respectively, operated around the world under the AAFES banner.

41 — Number of name-brand restaurant partners in AAFES' portfolio.

131 — Number of AAFES-operated stores in Afghanistan, Iraq and other "contingency locations."

43,725 — Number of AAFES associates around the world, including **13,648** military family members, **2,809** veterans and **76** "wounded warriors."

430+ — Number of AAFES associates deployed to Afghanistan, Iraq and throughout the Middle East to serve troops fighting the Global War on Terror.

4,500+ — Number of AAFES associates who have deployed—sometimes more than once—to global hot spots since the start of the war on terror after 9/11.

2.7 million — Number of 16-ounce Monster Energy Drinks sold in 2009 throughout the Middle East.

Cokes and tacos—providing troops with a delicious "taste of home" at Camp Buehring, Kuwait.

18 million-plus — The number of products available on AAFES' website, www.aafes.com.

3,200 — Number of products in the "Click to Brick" program, where shoppers who prefer the ease and comfort of Internet shopping on www.aafes.com can have their products delivered to nearby exchanges in the United States for pickup, thus saving shipping costs.

4 million — The number of meals served to children each year by AAFES on a break-even basis at **92** Department of Defense schools in nine countries.

$1.2 billion — Total investment of new and renovated construction for AAFES stores worldwide during the next five years.

17 — Number of phone centers for troops to call home in the Middle East, Afghanistan, Bosnia and Kosovo.

5 million — Number of pre-paid phone card minutes of phone conversation bought by Americans for Soldiers and Airmen on the front lines to call home.

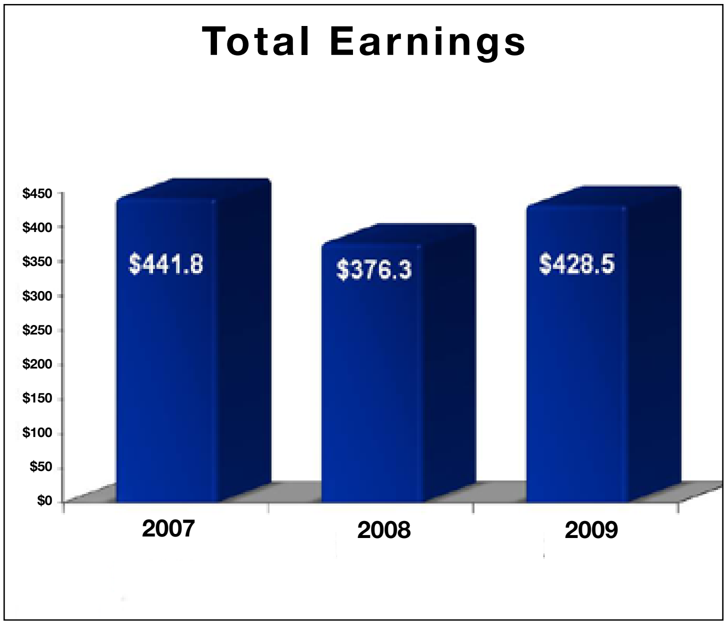
1,000+ and **2,254** — Number of AAFES followers on Twitter and Facebook, respectively. AAFES' site on YouTube averages **1,500** views a week.

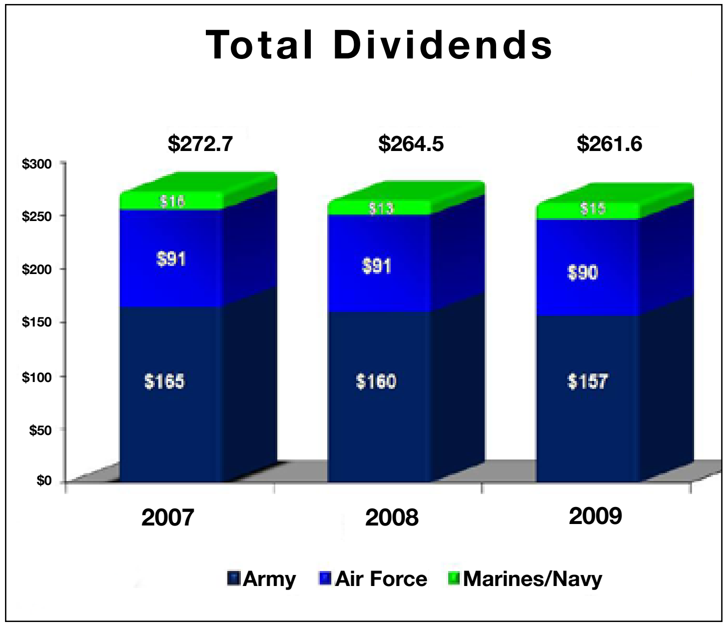
203,100 — Number of AAFES gift cards bought by Americans and distributed to troops and military families around the world.

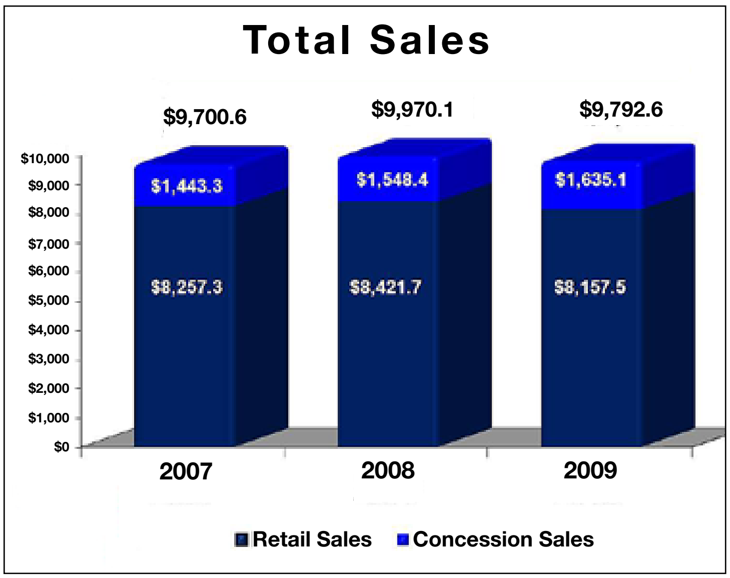
15 — The number of military training exercises supported by AAFES and our "mobile exchanges" throughout the world.

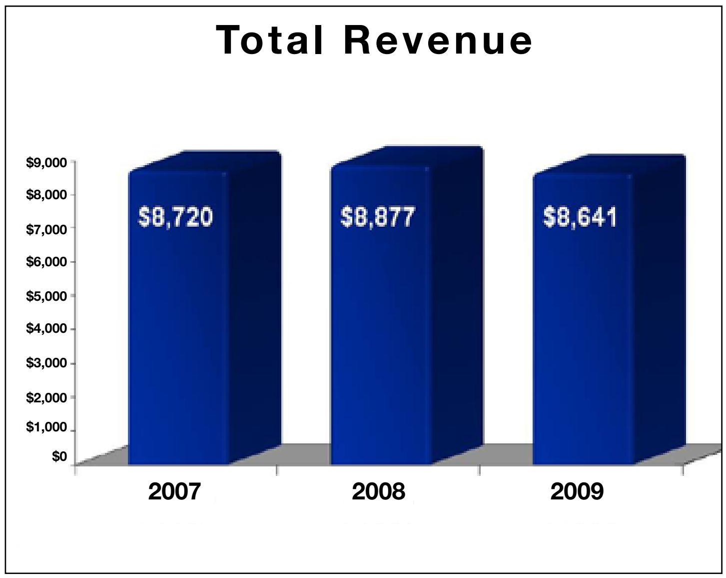
Associates at Fort Drum, N.Y., give "goody bags" of products to service members as they walk toward their Afghanistan-bound plane. The sign says it all: "We go where you go! See you there!"

The AAFES Story by the Charts









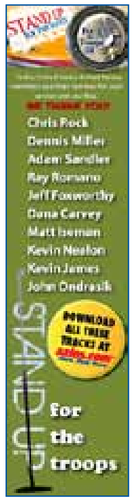
All audited figures in millions. Total sales, minus gas, increased by $26.3 million.

Financial Factoid

Despite being a Department of Defense "military command with a retail mission," AAFES receives almost no federal funds, relying instead on sales revenue from our stores, catalogs and website. In 2009, the Finance & Accounting Directorate expanded the organization's financial options by turning to private investors. This action allowed AAFES to diversify its debt portfolio and reduce risk by introducing long-term borrowing options other than standard bank loans. AAFES used private debt placement in 2009 for working capital and construction projects.

Snapshots of AAFES Success

Sustainability efforts. Nearly 2,900 tons of plastic hangers, bottles, shrink wrap, aluminum cans, publications, cardboard and paper were collected in 2009 in our "trash for cash" program at 152 stores in the continental United States. Energy-reduction programs also saved $3.2 million and 30 new construction projects are designed to meet LEED certification.



Humor for heroes. In collaboration with AAFES and Sony, Grammy-nominated, singer-songwriter John Ondrasik continued expanding his repertoire of free CDs for service members. In 2009, his "Stand Up for the Troops" featured the comedy antics of Dana Carvey, Jeff Foxworthy, Dennis Miller, Chris Rock, Ray Romano and other laughmeisters. Members of the armed forces can download the CD for free at www.cdforthetroops.com or from AAFES' website, www.aafes.com. About 200,000 CDs arrived at military bases, Armed Services YMCAs, USO Centers and other locations throughout the world.

Rolling billboards. About 100 of our 18-wheelers hit the road in 2009 as rolling billboards with the message, "Army Family Covenant: Keeping the Promise—Honoring Our Commitment to Soldiers and Families," in four-foot letters. We partnered with the Army's Family and Morale, Welfare and Recreation Command to create the mobile messages, which 69 million people will likely see during the next two years. The initiative reinforces the Army's commitment to providing families with health care, housing, schools, youth and childcare services, and career and educational opportunities.

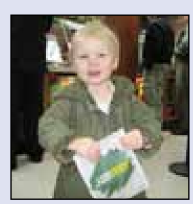
Comics for the troops. AAFES and Marvel Comics in 2009 expanded the free "New Avenger" comic books featuring Captain America. "An Army of One" is the seventh in the AAFES/Marvel series, which began in 2005. The books are available exclusively at BX/PXs throughout the continental United States and 90 exchanges in Afghanistan and Iraq.

Shopping concepts. More than 50 concept shops for Vera Bradley, Under Armour, Adidas, Nike, and Macy's Style & Co. and INC opened in AAFES stores in 2009, generating more than $7 million in revenue. Our first Martha Stewart concept shops opened at the Kaiserslautern Military Community Center in Germany and Kadena AB on Okinawa. Martha's products are sold in 60 AAFES stores around the world.

A special associate. Our associates are pretty special people, doing whatever is necessary to make the lives of our Fighting Heroes easier. For example, Wanda Clayton, credit-risk manager for AAFES, became the first recipient of the Air Force Wounded Warrior "Care Beyond Duty" award in March 2009 for helping a Senior Airman deal with severe financial hardship due to post traumatic stress disorder after he returned from Iraq.

