lululemon athletica inc.
Form 10-Q
December 06, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

(Mark One)
þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended October 28, 2018
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number 001-33608

lululemon athletica inc.
(Exact name of registrant as specified in its charter)

Delaware	20-3842867
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1818 Cornwall Avenue Vancouver, British Columbia	V6J 1C7
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code:
604-732-6124
Former name, former address and former fiscal year, if changed since last report:
N/A

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o
Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (of for such shorter period that the registrant was required to submit such files). Yes þ No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	þ	Accelerated filer	o
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller reporting company	o
Emerging growth company	o		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

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

At December 3, 2018, there were 122,627,574 shares of the registrant's common stock, par value $0.005 per share, outstanding.

Exchangeable and Special Voting Shares:

At December 3, 2018, there were outstanding 9,776,421 exchangeable shares of Lulu Canadian Holding, Inc., a wholly-owned subsidiary of the registrant. Exchangeable shares are exchangeable for an equal number of shares of the registrant's common stock.

In addition, at December 3, 2018, the registrant had outstanding 9,776,421 shares of special voting stock, through which the holders of exchangeable shares of Lulu Canadian Holding, Inc. may exercise their voting rights with respect to the registrant. The special voting stock and the registrant's common stock generally vote together as a single class on all matters on which the common stock is entitled to vote.

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PART I
FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
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CONSOLIDATED BALANCE SHEETS
(Unaudited; Amounts in thousands, except per share amounts)

	October 28, 2018	January 28, 2018
ASSETS		
Current assets		
Cash and cash equivalents	$703,607	$990,501
Accounts receivable	29,448	19,173
Inventories	495,991	329,562
Prepaid and receivable income taxes	76,593	48,948
Other prepaid expenses and other current assets	57,828	48,098
	1,363,467	1,436,282
Property and equipment, net	531,250	473,642
Goodwill and intangible assets, net	24,237	24,679
Deferred income tax assets	28,155	32,491
Other non-current assets	33,902	31,389
	$1,981,011	$1,998,483
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$153,140	$24,646
Accrued inventory liabilities	11,446	13,027
Accrued compensation and related expenses	85,446	70,141
Current income taxes payable	24,545	15,700
Unredeemed gift card liability	63,474	82,668
Other current liabilities	105,620	86,416
	443,671	292,598
Non-current income taxes payable	54,112	48,268
Deferred income tax liabilities	1,582	1,336
Other non-current liabilities	74,889	59,321
	574,254	401,523
Stockholders' equity		
Undesignated preferred stock, $0.01 par value: 5,000 shares authorized; none issued and outstanding	—	—
Exchangeable stock, no par value: 60,000 shares authorized; 9,776 and 9,781 issued and outstanding	—	—
Special voting stock, $0.000005 par value: 60,000 shares authorized; 9,776 and 9,781 issued and outstanding	—	—
Common stock, $0.005 par value: 400,000 shares authorized; 122,667 and 125,650 issued and outstanding	613	628
Additional paid-in capital	307,154	284,253
Retained earnings	1,310,452	1,455,002
Accumulated other comprehensive loss	(211,462)	(142,923)
	1,406,757	1,596,960
	$1,981,011	$1,998,483

See accompanying notes to the unaudited interim consolidated financial statements

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lululemon athletica inc.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(Unaudited; Amounts in thousands, except per share amounts)

	Quarter Ended		Three Quarters Ended	
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
Net revenue	$747,655	$619,018	$2,120,861	$1,720,379
Cost of goods sold	340,878	297,056	973,157	844,100
Gross profit	406,777	321,962	1,147,704	876,279
Selling, general and administrative expenses	270,874	215,367	773,288	640,032
Asset impairment and restructuring costs	—	21,007	—	36,524
Income from operations	135,903	85,588	374,416	199,723
Other income (expense), net	2,044	1,052	6,553	2,771
Income before income tax expense	137,947	86,640	380,969	202,494
Income tax expense	43,534	27,696	115,633	63,593
Net income	$94,413	$58,944	$265,336	$138,901
Other comprehensive (loss) income:				
Foreign currency translation adjustment	(7,318)	(31,018)	(68,539)	10,061
Comprehensive income	$87,095	$27,926	$196,797	$148,962
Basic earnings per share	$0.71	$0.44	$1.98	$1.02
Diluted earnings per share	$0.71	$0.43	$1.97	$1.02
Basic weighted-average number of shares outstanding	132,406	135,364	133,964	136,191
Diluted weighted-average number of shares outstanding	133,077	135,578	134,512	136,357

See accompanying notes to the unaudited interim consolidated financial statements

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lululemon athletica inc.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited; Amounts in thousands)

	Exchangeable Stock	Special Voting Stock		Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
	Shares	Shares	Par Value	Shares	Par Value				
Balance at January 28, 2018	9,781	9,781	$ —	125,650	$ 628	$ 284,253	$ 1,455,002	$ (142,923)	$ 1,596,960
Net income							265,336		265,336
Foreign currency translation adjustment								(68,539)	(68,539)
Common stock issued upon exchange of exchangeable shares	(5)	(5)	—	5	—	—			—
Stock-based compensation expense						18,616			18,616
Common stock issued upon settlement of stock-based compensation				524	3	17,254			17,257
Shares withheld related to net share settlement of stock-based compensation				(92)	(1)	(8,537)			(8,538)
Repurchase of common stock				(3,420)	(17)	(4,432)	(409,886)		(414,335)
Balance at October 28, 2018	9,776	9,776	$ —	122,667	$ 613	$ 307,154	$ 1,310,452	$ (211,462)	$ 1,406,757

See accompanying notes to the unaudited interim consolidated financial statements

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lululemon athletica inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited; Amounts in thousands)

	Three Quarters Ended	
	October 28, 2018	October 29, 2017
Cash flows from operating activities		
Net income	$ 265,336	$ 138,901
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	87,115	80,129
Deferred income taxes	2,382	(18,385)
Stock-based compensation expense	18,616	13,048
Asset impairment for ivivva restructuring	—	11,593
Settlement of derivatives not designated in a hedging relationship	(4,670)	4,178
Changes in operating assets and liabilities:		
Inventories	(177,890)	(95,475)
Prepaid and receivable income taxes	(27,645)	3,565
Other prepaid expenses and other current and non-current assets	(20,538)	(6,759)
Accounts payable	129,617	(11,141)
Accrued inventory liabilities	(392)	14,602
Accrued compensation and related expenses	18,009	6,579
Current income taxes payable	9,817	(26,420)
Unredeemed gift card liability	(17,827)	(18,272)
Non-current income taxes payable	5,844	—

Lease termination liabilities	(3,285)	12,164
Other current and non-current liabilities	32,387	23,002
Net cash provided by operating activities	316,876	131,309
Cash flows from investing activities		
Purchase of property and equipment	(156,746)	(107,128)
Settlement of net investment hedges	(8,397)	(4,599)
Other investing activities	(771)	(8,324)
Net cash used in investing activities	(165,914)	(120,051)
Cash flows from financing activities		
Proceeds from settlement of stock-based compensation	17,257	1,648
Taxes paid related to net share settlement of stock-based compensation	(8,538)	(3,086)
Repurchase of common stock	(414,335)	(99,269)
Other financing activities	(745)	—
Net cash used in financing activities	(406,361)	(100,707)
Effect of exchange rate changes on cash and cash equivalents	(31,495)	4,657
Decrease in cash and cash equivalents	(286,894)	(84,792)
Cash and cash equivalents, beginning of period	$ 990,501	$ 734,846
Cash and cash equivalents, end of period	$ 703,607	$ 650,054

See accompanying notes to the unaudited interim consolidated financial statements

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INDEX FOR NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

lululemon athletica inc.

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Nature of operations

lululemon athletica inc., a Delaware corporation ("lululemon" and, together with its subsidiaries unless the context otherwise requires, the "Company") is engaged in the design, distribution, and retail of healthy lifestyle inspired athletic apparel. The Company primarily conducts its business through company-operated stores and direct to consumer through e-commerce. It also generates net revenue from outlets, sales from temporary locations, sales to wholesale accounts, showrooms, warehouse sales, and license and supply arrangements. The Company operates stores in the United States, Canada, Australia, China, the United Kingdom, New Zealand, Germany, Japan, South Korea, Singapore, France, Ireland, Sweden, and Switzerland. There were 426 and 404 company-operated stores in operation as of October 28, 2018 and January 28, 2018, respectively.

Basis of presentation

The unaudited interim consolidated financial statements as of October 28, 2018 and for the quarters and three quarters ended October 28, 2018 and October 29, 2017 are presented in United States dollars and have been prepared by the Company under the rules and regulations of the Securities and Exchange Commission ("SEC"). The financial information is presented in accordance with United States generally accepted accounting principles ("GAAP") for interim financial information and, accordingly, does not include all of the information and footnotes required by GAAP for complete financial statements. The financial information as of January 28, 2018 is derived from the Company's audited consolidated financial statements and related notes for the fiscal year ended January 28, 2018, which are included in Item 8 in the Company's fiscal 2017 Annual Report on Form 10-K filed with the SEC on March 27, 2018. These unaudited interim consolidated financial statements reflect all adjustments which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These unaudited interim consolidated financial statements should be read in conjunction with the Company's consolidated financial statements and related notes included in Item 8 in the Company's fiscal 2017 Annual Report on Form 10-K.

The Company's fiscal year ends on the Sunday closest to January 31 of the following year, typically resulting in a 52-week year, but occasionally giving rise to an additional week, resulting in a 53-week year. Fiscal 2018 will end on February 3, 2019 and will be a 53-week year.

The Company's business is affected by the pattern of seasonality common to most retail apparel businesses. Historically, the Company has recognized a significant portion of its operating profit in the fourth fiscal quarter of each year as a result of increased net revenue during the holiday season.

Certain comparative figures have been reclassified to conform to the financial presentation adopted for the current year.

NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS

Recently adopted accounting pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers ("ASC 606") which supersedes the revenue recognition requirements in ASC 605 Revenue Recognition. This ASU requires that an entity recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

The Company adopted ASC 606 on January 29, 2018 on a modified retrospective basis. There were no changes to the consolidated statement of operations as a result of the adoption, and the timing and amount of its revenue recognition remained substantially unchanged under this new guidance. Under the provisions of ASC 606, the Company is now required to present its provision for sales returns on a gross basis, rather than a net basis. The Company's liability for sales return refunds is recognized within other current liabilities, and the Company now presents an asset for the value of inventory which is expected to be returned within other prepaid expenses and other current assets on the consolidated balance sheets. Under the modified retrospective approach, the comparative prior period information has not been restated for this change.

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The effect of adoption of ASC 606 on the Company's consolidated balance sheet as of October 28, 2018 was as follows:

	October 28, 2018		
	As Reported	Adjustment for ASC 606	Balances Without Adoption of ASC 606
	(In thousands)		
Other prepaid expenses and other current assets	$57,828	$ (3,090)	$ 54,738
Current assets	1,363,467	(3,090)	1,360,377
Total assets	1,981,011	(3,090)	1,977,921
Other current liabilities	105,620	3,090	108,710
Current liabilities	443,671	3,090	446,761
Total liabilities	574,254	3,090	577,344

In May 2017, the FASB amended ASC 718, Stock Compensation, to reduce diversity in practice and to clarify when a change to the terms or conditions of a share-based payment award must be accounted for as a modification and will result in fewer changes to the terms of an award being accounted for as modifications. The new guidance was effective beginning in the first quarter of fiscal 2018 and will apply on a prospective basis. The Company does not expect it to have a material impact on its consolidated financial statements.

Accounting policies as a result of recently adopted accounting pronouncements

Revenue recognition

Net revenue is comprised of company-operated store net revenue, direct to consumer net revenue through websites and mobile apps, including mobile apps on in-store devices that allow demand to be fulfilled via the Company's distribution centers, and other net revenue, which includes revenue from outlets, temporary locations, sales to wholesale accounts, showrooms, warehouse sales, and license and supply arrangement net revenue, which consists of royalties as well as sales of the Company's products to licensees. All revenue is reported net of sales taxes collected from customers on behalf of taxing authorities.

Revenue is recognized when performance obligations are satisfied through the transfer of control of promised goods to the Company's customers. Control transfers once a customer has the ability to direct the use of, and obtain substantially all of the benefits from, the product. This includes the transfer of legal title, physical possession, the risks and rewards of ownership, and customer acceptance. Revenue from company-operated stores and other retail locations is recognized at the point of sale. Direct to consumer revenue and sales to wholesale accounts are recognized upon receipt by the customer.

Revenue is presented net of an allowance for estimated returns, which is based on historic experience. The Company's liability for sales return refunds is recognized within other current liabilities, and an asset for the value of inventory which is expected to be returned is recognized within other prepaid expenses and other current assets on the consolidated balance sheets.

Shipping fees billed to customers are recorded as revenue, and shipping costs are recognized within selling, general and administrative expenses in the same period the related revenue is recognized.

Proceeds from the sale of gift cards are initially deferred and recognized within unredeemed gift card liability on the consolidated balance sheets, and are recognized as revenue when tendered for payment. Based on historical experience, and to the extent there is no requirement to remit unclaimed card balances to government agencies, an estimate of the gift card balances that will never be redeemed is recognized as revenue in proportion to gift cards which have been redeemed.

Recently issued accounting pronouncements

In February 2016, the FASB issued ASC 842, Leases ("ASC 842") to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. Under the new guidance, lessees are required to recognize a lease liability, which represents the discounted obligation to make future minimum lease payments, and a corresponding right-of-use asset on the balance sheet for most leases. This guidance will be effective for the Company beginning in its first quarter of fiscal 2019, with early application permitted. The new guidance can be applied using a modified retrospective approach at the beginning of the earliest period presented, or at the beginning of the period in which it is adopted.

The Company will adopt ASC 842 on February 4, 2019 and anticipates applying the modified retrospective approach from the beginning of the period in which the standard is adopted.

The Company expects to apply the transition package of three practical expedients which allow companies not to reassess whether agreements contain leases, the classification of leases, and the capitalization of initial direct costs.

The Company expects to make an accounting policy election to recognize lease expense for leases with a term of 12 months or less on a straight-line basis over the lease term and recognize no right of use asset or lease liability for those leases.

The Company is nearing completion of the implementation of new lease accounting software and continues to evaluate the impact this standard will have on its consolidated financial statements, disclosures, and internal controls. It is expected that the primary financial statement impact upon adoption will be the recognition, on a discounted basis, of the Company's minimum commitments under noncancelable operating leases as right of use assets and obligations on the consolidated balance sheets. It is expected that this will result in a significant increase in assets and liabilities on the consolidated balance sheets. The standard is not expected to have a material impact on the Company's net income or cash flows.

In August 2017, the FASB amended ASC 815, Derivatives and Hedging to more closely align hedge accounting with companies' risk management strategies, simplify the application of hedge accounting, and increase transparency as to the scope and results of hedging programs. It will make more financial and nonfinancial hedging strategies eligible for hedge accounting. It also amends the presentation and disclosure requirements and changes how companies assess effectiveness. This guidance will be effective for the Company beginning in its first quarter of fiscal 2019, with early application permitted. This standard is not expected to have a material impact on the Company's consolidated financial statements.

In January 2018, the FASB released guidance on the accounting for the global intangible low-taxed income ("GILTI") provisions of the tax bill H.R.1, commonly known as the U.S. Tax Cuts and Jobs Act ("U.S. tax reform"). The GILTI provisions impose a tax on foreign subsidiary earnings in excess of a deemed return on the foreign subsidiary's tangible assets. The guidance indicates that an accounting policy election can be made to treat the GILTI tax as either a current tax in the period in which it is incurred or as a deferred tax. The Company has not yet made its accounting policy election but will do so during the one-year measurement period as allowed by the SEC. In accordance with the FASB guidance, until an accounting policy election is made, any taxes related to the GILTI provisions will be treated as a current income tax expense in the period incurred.

In February 2018, the FASB amended ASC 220, Income Statement—Reporting Comprehensive Income. ASC 740, Income Taxes, requires that the effect of a change in tax laws or rates on deferred tax assets and liabilities be included in income from continuing operations. In situations in which the tax effects of a transaction were initially recognized directly in other comprehensive income, this results in "stranded" amounts in accumulated other comprehensive income related to the income tax rate differential. The amendments to ASC 220 allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the enactment of the U.S. tax reform. The guidance in the ASU is effective for the Company beginning in its first quarter of fiscal 2019 with early adoption permitted. The Company does not expect to elect to reclassify "stranded" amounts from accumulated other comprehensive income to retained earnings.

NOTE 3. CREDIT FACILITY

On June 6, 2018, the Company entered into Amendment No. 1 to its credit agreement. This amends the credit agreement to provide for (i) an increase in the aggregate commitments under the unsecured five-year revolving credit facility to $400.0 million, with an increase of the sub-limits for the issuance of letters of credit and extensions of swing line loans to $50.0 million for each, (ii) an increase in the option, subject to certain conditions as set forth in the credit agreement, to request increases in commitments under the revolving facility from $400.0 million to $600.0 million, and (iii) an extension in the maturity of the revolving facility from December 15, 2021 to June 6, 2023.

In addition, this amendment decreases the applicable margins for LIBOR loans from 1.00%-1.75% to 1.00%-1.50% and for alternate base rate loans from 0.00%-0.75% to 0.00%-0.50%, reduces the commitment fee on average daily unused amounts under the revolving facility from 0.125%-0.200% to 0.10%-0.20%, and reduces fees for unused

letters of credit from 1.00%-1.75% to 1.00%-1.50%.
The Company had no borrowings outstanding under this credit facility as of October 28, 2018 and January 28, 2018.
As of October 28, 2018, the Company had letters of credit of $1.2 million outstanding.

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NOTE 4. STOCK-BASED COMPENSATION AND BENEFIT PLANS

Stock-based compensation plans

The Company's eligible employees participate in various stock-based compensation plans, which are provided by the Company directly.

Stock-based compensation expense charged to income for the plans was $19.0 million and $13.0 million for the three quarters ended October 28, 2018 and October 29, 2017, respectively. Total unrecognized compensation cost for all stock-based compensation plans was $63.7 million at October 28, 2018, which is expected to be recognized over a weighted-average period of 2.2 years.

A summary of the balances of the Company's stock-based compensation plans as of October 28, 2018, and changes during the first three quarters then ended, is presented below:

	Stock Options		Performance-Based Restricted Stock Units		Restricted Shares		Restricted Stock Units		Restricted Stock Units (Liability Accounting)	
	Number	Weighted-Average Exercise Price	Number	Weighted-Average Grant Date Fair Value	Number	Weighted-Average Grant Date Fair Value	Number	Weighted-Average Grant Date Fair Value	Number	Weighted-Average Fair Value
	(In thousands, except per share amounts)									
Balance at January 28, 2018	1,117	$ 56.44	329	$ 60.42	21	$ 52.45	427	$ 57.54	—	$ —
Granted	382	96.70	122	102.40	6	124.19	253	88.34	44	134.82
Exercised/released	307	56.25	39	63.04	21	52.45	170	58.83	—	—
Forfeited/expired	299	59.07	130	61.47	—	—	56	65.59	—	—
Balance at October 28, 2018	893	$ 72.84	282	$ 77.78	6	$ 124.19	454	$ 73.22	44	$ 134.82
Exercisable at October 28, 2018	168	$ 55.01								

The grant date fair value of each stock option granted is estimated on the date of grant using the Black-Scholes model. The assumptions used to calculate the fair value of the options granted are evaluated and revised, as necessary, to reflect market conditions and the Company's historical experience. The expected term of the options is based upon the historical experience of similar awards, giving consideration to expectations of future employee behavior. Expected volatility is based upon the historical volatility of the Company's common stock for the period corresponding with the expected term of the options. The risk-free interest rate is based on the U.S. Treasury yield curve for the period corresponding with the expected term of the options. The following are weighted averages of the assumptions that were used in calculating the fair value of stock options granted during the first three quarters of fiscal 2018:

	Three Quarters Ended October 28, 2018	
Expected term	3.75 years	
Expected volatility	36.87	%
Risk-free interest rate	2.46	%
Dividend yield	—	%

The Company's performance-based restricted stock units are awarded to eligible employees and entitle the grantee to receive a maximum of two shares of common stock per performance-based restricted stock unit if the Company achieves specified performance goals and the grantee remains employed during the vesting period. The fair value of performance-based restricted stock units is based on the closing price of the Company's common stock on the award date. Expense for performance-based restricted stock units is recognized when it is probable that the performance goal will be achieved.

The grant date fair value of the restricted shares and restricted stock units is based on the closing price of the Company's common stock on the award date. Restricted stock units that are settled in cash or common stock at the election of the employee

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are remeasured to fair value at the end of each reporting period until settlement. This fair value is based on the closing price of the Company's common stock on the last business day before each period end.

Employee share purchase plan

The Company's board of directors and stockholders approved the Company's Employee Share Purchase Plan ("ESPP") in September 2007. Contributions are made by eligible employees, subject to certain limits defined in the ESPP, and the Company matches one-third of the contribution. The maximum number of shares authorized to be purchased under the ESPP is 6.0 million shares. All shares purchased under the ESPP are purchased in the open market. During the quarter ended October 28, 2018, there were 17.7 thousand shares purchased.

Defined contribution pension plans

The Company offers defined contribution pension plans to its eligible employees in Canada and the United States. Participating employees may elect to defer and contribute a portion of their eligible compensation to a plan up to limits stated in the plan documents, not to exceed the dollar amounts set by applicable laws. The Company matches 50% to 75% of the contribution depending on the participant's length of service, and the contribution is subject to a two year vesting period. The Company's net expense for the defined contribution plans was $4.7 million and $3.9 million in the first three quarters of fiscal 2018 and fiscal 2017, respectively.

NOTE 5. FAIR VALUE MEASUREMENT

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are made using a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value:

- Level 1 - defined as observable inputs such as quoted prices in active markets;
- Level 2 - defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and
- Level 3 - defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

Assets and liabilities measured at fair value on a recurring basis

The fair value measurement is categorized in its entirety by reference to its lowest level of significant input. As of October 28, 2018 and January 28, 2018, the Company held certain assets and liabilities that are required to be measured at fair value on a recurring basis:

	October 28, 2018	Level 1	Level 2	Level 3	Balance Sheet Classification
	(In thousands)				
Money market funds	$73,198	$73,198	$ —	$ —	Cash and cash equivalents
Treasury bills	15,266	15,266	—	—	Cash and cash equivalents
Term deposits	357,013	—	357,013	—	Cash and cash equivalents
Net forward currency contract assets	1,661	—	1,661	—	Other prepaid expenses and other current assets
Net forward currency contract liabilities	4,743	—	4,743	—	Other current liabilities

	January 28, 2018	Level 1	Level 2	Level 3	Balance Sheet Classification
	(In thousands)				
Term deposits	$258,238	$ —	$258,238	$ —	Cash and cash equivalents
Net forward currency contract assets	7,889	—	7,889	—	Other prepaid expenses and other current assets
Net forward currency contract liabilities	8,771	—	8,771	—	Other current liabilities

The Company records accounts receivable, accounts payable, accrued liabilities, and borrowings under the revolving credit facility at cost. The carrying values of these instruments approximate their fair value due to their short-term maturities.