Bringing movies to the troops. AAFES held 15 advanced screenings of major movies to troops in Operation Enduring Freedom and Operation Iraqi Freedom, part of a collaboration between AAFES and motion-picture distributors. The movies played a week before their theatrical release in the United States. At right, Soldiers at Camp Buehring, Kuwait, meet stars of "Star Trek."

Welcome Home! Through a "Welcome Home" program, AAFES supports troops returning from battle in the Middle East for rest and recuperation. Waving banners and signs, associates greeted 13,000 troops at the Dallas and Atlanta airports.



Winning restaurants. Subway recognized AAFES in 2009 as a top 10 international non-traditional developer. Popeyes at Schofield Barracks in Hawaii won the International Gold Plate Award from the corporation for exceptional service and operation.

Throughout 2009, managers and associates brought to customers the latest in brand-name and AAFES exclusive styles and fashions for men, women and children.

Firestone, GameStop, UPS and other major retailers became AAFES business partners in 2009.

Chief Operating Officer Michael Howard, center, helps cut the ribbon on a new AAFES store at Eielson AFB, Alaska, one of five new main stores opened in 2009.

U.S. embassy employees enjoy the new AAFES shoppette at the American embassy in London.

Right products, right people, right places

Con't from Page 3

fighting America's enemies. We even delivered food from Dominos, Papa John's and Pizza Hut in 19 locations, generating $19 million in sales.

GameStop, the world's largest video-game retailer, created a welcomed presence for troops.

Strategic collaborations

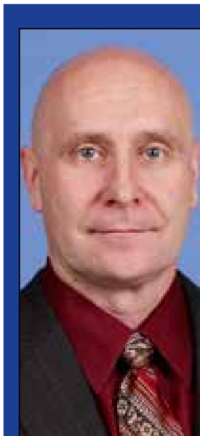
Moreover, GameStop, the world's largest video-game retailer, opened 25 new stores in 2009. Other strategic collaborations resulted in 29 Firestone car-care operations and new outlets for Footlocker, General Nutrition Center, Paul Mitchell Salons, UPS and Hertz, among others. The partnerships boosted our bottom line by hundreds of millions of dollars. For instance, at MacDill AFB, Fla., GameStop, Firestone and UPS boosted sales by 7 percent and earnings by 22 percent.

Leveraging technology to improve productivity, profit

In 2009, we continued to cut costs and squeeze inefficiencies out of our supply chain by investing millions of dollars in technology to get the right products in the right quantities to the right people at the right places. For instance, our global distribution centers now use voice technology to streamline workflow. In 2009, we began preparing for this year's $33 million centralized warehouse management system that will reduce inventory-carrying and labor costs as well as inventory cycle times.

Throughout 2009, the Sales and IT directorates, store managers and associates laid the groundwork for this year's rollout of auto-replenishment—automatic reordering of merchandise based on store product levels.

Industry-best practices



Hunter Cole

The retail management system is part of Oracle's $177 million technology that affords us with industry-best inventory practices. For instance, the Sales Directorate implemented the Oracle Markdown Optimization, which resulted in a savings of $2.4 million.

"Having this knowledge allows our buyers, planners, forecasters and analysts to make the best decisions," said Hunter Cole, vice president of planning, allocation and replenishment. "We will have more control to improve our inventory productivity, profit margins and gross profit."

Now that's a perfect recipe for making AAFES our valued customers' first choice.

Changing Strategy in a Changing War

AAFES handles a troop drawdown in Iraq, surge in Afghanistan

Nearly every day for a few blessed hours, Staff Sgt. Bridgett Niblet opens the 8-foot-by-20-foot store at Afghanistan's Forward Operating Base (FOB) Tarin Kowt in an area so forbiddingly remote that the only things Soldiers see in all directions are endless stretches of farmland enclosed by skyscraping mountains.

To service members at strategic outposts like this one 100 miles north of Kandahar, AAFES' troop-run stores, known as "imprest-fund sites," make life a little more bearable right on "the tip of the spear," as one manager put it. Located mostly in postage-stamp Afghan villages, the facilities are nowhere near as big, or their product selections as vast, as typical AAFES-operated exchanges at Kandahar AB and Bagram AB, but these troops at FOB Tarin Kowt don't mind.

"Our store is the only place for Soldiers to get a taste of home for those 10 to 15 minutes they want to get away from the dust and blazing sun," said Capt. Jadore Scovell, who helps Sgt. Niblet at the store. "They think it's awesome. Many AAFES employees are working every day to make sure we have everything we need and what they want from us."

A "different battle rhythm"

As the Global War on Terror shifts from Iraq, AAFES is prepared to boost the number of troop-run sites in Afghanistan within the next year from the present 25. The number depends almost exclusively on how many thousands of additional troops flood into the country to fight the Taliban, said AAFES Supervisor Mary Moreno.

"What does a bag of chips or tobacco, or body wash, or magazines, or sodas, toothpaste, Monster and Red Bull mean to troops out on the frontier? The value can't be expressed in dollars," said Moreno, who oversees the operations for AAFES from her office at Bagram AB. "They rely on us, and we get to serve tried-and-tested Soldiers."

In fact, the troop-run facility is perfect for service members located far from their main bases.

"People at smaller, outlying FOBs are often accustomed to a different battle rhythm, so consequently, the troop-run facilities establish operating hours that meet their needs," said Norm Griffith, a strategic planner with AAFES-Europe. "We support them 100 percent because they are the front line and our priority."

The stores are called "imprest-fund sites" because of the account through which AAFES provides start-up costs, which average about $15,000. Service members must sell merchandise at AAFES prices, make no profit and use revenue to buy more products. After shuttering a store, they return all money back to AAFES for other troop-run operations.

"The AAFES imprest site is a force multiplier that is needed wherever troops are," said Capt. Demetrick Thomas, who runs a store located two hours away by Blackhawk chopper from Kandahar AB. "We're glad to see them coming."

"What does a bag of chips or body wash or magazines or sodas, tooth-paste, Monster and Red Bull mean to troops out on the frontier? The value can't be expressed in dollars."

—Mary Moreno, AAFES supervisor, Bagram AB, Afghanistan

Early one morning in Afghanistan in 2009, American troops wait for the AAFES imprest-fund store at isolated Forward Operating Base Farah, left, to open. Below, troops at FOB Ashraf help themselves to cold drinks at another imprest-fund site.

KMCC, Kadena: “Wow!” factors for world’s best customers

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Stephanie Burns

outperforming our wildest dreams. As in the words of the KMCC store manager, Stephanie Burns, customers are definitely experiencing the “Wow!” factor.

We’re excited that hundreds of thousands of consumers are enjoying 43 concept shops, featuring big-name brands, including S. Oliver, Nike, Under Armour, Jack Wolfskin, Coach, Northface, Vera Bradley, Martha Stewart, Apple, Nintendo, and 40-plus concessions, some available for the first time on U.S. military installations in Europe, such as Harley Davidson motorcycles. Victoria’s Secret Pink Shop is the first one in an AAFES store anywhere in the world.

The KMCC food court, which seats 1,000 folks, features the tasty creations of Baskin Robbins, Taco Bell, Charley’s Steakery, Subway, AAFES-brand Anthony’s Pizza, and AAFES’ first Johnny Rockets American-style food and the European military community’s only Captain D’s and Manchu Wok. Outside the food court, customers can dine at Romano’s Macaroni Grill and Ramstein Sports Lounge, both operated by Air Force Services, and then stop by AAFES’ rental car agency and Exchange New Car Sales.

Festive grand opening

Nearly 6,100 miles away on Okinawa, thousands of other shoppers enjoyed early October’s festive grand opening of the $80 million, 324,000-square-foot Kadena AB Shopping Center, spending $1.2 million on the first day and $12 million in December. More than 50,000 military members and civilians live on the base and in the area.

Double the size of the old store, the exchange features a 19-shop concession mall and 200-table food court with the same brand-name eateries as at KMCC, along with Popeyes, Burger King, and AAFES-brand Main Street Expresso and Anthony’s Pizza on the first floor. The main BX takes up the entire second floor.


Robert Rice

“The Kadena Experience”

Store Manager Robert Rice said customers can enjoy the “Kadena Experience” with traditional BX merchandise and brand-name products. Interactive stations allow patrons to try out the latest technology. A beauty bar offers Philosophy, Susan Posnick, Smashbox and Carol’s Daughter, and other brand-name cosmetics, while the BookMark is packed with twice as many books and three times the magazines as the old store. Customers can get their hair cut and styled, film developed, packages wrapped, computers repaired, get pampered in a spa, buy eyeglasses and contacts, and send flowers to loved ones.

We expect revenues at KMCC and Kadena to grow well into the future. However, as AAFES Commander Maj. Gen. Bruce Casella says, our success is measured by the smiles on the faces of our customers—members of America’s armed forces and their families. After all, these are the “best customers in the world.”


Customers, above, shop at the new Victoria’s Secret at the KMCC BX/PX, while the exchange at Kadena AB delighted shoppers with seemingly endless aisles of brand-name and AAFES exclusive-label merchandise.

Coach handbags remained one of AAFES’ top sellers in 2009.

Commander's column

Serving America's Fighting Heroes is our mission

Con't from Page 1

> "AAFES stands firmly on the right course to remain a strong and viable exchange for customers, stakeholders, partners, associates, and the military communities we serve."
>
> *—Maj. Gen. Bruce Casella, AAFES commander*

world—all providing a "taste of home" to America's warriors.

Our overseas bakeries and water-bottling facilities provide Wonder and Home Pride breads, Culligan Water and other products to exchanges, commissaries, troop dining halls, military hospitals and MWR clubs. AAFES also provides 24,000 nutritious meals a day on a break-even basis to students in grades K-12 at 92 Defense Department schools in nine countries.

Double-digit savings

We took deliberate actions that buoyed the organization during the country's economic storms and will enable us to face the future successfully by refining our value proposition to be so clear and convincing that customers turn to us as their first choice for quality merchandise and services.

For example, budget-conscious families appreciate the 20 percent savings they receive on a market basket of common products when we're compared to our competitors. They also save up to 60 percent on nearly 600 of our exclusive-label Exchange Select products and find prices as low as $7.99 for our exclusive-label quality clothes, such as Passports for women, Decoded for young men and Buzzcuts for kids.

They also enjoy competitive prices on our many brand-name products and services from some of the country's best-known companies that have joined our family of valuable third-party vendors.

In our PowerZone electronics departments, consumers can interact with the most popular iPods, video games, laptops, GPS devices, you name it.

AAFES will continue building strategies such as these to capture a larger share of the market. We will continually trumpet the value story and relevancy of AAFES as a family, market and combat multiplier—and never take our eyes off our mission and patrons, the reasons we exist.

AAFES stands firmly on the right course to remain a strong and viable exchange for customers, stakeholders, partners, associates and the military communities. We are releasing the power of AAFES.

Maj. Gen. Bruce A. Casella, AAFES Commander

AAFES' rich 115-year history includes remarkable stories of associates serving the troops during both world wars, the Korean Conflict, Vietnam War, at the scenes of natural disasters and during humanitarian missions throughout the world.

Since 1990 and Operation Desert Storm, AAFES has stood beside America's warfighters and continued to serve them in Afghanistan, Iraq, Kuwait and elsewhere in the Middle East in 2009 and well into 2010 for Operation Enduring Freedom and Operation Iraqi Freedom. More than 4,500 AAFES associates have voluntarily deployed to serve throughout the Middle East to serve troops fighting the Global War on Terror.