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The Company has short-term, highly liquid investments classified as cash equivalents, which are invested in money market funds, Treasury bills, and term deposits. The Company records cash equivalents at their original purchase prices plus interest that has accrued at the stated rate.

The fair values of the forward currency contract assets and liabilities are determined using observable Level 2 inputs, including foreign currency spot exchange rates, forward pricing curves, and interest rates. The fair values consider the credit risk of the Company and its counterparties. They are presented at their gross fair values. However, the Company's Master International Swap Dealers Association, Inc., Agreements and other similar arrangements allow net settlements under certain conditions.

Assets and liabilities measured at fair value on a non-recurring basis

In addition to assets and liabilities that are recorded at fair value on a recurring basis, the Company has impaired certain long-lived assets and recorded them at their estimated fair value on a non-recurring basis. The fair value of these long-lived assets was determined using Level 3 inputs, principally the present value of the estimated future cash flows expected from their use and eventual disposition. Please refer to Note 7 of these unaudited interim consolidated financial statements for further details regarding the impairment of long-lived assets as a result of the ivivva restructuring.

The Company has also recorded certain lease termination liabilities at fair value on a non-recurring basis, determined using Level 3 inputs based on remaining lease rentals and reduced by estimated sublease income. As of October 28, 2018 and January 28, 2018, the Company had lease termination liabilities of $2.8 million and $6.4 million, respectively. This was primarily as a result of the ivivva restructuring.

NOTE 6. DERIVATIVE FINANCIAL INSTRUMENTS

Foreign exchange risk

The Company is exposed to risks associated with changes in foreign currency exchange rates and uses derivative financial instruments to manage its exposure to certain of these foreign currency exchange rate risks. The Company does not enter into derivative contracts for speculative or trading purposes.

The Company currently hedges against changes in the Canadian dollar to U.S. dollar exchange rate using forward currency contracts.

Net investment hedges

The Company is exposed to foreign exchange gains and losses which arise on translation of its foreign subsidiaries' balance sheets into U.S. dollars. These gains and losses are recorded as a foreign currency translation adjustment in accumulated other comprehensive income or loss within stockholders' equity.

The Company holds a significant portion of its assets in Canada and enters into forward currency contracts designed to hedge a portion of the foreign currency exposure that arises on translation of a Canadian subsidiary into U.S. dollars. These forward currency contracts are designated as net investment hedges. The effective portions of the hedges are reported in accumulated other comprehensive income or loss and will subsequently be reclassified to net earnings in the period in which the hedged investment is either sold or substantially liquidated. Hedge effectiveness is measured using a method based on changes in forward exchange rates. The Company recorded no ineffectiveness from net investment hedges during the first three quarters of fiscal 2018.

The Company classifies the cash flows at settlement of its net investment hedges within investing activities in the consolidated statements of cash flows.

Derivatives not designated as hedging instruments

The Company is exposed to gains and losses arising from changes in foreign exchange rates associated with transactions which are undertaken by its subsidiaries in currencies other than their functional currency. Such transactions include intercompany transactions and inventory purchases. These transactions result in the recognition of certain foreign currency denominated monetary assets and liabilities which are remeasured to the quarter-end or settlement date exchange rate. The resulting foreign currency gains and losses are recorded in selling, general and administrative expenses.

During the first three quarters of fiscal 2018, the Company entered into certain forward currency contracts designed to economically hedge the foreign exchange revaluation gains and losses that are recognized by its Canadian subsidiaries on U.S.

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dollar denominated monetary assets and liabilities. The Company has not applied hedge accounting to these instruments and the change in fair value of these derivatives is recorded within selling, general and administrative expenses.

The Company classifies the cash flows at settlement of its forward currency contracts which are not designated in hedging relationships within operating activities in the consolidated statements of cash flows.

Outstanding notional amounts

The Company had foreign exchange forward contracts outstanding with the following notional amounts:

	October 28, 2018	January 28, 2018
	(In thousands)	
Derivatives designated as net investment hedges	$389,000	$ 262,000
Derivatives not designated in a hedging relationship	340,000	240,000

The forward currency contracts designated as net investment hedges outstanding as of October 28, 2018 mature on different dates between December 2018 and April 2019.

The forward currency contracts not designated in a hedging relationship outstanding as of October 28, 2018 mature on different dates between November 2018 and March 2019.

Quantitative disclosures about derivative financial instruments

The Company presents its derivative assets and derivative liabilities at their gross fair values within other prepaid expenses and other current assets and other current liabilities on the consolidated balance sheets. However, the Company's Master International Swap Dealers Association, Inc., Agreements and other similar arrangements allow net settlements under certain conditions. As of October 28, 2018, there were derivative assets of $1.7 million and derivative liabilities of $4.7 million subject to enforceable netting arrangements.

The fair values of forward currency contracts were as follows:

	October 28, 2018	January 28, 2018
	(In thousands)	
Net forward currency contract assets, recognized within other prepaid expenses and other current assets:		
Derivatives designated as net investment hedges	$ 1,661	$ —
Derivatives not designated in a hedging relationship	—	7,889
Net forward currency contract liabilities, recognized within other current liabilities:		
Derivatives designated as net investment hedges	—	8,771
Derivatives not designated in a hedging relationship	4,743	—

The pre-tax gains and losses on foreign exchange forward contracts recorded in accumulated other comprehensive income are as follows:

	Quarter Ended		Three Quarters Ended	
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)			
Gains (losses) recognized in foreign currency translation adjustment:				
Derivatives designated as net investment hedges	$2,291	$ 1,424	$18,829	$ (7,501)

No gains or losses have been reclassified from accumulated other comprehensive income into net income for derivative financial instruments in a net investment hedging relationship, as the Company has not sold or liquidated (or substantially liquidated) its hedged subsidiary.

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The pre-tax net foreign exchange and derivative gains and losses recorded in the consolidated statement of operations are as follows:

	Quarter Ended		Three Quarters Ended	
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)			
Gains (losses) recognized in selling, general and administrative expenses:				
Foreign exchange gains	$395	$ 3,871	$12,999	$ 360
Derivatives not designated in a hedging relationship	(1,715)	(1,137)	(17,301)	6,497
Net foreign exchange and derivative (losses) gains	$(1,320)	$ 2,734	$(4,302)	$ 6,857

Credit risk

The Company is exposed to credit-related losses in the event of nonperformance by the counterparties to the forward currency contracts. The credit risk amount is the Company's unrealized gains on its derivative instruments, based on foreign currency rates at the time of nonperformance.

The Company's forward currency contracts are entered into with large, reputable financial institutions that are monitored by the Company for counterparty risk.

The Company's derivative contracts contain certain credit risk-related contingent features. Under certain circumstances, including an event of default, bankruptcy, termination, and cross default under the Company's revolving credit facility, the Company may be required to make immediate payment for outstanding liabilities under its derivative contracts.

NOTE 7. ASSET IMPAIRMENT AND RESTRUCTURING

During fiscal 2017, the Company restructured its ivivva operations. On August 20, 2017, the Company closed 48 of its 55 ivivva branded company-operated stores and all other ivivva branded temporary locations. As a result of this restructuring, the Company recognized aggregate pre-tax charges of $47.2 million during fiscal 2017, inclusive of $45.4 million recognized during the first three quarters of fiscal 2017.

A summary of the pre-tax charges recognized in connection with the Company's restructuring of its ivivva operations is as follows:

	Quarter Ended		Three Quarters Ended	
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)			
Costs recorded in cost of goods sold:				
Provision to reduce inventories to net realizable value	$—	$1,934	$—	$4,838
Loss (reversal of loss) on committed inventory purchases	—	(2,286)	—	250
Accelerated depreciation	—	1,530	—	3,753
	—	1,178	—	8,841
Costs recorded in operating expenses:				
Lease termination costs	—	19,441	—	19,884
Impairment of property and equipment	—	—	—	11,593
Employee related costs	—	804	—	4,000
Other restructuring costs	—	762	—	1,047
Asset impairment and restructuring costs	—	21,007	—	36,524
Restructuring and related costs	$—	$22,185	$—	$45,365

Income tax recoveries of $5.8 million and $11.9 million were recorded on the above items in the third quarter and the first three quarters of fiscal 2017, respectively. These income tax recoveries were based on the expected annual tax rate of the applicable tax jurisdictions.

Costs recorded in cost of goods sold
During the first three quarters of fiscal 2017, the Company recognized expenses of $8.8 million in cost of goods sold as a result of the restructuring of its ivivva operations. This included $4.8 million to reduce inventories to their estimated net realizable value, and $0.3 million for the losses the Company expected to incur on certain inventory and fabric purchase commitments.
During the second and third quarters of fiscal 2017, the Company took delivery of inventory that it had previously committed to purchase. As a result, there was a reduction in the Company's liability for expected losses on committed inventory purchases and a corresponding increase in its provision to reduce inventories to net realizable value.
The Company also recorded accelerated depreciation charges of $3.8 million during the first three quarters of fiscal 2017, primarily related to leasehold improvements and furniture and fixtures for company operated-stores that closed during the third quarter of fiscal 2017.
Costs recorded in operating expenses
The Company recognized asset impairment and restructuring costs of $36.5 million during the first three quarters of fiscal 2017 as a result of the restructuring of its ivivva operations.
As a result of the plan to close the majority of the ivivva branded locations, the long-lived assets of each ivivva branded location were tested for impairment as of April 30, 2017. For impaired locations, a loss was recognized representing the difference between the net book value of the long-lived assets and their estimated fair value. Impairment losses totaling $11.6 million were recognized during the first quarter of fiscal 2017. These losses primarily relate to leasehold improvements and furniture and fixtures of the company-operated stores segment. These assets were retired during the third quarter of fiscal 2017 in conjunction with the closures of the company-operated stores.
During the first three quarters of fiscal 2017, the Company recognized lease termination costs of $19.9 million, employee related expenses as a result of the restructuring of $4.0 million as well as other restructuring costs of $1.0 million.
NOTE 8. INCOME TAXES
The U.S. tax reform was enacted on December 22, 2017 and introduced significant changes to U.S. income tax laws. The U.S. tax reform reduced the U.S. federal income tax rate from 35% to 21%, introduced a shift to a territorial tax system and changed how foreign earnings are subject to U.S. tax, and imposed a mandatory one-time transition tax on the deemed repatriation of accumulated undistributed earnings of foreign subsidiaries. The U.S. tax reform also introduced new taxes on certain foreign-sourced earnings and certain related-party payments, which are referred to as the GILTI tax and the base erosion anti-abuse tax. Accounting for the income tax effects of the U.S. tax reform is complex and requires significant judgement and estimates in the interpretation and calculations of its provisions.
The SEC issued Staff Accounting Bulletin 118 ("SAB 118") which allows companies to record and adjust provisional estimates of the impacts of the U.S. tax reform within a one year measurement period. As disclosed in Note 14 to the audited consolidated financial statements included in Item 8 of the Company's fiscal 2017 Annual Report on Form 10-K filed with the SEC on March 27, 2018, the Company recorded certain provisional amounts in the fourth quarter of fiscal 2017.
During the third quarter of fiscal 2018, the Company adjusted the provisional amount recorded for the mandatory one-time transition tax as a result of completing its U.S. federal income tax return and incorporating recently issued guidance into its calculations. This resulted in the recognition of an additional tax expense of $5.2 million during the third quarter of fiscal 2018 which increased the Company’s effective tax rate by 380 basis points during the third quarter and by 140 basis points during the first three quarters of fiscal 2018. The Company continues to analyze additional interpretations and guidance that are issued, and is continuing to assess the impact of the mandatory one-time transition tax on U.S. state income taxes. Any additional adjustments may materially impact the provision for income taxes and the effective income tax rate in the period in which the adjustments are made.
As of October 28, 2018, no deferred income tax liabilities have been recognized on any of the undistributed earnings of the Company's foreign subsidiaries as these earnings were indefinitely reinvested outside of the United States. The Company is continuing to evaluate the impact that the U.S. tax reform will have upon the taxes which may become

payable upon repatriation, its reinvestment plans, and the most efficient means of deploying its capital resources globally. As this analysis has not yet been completed, it is possible that amounts determined to be indefinitely reinvested outside of the U.S. may ultimately be repatriated, resulting in additional tax liabilities being recognized. The Company expects the accounting for the income tax effects of the U.S. tax reform to be completed in fiscal 2018.

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NOTE 9. EARNINGS PER SHARE

The details of the computation of basic and diluted earnings per share are as follows:

	Quarter Ended		Three Quarters Ended	
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands, except per share amounts)			
Net income	$94,413	$ 58,944	$265,336	$ 138,901
Basic weighted-average number of shares outstanding	132,406	135,364	133,964	136,191
Assumed conversion of dilutive stock options and awards	671	214	548	166
Diluted weighted-average number of shares outstanding	133,077	135,578	134,512	136,357
Basic earnings per share	$0.71	$ 0.44	$1.98	$ 1.02
Diluted earnings per share	$0.71	$ 0.43	$1.97	$ 1.02

The Company's calculation of weighted-average shares includes the common stock of the Company as well as the exchangeable shares. Exchangeable shares are the equivalent of common shares in all material respects. All classes of stock have, in effect, the same rights and share equally in undistributed net income. For the three quarters ended October 28, 2018 and October 29, 2017, 41.5 thousand and 0.2 million stock options and awards, respectively, were anti-dilutive to earnings per share and therefore have been excluded from the computation of diluted earnings per share.

On December 1, 2016, the Company's board of directors approved a program to repurchase shares of the Company's common stock up to an aggregate value of $100.0 million. This stock repurchase program was completed during the third quarter of fiscal 2017.

On November 29, 2017, the Company's board of directors approved a stock repurchase program for up to $200.0 million. On June 6, 2018, the board of directors approved an increase to this stock repurchase program, authorizing the repurchase of up to a total of $600.0 million of the Company's common shares on the open market or in privately negotiated transactions. Common shares repurchased on the open market are at prevailing market prices, including under plans complying with the provisions of Rule 10b5-1 and Rule 10b-18 of the Securities Exchange Act of 1934. The timing and actual number of common shares to be repurchased will depend upon market conditions, eligibility to trade, and other factors, in accordance with Securities and Exchange Commission requirements, and the repurchase program is expected to be completed by November 2019. As of October 28, 2018, the remaining aggregate value of shares available to be repurchased under this program was $184.7 million.

During the three quarters ended October 28, 2018 and October 29, 2017, 3.4 million and 1.8 million shares, respectively, were repurchased under the program at a total cost of $414.3 million and $99.3 million, respectively. Subsequent to October 28, 2018, and up to December 3, 2018, 41.5 thousand shares were repurchased at a total cost of $5.2 million.

NOTE 10. SUPPLEMENTARY FINANCIAL INFORMATION

A summary of certain consolidated balance sheet accounts is as follows:

	October 28, 2018	January 28, 2018
	(In thousands)	
Inventories:		
Finished goods	$513,800	$344,695
Provision to reduce inventories to net realizable value	(17,809)	(15,133)
	$495,991	$329,562

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	October 28, 2018	January 28, 2018
	(In thousands)	
Property and equipment, net:		
Land	$78,608	$83,048
Buildings	38,020	39,278
Leasehold improvements	330,501	301,449
Furniture and fixtures	98,681	91,778
Computer hardware	63,033	61,734
Computer software	216,783	173,997
Equipment and vehicles	14,874	14,806
Work in progress	74,689	51,260
Property and equipment, gross	915,189	817,350
Accumulated depreciation	(383,939)	(343,708)
	$531,250	$473,642
Goodwill and intangible assets, net:		
Goodwill	$25,496	$25,496
Changes in foreign currency exchange rates	(1,259)	(890)
	24,237	24,606
Intangible assets, net	—	73
	$24,237	$24,679
Other non-current assets:		
Security deposits	$14,402	$11,599
Deferred lease assets	9,409	10,458
Other	10,091	9,332
	$33,902	$31,389
Other current liabilities:		
Accrued duty, freight, and other operating expenses	$50,952	$33,695
Sales tax collected	11,286	11,811
Sales return allowance	9,718	6,293
Accrued capital expenditures	9,121	5,714
Accrued rent	5,978	7,074
Forward currency contract liabilities	4,743	8,771
Lease termination liabilities	2,845	6,427
Other	10,977	6,631
	$105,620	$86,416
Other non-current liabilities:		
Deferred lease liabilities	$32,499	$27,186
Tenant inducements	36,858	26,250
Other	5,532	5,885
	$74,889	$59,321

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NOTE 11. SEGMENT REPORTING

The Company applies ASC Topic 280, Segment Reporting ("ASC 280"), in determining reportable segments for its financial statement disclosure. The Company reports segments based on the financial information it uses in managing its business. The Company's reportable segments are comprised of company-operated stores and direct to consumer. Direct to consumer represents sales from the Company's e-commerce websites and mobile apps. Outlets, temporary locations, sales to wholesale accounts, showrooms, warehouse sale net revenue, and license and supply arrangements have been combined into other. During the first quarter of fiscal 2018, the Company reviewed its general corporate expenses and determined certain costs which were previously classified as general corporate expense are more appropriately classified within the direct to consumer segment. Accordingly, comparative figures have been reclassified to conform to the financial presentation adopted for the current year.

	Quarter Ended		Three Quarters Ended	
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)			
Net revenue:				
Company-operated stores	$476,877	$ 425,084	$1,396,376	$1,218,127
Direct to consumer	189,375	131,181	514,623	341,453
Other	81,403	62,753	209,862	160,799
	$747,655	$ 619,018	$2,120,861	$1,720,379
Segmented income from operations:				
Company-operated stores	$117,804	$ 97,015	$342,959	$267,178
Direct to consumer	76,435	50,229	205,735	123,045
Other	15,019	9,319	39,336	19,076
	209,258	156,563	588,030	409,299
General corporate expense	73,355	48,790	213,614	164,211
Restructuring and related costs	—	22,185	—	45,365
Income from operations	135,903	85,588	374,416	199,723
Other income (expense), net	2,044	1,052	6,553	2,771
Income before income tax expense	$137,947	$ 86,640	$380,969	$202,494
Capital expenditures:				
Company-operated stores	$38,053	$ 29,747	$85,054	$53,549
Direct to consumer	540	7,582	1,854	16,423
Corporate and other	34,146	19,910	69,838	37,156
	$72,739	$ 57,239	$156,746	$107,128
Depreciation and amortization:				
Company-operated stores	$19,383	$ 16,549	$54,954	$47,630
Direct to consumer	2,336	3,740	7,237	10,087
Corporate and other	9,967	8,271	24,924	22,412
	$31,686	$ 28,560	$87,115	$80,129

The accelerated depreciation related to the restructuring of the ivivva operations is included in corporate and other in the above breakdown of depreciation and amortization.

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The following table disaggregates the Company's net revenue by geographic area. The economic conditions in these areas could affect the amount and timing of the Company's net revenue and cash flows.

	Quarter Ended		Three Quarters Ended	
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)			
United States	$527,331	$433,509	$1,502,013	$1,226,610
Canada	137,991	125,564	374,418	325,656
Outside of North America	82,333	59,945	244,430	168,113
	$747,655	$619,018	$2,120,861	$1,720,379

NOTE 12. LEGAL PROCEEDINGS AND OTHER CONTINGENCIES

In addition to the legal proceedings described below, the Company is, from time to time, involved in routine legal matters, and audits and inspections by governmental agencies and other third parties which are incidental to the conduct of its business. This includes legal matters such as initiation and defense of proceedings to protect intellectual property rights, personal injury claims, product liability claims, employment claims, and similar matters. The Company believes the ultimate resolution of any such legal proceedings, audits, and inspections will not have a material adverse effect on its consolidated balance sheets, results of operations or cash flows.

On October 9, 2015, certain current and former hourly employees of the Company filed a class action lawsuit in the Supreme Court of New York entitled Rebecca Gathmann-Landini et al v. lululemon USA inc. On December 2, 2015, the case was moved to the United States District Court for the Eastern District of New York. The lawsuit alleges that the Company violated various New York labor codes by failing to pay all earned wages, including overtime compensation. The plaintiffs are seeking an unspecified amount of damages. The Company intends to vigorously defend this matter.

On December 20, 2017, former lululemon employee Shayla Famouri filed a lawsuit in Los Angeles Superior Court against the Company and a former employee of the Company. The plaintiff alleges claims for sexual assault and battery, sexual harassment, retaliation, creating a hostile work environment and related claims. The complaint seeks damages in the amount of $3.0 million, as well as non-monetary relief such as policy change and an apology. The Company intends to vigorously defend this matter.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Some of the statements contained in this Form 10-Q and any documents incorporated herein by reference constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements, other than statements of historical facts, included or incorporated in this Form 10-Q are forward-looking statements, particularly statements which relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts, such as statements regarding our future financial condition or results of operations, our prospects and strategies for future growth, the development and introduction of new products, and the implementation of our marketing and branding strategies. In many cases, you can identify forward-looking statements by terms such as "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "intends," "predicts," "potential" or the negative of these terms or other comparable terminology.

The forward-looking statements contained in this Form 10-Q and any documents incorporated herein by reference reflect our current views about future events and are subject to risks, uncertainties, assumptions, and changes in circumstances that may cause events or our actual activities or results to differ significantly from those expressed in any forward-looking statement. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future events, results, actions, levels of activity, performance, or achievements. Readers are cautioned not to place undue reliance on these forward-looking statements. A number of important factors could cause actual results to differ materially from those indicated by the forward-looking statements, including, but not limited to, those factors described in "Risk Factors" and elsewhere in this report.

The forward-looking statements contained in this Form 10-Q reflect our views and assumptions only as of the date of this Form 10-Q and are expressly qualified in their entirety by the cautionary statements included in this Form 10-Q. Except as required by applicable securities law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

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This information should be read in conjunction with the unaudited interim consolidated financial statements and the notes included in Item 1 of Part I of this Quarterly Report on Form 10-Q and the audited consolidated financial statements and notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations, contained in our fiscal 2017 Annual Report on Form 10-K filed with the SEC on March 27, 2018.

We disclose material non-public information through one or more of the following channels: our investor relations website (http://investor.lululemon.com/), the social media channels identified on our investor relations website, press releases, SEC filings, public conference calls, and webcasts.

Overview

lululemon athletica inc. is principally a designer, distributor, and retailer of healthy lifestyle inspired athletic apparel and accessories. We have a mission to create transformational products and experiences which enable people to live a life they love, and have developed a brand for those pursuing an active, mindful lifestyle. Since our inception, we have fostered a distinctive corporate culture; we promote a set of core values in our business which include taking personal responsibility, nurturing entrepreneurial spirit, acting with honesty and courage, valuing connection, and choosing to have fun. These core values attract passionate and motivated employees who are driven to achieve personal and professional goals, and share our purpose of "elevating the world through the power of practice."

Our healthy lifestyle inspired athletic apparel and accessories are marketed under the lululemon and ivivva brand names. We offer a comprehensive line of apparel and accessories for women, men, and female youth. Our apparel assortment includes items such as pants, shorts, tops, and jackets designed for a healthy lifestyle and athletic activities such as yoga, running, training, and most other sweaty pursuits. We also offer fitness-related accessories, including items such as bags, socks, underwear, yoga mats and equipment, and water bottles.