FINANCIAL STATEMENTS

Army and Air Force Exchange Service
Years Ended January 30, 2010 and January 31, 2009

Ernst & Young LLP

ERNST & YOUNG

Army and Air Force Exchange Service

Financial Statements

Years Ended January 30, 2010 and January 31, 2009

Contents

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Report of Independent Auditors

The Board of Directors
Army and Air Force Exchange Service
Departments of the Army and Air Force

We have audited the accompanying balance sheets of Army and Air Force Exchange Service (AAFES or the Company) as of January 30, 2010 and January 31, 2009, and the related statements of earnings, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of AAFES' internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Army and Air Force Exchange Service at January 30, 2010 and January 31, 2009, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1, on January 31, 2009, the Company adopted the measurement date provisions of ASC 715-30, *Compensation – Retirement Benefits*.

Ernst + Young LLP

May 12, 2010

0910-1094875

Army and Air Force Exchange Service

Balance Sheets

(Dollars in thousands, unless otherwise noted)

	January 30, 2010	January 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	**$ 135,683**	$ 189,812
Trade and other accounts receivable, less allowance for uncollectible accounts (at January 30, 2010 – $40,980, at January 31, 2009 – $59,937)	**3,325,334**	2,986,520
Merchandise inventories	**1,524,112**	1,569,440
Short-term investments	**21,127**	19,635
Supplies and other current assets	**41,729**	33,549
Total current assets	**5,047,985**	4,798,956
Buildings and improvements	**2,878,578**	2,571,525
Fixtures and equipment	**1,236,232**	1,208,297
Construction-in-progress	**317,036**	354,358
	4,431,846	4,134,180
Accumulated depreciation	**(2,173,032)**	(2,046,402)
	2,258,814	2,087,778
Other assets	**642**	1,711
Prepaid pension assets	**121,832**	394,274
Long-term investments and supplemental plan assets	**21,741**	258,855
Total assets	**$ 7,451,014**	$ 7,541,574
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 625,763**	$ 633,290
Notes payable to banks	**1,459,202**	1,949,000
Accrued salaries, separation pay and other employee benefits	**155,936**	153,858
Dividends payable	**61,531**	59,081
Other current liabilities	**196,959**	232,385
Total current liabilities	**2,499,391**	3,027,614
Notes payable to banks – long term	**734,779**	–
Accrued pension and other benefits	**679,177**	1,111,263
Other noncurrent liabilities	**56,761**	56,747
Total liabilities	**3,970,108**	4,195,624
Net assets:		
Accumulated other comprehensive loss:		
Pension liability	**(1,525,186)**	(1,485,615)
Derivative instruments	**(4,732)**	(12,384)
Total accumulated other comprehensive loss	**(1,529,918)**	(1,497,999)
Retained earnings	**5,010,824**	4,843,949
Total net assets	**3,480,906**	3,345,950
Total liabilities and net assets	**$ 7,451,014**	$ 7,541,574

See accompanying notes.

Army and Air Force Exchange Service

Statements of Earnings

(Dollars in thousands, unless otherwise noted)

	Years Ended January 30, 2010	Years Ended January 31, 2009
Net sales	**$ 8,157,519**	$ 8,421,671
Finance revenue	**230,309**	213,107
Concession income	**222,086**	206,223
Other operating income	**30,788**	35,579
Total revenue	**8,640,702**	8,876,580
Cost of sales and operating expenses:		
Cost of goods sold	**6,205,938**	6,514,148
Selling, general and administrative:		
Employee compensation and benefits	**1,139,552**	1,094,038
Depreciation and amortization	**263,631**	246,821
Other	**586,352**	553,890
Total selling, general and administrative	**1,989,535**	1,894,749
Interest expense	**46,558**	45,955
Bad debt expense (recoveries)	**6,084**	(28,067)
	8,248,115	8,426,785
Operating income	**392,587**	449,795
Other income (expense)	**35,887**	(73,505)
Net earnings	**$ 428,474**	$ 376,290

See accompanying notes.

Army and Air Force Exchange Service

Statements of Changes in Net Assets

(Dollars in thousands, unless otherwise noted)

	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Net Assets
Balance at February 2, 2008	$ 4,732,861	$ 112,166	$ 4,845,027
Adjustment for measurement date change from adoption of FASB 158	(703)	–	(703)
Adjusted balance at February 2, 2008	4,732,158	112,166	4,844,324
Net earnings	376,290	–	376,290
Change in funded status of pension and other postretirement benefit liabilities	–	(1,594,050)	(1,594,050)
Net change in fair value of derivative instruments	–	(16,115)	(16,115)
Comprehensive loss			(1,233,875)
Dividends to the Central Welfare Funds, Departments of the Army, the Air Force, the Navy, and the Marine Corps	(264,499)	–	(264,499)
Balance at January 31, 2009	**4,843,949**	**(1,497,999)**	**3,345,950**
Net earnings	**428,474**	**–**	**428,474**
Change in funded status of pension and other postretirement benefit liabilities	–	**(39,572)**	**(39,572)**
Net change in fair value of derivative instruments	–	**7,653**	**7,653**
Comprehensive income	**–**	**–**	**396,555**
Dividends to the Central Welfare Funds, Departments of the Army, the Air Force, the Navy, and the Marine Corps	**(261,599)**	**–**	**(261,599)**
Balance at January 30, 2010	**$ 5,010,824**	**$ (1,529,918)**	**$ 3,480,906**

See accompanying notes.

0910-1094875

Army and Air Force Exchange Service

Statements of Cash Flows

(Dollars in thousands, unless otherwise noted)

	Years Ended January 30, 2010	Years Ended January 31, 2009
Operating activities		
Net earnings	**$ 428,474**	$ 376,290
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	**284,262**	269,201
Loss on disposal of property and equipment	**963**	1,077
(Gain) loss on supplemental pension plan assets	**(28,342)**	82,394
Bad debt expense (income)	**6,084**	(28,067)
Changes in operating assets and liabilities:		
Accounts receivable	**(344,898)**	(208,862)
Merchandise inventories	**45,328**	(50,355)
Supplies and other current assets	**(8,180)**	2,765
Other assets	**1,068**	2,610
Prepaid pension assets	**(62,001)**	(73,399)
Supplemental plan assets	**(259)**	24,066
Accounts payable	**(13,916)**	(160,348)
Accrued salaries, separation pay and other employee benefits	**14,041**	(67,148)
Other current liabilities	**17,699**	(7,634)
Accrued pension and other benefits	**75,015**	(722)
Other noncurrent liabilities	**16**	287
Net cash provided by operating activities	**415,354**	162,155
Investing activities		
Purchases of property and equipment	**(477,010)**	(378,431)
Proceeds from the sale of property and equipment	**20,750**	12,392
Purchases of investments	**(29,427)**	(28,037)
Proceeds from the disposition of investments	**27,935**	29,084
Net cash used in investing activities	**(457,752)**	(364,992)
Financing activities		
Net proceeds from senior notes	**738,981**	–
Proceeds under line-of-credit agreements	**1,455,000**	1,949,000
Repayments under line-of-credit agreements	**(1,949,000)**	(1,465,000)
Change in cash overdraft	**2,437**	16,520
Payment of dividends	**(259,149)**	(275,622)
Net cash (used in) provided by financing activities	**(11,731)**	224,898
Net (decrease) increase in cash and cash equivalents	**(54,129)**	22,061
Cash and cash equivalents at beginning of year	**189,812**	167,751
Cash and cash equivalents at end of year	**$ 135,683**	$ 189,812

See accompanying notes.

(Dollars in thousands, unless otherwise noted)

1. Description of Business and Summary of Significant Accounting Policies

General

The Army and Air Force Exchange Service (AAFES or the Company) is a non-appropriated fund instrumentality (NAFI) of the United States (U.S.) and is organized as a joint major command of the U.S. Army and the U.S. Air Force. AAFES provides retail services to soldiers, airmen, and their families through a network of stores principally located in the U.S., Europe, the Pacific Rim, and the Middle East, primarily Iraq and Afghanistan in support of Operation Enduring Freedom and Operation Iraqi Freedom (OEF/OIF), substantially all of which are located on U.S. government installations. In addition to providing merchandise and services of necessity and convenience to authorized patrons at uniformly low prices, AAFES' mission is to generate reasonable earnings to supplement appropriated funds for the support of Army and Air Force morale, welfare, and recreation programs. AAFES maintains custody of and control over its non-appropriated funds. Funds that are not distributed as dividends are reinvested in AAFES' operations. AAFES is exempt from direct State taxation and from State regulatory laws, whose application would result in interference with the performance by AAFES of its assigned Federal functions. Such laws include licensing and price control statutes. AAFES summarizes its revenues on the basis of its customers' locations. Long-lived assets are comprised of property and equipment.

Net sales by geographic region are summarized below:

	Years Ended	
	January 30, 2010	**January 31, 2009**
Continental U.S.	**$ 5,138,985**	$ 5,300,672
Pacific Rim, including Alaska and Hawaii	**1,128,614**	1,140,998
Germany	**808,106**	825,906
OEF/OIF	**804,669**	839,392
Other countries	**277,145**	314,703
Total net sales	**$ 8,157,519**	$ 8,421,671

(Dollars in thousands, unless otherwise noted)

1. Description of Business and Summary of Significant Accounting Policies (continued)

Long-lived assets, net of accumulated depreciation and amortization, by geographic region are summarized below:

	Years Ended	
	January 30, 2010	**January 31, 2009**
Continental U.S.	**$ 1,574,780**	$ 1,418,197
Pacific Rim, including Alaska and Hawaii	**381,589**	364,696
Europe, primarily Germany	**294,730**	296,230
OEF/OIF	**7,715**	8,655
Total long-lived assets	**$ 2,258,814**	$ 2,087,778

AAFES utilizes accounting principles generally accepted in the United States applicable to "for profit" organizations, because of the nature of its commercial-type operations. AAFES' financial statements include the operations of all exchanges at Army and Air Force bases throughout the world.

In accordance with applicable Army and Air Force regulations, AAFES is not required to pay rent for the use of properties owned by the U.S. Government or utility costs associated with overseas exchanges. Permanent structures that are constructed by AAFES and paid for from AAFES funds become the property of the U.S. Government; however, AAFES has the right to occupy and use the structures. The structures cannot be used for other than AAFES' purposes without prior approval by the AAFES Commander and the relevant Department of the U.S. Government. As such, AAFES has included the cost of the structures on its balance sheet and depreciates the cost of the structures on a straight-line basis over their estimated useful lives. Services such as ocean transportation of merchandise to certain locations on U.S. chartered vessels and performance of administrative and supervisory functions by military personnel have been provided without charge to AAFES.

Management believes the value of transportation costs provided by the U.S. Government for AAFES materials shipped to and from overseas AAFES facilities totaled approximately $133,344 and $145,064 for fiscal years 2009 and 2008, respectively. In addition, OEF/OIF transportation costs of $147,805 and $146,078 were paid by the U.S. Government for fiscal years 2009 and 2008, respectively.