During fiscal 2017, we restructured our ivivva operations. On August 20, 2017, we closed 48 of our 55 ivivva branded company-operated stores and all other ivivva branded temporary locations. We now operate ivivva primarily as an e-commerce business.

Financial Highlights

The summary below provides both GAAP and adjusted non-GAAP financial measures. During the third quarter of fiscal 2018, we adjusted the provisional amount recorded for the transition tax under the U.S. Tax Cuts and Jobs Act, resulting in the recognition of an additional tax expense of $5.2 million. In the third quarter of fiscal 2017, in connection with the restructuring of our ivivva operations, we recognized pre-tax costs totaling $22.2 million, and a related tax recovery of $5.8 million. The adjusted financial measures for the third quarters of fiscal 2018 and 2017 exclude these items.

For the third quarter of fiscal 2018, compared to the third quarter of fiscal 2017:

- Net revenue increased 21% to $747.7 million. On a constant dollar basis, net revenue increased 22%.
- Total comparable sales, which includes comparable store sales and direct to consumer, increased 17%. On a constant dollar basis, total comparable sales increased 18%.
- Comparable store sales increased 6%, or increased 7% on a constant dollar basis.
- Direct to consumer net revenue increased 44%, or increased 46% on a constant dollar basis.
- Gross profit increased 26% to $406.8 million. It increased 26% compared to adjusted gross profit for the third quarter of fiscal 2017.
- Gross margin increased 240 basis points to 54.4%. It increased 220 basis points compared to adjusted gross margin for the third quarter of fiscal 2017.
- Income from operations increased 59% to $135.9 million. It increased 26% compared to adjusted income from operations for the third quarter of fiscal 2017.
- Operating margin increased 440 basis points to 18.2%. It increased 80 basis points compared to adjusted operating margin for the third quarter of fiscal 2017.
- Income tax expense increased 57% to $43.5 million. Our effective tax rate for the third quarter of fiscal 2018 was 31.6% compared to 32.0% for the third quarter of fiscal 2017. The adjusted effective tax rate was 27.8% compared to 30.8% in the third quarter of fiscal 2017.

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- Diluted earnings per share were $0.71 compared to $0.43 in the third quarter of fiscal 2017. Adjusted diluted earnings per share were $0.75 compared to $0.56 for the third quarter of fiscal 2017.

Refer to the non-GAAP reconciliation tables contained in the "Non-GAAP Financial Measures" section of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations" for reconciliations between constant dollar changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue, and adjusted gross profit, gross margin, income from operations, operating margin, income tax expense, effective tax rates, and diluted earnings per share, and the most directly comparable measures calculated in accordance with GAAP.

Results of Operations

Third Quarter Results

The following table summarizes key components of our results of operations for the quarters ended October 28, 2018 and October 29, 2017. The percentages are presented as a percentage of net revenue.

	Quarter Ended			
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)		(Percentages)	
Net revenue	$747,655	$ 619,018	100.0%	100.0 %
Cost of goods sold	340,878	297,056	45.6	48.0
Gross profit	406,777	321,962	54.4	52.0
Selling, general and administrative expenses	270,874	215,367	36.2	34.8
Asset impairment and restructuring costs	—	21,007	—	3.4
Income from operations	135,903	85,588	18.2	13.8
Other income (expense), net	2,044	1,052	0.3	0.2
Income before income tax expense	137,947	86,640	18.5	14.0
Income tax expense	43,534	27,696	5.8	4.5
Net income	$94,413	$ 58,944	12.6 %	9.5 %

Net Revenue

Net revenue increased $128.6 million, or 21%, to $747.7 million for the third quarter of fiscal 2018 from $619.0 million for the third quarter of fiscal 2017. On a constant dollar basis, assuming the average exchange rates for the third quarter of fiscal 2018 remained constant with the average exchange rates for the third quarter of fiscal 2017, net revenue increased $138.0 million, or 22%.

The increase in net revenue was primarily due to increased direct to consumer net revenue, increased company-operated store net revenue, including from new company-operated stores as well as an increase in comparable store sales, and an increase in net revenue from our other retail locations. Total comparable sales, which includes comparable store sales and direct to consumer, increased 17% in the third quarter of fiscal 2018 compared to the third quarter of fiscal 2017. Total comparable sales increased 18% on a constant dollar basis.

Net revenue on a segment basis for the quarters ended October 28, 2018 and October 29, 2017 is summarized below. The percentages are presented as a percentage of total net revenue.

	Quarter Ended			
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)		(Percentages)	
Company-operated stores	$476,877	$ 425,084	63.8 %	68.7 %
Direct to consumer	189,375	131,181	25.3	21.2
Other	81,403	62,753	10.9	10.1
Net revenue	$747,655	$ 619,018	100.0%	100.0 %

Company-Operated Stores. Net revenue from our company-operated stores segment increased $51.8 million, or 12%, to $476.9 million in the third quarter of fiscal 2018 from $425.1 million in the third quarter of fiscal 2017. The following contributed to the increase in net revenue from our company-operated stores segment:

- Net revenue from company-operated stores we opened or significantly expanded subsequent to October 29, 2017, and therefore not included in comparable store sales, contributed $41.3 million to the increase. We opened 38 net new lululemon branded company-operated stores since the third quarter of fiscal 2017, including 18 stores in North America, 11 stores in Asia, seven stores in Europe, and two stores in Australia/New Zealand.
- A comparable store sales increase of 6% in the third quarter of fiscal 2018 compared to the third quarter of fiscal 2017 resulted in a $16.7 million increase to net revenue. Comparable store sales increased 7%, or $21.4 million on a constant dollar basis. The increase in comparable store sales was primarily a result of increased store traffic and improved conversion rates. This was partially offset by a decrease in dollar value per transaction.

The increase in net revenue was partially offset by the closure of 48 of our ivivva branded company-operated stores as part of the restructuring of our ivivva operations. These closures reduced our net revenue from company-operated stores for the third quarter of fiscal 2018 by $6.2 million compared to the third quarter of fiscal 2017.

Direct to Consumer. Net revenue from our direct to consumer segment increased $58.2 million, or 44%, to $189.4 million in the third quarter of fiscal 2018 from $131.2 million in the third quarter of fiscal 2017. Direct to consumer net revenue increased 46% on a constant dollar basis. This was primarily a result of increased website traffic and improved conversion rates. This was partially offset by a decrease in dollar value per transaction.

Other. Net revenue from our other segment increased $18.7 million, or 30%, to $81.4 million in the third quarter of fiscal 2018 from $62.7 million in the third quarter of fiscal 2017. This increase was primarily the result of an increased number of temporary locations, including seasonal stores, open during the third quarter of fiscal 2018 compared to the third quarter of fiscal 2017.

Gross Profit

Gross profit increased $84.8 million, or 26%, to $406.8 million for the third quarter of fiscal 2018 from $322.0 million for the third quarter of fiscal 2017.

Gross profit as a percentage of net revenue, or gross margin, increased 240 basis points to 54.4% in the third quarter of fiscal 2018 from 52.0% in the third quarter of fiscal 2017. The increase in gross margin was primarily the result of:

- an increase in product margin of 280 basis points, which was primarily due to lower product costs, a favorable mix of higher margin product, lower markdowns, and lower inventory provision expense; and
- the costs incurred in the third quarter of fiscal 2017 in connection with the restructuring of our ivivva operations, which reduced gross margin in that quarter by 20 basis points.

This was partially offset by an increase in costs as a percentage of revenue related to our distribution centers and additional costs related to our product departments of 30 basis points, and an unfavorable impact of foreign exchange rates of 30 basis points.

During the third quarter of fiscal 2017, as a result of the restructuring of our ivivva operations, we recognized costs totaling $1.2 million within costs of goods sold, as outlined in Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report. Excluding these charges from the comparatives for the third quarter of fiscal 2017, gross profit increased 26% and gross margin increased 220 basis points.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased $55.5 million, or 26%, to $270.9 million in the third quarter of fiscal 2018 from $215.4 million in the third quarter of fiscal 2017. The increase in selling, general and administrative expenses was primarily due to:

- an increase in costs related to our operating channels of $28.6 million, comprised of:
  - an increase in employee costs of $12.9 million primarily from a growth in labor hours and benefits, mainly associated with new company-operated stores and other new operating locations, and due to higher retail bonus expenses;

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- an increase in variable costs of $10.8 million primarily due to an increase in distribution costs, credit card fees, and packaging costs as a result of increased net revenue; and
- an increase in other costs of $5.0 million primarily due to an increase in digital marketing expenses and other costs associated with our operating locations;

- an increase in head office costs of $22.9 million, comprised of:
  - an increase in employee costs of $10.0 million primarily due to additional employees to support the growth in our business and increased incentive and stock-based compensation expense; and
  - an increase in other costs of $12.8 million primarily due to increases in brand and community costs, information technology costs, professional fees, depreciation, and other head office costs; and
- an increase in net foreign exchange and derivative revaluation losses of $4.1 million.

As a percentage of net revenue, selling, general and administrative expenses increased 140 basis points, to 36.2% in the third quarter of fiscal 2018 from 34.8% in the third quarter of fiscal 2017.

Asset Impairment and Restructuring Costs

During the third quarter of fiscal 2017, we incurred asset impairment and restructuring costs totaling $21.0 million in connection with the restructuring of our ivivva operations. This included lease termination costs of $19.4 million, employee related costs of $0.8 million, and other restructuring costs of $0.8 million. Please refer to Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

We did not have any asset impairment and restructuring costs in the third quarter of fiscal 2018.

Income from Operations

Income from operations increased $50.3 million, or 59%, to $135.9 million in the third quarter of fiscal 2018 from $85.6 million in the third quarter of fiscal 2017. Operating margin increased 440 basis points to 18.2% compared to 13.8% in the third quarter of fiscal 2017.

In connection with the restructuring of our ivivva operations, we recognized pre-tax costs totaling $22.2 million in the third quarter of fiscal 2017. This included costs of $1.2 million recognized in cost of goods sold, and asset impairment and restructuring costs totaling $21.0 million. Excluding these charges from the comparatives for the third quarter of fiscal 2017, income from operations increased 26% and operating margin increased 80 basis points.

On a segment basis, we determine income from operations without taking into account our general corporate expenses and the costs we incurred in connection with the restructuring of our ivivva operations. In the first quarter of fiscal 2018, we reviewed our general corporate expenses and determined certain costs which were previously classified as general corporate expenses are more appropriately classified within our direct to consumer segment. Accordingly, comparative figures have been reclassified to conform to the financial presentation adopted for the current year.

Segmented income from operations for the quarters ended October 28, 2018 and October 29, 2017 is summarized below. The percentages are presented as a percentage of net revenue of the respective operating segments.

	Quarter Ended			
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)		(Percentage of segment revenue)	
Segmented income from operations:				
Company-operated stores	$117,804	$ 97,015	24.7%	22.8 %
Direct to consumer	76,435	50,229	40.4	38.3
Other	15,019	9,319	18.5	14.9
	209,258	156,563		
General corporate expense	73,355	48,790		
Restructuring and related costs	—	22,185		
Income from operations	$135,903	$ 85,588		

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Company-Operated Stores. Income from operations from our company-operated stores segment increased $20.8 million, or 21%, to $117.8 million for the third quarter of fiscal 2018 from $97.0 million for the third quarter of fiscal 2017. The increase was primarily the result of increased gross profit of $32.3 million which was primarily due to increased net revenue and higher gross margin. This was partially offset by an increase in selling, general and administrative expenses, primarily due to an increase in employee costs as well as increased store operating expenses including higher credit card fees, distribution costs, and packaging costs as a result of higher net revenue. Income from operations as a percentage of company-operated stores net revenue increased 190 basis points due to higher gross margin and leverage on selling, general and administrative expenses.

Direct to Consumer. Income from operations from our direct to consumer segment increased $26.2 million, or 52%, to $76.4 million for the third quarter of fiscal 2018 from $50.2 million for the third quarter of fiscal 2017. The increase was primarily the result of increased gross profit of $38.3 million which was primarily due to increased net revenue. This was partially offset by an increase in selling, general and administrative expenses primarily due to higher variable costs including distribution costs and credit card fees as a result of higher net revenue, as well as higher digital marketing expenses and increased employee costs. Income from operations as a percentage of direct to consumer net revenue increased 210 basis points primarily due to leverage on selling, general and administrative expenses.

Other. Other income from operations increased $5.7 million, or 61%, to $15.0 million for the third quarter of fiscal 2018 from $9.3 million for the third quarter of fiscal 2017. The increase was primarily the result of increased gross profit of $13.1 million which was primarily due to increased net revenue and higher gross margin. The increase in gross profit was partially offset by an increase in selling, general and administrative expenses, primarily due to increased employee costs, increased operating expenses including increases in professional fees, repairs and maintenance costs, security costs, and higher distribution costs and credit card fees as a result of higher net revenue, and higher community costs. Income from operations as a percentage of other net revenue increased 360 basis points due to higher gross margin and leverage on selling, general and administrative expenses.

General Corporate Expense. General corporate expense increased $24.6 million, or 50%, to $73.4 million for the third quarter of fiscal 2018 from $48.8 million for the third quarter of fiscal 2017. This increase was primarily due to increases in head office employee costs, brand and community costs, information technology costs, professional fees, depreciation, and an increase in net foreign exchange and derivative revaluation losses of $4.1 million.

Other Income (Expense), Net

Other income, net increased $1.0 million, or 94%, to $2.0 million for the third quarter of fiscal 2018 from income of $1.1 million for the third quarter of fiscal 2017. The increase was primarily due to an increase in net interest income, primarily due to higher rates of return on our cash and cash equivalents, including money market funds, treasury bills, and term deposits, and due to an increase in cash and cash equivalents in the third quarter of fiscal 2018 compared to third quarter of fiscal 2017. This was partially offset by an increase in interest expense primarily related to borrowings on our revolving credit facility during the third quarter of fiscal 2018. We repaid the outstanding balance on our revolving credit facility during the third quarter of fiscal 2018 and had no borrowings outstanding under this credit facility as of October 28, 2018.

Income Tax Expense

Income tax expense increased $15.8 million, or 57%, to $43.5 million for the third quarter of fiscal 2018 from $27.7 million for the third quarter of fiscal 2017.

The U.S. Tax Cuts and Jobs Act ("U.S. tax reform") was enacted on December 22, 2017 and introduced significant changes to U.S. income tax law. We recorded certain provisional amounts in the fourth quarter of fiscal 2017. During the third quarter of fiscal 2018, we adjusted the provisional amount recorded for the mandatory one-time transition tax on the deemed repatriation of accumulated undistributed earnings of foreign subsidiaries. This resulted in the recognition of an additional tax expense of $5.2 million. We expect the accounting for the income tax effects of the U.S. tax reform to be completed in fiscal 2018. Please refer to Note 8 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

During the third quarter of fiscal 2017, we recognized a net income tax recovery of $5.8 million on the costs recognized in connection with the ivivva restructuring. Please refer to Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

The effective tax rate for the third quarter of fiscal 2018 was 31.6% compared to 32.0% for the third quarter of fiscal 2017. Excluding the above tax adjustments, the adjusted effective tax rate was 27.8% compared to 30.8% for the third quarter of fiscal 2017. The decrease in the adjusted effective tax rate was primarily due to the lower U.S. federal income tax rate as a

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result of the U.S. tax reform, partially offset by the amounts recognized for global intangible low-taxed income ("GILTI") taxes. During the third quarter of fiscal 2018 we reduced our expected effective tax rate for fiscal 2018 as a result of a more favorable mix of earnings amongst jurisdictions with differing statutory tax rates, certain adjustments resulting from the filing of tax returns, and higher than expected tax credits related to research and development. This reduced the effective tax rate for the third quarter of fiscal 2018.

Net Income

Net income increased $35.5 million, or 60%, to $94.4 million for the third quarter of fiscal 2018 from $58.9 million for the third quarter of fiscal 2017. This was primarily due to an increase in gross profit of $84.8 million, a reduction in asset impairment and restructuring costs of $21.0 million, and an increase in other income (expense), net of $1.0 million, partially offset by an increase in selling, general and administrative expenses of $55.5 million and an increase in income tax expense of $15.8 million.

First Three Quarters Results

The following table summarizes key components of our results of operations for the first three quarters ended October 28, 2018 and October 29, 2017. The percentages are presented as a percentage of net revenue.

	Three Quarters Ended			
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)		(Percentages)	
Net revenue	$2,120,861	$1,720,379	100.0%	100.0 %
Cost of goods sold	973,157	844,100	45.9	49.1
Gross profit	1,147,704	876,279	54.1	50.9
Selling, general and administrative expenses	773,288	640,032	36.5	37.2
Asset impairment and restructuring costs	—	36,524	—	2.1
Income from operations	374,416	199,723	17.7	11.6
Other income (expense), net	6,553	2,771	0.3	0.2
Income before income tax expense	380,969	202,494	18.0	11.8
Income tax expense	115,633	63,593	5.5	3.7
Net income	$265,336	$138,901	12.5 %	8.1 %

Net Revenue

Net revenue increased $400.5 million, or 23%, to $2.121 billion for the first three quarters of fiscal 2018 from $1.720 billion for the first three quarters of fiscal 2017. On a constant dollar basis, assuming the average exchange rates for the first three quarters of fiscal 2018 remained constant with the average exchange rates for the first three quarters of fiscal 2017, net revenue increased $397.9 million, or 23%.

The increase in net revenue was primarily due to increased direct to consumer net revenue, net revenue generated by new company-operated stores, and an increase in comparable store sales. Total comparable sales, which includes comparable store sales and direct to consumer, increased 19% in the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017. Total comparable sales increased 19% on a constant dollar basis.

Net revenue on a segment basis for the first three quarters ended October 28, 2018 and October 29, 2017 is summarized below. The percentages are presented as a percentage of total net revenue.

	Three Quarters Ended			
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)		(Percentages)	
Company-operated stores	$1,396,376	$1,218,127	65.8 %	70.8 %
Direct to consumer	514,623	341,453	24.3	19.8
Other	209,862	160,799	9.9	9.4
Net revenue	$2,120,861	$1,720,379	100.0%	100.0%

Company-Operated Stores. Net revenue from our company-operated stores segment increased $178.2 million, or 15%, to $1.396 billion in the first three quarters of fiscal 2018 from $1.218 billion in the first three quarters of fiscal 2017. The following contributed to the increase in net revenue from our company-operated stores segment:

- Net revenue from company-operated stores we opened or significantly expanded subsequent to October 29, 2017, and therefore not included in comparable store sales, contributed $134.5 million to the increase. We opened 38 net new lululemon branded company-operated stores since the third quarter of fiscal 2017, including 18 stores in North America, 11 stores in Asia, seven stores in Europe, and two stores in Australia/New Zealand.
- A comparable store sales increase of 8% in the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017 resulted in a $75.4 million increase to net revenue. Comparable store sales increased 8%, or $74.5 million on a constant dollar basis. The increase in comparable store sales was primarily a result of increased store traffic and improved conversion rates.

The increase in net revenue was partially offset by the closure of 48 of our ivivva branded company-operated stores as part of the restructuring of our ivivva operations. These closures reduced our net revenue from company-operated stores for the first three quarters of fiscal 2018 by $31.6 million compared to the first three quarters of fiscal 2017.

Direct to Consumer. Net revenue from our direct to consumer segment increased $173.2 million, or 51%, to $514.6 million in the first three quarters of fiscal 2018 from $341.5 million in the first three quarters of fiscal 2017. Direct to consumer net revenue increased 50% on a constant dollar basis. This was primarily a result of increased website traffic and improved conversion rates, and due to increased dollar value per transaction. During the second quarter of fiscal 2017, we held an online warehouse sale in the United States and Canada which generated net revenue of $12.3 million. We did not hold any online warehouse sales during the first three quarters of fiscal 2018.

Other. Net revenue from our other segment increased $49.1 million, or 31%, to $209.9 million in the first three quarters of fiscal 2018 from $160.8 million in the first three quarters of fiscal 2017. This increase was primarily the result of an increase in net revenue from new and existing outlets during the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017. There was also an increased number of temporary locations, including seasonal stores, open during the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017. The increase in net revenue from our other segment was partially offset by lower net revenue from showrooms, primarily due to a decreased number of showrooms open during the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017.

Gross Profit

Gross profit increased $271.4 million, or 31%, to $1.148 billion for the first three quarters of fiscal 2018 from $876.3 million for the first three quarters of fiscal 2017.

Gross profit as a percentage of net revenue, or gross margin, increased 320 basis points, to 54.1% in the first three quarters of fiscal 2018 from 50.9% in the first three quarters of fiscal 2017. The increase in gross margin was primarily the result of:

- an increase in product margin of 230 basis points, which was primarily due to lower product costs, a favorable mix of higher margin product, lower markdowns, and lower inventory provision expense;
- a decrease in occupancy and depreciation costs as a percentage of revenue of 50 basis points; and
- the costs incurred in the first three quarters of fiscal 2017 in connection with the restructuring of our ivivva operations, which reduced gross margin in that quarter by 50 basis points.

This was partially offset by an increase in costs as a percentage of revenue related to our distribution centers of 10 basis points.

During the first three quarters of fiscal 2017, as a result of the restructuring of our ivivva operations, we recognized costs totaling $8.8 million within costs of goods sold, as outlined in Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report. Excluding these charges from the comparatives for the first three quarters of fiscal 2017, gross profit increased 30% and gross margin increased 270 basis points.

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Selling, General and Administrative Expenses

Selling, general and administrative expenses increased $133.3 million, or 21%, to $773.3 million in the first three quarters of fiscal 2018 from $640.0 million in the first three quarters of fiscal 2017. The increase in selling, general and administrative expenses was primarily due to:

- an increase in costs related to our operating channels of $80.9 million, comprised of:
  - an increase in employee costs of $35.3 million primarily from a growth in labor hours and benefits, mainly associated with new company-operated stores and other new operating locations, and due to higher retail bonus expenses;
  - an increase in variable costs of $28.4 million primarily due to an increase in distribution costs, credit card fees, and packaging costs as a result of increased net revenue; and
  - an increase in other costs of $17.1 million primarily due to an increase in digital marketing expenses, brand and community costs, and other costs associated with our operating locations including security and repairs and maintenance;
- an increase in head office costs of $41.3 million, comprised of:
  - an increase in employee costs of $22.8 million primarily due to additional employees to support the growth in our business and increased incentive and stock-based compensation expense; and
  - an increase in other costs of $18.5 million primarily due to an increase in brand and community costs, information technology costs, depreciation, professional fees, and other head office costs; and
- an increase in net foreign exchange and derivative revaluation losses of $11.2 million.

As a percentage of net revenue, selling, general and administrative expenses decreased 70 basis points, to 36.5% in the first three quarters of fiscal 2018 from 37.2% in the first three quarters of fiscal 2017.

Asset Impairment and Restructuring Costs

During the first three quarters of fiscal 2017, we incurred asset impairment and restructuring costs totaling $36.5 million in connection with the restructuring of our ivivva operations. This included lease termination costs of $19.9 million, long-lived asset impairment charges of $11.6 million, employee related costs of $4.0 million, and other restructuring costs of $1.0 million. Please refer to Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

We did not have any asset impairment and restructuring costs in the first three quarters of fiscal 2018.