1. Description of Business and Summary of Significant Accounting Policies (continued)

Additionally, AAFES has received appropriations from the U.S. Government primarily related to costs incurred by AAFES in relation to OEF/OIF. Such appropriations are recorded when received. In fiscal 2009, AAFES received $79,814 in other appropriations in relation to OEF/OIF. Of this amount, $15,466 was recognized for inventory markdowns and shortages, $22,423 for personnel costs, $37,955 for in-theater transportation and $3,970 for other expenses. In fiscal 2008, AAFES received $98,742 in other appropriations related to OEF/OIF. Of this amount, $7,749 was recognized for inventory markdowns and shortages, $26,035 for personnel costs, $5,462 for other expenses, and $59,496 for in-theater transportation.

On May 13, 2005, the Department of Defense (DoD) announced the 2005 Base Realignment and Closure (BRAC) listing that impacts the existence of various military installations and personnel around the world. The goal of this global base realignment is to strategically position the military to accomplish future objectives. The list was formally approved by Congress and became law on November 9, 2005. Under this law, the DoD is required to complete these actions by September 15, 2011. As the realignments are still pending by the DoD, AAFES is unable to determine the impact on the Company's future operations. The net book value recorded for property at the BRAC locations was $8,329 as of January 30, 2010, compared to $11,658 as of January 31, 2009, and is being depreciated over the estimated remaining lives of the assets based on the expected dates of the closures.

In the event of closure of certain military bases around the world or a reduction in military forces, a decrease in sales at AAFES stores and a related decrease in the use of MILITARY STAR® Card credit due to the reduction of the customer base would likely occur.

Fiscal Year

AAFES' fiscal year-end is the Saturday nearest January 29. References to fiscal 2009 and fiscal 2008 herein are to the fiscal years ended January 30, 2010 and January 31, 2009, respectively.

Dividends

AAFES is required, under various agreements, to distribute a portion of each year's net earnings in the form of dividend payments to the Central Welfare Funds, Departments of the Army, the Air Force, the Navy, and the Marine Corps.

1. Description of Business and Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Pension assets include alternative investments in limited partnerships, real estate properties, private equity, timber, agriculture, and alternative debt, which do not have readily available market values. In these instances, management reviews and takes responsibility for assessing, concluding on, and recording the fair market values for alternative investments provided by the general partner, investment manager, or appraiser, as appropriate. Management believes estimated fair values have been reported in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, *Fair Value Measurements and Disclosures* (ASC 820), but may differ significantly from the values that would have been used had a ready market for these investments existed and such differences could be material.

Translation of Foreign Currencies

AAFES maintains foreign currencies only to the extent necessary to pay local current liabilities. Current liabilities are recorded daily and translated to U.S. dollars at "pegged" rates. Payments of current liabilities are recorded based on the "pegged" rate. At year-end, the current liabilities are translated from the pegged rates to the end-of-period market rates. The majority of such resulting gain or loss is recorded as foreign currency gain or loss with the remainder to the expense or asset account that gave rise to the current liability. The Company recognized a net loss on foreign currency of approximately $5,200 compared to a net gain of $9,700 for the years ended January 30, 2010 and January 31, 2009, respectively. In addition, the noncurrent liability for local national separation pay has been adjusted to end-of-period market rates.

Cash and Cash Equivalents

Cash equivalents represent cash on hand in stores, deposits in banks, and third-party credit card receivables. Cash and cash equivalents are carried at cost, which approximates fair value. All book overdraft balances have been reclassified to accounts payable.

1. Description of Business and Summary of Significant Accounting Policies (continued)

Investments in Debt Securities

Investments in debt securities have original maturities greater than 90 days. These investments are typically held to maturity, and are classified as such because the Company has the intent and ability to hold them to maturity. Held-to-maturity securities are carried at amortized cost.

Accounts Receivable

Customer accounts receivable are classified as current assets and include some amounts which are due after one year. Concentrations of credit risk, with respect to customer receivables, are limited due to the large number of customers comprising the Company's credit card base, and their dispersion throughout the world. The Company believes the carrying value of existing customer receivables is the best estimate of fair value.

The Company's accounts receivable balance includes $174,270 and $152,719 of receivables from the Marine Exchange (MCX) for Marine MILITARY STAR® Card outstanding balances and related processing fees as of January 30, 2010 and January 31, 2009, respectively.

As of January 30, 2010 and January 31, 2009, approximately $2,623,645 and $2,362,044 respectively, of the accounts receivable balance represents amounts due to AAFES under its in-house credit program, the MILITARY STAR® Card. MILITARY STAR® Card extends credit to eligible AAFES customers for the purchase of retail goods at AAFES stores worldwide. Minimum payments are calculated over a 36-month term.

Finance revenue is calculated based upon the customer account balance outstanding during the period after consideration of the applicable grace period, typically 30 days following the billing date. The finance rate charged is a variable interest rate calculated at a variable amount above the U.S. Prime Rate reported in *The Wall Street Journal*. The average finance rate charged for fiscal 2009 and 2008 was 9.99% and 10.20%, respectively. Finance charges are recorded unless an account balance has been outstanding for more than 180 days. The recorded investment in customer receivables past due 90 days or more and still accruing interest is approximately $51,263 and $87,282 as of January 30, 2010 and January 31, 2009, respectively.

1. Description of Business and Summary of Significant Accounting Policies (continued)

Accounts past due for 30 days or more are considered delinquent. Accounts delinquent for 180 days are submitted to the Collection Department. AAFES utilizes various means to collect past due accounts, as well as accounts written off, including some methods not available to other retail organizations. AAFES has agreements with other U.S. Government entities that allow AAFES to garnish wages of service personnel, as well as claim the debtors' future payments from such U.S. Government entities, including U.S. Treasury income tax refunds. Personal contact, external collection agencies, and letters to service personnel superiors are also used to pursue delinquent accounts.

A provision for possible credit loss is recorded each month related to AAFES' current credit card portfolio based on a percentage of total projected charge-offs that are considered uncollectible. Additionally, AAFES records a net receivable each month related to accounts previously written off based upon estimated ultimate recoveries. AAFES periodically evaluates the adequacy of the provision using such factors as prior account loss experience, changes in the volume of the account portfolio, changes in the estimates of anticipated recoveries on delinquent or written off balances, and changes in credit policy. It is reasonably possible that the amounts AAFES will ultimately recover on delinquent balances could differ materially in the near term from the amounts assumed in arriving at the allowance for doubtful accounts.

Collections on delinquent balances submitted to U.S. Government entities totaled approximately $131,769 and $170,365 in fiscal years 2009 and 2008, respectively. Increased collections in fiscal 2008 resulted from the Economic Stimulus Act of 2008, which allowed AAFES to garnish approximately $35,000 in additional disbursements made by the U.S. Government. No similar stimulus was provided in fiscal 2009. Decreased collections in fiscal 2009 resulted in bad debt expense of $6,084 compared to bad debt recoveries of $28,067 in fiscal 2008. Given the uncertainty with regard to anticipating future stimulus payments by the U.S. Government, the allowance for bad debt as of January 30, 2010, was calculated based on historical collection experience. Management will continue to refine its reserve policy as new customer information and trends develop.

(Dollars in thousands, unless otherwise noted)

1. Description of Business and Summary of Significant Accounting Policies (continued)

Merchandise Inventories

AAFES inventories are valued at the lower of cost or market, as determined primarily by the retail inventory method of accounting, except for distribution center inventories, which are based on the first-in, first-out inventory method. Certain warehousing, distribution, and procurement expenses are included in the cost that can be inventoried. For the years ended January 30, 2010 and January 31, 2009, $11,440 and $11,450 of these expenses were capitalized in merchandise inventory.

Buildings and Improvements

Buildings and improvements primarily represent permanent structures constructed by AAFES and owned by the U.S. Government. These assets are recorded at cost with depreciation provided using the straight-line method over the estimated useful lives of the assets. The useful lives are governed, to a large extent, by the deployment of Army and Air Force personnel and, to some extent, by the requirements of the Departments of the Army and the Air Force with respect to space occupied by AAFES. Buildings are generally depreciated over 30 years and improvements are depreciated from 7 to 15 years. AAFES loses its rights to buildings and improvements in the event of base closures and accelerates amortization of its assets when such closures are probable.

Fixtures and Equipment

Fixtures and equipment are carried at cost with depreciation provided using the straight-line method over the estimated useful lives of the assets.

Depreciable lives used are as follows:

Asset Type	Depreciable Life
Motor vehicles	5 to 10 years
Equipment	2 to 10 years
Software	3 to 7 years

At January 30, 2010, property and equipment included approximately $1,438,270 of fully depreciated assets that remain in use.

1. Description of Business and Summary of Significant Accounting Policies (continued)

Self-Insurance

AAFES acts as self-insurer for property, automobile, public liability, workers' compensation, comprehensive casualty losses, ocean marine, and other casualty losses. However, AAFES has commercial property insurance covering the buildings, contents, and inventories at certain locations. The provision for certain self-insurance losses is based on calculations performed by AAFES' independent actuarial consultants using loss development factors to estimate ultimate loss. The Company has established self-insurance reserves of $72,499 and $73,449 as of January 30, 2010 and January 31, 2009, respectively. Workers' compensation reserves have been discounted at a rate of 4.75% and property and liability reserves at a 3.50% rate for January 30, 2010. The reserves for both workers' compensation and property and liability were discounted based on a rate of 6.2% for January 31, 2009.

Separation Pay and Vacation Leave Accruals

Separation pay and vacation leave for local national employees in foreign countries are accrued as earned based upon the labor laws of host countries and upon agreements between the U.S. and foreign governments. In order to estimate this liability, the Company and its actuaries make certain assumptions, including the amounts considered recoverable from foreign governments under existing agreement terms. Actual results may vary from these assumptions. Additionally, the liability for vacation leave earned by U.S. citizens is accrued as earned.

Advertising Costs

Advertising costs are expensed in the period in which the advertising first occurs. AAFES cooperative advertising allowances are generally accounted for as a reduction in the purchase price of inventory.

Advertising expense was $70,729 and $75,908 for the years ended January 30, 2010 and January 31, 2009, respectively, and is included in selling, general, and administrative expenses.

1. Description of Business and Summary of Significant Accounting Policies (continued)

Revenue Recognition

Revenue from retail sales is recognized at the time of sale. Revenue from sales made under a layaway program is recognized upon delivery of the merchandise to the customer. Finance revenue includes finance charges and administrative fees on credit sales. Concession income includes fees charged to concessionaires based on a percentage of their sales and is recognized at the time of sale. Other operating income includes fees received from sources such as Western Union, sale of money orders, delivery and layaway services, POSA gift card, ESSO gas cards, backhaul and related services.

Income Taxes

AAFES is a non-appropriated fund instrumentality of the U.S. and, as such, is not subject to the payment of income taxes.

401(k)

The Company has a 401(k) voluntary savings and investment plan open to regular full- and part-time employees who meet certain minimum requirements. The employees can make voluntary contributions to the Plan not to exceed the lesser of 99% of eligible participant compensation or the applicable 401(k) maximum deferral contribution limit for the year.

Reclassifications

Certain reclassifications have been made to the accompanying fiscal 2008 financial statements to conform to the fiscal 2009 presentation.