Income from Operations

Income from operations increased $174.7 million, or 87%, to $374.4 million in the first three quarters of fiscal 2018 from $199.7 million in the first three quarters of fiscal 2017. Operating margin increased 610 basis points to 17.7% compared to 11.6% in the first three quarters of fiscal 2017.

In connection with the restructuring of our ivivva operations, we recognized pre-tax costs totaling $45.4 million in the first three quarters of fiscal 2017. This included costs of $8.8 million recognized in cost of goods sold, and asset impairment and restructuring costs totaling $36.5 million. Excluding these charges from the comparatives for the first three quarters of fiscal 2017, income from operations increased 53% and operating margin increased 350 basis points.

On a segment basis, we determine income from operations without taking into account our general corporate expenses and the costs we incurred in connection with the restructuring of our ivivva operations. In the first quarter of fiscal 2018, we reviewed our general corporate expenses and determined certain costs which were previously classified as general corporate expenses are more appropriately classified within our direct to consumer segment. Accordingly, comparative figures have been reclassified to conform to the financial presentation adopted for the current year.

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Segmented income from operations for the first three quarters ended October 28, 2018 and October 29, 2017 is summarized below. The percentages are presented as a percentage of net revenue of the respective operating segments.

	Three Quarters Ended			
	October 28, 2018	October 29, 2017	October 28, 2018	October 29, 2017
	(In thousands)		(Percentage of segment revenue)	
Segmented income from operations:				
Company-operated stores	$342,959	$267,178	24.6%	21.9 %
Direct to consumer	205,735	123,045	40.0	36.0
Other	39,336	19,076	18.7	11.9
	588,030	409,299		
General corporate expense	213,614	164,211		
Restructuring and related costs	—	45,365		
Income from operations	$374,416	$199,723		

Company-Operated Stores. Income from operations from our company-operated stores segment increased $75.8 million, or 28%, to $343.0 million for the first three quarters of fiscal 2018 from $267.2 million for the first three quarters of fiscal 2017. The increase was primarily the result of increased gross profit of $110.5 million which was primarily due to increased net revenue and higher gross margin. This was partially offset by an increase in selling, general and administrative expenses, primarily due to increased employee costs, increased store operating expenses including higher credit card fees, distribution costs, and packaging costs as a result of higher net revenue, and due to increased community costs. Income from operations as a percentage of company-operated stores net revenue increased by 270 basis points, primarily due to an increase in gross margin and leverage on selling, general and administrative expenses.

Direct to Consumer. Income from operations from our direct to consumer segment increased $82.7 million, or 67%, to $205.7 million for the first three quarters of fiscal 2018 from $123.0 million for the first three quarters of fiscal 2017. The increase was primarily the result of increased gross profit of $118.9 million which was primarily due to increased net revenue and higher gross margin. This was partially offset by an increase in selling, general and administrative expenses primarily due to higher variable costs including distribution costs, credit card fees, and packaging costs as a result of higher net revenue, higher digital marketing expenses, and increased employee costs. Income from operations as a percentage of direct to consumer net revenue increased 400 basis points, primarily due to leverage on selling, general and administrative expenses and an increase in gross margin.

Other. Other income from operations increased $20.3 million, or 106%, to $39.3 million for the first three quarters of fiscal 2018 from $19.1 million for the first three quarters of fiscal 2017. The increase was primarily the result of increased gross profit of $33.2 million which was primarily due to increased net revenue and higher gross margin. The increase in gross profit was partially offset by an increase in selling, general and administrative expenses, including increased employee costs, increased operating expenses including higher distribution costs and higher credit card fees as a result of higher net revenue, and due to higher community costs. Income from operations as a percentage of other net revenue increased 680 basis points, primarily due to an increase in gross margin and leverage on selling, general and administrative expenses.

General Corporate Expense. General corporate expense increased $49.4 million, or 30%, to $213.6 million for the first three quarters of fiscal 2018 from $164.2 million for the first three quarters of fiscal 2017. This increase was primarily due to increases in head office employee costs, brand and community costs, information technology costs, professional fees, and depreciation and an increase in net foreign exchange and derivative revaluation losses of $11.2 million.

Other Income (Expense), Net

Other income, net increased $3.8 million, or 136%, to $6.6 million for the first three quarters of fiscal 2018 from income of $2.8 million for the first three quarters of fiscal 2017. The increase was primarily due to an increase in net interest income, primarily due to higher rates of return on our cash and cash equivalents, including money market funds, treasury bills, and term deposits, and due to an increase in cash and cash equivalents in the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017. This was partially offset by an increase in interest expense, primarily related to borrowings on our revolving credit facility during the first three quarters of fiscal 2018. We repaid the outstanding balance on our revolving credit facility during the third quarter of fiscal 2018 and had no borrowings outstanding under this credit facility as of October 28, 2018.

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Income Tax Expense

Income tax expense increased $52.0 million, or 82%, to $115.6 million for the first three quarters of fiscal 2018 from $63.6 million for the first three quarters of fiscal 2017.

U.S. tax reform was enacted on December 22, 2017 and introduced significant changes to U.S. income tax law. We recorded certain provisional amounts in the fourth quarter of fiscal 2017. During the third quarter of fiscal 2018, we adjusted the provisional amount recorded for the mandatory one-time transition tax on the deemed repatriation of accumulated undistributed earnings of foreign subsidiaries. This resulted in the recognition of an additional tax expense of $5.2 million. We expect the accounting for the income tax effects of the U.S. tax reform to be completed in fiscal 2018. Please refer to Note 8 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

During the first three quarters of fiscal 2017, we recognized a net income tax recovery of $11.9 million on the costs recognized in connection with the ivivva restructuring. Please refer to Note 7 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report.

The effective tax rate for the first three quarters of fiscal 2018 was 30.4% compared to 31.4% for the first three quarters of fiscal 2017. Excluding the above tax adjustments, the adjusted effective tax rate was 29.0% for the first three quarters of fiscal 2018 compared to 30.5% for the first three quarters of fiscal 2017. The decrease in the adjusted effective tax rate was primarily due to the lower U.S. federal income tax rate as a result of the U.S. tax reform, as well as increased tax deductions related to stock-based compensation and increased research and development tax credits. This was partially offset by the amounts recognized for GILTI taxes.

Net Income

Net income increased $126.4 million, or 91%, to $265.3 million for the first three quarters of fiscal 2018 from $138.9 million for the first three quarters of fiscal 2017. This was primarily due to an increase in gross profit of $271.4 million, a reduction in long-lived asset impairment and restructuring costs of $36.5 million, and an increase in other income (expense), net of $3.8 million, partially offset by an increase in selling, general and administrative expenses of $133.3 million and an increase in income tax expense of $52.0 million.

Comparable Store Sales and Total Comparable Sales

We separately track comparable store sales, which reflect net revenue from company-operated stores that have been open for at least 12 months, or open for at least 12 months after being significantly expanded. Net revenue from a store is included in comparable store sales beginning with the first month for which the store has a full month of sales in the prior year. Comparable store sales exclude sales from new stores that have not been open for at least 12 months, from stores which have not been in their significantly expanded space for at least 12 months, and from stores which have been temporarily relocated for renovations. Comparable store sales also exclude sales from direct to consumer, outlets, temporary locations, wholesale accounts, showrooms, warehouse sales, license and supply arrangements, and sales from company-operated stores that we have closed. Total comparable sales combines comparable store sales and direct to consumer sales. The comparable sales measures we report may not be equivalent to similarly titled measures reported by other companies.

Non-GAAP Financial Measures

Constant dollar changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue, and the adjusted financial results are non-GAAP financial measures.

A constant dollar basis assumes the average foreign exchange rates for the period remained constant with the average foreign exchange rates for the same period of the prior year. We provide constant dollar changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue because we use these measures to understand the underlying growth rate of net revenue excluding the impact of changes in foreign exchange rates. We believe that disclosing these measures on a constant dollar basis is useful to investors because it enables them to better understand the level of growth of our business.

Adjusted gross profit, gross margin, income from operations, operating margin, income tax expense, effective tax rates, and diluted earnings per share exclude the amounts recognized in connection with the U.S. tax reform and the costs and related tax effects recognized in connection with the restructuring of our ivivva operations. We believe these adjusted financial measures are useful to investors as the adjustments do not directly relate to our ongoing business operations and therefore do not contribute to a meaningful evaluation of the trend in our operating performance. Furthermore, we do not believe the adjustments are reflective of our expectations of our future operating performance and believe these non-GAAP measures are useful to investors because of their comparability to our historical information.

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The presentation of this financial information is not intended to be considered in isolation or as a substitute for, or with greater prominence to, the financial information prepared and presented in accordance with GAAP. A reconciliation of the non-GAAP financial measures follows, which includes more detail on the GAAP financial measure that is most directly comparable to each non-GAAP financial measure, and the related reconciliations between these financial measures.

The below changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue, show the change compared to the corresponding period in the prior year.

Constant dollar changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue

	Quarter Ended October 28, 2018		Three Quarters Ended October 28, 2018	
	(In thousands)	(Percentages)	(In thousands)	(Percentages)
Change in net revenue	$128,637	21 %	$400,482	23 %
Adjustments due to foreign exchange rate changes	9,324	1	(2,567)	—
Change in net revenue in constant dollars	$137,961	22 %	$397,915	23 %

	Quarter Ended October 28, 2018	Three Quarters Ended October 28, 2018
Change in total comparable sales[(1),(2)]	17 %	19 %
Adjustments due to foreign exchange rate changes	1	—
Change in total comparable sales in constant dollars[(1),(2)]	18 %	19 %

	Quarter Ended October 28, 2018		Three Quarters Ended October 28, 2018	
	(In thousands)	(Percentages)	(In thousands)	(Percentages)
Change in comparable store sales[(2)]	$16,719	6 %	$75,376	8 %
Adjustments due to foreign exchange rate changes	4,674	1	(847)	—
Change in comparable store sales in constant dollars[(2)]	$21,393	7 %	$74,529	8 %

	Quarter Ended October 28, 2018	Three Quarters Ended October 28, 2018
Change in direct to consumer net revenue	44 %	51 %
Adjustments due to foreign exchange rate changes	2	(1)
Change in direct to consumer net revenue in constant dollars	46 %	50 %

(1) Total comparable sales includes comparable store sales and direct to consumer sales.

(2) Comparable store sales reflects net revenue from company-operated stores that have been open for at least 12 months, or open for at least 12 months after being significantly expanded.

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Adjusted financial measures

The following tables reconcile the adjusted financial measures with the most directly comparable measures calculated in accordance with GAAP. The adjustments relate to U.S. tax reform and the restructuring of our ivivva operations and its related tax effects. Please refer to Notes 7 and 8 to the unaudited interim consolidated financial statements included in Item 1 of Part I of this report for further information on these adjustments.

	Quarter Ended October 28, 2018			Quarter Ended October 29, 2017		
	GAAP Results	U.S. Tax Reform	Adjusted Results (Non-GAAP)	GAAP Results	Restructuring of ivivva Operations Adjustments	Adjusted Results (Non-GAAP)
	(In thousands, except per share amounts)					
Gross profit	$406,777	$—	$406,777	$321,962	$1,178	$323,140
Gross margin	54.4 %	— %	54.4 %	52.0 %	0.2 %	52.2 %
Income from operations	135,903	—	135,903	85,588	22,186	107,774
Operating margin	18.2 %	— %	18.2 %	13.8 %	3.6 %	17.4 %
Income before income tax expense	137,947	—	137,947	86,640	22,185	108,825
Income tax expense	43,534	(5,163)	38,371	27,696	5,813	33,509
Effective tax rate	31.6 %	(3.8)%	27.8 %	32.0 %	(1.2)%	30.8 %
Diluted earnings per share	$0.71	$0.04	$0.75	$0.43	$0.13	$0.56

	Three Quarters Ended October 28, 2018			Three Quarters Ended October 29, 2017		
	GAAP Results	U.S. Tax Reform	Adjusted Results (Non-GAAP)	GAAP Results	Restructuring of ivivva Operations Adjustments	Adjusted Results (Non-GAAP)
	(In thousands, except per share amounts)					
Gross profit	$1,147,704	$—	$1,147,704	$876,279	$8,841	$885,120
Gross margin	54.1 %	— %	54.1 %	50.9 %	0.5 %	51.4 %
Income from operations	374,416	—	374,416	199,723	45,365	245,088
Operating margin	17.7 %	— %	17.7 %	11.6 %	2.6 %	14.2 %
Income before income tax expense	380,969	—	380,969	202,494	45,365	247,859
Income tax expense	115,633	(5,163)	110,471	63,593	11,886	75,479
Effective tax rate	30.4 %	(1.4)%	29.0 %	31.4 %	(0.9)%	30.5 %
Diluted earnings per share	$1.97	$0.04	$2.01	$1.02	$0.24	$1.26

Seasonality

Our business is affected by the general seasonal trends common to the retail apparel industry. Our annual net revenue is weighted more heavily toward our fourth fiscal quarter, reflecting our historical strength in sales during the holiday season, while our operating expenses are more equally distributed throughout the year. As a result, a substantial portion of our operating profits are generated in the fourth quarter of our fiscal year. For example, we generated approximately 56%, 47%, and 45% of our full year operating profit during the fourth quarters of fiscal 2017, fiscal 2016, and fiscal 2015, respectively. Excluding the costs we incurred in connection with the ivivva restructuring, we generated approximately 51% of our operating profit during the fourth quarter of fiscal 2017.

Liquidity and Capital Resources

Our primary sources of liquidity are our current balances of cash and cash equivalents, cash flows from operations, and capacity under our revolving credit facility. Our primary cash needs are capital expenditures for opening new stores and remodeling or relocating existing stores, making information technology system investments and enhancements, funding working capital requirements, and making other strategic capital investments both in North

America and internationally. We may also use cash to repurchase shares of our common stock. Cash and cash equivalents in excess of our needs are held in interest bearing accounts with financial institutions, as well as in money market funds, treasury bills, and term deposits.

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As of October 28, 2018, our working capital, excluding cash and cash equivalents, was $216.2 million, our cash and cash equivalents were $703.6 million, and our capacity under our revolving facility was $398.8 million.

The following table summarizes our net cash flows provided by and used in operating, investing, and financing activities for the periods indicated:

	Three Quarters Ended	
	October 28, 2018	October 29, 2017
	(In thousands)	
Total cash provided by (used in):		
Operating activities	$316,876	$131,309
Investing activities	(165,914)	(120,051)
Financing activities	(406,361)	(100,707)
Effect of exchange rate changes on cash	(31,495)	4,657
Decrease in cash and cash equivalents	$(286,894)	$(84,792)

Operating Activities

Cash flows provided by operating activities consist primarily of net income adjusted for certain items including depreciation and amortization, stock-based compensation expense, and the effect of changes in operating assets and liabilities.

Cash provided by operating activities increased $185.6 million, to $316.9 million for the first three quarters of fiscal 2018 compared to $131.3 million for the first three quarters of fiscal 2017, primarily as a result of the following:

Net income and non-cash items

- an increase of $126.4 million in net income, and an increase of $12.9 million in non-cash expenses primarily related to an increase in deferred income taxes, depreciation, and stock-based compensation, partially offset by a decrease in asset impairment costs related to the restructuring of our ivivva operations and the settlement of derivatives not designated in a hedging relationship.

Changes in operating assets and liabilities

- an increase of $46.3 million in the change in operating assets and liabilities, primarily due to the following:
  - an increase of $140.8 million related to accounts payable, primarily due to a change in our payment terms;
  - partially offset by an increase of $97.4 million related to inventory, primarily due to an increase in inventory purchases.

Investing Activities

Cash flows used in investing activities relate to capital expenditures, the settlement of net investment hedges, and other investing activities. The capital expenditures were primarily for opening new company-operated stores, remodeling or relocating certain stores, and ongoing store refurbishment. We also had capital expenditures related to information technology and business systems, related to corporate buildings, and for opening retail locations other than company-operated stores.

Cash used in investing activities increased $45.9 million to $165.9 million for the first three quarters of fiscal 2018 from $120.1 million for the first three quarters of fiscal 2017. The increase was primarily the result of an increase in corporate capital expenditures related to information technology and business systems. Increased capital expenditures related to our company-operated stores also contributed to the increase in cash used in investing activities, primarily as a result of an increase in renovations and relocations of existing stores. The increase in cash used in investing activities was partially offset by a decrease in direct to consumer capital expenditures.

Financing Activities

Cash flows used in financing activities consist primarily of cash used to repurchase shares of our common stock, certain cash flows related to stock-based compensation, and other financing activities.

Cash used in financing activities increased $305.7 million to $406.4 million for the first three quarters of fiscal 2018 compared to $100.7 million for the first three quarters of fiscal 2017. The increase was primarily the result of our stock repurchases.

On December 1, 2016, our board of directors approved a program to repurchase shares of our common stock up to an aggregate value of $100.0 million. This stock repurchase program was completed during the third quarter of fiscal 2017. On November 29, 2017, our board of directors approved a program to repurchase shares of our common stock up to an aggregate value of $200.0 million. On June 6, 2018, the board of directors approved an increase to this stock repurchase program, authorizing the repurchase of up to a total of $600.0 million of our common shares on the open market or in privately negotiated transactions.

Our cash used in financing activities for the first three quarters of fiscal 2018 included $414.3 million to repurchase 3.4 million shares of our common stock compared to $99.3 million to repurchase 1.8 million shares for the first three quarters of fiscal 2017. During the second quarter of fiscal 2018, we repurchased 3.3 million shares in a private transaction. The other common stock was repurchased in the open market at prevailing market prices, including under plans complying with the provisions of Rule 10b5-1 and Rule 10b-18 of the Securities Exchange Act of 1934, with the timing and actual number of shares repurchased depending upon market conditions, eligibility to trade, and other factors.

We believe that our cash and cash equivalent balances, cash generated from operations, and borrowings available to us under our revolving credit facility will be adequate to meet our liquidity needs and capital expenditure requirements for at least the next 12 months. Our cash from operations may be negatively impacted by a decrease in demand for our products as well as the other factors described in Item 1 of Part II of this Quarterly Report on Form 10-Q. In addition, we may make discretionary capital improvements with respect to our stores, distribution facilities, headquarters, or systems, or we may repurchase shares under an approved stock repurchase program, which we would expect to fund through the use of cash, issuance of debt or equity securities or other external financing sources to the extent we were unable to fund such capital expenditures out of our cash and cash equivalents and cash generated from operations.

Revolving Credit Facility

On December 15, 2016, we entered into a credit agreement for $150.0 million under an unsecured five-year revolving credit facility. Bank of America, N.A., is administrative agent and HSBC Bank Canada is the syndication agent and letter of credit issuer, and the lenders party thereto. Borrowings under the revolving credit facility may be made, in U.S. Dollars, Euros, Canadian Dollars, and in other currencies, subject to the approval of the administrative agent and the lenders. Up to $35.0 million of the revolving credit facility is available for the issuance of letters of credit and up to $25.0 million is available for the issuance of swing line loans. Commitments under the revolving credit facility may be increased by up to $200.0 million, subject to certain conditions, including the approval of the lenders. Borrowings under the agreement may be prepaid and commitments may be reduced or terminated without premium or penalty (other than customary breakage costs). The principal amount outstanding under the credit agreement, if any, will be due and payable in full on December 15, 2021, subject to provisions that permit us to request a limited number of one year extensions annually.

Borrowings made under the revolving credit facility bear interest at a rate per annum equal to, at our option, either (a) a rate based on the rates applicable for deposits on the interbank market for U.S. Dollars or the applicable currency in which the borrowings are made ("LIBOR") or (b) an alternate base rate, plus, in each case, an applicable margin. The applicable margin is determined by reference to a pricing grid, based on the ratio of indebtedness to earnings before interest, tax depreciation, amortization, and rent ("EBITDAR") and ranges between 1.00%-1.75% for LIBOR loans and 0.00%-0.75% for alternate base rate loans. Additionally, a commitment fee of between 0.125%-0.200%, also determined by reference to the pricing grid, is payable on the average daily unused amounts under the revolving credit facility.

The credit agreement contains negative covenants that, among other things and subject to certain exceptions, limit the ability of our subsidiaries to incur indebtedness, incur liens, undergo fundamental changes, make dispositions of all or substantially all of their assets, alter their businesses and enter into agreements limiting subsidiary dividends and distributions.

We are also required to maintain a consolidated rent-adjusted leverage ratio of not greater than 3.50:1.00 and we are not permitted to allow the ratio of consolidated EBITDAR to consolidated interest charges (plus rent) to be less than 2.00:1.00. The credit agreement also contains certain customary representations, warranties, affirmative covenants,

and events of default (including, among others, an event of default upon the occurrence of a change of control). If an event of default occurs, the credit agreement may be terminated and the maturity of any outstanding amounts may be accelerated.
On June 6, 2018, we entered into Amendment No. 1 to the credit agreement. The Amendment amends the credit agreement to provide for (i) an increase in the aggregate commitments under the unsecured five-year revolving credit facility to $400.0 million, with an increase of the sub-limits for the issuance of letters of credit and extensions of swing line loans to $50.0 million for each, (ii) an increase in the option, subject to certain conditions as set forth in the credit agreement, to request increases in commitments under the revolving facility from $400.0 million to $600.0 million and (iii) an extension in the maturity of the revolving facility from December 15, 2021 to June 6, 2023.

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In addition, the Amendment decreases the applicable margins for LIBOR loans from 1.00%-1.75% to 1.00%-1.50% and for alternate base rate loans from 0.00%-0.75% to 0.00%-0.50%, reduces the commitment fee on average daily unused amounts under the revolving facility from 0.125%-0.200% to 0.10%-0.20%, and reduces fees for unused letters of credit from 1.00%-1.75% to 1.00%-1.50%.

As of October 28, 2018, aside from letters of credit of $1.2 million, we had no other borrowings outstanding under this credit facility.

Off-Balance Sheet Arrangements

We enter into standby letters of credit to secure certain of our obligations, including leases, taxes, and duties. As of October 28, 2018, letters of credit and letters of guarantee totaling $1.2 million had been issued.

We have not entered into any transactions, agreements or other contractual arrangements to which an entity unconsolidated with us is a party and under which we have (i) any obligation under a guarantee, (ii) any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity, (iii) any obligation under derivative instruments that are indexed to our shares and classified as equity in our consolidated balance sheets, or (iv) any obligation arising out of a variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions. Predicting future events is inherently an imprecise activity and, as such, requires the use of judgment. Actual results may vary from our estimates in amounts that may be material to the financial statements. An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact our consolidated financial statements. Our critical accounting policies and estimates are discussed in our fiscal 2017 Annual Report on Form 10-K filed with the SEC on March 27, 2018, and in Notes 2, 5, and 6 included in Item 1 of Part I of this Quarterly Report on Form 10-Q.

Operating Locations

Our company-operated stores by country as of October 28, 2018 and January 28, 2018 are summarized in the table below.

	October 28, 2018	January 28, 2018
United States [1]	282	274
Canada	61	60
Australia	29	28
China [2]	17	15
United Kingdom	12	9
New Zealand	6	6
Germany	4	2
Japan	4	2
South Korea	4	3
Singapore	3	3
France	1	—
Ireland		