Foreign Currency Hedging

As part of an overall risk management strategy, the Company uses foreign currency exchange contracts to hedge exposures to changes in foreign currency rates on AAFES payroll and foreign vendor obligations denominated in foreign currencies. These derivative instruments are accounted for in accordance with ASC 815, *Derivatives and Hedging* (ASC 815). ASC 815 requires that all derivative financial instruments be recognized in the financial statements and

1. Description of Business and Summary of Significant Accounting Policies (continued)

measured at fair value. Derivatives that are not hedges must be adjusted to fair value through earnings. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognized in net assets until the hedged item is recognized in earnings. Hedged items are reclassified from accumulated other comprehensive income (loss) and into earnings using the specific identification method. The Company's policy is that it does not speculate in hedging activities. The maximum length of time over which the Company is hedging its exposure to the variability of future cash flows for forecasted transactions is one year.

Fair Value Measurements

AAFES values financial instruments in accordance with ASC 820. Under ASC 820, fair value is considered to be the exchange price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. The fair value definition under ASC 820 focuses on an exit price, which is the price that would be received to sell an asset or paid to transfer a liability versus an entry price, which would be the price paid to acquire an asset or received to assume a liability.

Financial instruments that potentially subject AAFES to concentrations of credit risk consist principally of investments held by the Supplemental Plan and derivative financial instruments. The Company uses high credit quality counterparties when executing derivative transactions.

Recent Accounting Pronouncements

In March 2008, the FASB issued an amendment to ASC 815, *Derivatives and Hedging*, which requires enhanced disclosure about derivative instruments and hedging activities. The Company adopted the new standard on February 1, 2009. The standard supplements previously required disclosures with additional qualitative and quantitative information, including information regarding our use of derivatives and the effects derivative positions have on our earnings. See information in Note 5 to the Financial Statements for further disclosure required by this new standard.

1. Description of Business and Summary of Significant Accounting Policies (continued)

In December 2008, the FASB issued ASC 715-20, *Employers Disclosures about Postretirement Benefit Plan Assets* (ASC 715-20), an update to accounting standards regarding employers' disclosures about postretirement benefit plan assets, which requires additional disclosures for pension and other postretirement benefit plan assets. As pension and other postretirement benefit plan assets were not included within the scope of new accounting standards previously issued on fair value, the update requires employers to disclose information about fair value measurements of plan assets, including the investment policies and strategies for the major categories of plan assets, and significant concentrations of risk within plan assets. The accounting update is effective for fiscal years ending after December 15, 2009. As the update provides only disclosure requirements, the adoption of this standard did not have a material impact on the Company's results of operations, cash flows or financial position. See Note 7 to the Financial Statements for disclosures regarding the fair value of the Company's pension assets.

In June 2009, the Financial Accounting Standards Board, or FASB, issued the FASB Accounting Standards Codification (Codification). The Codification has become the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in accordance with U. S. generally accepted accounting principles (GAAP). All existing accounting standard documents are superseded by the Codification and any accounting literature not included in the Codification will not be authoritative. The Codification did not change or alter existing GAAP and, therefore, the Company's adoption of references to the Codification did not have an impact on the Company's financial position, results of operations or cash flows.

In January 2010, the FASB issued Accounting Standards Update (ASU) 2010-06, *Improving Disclosures about Fair Value Measurements.* The update amends existing accounting rules regarding fair value measurements and disclosures to add new requirements for disclosures related to transfers into and out of investment Levels 1 and 2, and separate disclosures about purchases, sales, issuances, and settlements relating to Level 3 investment measurements. It also clarifies existing fair value disclosures about the level of disaggregation, as well as inputs and valuation techniques used to measure fair value. The update is effective for the first reporting period beginning after December 15, 2009, except for the requirement to provide the Level 3 activity of purchases, sales, issuances, and settlements on a gross basis, which will be effective for fiscal years beginning after December 15, 2010. As this update only relates to financial statement disclosures, AAFES does not expect it will have an impact on our results of operations, cash flows or financial positions.

1. Description of Business and Summary of Significant Accounting Policies (continued)

Effective April 1, 2009, the Company adopted authoritative guidance issued by the FASB on subsequent events, which establishes general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. This guidance also requires entities to disclose the date through which subsequent events were evaluated as well as the rationale for why that date was selected. This disclosure should alert all users of financial statements that subsequent events have not been evaluated after the date set in the financial statements being presented. This guidance is effective for periods ending after June 15, 2009. The adoption did not have a material impact on the financial statements other than disclosure. AAFES has evaluated subsequent events through the issuance date of the financial statements on May 12, 2010.

2. Investments in Debt Securities

As of January 30, 2010, the Company held an investment carried at $8,300, which matures in January 2012, in support of non-German, Local National separation pay. This investment is classified as "held-to-maturity" in accordance with ASC 320-10, *Investments – Debt and Equity Securities* (ASC 720-10), and is classified on the balance sheet in long-term investments and supplemental plan assets.

As of January 31, 2009, the Company held a €15,000 (approximately $19,737) German government security to support the liability for German Local National separation pay, which was classified as and included in short-term investments on the balance sheet. In September 2009 this bond matured and a new bond, valued at €15,000 (approximately $21,482), was purchased. The new bond is due to mature on December 10, 2010, is valued at $21,127 as of January 30, 2010, and is classified as a short-term investment on the balance sheet.

3. Fair Value Measurements

As prescribed by ASC 820, the fair value of financial assets and liabilities was based on the following fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 inputs—unadjusted quoted prices in active markets for identical assets or liabilities to which the Company has access. An active market for the asset or liability is one in which transactions for the asset or liability occurs with sufficient frequency and volume to provide ongoing pricing information.

(Dollars in thousands, unless otherwise noted)

3. Fair Value Measurements (continued)

Level 2 inputs—significant inputs other than quoted market prices included in Level 1 that are observable, either directly or indirectly, for the asset or liability. Level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest rate curves and yield curves observable at commonly quoted intervals, volatilities, credit risk and default rates.

Level 3 inputs—unobservable inputs for the asset or liability.

The following table sets forth by level, within the fair value hierarchy, the Company's assets and liabilities that are measured at fair value as of January 30, 2010 and January 31, 2009:

	Assets at Fair Value as of January 30, 2010			
	Total	**Level 1**	**Level 2**	**Level 3**
Assets[1]:				
Cash and equivalents	$ 40	$ 40	$ –	$ –
Equity securities[3]:				
Collective investment funds	$ 13,012	$ –	$ 13,012	$ –
Total assets	$ 13,052	$ 40	$ 13,012	$ –
Liabilities[2]:				
Foreign currency derivative liabilities	(4,732)	–	(4,732)	–
Total liabilities	$ (4,732)	$ –	$ (4,732)	$ –

(Dollars in thousands, unless otherwise noted)

3. Fair Value Measurements (continued)

	Assets at Fair Value as of January 31, 2009			
	Total	Level 1	Level 2	Level 3
Assets[1]:				
Cash and equivalents	$ 1,381	$ 1,381	$ –	$ –
Equity securities[3]:				
Common and preferred stock	56,560	56,560	–	–
Common or collective trusts	39,076	–	39,076	–
Limited partnerships	11,813	–	92	11,721
Debt securities[3]:				
Government bonds	30,725	30,725	–	–
Corporate debt	19,747	19,747	–	–
Asset-backed securities	23,511	23,511	–	–
Common or collective trusts	3,123	–	3,123	–
Limited partnerships	14,374	–	–	14,374
Real estate and commodities[3]:				
Common and preferred stock	3,396	3,396	–	–
Common or collective trusts	38,787	–	3,674	35,113
Limited partnerships	7,985	–	–	7,985
Total assets	$ 250,478	$ 135,320	$ 45,965	$ 69,193
Liabilities[2]:				
Foreign currency derivative liabilities	$ (12,384)	$ –	$ (12,384)	$ –
Total liabilities	$ (12,384)	$ –	$ (12,384)	$ –

(1) Supplemental Plan assets are included in Long-term investments and Supplemental Plan assets on the balance sheet.

(2) Derivative liabilities are included on the balance sheet in Accounts Payable and Accrued salaries, separation pay, and other employee benefits.

(3) Investments held by the Supplemental Plan are consistent with those held by the Basic Plan. See Note 7 for further description of these assets.

The Company holds investments related to the Supplemental Plan totaling $13,052 and $250,478 at January 30, 2010 and January 31, 2009, respectively. Supplemental Plan assets are classified as trading securities since gains and losses from these investments are intended to offset the cost of the Supplemental Plan. Net income on trading securities was $28,342 in fiscal 2009 and a net loss on trading securities of $91,857 was recorded in fiscal 2008. The cost of securities sold is determined primarily on a specific identification method. (Refer to Note 7 for further discussion of the Supplemental Plan, and refer to Note 5 for further discussion of the Company's derivative positions.)

(Dollars in thousands, unless otherwise noted)

3. Fair Value Measurements (continued)

Cash and cash equivalents, trade and other accounts receivable, accounts payable, and accrued liabilities are reflected in the consolidated balance sheet at cost, which approximates fair value due to the short-term nature of these instruments. The fair value of our debt is disclosed in Note 4. The table below sets forth a summary of changes in the fair value of the Company's Level 3 assets for the years ended January 30, 2010 and January 31, 2009:

	Year Ended January 30, 2010		
	Equity Securities	**Debt Securities**	**Real Estate/ Commodities**
Balance, beginning of year	$ 11,721	$ 14,374	$ 43,098
Realized gains (losses)	(29)	–	749
Unrealized gains (losses)	767	(2,843)	(4,987)
Net purchases, sales, issuances and settlements	(46)	–	(532)
Aggregation transfers[1]	(12,413)	(11,531)	(38,328)
Balance, end of year	$ –	$ –	$ –

(1) Refer to Note 7 for discussion of aggregation transfers.

	Year Ended January 31, 2009		
	Equity Securities	**Debt Securities**	**Real Estate/ Commodities**
Balance, beginning of year	$ 8,230	$ 14,212	$ 49,968
Realized gains (losses)	194	–	93
Unrealized gains (losses)	(765)	(3,838)	(2,189)
Net purchases, sales, issuances and settlements	4,062	4,000	(4,774)
Balance, end of year	$ 11,721	$ 14,374	$ 43,098

(Dollars in thousands, unless otherwise noted)

3. Fair Value Measurements (continued)

The allocation of Supplemental Plan assets at January 30, 2010 and January 31, 2009, by asset category, is as follows:

	2009	2008
Domestic equity securities	**97%**	25%
International equity securities	–	9
Emerging market equity securities	–	5
Investment grade fixed income	**3**	21
High yield fixed income	–	6
Treasury inflation protected securities	–	10
Real estate–private	–	7
Real estate–public	–	1
Private equity	–	5
Commodities	–	7
Alternative debt	–	4
Total	**100%**	100%

4. Indebtedness

Syndicated Lines of Credit

As of January 30, 2010, AAFES has an unsecured, revolving line of credit that is facilitated by a 12-bank syndicate led by Wells Fargo/Wachovia aggregating to $750,000. This agreement expires in December 2011. There was $100,000 outstanding under this line of credit at January 30, 2010. AAFES also has an unsecured, multiyear revolving credit line facilitated by a 15-bank syndicate led by JPMorgan Chase aggregating $755,000. This agreement expires in October 2012. At January 30, 2010, $150,000 was outstanding on this line of credit.

Uncommitted Lines of Credit

As of January 30, 2010, AAFES maintains two uncommitted lines of credit aggregating to approximately $1,450,000, one with JPMorgan Chase, and the other with Army Family and Morale, Welfare and Recreation Command (Army FMWRC), a separate NAFI. Borrowings under these lines of credit were $1,205,000 at January 30, 2010. While both of these lines are open ended, the outstanding balances under these lines have various maturity dates, with the latest being May 2010.

(Dollars in thousands, unless otherwise noted)

4. Indebtedness (continued)

Borrowings under all lines of credit, both committed and uncommitted, bear interest rates ranging from 0.36% to 1.65%. The average interest rate under these lines of credit was 1.46% for the year ended January 30, 2010.

Senior Notes

In June 2009, AAFES completed a $650,000 offering of debt in a private placement. This offering provided AAFES with $650,000 in fixed-rate, committed senior notes (the "Series A, B, and C senior notes"), which were issued in three tranches.

In October 2009, AAFES completed another private placement debt offering of $90,000 in senior notes (the "2024 senior notes"), which comprise a 15-year amortizing principal. As of January 30, 2010, these senior notes have a total remaining obligation of $88,981.

Debt obligations as of January 30, 2010 and January 31, 2009, consisted of the following:

Outstanding debt principal balances:	**2009**	**2008**
Wachovia revolving line of credit, expiring 2011	**$ 100,000**	$ 700,000
JPMorgan Chase revolving line of credit, expiring 2012	**150,000**	265,000
JPMorgan Chase uncommitted line of credit	**1,005,000**	884,000
Citibank uncommitted line of credit	**–**	100,000
Army FMWRC uncommitted line of credit	**200,000**	–
5.24% series A senior notes due 2012	**150,000**	–
5.47% series B senior notes due 2013	**150,000**	–
5.74% series C senior notes due 2014	**350,000**	–
4.95% senior notes due 2024	**88,981**	–
Total debt obligations	**2,193,981**	1,949,000
Current maturities	**(1,459,202)**	–
Total long-term debt obligations	**$ 734,779**	$ 1,949,000

Based on the short-term nature of the Company's line of credit borrowings, AAFES believes that the carrying values of amounts outstanding under the line-of-credit agreements approximate fair value given the term of the debt and floating interest rates. The estimated aggregate fair value for the senior notes (A–C) is $772,000 as of January 30, 2010, and the estimated fair value of the 2024 senior notes is $89,000. Fair value is calculated using a discounted cash flow analysis with estimated interest rates offered for notes with similar terms and maturities.

4. Indebtedness (continued)

Cash paid for interest for fiscal years 2009 and 2008 was approximately $45,954 and $49,322, respectively. AAFES has complied with all financial and non-financial covenants per loan agreements as of January 30, 2010.

Principal maturities of debt obligations as of January 30, 2010, are as follows (in thousands):

2010	$ 1,459,202
2011	4,415
2012	154,639
2013	154,874
2014	355,121
Thereafter	65,730
	$ 2,193,981

5. Derivative Financial Instruments

Forward and option collar foreign exchange contracts are used primarily to hedge the risk of the Company's Euro-denominated payroll and foreign vendor obligations against adverse changes in foreign currency exchange rates. Under the foreign exchange contracts, the Company agrees to pay an amount equal to a specified exchange rate multiplied by a Euro notional principal amount, and to receive in return an amount equal to a specified monthly pegged exchange rate multiplied by the same Euro notional principal amount. No other cash payments are made under the contracts, and the contracts cannot be terminated. Under the option collar contracts (effectively the simultaneous purchase of a put and call option for the same notional amount and maturity, with the put being the floor strike rate and the call being the ceiling strike rate) the user maintains full protection against adverse movements, but gains due to favorable exchange rate moves are limited to the strike price of the sold option.

The Company has designated the forward and option collar foreign exchange contracts as cash flow hedges of its exposure to changes in its functional-currency-equivalent cash flows on the associated payroll and foreign vendor obligations. Accordingly, the changes in the fair value of the Company's forward and option collar foreign exchange contracts are recorded in the Company's balance sheet as an asset or liability and in net assets (as a component of accumulated other comprehensive income (loss). As the notional amounts and terms of each

(Dollars in thousands, unless otherwise noted)

5. Derivative Financial Instruments (continued)

forward and option collar foreign exchange contract match those of its liability counterpart at maturity, any ineffectiveness is immaterial in the foreign exchange contracts.

Upon expiration of the hedge contracts, the amount of the hedged item that affects earnings is reclassified from accumulated other comprehensive income (loss).

As of January 30, 2010, the Company had various foreign exchange contracts (forwards and option collars) outstanding related to approximately $181,690 (€129,000) of its forecasted payroll and inventory purchase liabilities. As of January 30, 2010, the notional value of the outstanding forward contracts (€31,000) was $43,662 with a corresponding unrecognized loss of $618. The notional value of outstanding option collar contracts (€98,000) was $138,028, with a corresponding unrecognized loss of $4,114. The net unrecognized loss of $4,732 is included in accrued salaries, separation pay and other benefits and accounts payable on the accompanying balance sheet and is included as a component of accumulated other comprehensive income (loss). The balance of $4,732 in accumulated other comprehensive loss is expected to be reclassified into earnings within the next 12 months. In addition, the Company has recognized approximately $9 in losses on foreign currency hedge transactions during fiscal 2009.

Unrealized gains and losses on foreign exchange hedges that are included in accumulated other comprehensive loss are recognized into earnings as the related payroll expenses are paid or the related inventory is purchased.

	Derivative Assets (Liabilities)		
		Fair Value	
	Balance Sheet Location	**January 30, 2010**	**January 31, 2009**
Derivatives Designated as hedging instruments			
Foreign currency exchange contracts	Accounts payable	**$ (3,549)**	$ (9,288)
	Accrued salaries, separation pay and other employee benefits	**(1,183)**	(3,096)
Total derivatives designated as hedging instruments		**$ (4,732)**	$ (12,384)

Reclassifications from Accumulated OCI are recognized in selling, general and administrative other expense in the Statements of Earnings.

(Dollars in thousands, unless otherwise noted)

6. Lease Obligations

The Company's operating lease commitments primarily include real estate and information technology leases. The Company recorded rent expense of $21,142 and $17,488 for the fiscal years ended January 30, 2010 and January 31, 2009, respectively. The following is a schedule, by year, of the future minimum rental payments required under all noncancellable leases as of January 30, 2010:

2010	$	25,003
2011		13,036
2012		5,608
2013		4,144
2014		204
Thereafter		447
Total	$	48,442

7. Benefit Plans

AAFES has a defined benefit pension plan, the Retirement Annuity Plan (the Basic Plan), covering regular full-time civilian employees of the Company who are citizens or residents of the U.S. In addition, a noncontributory supplemental deferred compensation plan (the Supplemental Plan) provides for selected benefits to employees in the Executive Management Program. AAFES' policy is to annually fund actuarially determined postretirement expense unless the respective plan is fully funded or unless an asset-liability model has shown the respective plan will likely become fully funded even in the absence of future contributions. The benefits are based on years of service and the employees' highest three-year average compensation. Assets of the plans consist primarily of marketable debt and equity securities.

In addition to AAFES' pension plan, certain medical and dental (health care) and life insurance benefits are also provided to retired employees through the Postretirement Medical/Dental (PRM) and Life Insurance (Other Postretirement) plans for employees of AAFES. All regular full-time U.S. civilian employees who are paid on the U.S. dollar payroll may become eligible for these benefits if they satisfy eligibility requirements during their working lives. AAFES' policy is to annually fund actuarially determined postretirement expense unless the respective plan is fully funded or unless an asset-liability model has shown the respective plan will likely become fully funded, even in the absence of future contributions.

7. Benefit Plans (continued)

AAFES also provides certain life insurance, disability, and other related postemployment benefits for active employees. Benefits are paid from a VEBA trust maintained by AAFES and to which AAFES contributes each year. Prior to fiscal 2009, trust assets were deemed sufficient to cover estimated medical, dental, and postemployment liabilities. However, in fiscal 2009, AAFES determined that estimated liabilities exceeded trust asset amounts and recorded a net liability at January 30, 2010 of approximately $16,169. The effect to prior periods was deemed to be immaterial.

In addition, the Company provides a noncontributory defined benefit pension plan to its employees in the United Kingdom (UK Plan). AAFES also provides postemployment benefits through its Local National benefit plans to employees in Germany, Japan, Okinawa, Azores, Italy, and Turkey.

AAFES measures the cost of the its pension plans and other benefit plans in accordance with ASC 715 (formerly Statement of Financial Accounting Standards No. 87, *Employers' Accounting for Pensions* (SFAS 87), and Statement of Financial Accounting Standards No. 106, *Employers' Accounting for Post-retirement Benefits Other than Pensions* (SFAS 106) as amended by SFAS 158). In addition, assets of the Supplemental Plan do not qualify as plan assets as defined in ASC 715 and, as a result, are accounted for in accordance with ASC 320 (formerly Statement of Financial Accounting Standards No. 115, *Accounting for Certain Investments in Debt and Equity Securities* (SFAS 115)).

In fiscal 2008, in accordance with ASC 715-30, the Company changed the measurement date of its defined benefit and other postretirement benefits from December 31 to the Company's fiscal year-end date, January 31, 2009. The adoption of the measurements of SFAS 158 resulted in a net increase to the projected benefit obligation of $32,000 and a net decrease to retained earnings of $703.

Aggregation

In December 1997, AAFES approved a proposal to: (1) transfer accumulated plan benefit obligations related to participants in the Supplemental Plan, to the extent such benefits are limited under Internal Revenue Code 415 (IRC Section 415) to the Basic Plan and fund such obligations using the Basic Plan assets, (2) retain sufficient assets in the Supplemental Plan to make benefit payments in excess of IRC Section 415 limits, and (3) transfer residual assets from

7. Benefit Plans (continued)

the Supplemental Plan to the Postretirement Medical/Dental and Life Insurance Plan for Employees of the Army and Air Force Exchange Service (Postretirement Plan), collectively referred to as "aggregation". This proposal was approved by the Internal Revenue Service (IRS) on July 23, 1998.

The proposal included an amendment to allow the Supplemental Plan to utilize its assets to pay postretirement medical benefits in addition to the pension benefits provided by the Supplemental Plan related to eligible employees' incomes in excess of IRC Section 415 limits. In addition, the Basic Plan will pay benefits to the participants who were previously provided for under the Supplemental Plan up to the IRC Section 415 limits. AAFES obtained a private letter ruling from the IRS on August 8, 2000, that concluded the qualification of the Plan is not affected by the proposed change. AAFES notified the Assistant Undersecretary of Defense, the Honorable Charles Abell, in May 2001 of AAFES' intention to proceed with the aggregation. On May 31, 2001, the Assistant Undersecretary of Defense notified AAFES that aggregation could not be implemented until such time that the Department of Defense (DoD) Office of General Counsel could review the documents provided.

Effective July 1, 2009, the aggregation plan was approved by DoD and was commenced by AAFES, whereas AAFES transferred approximately $364 million in projected benefit obligations of the Supplemental Plan to the Basic Plan. Additionally, AAFES transferred approximately $245 million in assets of the Supplemental Plan to the Postretirement Plan. The transfer of assets created an actuarial prepayment equivalent to the value of the assets transferred to the Postretirement Plan. Accordingly, the Company intends to amortize this prepayment as a credit towards its annual funding policy evenly over nine years. As of July 1, 2009, $12 million in assets and accumulated plan benefit obligations remained in the Supplemental Plan.

7. Benefit Plans (continued)

The following tables provide a reconciliation of the changes in the plans' benefit obligations and fair value of assets for the years ended January 30, 2010 and January 31, 2009. Amounts are stated in millions.

	Pension Benefits				Other Benefits			
	The Basic Plan		Supplemental Plan		Postretirement		Foreign Plans	
	2009	2008	2009	2008	2009	2008	2009	2008
Change in projected benefit obligations (PBO)								
PBO at prior measurement date	**$ 2,442**	$ 2,572	**$ 352**	$ 355	**$ 1,578**	$ 1,559	**$ 86**	$ 100
Service cost	**66**	68	**1**	3	**20**	21	**4**	4
Interest cost	**174**	167	**10**	24	**106**	97	**4**	4
Plan participants' contributions	**4**	4	**–**	–	**–**	–	**–**	–
Change in measurement date	**–**	20	**–**	2	**–**	10	**–**	–
Aggregation	**364**	–	**(364)**	–	**–**	–	**–**	–
Actuarial gain (loss)	**270**	(184)	**29**	(4)	**171**	(34)	**11**	(9)
Foreign exchange impact	**–**	–	**–**	–	**–**	–	**5**	(8)
Benefits paid	**(186)**	(184)	**(21)**	(28)	**(72)**	(75)	**(2)**	(5)
Administrative expenses paid	**(15)**	(21)	**–**	–	**(5)**	–	**–**	–
PBO at current measurement date	**$ 3,119**	$ 2,442	**$ 7**	$ 352	**$ 1,798**	$ 1,578	**$ 108**	$ 86

	Pension Benefits				Other Benefits			
	The Basic Plan		Supplemental Plan		Postretirement		Foreign Plans	
	2009	2008	2009	2008	2009	2008	2009	2008
Change in plan assets								
Fair value of assets at prior measurement date	**$ 2,836**	$ 4,087	**$ 250**	$ 373	**$ 787**	$ 1,161	**$ 20**	$ 36
Actual return on assets	**602**	(1,051)	**29**	(92)	**205**	(362)	**5**	(8)
Employer contributions	–	–	–	–	**14**	63	**1**	2
Plan participants' contributions	**4**	4	–	–	–	–	–	–
Aggregation	–	–	**(245)**	–	**245**	–	–	–
Benefits paid	**(186)**	(183)	**(21)**	(29)	**(72)**	(75)	**(2)**	(2)
Administrative expenses paid/foreign exchange impact	**(15)**	(21)	–	(2)	**(5)**	–	**3**	(8)
Fair value of assets at current measurement date	**$ 3,241**	$ 2,836	**$ 13**	$ 250	**$ 1,174**	$ 787	**$ 27**	$ 20

7. Benefit Plans (continued)

The following tables reflect a reconciliation of funded status and amounts recognized in the balance sheets as of January 30, 2010 and January 31, 2009. Amounts are stated in millions.

	Pension Benefits				Other Benefits			
	The Basic Plan		Supplemental Plan		Postretirement		Foreign Plans	
	2009	**2008**	**2009**	**2008**	**2009**	**2008**	**2009**	**2008**
Reconciliation of funded status								
Funded status at current measurement date	**$ 122**	$ 394	**$ (7)**	$ (352)	**$ (624)**	$ (791)	**$ (81)**	$ (66)
Contribution after measurement date and on or before fiscal year-end	–	–	–	–	–	–	–	–
Funded status at fiscal year-end	**$ 122**	$ 394	**$ (7)**	$ (352)	**$ (624)**	$ (791)	**$ (81)**	$ (66)
Amounts recognized in the balance sheets								
Prepaid pension asset	**$ 122**	$ 394	**$ –**	$ –	**$ –**	$ –	**$ –**	$ –
Other current liabilities	–	–	–	27	**40**	66	**6**	6
Accrued pension and other benefits liability	–	–	**7**	325	**584**	725	**75**	60
Accumulated other comprehensive (loss) income	**$ (664)**	$ (662)	**$ (10)**	$ (13)	**$ (822)**	$ (791)	**$ (28)**	$ (19)

A summary of the components of net periodic benefit cost (income) for the benefit plans is as follows for the years ended January 30, 2010 and January 31, 2009:

	Pension Benefits				Other Benefits			
	The Basic Plan		Supplemental Plan		Postretirement		Foreign Plans	
	2009	**2008**	**2009**	**2008**	**2009**	**2008**	**2009**	**2008**
Net periodic cost								
Service cost	**$ 66**	$ 68	**$ 1**	$ 3	**$ 20**	$ 21	**$ 4**	$ 4
Interest cost	**174**	167	**10**	24	**106**	97	**4**	4
Expected return on assets	**(302)**	(308)	–	–	**(100)**	(91)	**(2)**	(2)
Prior service cost amortization	–	–	–	–	**(4)**	(4)	–	–
Net loss amortization	–	–	–	1	**40**	29	**1**	1
Net periodic benefit (income) cost	**$ (62)**	$ (73)	**$ 11**	$ 28	**$ 62**	$ 52	**$ 7**	$ 7

7. Benefit Plans (continued)

Information for benefit plans with an accumulated benefit obligation in excess of plan assets (dollars in millions):

	Pension Benefits Supplemental Plan		Other Benefits Postretirement		Pension Benefits Foreign Plans	
	2009	**2008**	**2009**	**2008**	**2009**	**2008**
Projected benefit obligation	**$ 7**	$ 352	**$ 1,798**	$ 1,578	**$ 108**	$ 86
Accumulated benefit obligation	**7**	350	**1,798**	1,578	**87**	72
Fair value of plan assets	**–**	–	**1,174**	787	**27**	20

Amounts included in accumulated other comprehensive income (loss) for all plans at January 30, 2010, consist of net actuarial losses of $1,537,658 and a net prior service credit of $12,471. Amortization of these amounts expected to be recognized in fiscal year 2010 is $55,160 for net actuarial losses and $4,063 for prior service cost.

(Dollars in thousands, unless otherwise noted)

7. Benefit Plans (continued)

Actuarial Assumptions

Actuarial weighted-average assumptions used in determining plan liabilities are as follows:

	Pension Benefits The Plan		Pension Benefits Supplemental Plan		Other Benefits Postretirement	
	2009	**2008**	**2009**	**2008**	**2009**	**2008**
Assumptions used to determine expense:						
Discount rate	**6.75%**	6.50%	**6.75%**	6.50%	**6.75%**	6.50%
Long-term rate of return on assets	**8.25%**	8.25%	–	–	**8.75%**	8.75%
Compensation increase rate	**5.50%**	5.50%	**5.50%**	5.50%	**5.50%**	5.50%
Assumptions used at disclosure:						
Discount rate	**6.00%**	6.75%	**6.00%**	6.75%	**6.00%**	6.75%
Compensation increase rate	**5.50%**	5.50%	**5.50%**	5.50%	**5.50%**	5.50%

	Other Benefits UK Plan		Other Benefits Local National Plan	
	2009	**2008**	**2009**	**2008**
Assumptions used to determine expense:				
Discount rate	**7.00%**	5.80%	**4.12%**	3.68%
Long-term rate of return on assets	**6.90%**	6.90%	**–**	–
Compensation increase rate	**4.50%**	4.80%	**2.69%**	2.71%
Assumptions used at disclosure:				
Discount rate	**5.65%**	7.00%	**3.26%**	3.71%
Compensation increase rate	**4.50%**	4.50%	**2.58%**	2.57%

Actuarial assumptions are based on management's best estimates and judgment. AAFES reassesses its benefit plan assumptions on a regular basis. The expected rate of return for the pension plans represents the average rate of return to be earned on the plan assets over the period that the benefits included in the benefit obligation are to be paid. In developing the expected rate of return, AAFES considers the impact of long-term compound annualized returns on the plan assets.

7. Benefit Plans (continued)

Pension Plan Assets

In December 2008, the FASB issued ASC 715-20, *Employers Disclosures about Postretirement Benefit Plan Assets* (ASC 715-20), requiring companies to provide additional disclosures about plan assets of a defined benefit or other postretirement plan. The additional disclosure requirements under ASC 715-20 include expanded disclosure about an entity's investment policies and strategies, the categories of plan assets, concentrations of credit risk, and fair value measurements of plan assets. This standard is effective for fiscal years ending after December 15, 2009, and the Company adopted these provisions in fiscal 2009. The adoption did not have an impact on the company's financial position, results of operations, or cash flows.

Equity securities are diversified across various industries and are comprised of common and preferred stocks of U.S. and international companies and equity positions in privately held companies controlled through limited partnerships. Publicly traded corporate equity securities are valued at the last reported sale price on the last business day of the year of the plans. The estimated fair value of the investments in the collective investment funds represents the underlying net asset value of the shares or units of such funds as determined by the issuer. Limited partnerships are valued at the plan's proportionate share of the estimated fair value of the underlying net assets as determined by the general partners. The limited partnerships are classified as Level 3 investments.

Debt securities are comprised of corporate bonds, government securities, and asset backed or collective investment funds and limited partnerships with underlying debt securities. Corporate bonds primarily consist of investment-grade rated bonds and notes, of which no significant concentration exists in any one rating category or industry. Government securities include inflation-indexed U.S. treasury notes and U.S. government bonds. Asset-backed securities are publicly traded securities with coupon payments based on the performance of the underlying assets. Corporate bonds, government securities, and asset-backed securities are valued at the last reported sale price. The estimated fair value of the investments in the collective investment funds represents the underlying net asset value of the shares or units of such funds as determined by the issuer. Limited partnerships are valued at the plan's proportionate share of the estimated fair value of the underlying net assets as determined by the general partners. The limited partnerships are classified as Level 3 investments.

7. Benefit Plans (continued)

Real estate and commodities are comprised of investments whose underlying value is based on real estate or commodities. Publicly traded securities are equity shares in Real Estate Investment Trusts (REITs) and valued at the last reported sale price. Collective investment funds with underlying investments in exchange traded positions are classified as Level 2 investments. Collective investment funds and limited partnerships with underlying investments in real estate are classified as Level 3 investments. The estimated fair value of the underlying real estate is based on the selling price of the property, income the property is expected to generate, and the market values of any commodities currently on the land.

Other investments consist primarily of investment contracts and are valued at the quoted price as determined by the issuer. Contracts classified as Level 2 assets are guaranteed an issuer with high creditworthiness. Contracts classified as Level 3 have valuations based on underlying assets with unobservable inputs.

AAFES' investment objectives for the pension plans are designed to generate asset returns that will enable the plans to meet their future benefit obligations. The precise amount for which these obligations will be settled depends on future events, including interest rates, salary increases, and the life expectancy of the plans' members. The obligations are estimated using actuarial assumptions, based on the current economic environment.

The pension plans seek to achieve total returns sufficient to meet expected future obligations, as well as returns greater than their policy benchmark reflecting the target weights of the asset classes used in their targeted strategic asset allocation. The plans' targeted strategic allocation to each asset class was determined through an asset-liability modeling study.

(Dollars in thousands, unless otherwise noted)

7. Benefit Plans (continued)

The following table sets forth the target allocations of plan assets:

	Pension Benefits The Plan		Other Benefits Postretirement Plan		Other Benefits UK Plan	
	2009	**2008**	**2009**	**2008**	**2009**	**2008**
Domestic equity securities	**17%**	25%	**22%**	25%	**26%**	26%
International equity securities	**12**	10	**16**	17	**35**	35
Emerging market equity securities	**5**	5	**5**	5	**4**	4
Investment grade fixed income	**21**	19	**12**	16	**35**	35
High yield fixed income	**10**	5	**10**	5	**–**	–
TIPS	**5**	9	**5**	5	**–**	–
Real estate–private	**8**	5	**8**	5	**–**	–
Real estate–public	**2**	2	**2**	2	**–**	–
Private equity	**10**	10	**10**	10	**–**	–
Commodities	**5**	5	**5**	5	**–**	–
Alternative debt	**5**	5	**5**	5	**–**	–
Total	**100%**	100%	**100%**	100%	**100%**	100%

AAFES' pension plans asset allocations at January 30, 2010 and January 31, 2009, by asset class category are as follows:

	Pension Benefits The Plan		Other Benefits Postretirement Plan		Other Benefits UK Plan	
	2009	**2008**	**2009**	**2008**	**2009**	**2008**
Domestic equity securities	**28%**	25%	**28%**	26%	**26%**	26%
International equity securities	**12**	9	**18**	16	**35**	35
Emerging market equity securities	**6**	5	**6**	5	**4**	4
Investment grade fixed income	**19**	23	**15**	19	**35**	35
High yield fixed income	**6**	5	**6**	6	**–**	–
TIPS	**8**	10	**6**	5	**–**	–
Real estate–private	**4**	6	**4**	7	**–**	–
Real estate–public	**2**	2	**2**	1	**–**	–
Private equity	**6**	6	**6**	6	**–**	–
Commodities	**5**	6	**6**	6	**–**	–
Alternative debt	**4**	3	**3**	3	**–**	–
Total	**100%**	100%	**100%**	100%	**100%**	100%

(Dollars in thousands, unless otherwise noted)

7. Benefit Plans (continued)

The following table sets forth by level, within the fair value hierarchy, the Company's plan assets and liabilities that are measured at fair value as of January 30, 2010:

	Benefit Plans			
	Total	Level 1 Quoted Prices in Active Markets	Level 2 Significant Observable Inputs	Level 3 Significant Unobservable Inputs
Cash	$ 22,402	$ 22,402	$ –	$ –
Equity securities:				
Common and preferred stock	1,304,857	1,304,857	–	–
Collective investment funds	762,863	–	762,863	–
Limited partnerships	254,953	–	–	254,953
Debt securities:				
Government bonds	368,070	368,070	–	–
Corporate debt	325,724	325,724	–	–
Asset-backed securities	135,265	135,265	–	–
Collective investment funds	385,754	–	385,754	–
Limited partnerships	207,946	–	9,274	198,672
Real estate and commodities:				
Common and preferred stock	78,536	78,536	–	–
Collective investment funds	460,686	–	69,428	391,258
Limited partnerships	104,827	–	–	104,827
Other	29,424	–	29,234	190
Total	$ 4,441,307	$ 2,234,854	$ 1,256,553	$ 949,900

(Dollars in thousands, unless otherwise noted)

7. Benefit Plans (continued)

Level 3 Gains and Losses

The table below sets forth a summary of changes in the fair value of the Plan's Level 3 assets for the year ended January 30, 2010:

	Year Ended January 30, 2010		
	Equity Securities	Debt Securities	Real Estate/ Commodities
Balance, beginning of year	$ 231,670	$ 121,700	$ 566,764
Realized gains (losses)	(3,571)	4,357	20,538
Unrealized gains (losses) relating to instruments still held at the reporting date	(7,426)	45,171	(123,117)
Net purchases, sales, issuances and settlements	21,867	15,913	(6,238)
Aggregation transfers	12,413	11,531	38,328
Balance, end of year	$ 254,953	$ 198,672	$ 496,275

Employer Contributions

AAFES expects to contribute approximately $418 to The Supplemental Plan and $39,632 to the other postretirement benefit plans in fiscal 2010.

(Dollars in thousands, unless otherwise noted)

7. Benefit Plans (continued)

Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

Fiscal Years	The Pension Plan	Supplemental Pension Plan	Other Postretirement	Foreign Plans
2010	$ 204,749	$ 418	$ 90,441	$ 7,609
2011	207,600	421	98,155	7,698
2012	210,935	426	104,363	7,411
2013	214,817	431	109,989	7,596
2014	219,730	441	114,651	6,922
2015–2019	1,172,878	2,327	625,529	35,769

Assumed Health Care Cost Trend Rates at January 30:

	2009	2008
Health care cost trend rate assumed for next year	**8.00%**	9.00%
Rate to which the cost trend rate is assumed to decline (ultimate trend rate)	**4.50%**	4.50%
Year that the rate reaches the ultimate trend rate	**2014**	2014

8. Dividends

AAFES is required, under various agreements, to distribute a portion of each year's net earnings before bonuses in the form of dividend payments to the Central Welfare Funds, Departments of the Army, the Air Force, the Navy, and the Marine Corps.

If dividends were paid on the pension income and realized and unrealized gains and losses recorded in accordance with ASC 715 and ASC 320, AAFES would be paying dividends to the Central Welfare Funds, Departments of the Army, the Air Force, the Navy, and the Marine Corps, on noncash amounts which would impact cash reserves used in the normal operation of the business. Accordingly, under the current dividend policy, these items are excluded from net

8. Dividends (continued)

earnings subject to dividends. Any other exclusion used in the calculation of net earnings subject to dividends must be approved by the Board.

AAFES' policy is to annually fund actuarially determined postretirement expense unless the plan is fully funded or unless an asset-liability model has shown the plan will likely become fully funded, even in the absence of future contributions. Therefore, each year, pension expense generally reduces the net earnings subject to dividends to the extent cash contributions have actually been made.

9. Commitments and Contingencies

The Company is a defendant in various lawsuits and claims. In the opinion of management, the amounts, if any, which might ultimately be paid in connection with settlement of the litigation would not have a material effect on the financial condition, results of operations, or cash flows of the Company.

10. Operation Enduring Freedom/Operation Iraqi Freedom (OEF/OIF)

On March 19, 2003, the United States declared war against Iraq. As a result, the Company increased its presence in Iraq, Qatar, Afghanistan and Kuwait from 12 stores as of February 1, 2003, to 124 stores as of January 30, 2010. The inventory balance in OEF/OIF has decreased from $112,691 at January 31, 2009, to $86,038 at January 30, 2010. Current conditions in Iraq and Afghanistan are uncertain. As a result, it is difficult to estimate the potential inventory that may be forfeited if the United States must quickly exit either country. Any related loss on inventory could adversely affect the Company's results of operations. Approximately $804,670 (9.9%) and $839,392 (10.0%) of the Company's net revenues in the fiscal years ended January 30, 2010 and January 31, 2009, respectively, were derived from sales to U.S. Troops stationed in OEF/OIF regions.

Any significant disruption or retreat from the locale directed by the United States military could have an adverse impact on the results of operations.

As a result of the lack of depository banks in the region, cash sales are deposited with United States Military Finance offices in the Middle East and are then reimbursed to the Company within 90 days. Receivables from Military Finance offices were $8,269 and $9,457 as of January 30, 2010 and January 31, 2009, respectively.

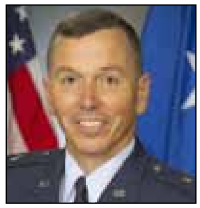
11. Post Allowance for Overseas Personnel

On March 21, 2008, AAFES received a letter from the Department of Defense confirming that U.S. citizens hired overseas in DOD NAFI positions from December 2001 to the present are eligible for a post allowance in accordance with DOD 1401.1-M, *Personnel Policy Manual for Non-appropriated Fund Instrumentalities,* and DOD 1400-.25-M, *DOD Civilian Personnel Manual.* Subchapter 1250 of DOD 1400.25-M states that employees who are U.S. citizens are eligible for post allowance unless they are part-time, intermittent, or family member summer/winter hire employees.

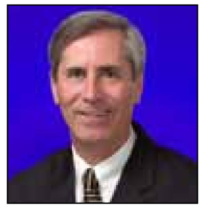
AAFES and certain other NAFIs did not previously pay this particular post allowance under the good faith interpretation that the post allowance was intended only for U.S. employees transferred to an overseas post. At February 2, 2008, AAFES recorded a charge for its best estimate of its obligation of $33,572. During fiscal 2008, the DOD issued final guidance on payments of the obligation. Individuals have six years to file a claim. The Company paid $27,290 in fiscal 2008 and $1,882 in fiscal 2009 in accordance with DOD guidelines. At January 30, 2010, the Company has a remaining obligation of $4,400 included in current liabilities and is based on its best estimate of claims remaining to be paid.

AAFES Leadership

U.S. Army
Maj. Gen.
Bruce Casella
Commander



U.S. Air Force
Brig. Gen.
Fran Hendricks
Deputy
Commander



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Officer

U.S. Army
Col.
Virgil Williams
Chief of Staff

U.S. Air Force
Chief Master
Sgt. Jeffry Helm
Assistant to the
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Maj. Gen. Bruce Casella, USA
Commander, Army and Air Force Exchange Service

Maj. Gen. Reuben D. Jones, USA
Commander, U.S. Army Family and MWR Command

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Edmundo A. Gonzales, SES
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Kathleen I. Ferguson, SES
Deputy Assistant Secretary of the Air Force
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Charles E. Milam, SES
Director, Air Force Services
(HQ USAF/A1S)

Joseph M. McDade, SES
Assistant Deputy Chief of Staff, G-1

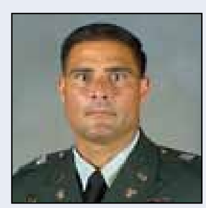
Brig. Gen. David E. Price, USAF
Director of Budget Operations, HQ USAF

Brig. Gen. John E. Seward, USA
Deputy Chief of Staff, HQ U.S. Army Pacific

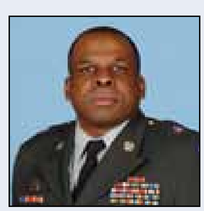
Brig. Gen. Karen E. Dyson, USA
Director, Operations & Support, Army Budget Office, OASA (FMC)

Regional Commanders

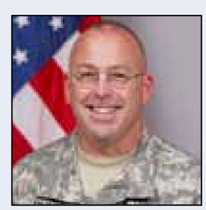
Col. Mark White
Pacific Region



Col. Chuck Salvo
Europe Region



Sgt. Maj.
James Pigford
Assistant to the
Commander



Sgt. Maj.
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