

GUESS INC
Form 10-Q
December 07, 2018
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended November 3, 2018

OR

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: 1-11893

GUESS?, INC.

(Exact name of registrant as specified in its charter)

Delaware 95-3679695

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1444 South Alameda Street

Los Angeles, California 90021

(Address of principal executive offices) (Zip Code)

(213) 765-3100

(Registrant's telephone number, including area code)

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 No

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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.

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Emerging growth company

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.

Edgar Filing: GUESS INC - Form 10-Q

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

As of December 4, 2018, the registrant had 81,038,868 shares of Common Stock, \$.01 par value per share, outstanding.

Table of Contents

GUESS?, INC.	
FORM 10-Q	
TABLE OF CONTENTS	
PART I. FINANCIAL INFORMATION	
<u>Item 1. Financial Statements (unaudited)</u>	<u>1</u>
<u>Condensed Consolidated Balance Sheets as of November 3, 2018 and February 3, 2018</u>	<u>1</u>
<u>Condensed Consolidated Statements of Loss — Three and Nine Months Ended November 3, 2018 and October 28, 2017</u>	<u>2</u>
<u>Condensed Consolidated Statements of Comprehensive Income (Loss) — Three and Nine Months Ended November 3, 2018 and October 28, 2017</u>	<u>3</u>
<u>Condensed Consolidated Statements of Cash Flows — Nine Months Ended November 3, 2018 and October 28, 2017</u>	<u>4</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>5</u>
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>34</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>57</u>
<u>Item 4. Controls and Procedures</u>	<u>60</u>
PART II. OTHER INFORMATION	
<u>Item 1. Legal Proceedings</u>	<u>60</u>
<u>Item 1A. Risk Factors</u>	<u>60</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>61</u>
<u>Item 6. Exhibits</u>	<u>62</u>

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. Financial Statements.****GUESS?, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(in thousands, except share data)

Nov 3, 2018 Feb 3, 2018
(unaudited)**ASSETS**

Cash and cash equivalents	\$ 138,922	\$ 367,441
Accounts receivable, net	286,106	259,996
Inventories	548,517	428,304
Other current assets	109,178	52,964
Total current assets	1,082,723	1,108,705
Property and equipment, net	297,173	294,254
Goodwill	36,893	38,481
Other intangible assets, net	7,063	5,977
Deferred tax assets	64,437	68,386
Restricted cash	532	241
Other assets	135,325	139,590
	\$ 1,624,146	\$ 1,655,634

LIABILITIES AND STOCKHOLDERS' EQUITY**Current liabilities:**

Current portion of capital lease obligations and borrowings	\$ 3,538	\$ 2,845
Accounts payable	314,068	264,438
Accrued expenses	243,058	200,562
Total current liabilities	560,664	467,845
Long-term debt and capital lease obligations	36,254	39,196
Deferred rent and lease incentives	81,765	81,564
Other long-term liabilities	110,104	127,964
Redeemable noncontrolling interests	788,787	716,569
	4,804	5,590

Commitments and contingencies (Note 12)**Stockholders' equity:**

Preferred stock, \$.01 par value. Authorized 10,000,000 shares; no shares issued and outstanding	—	—
Common stock, \$.01 par value. Authorized 150,000,000 shares; issued 142,342,270 and 141,623,687 shares, outstanding 81,007,525 and 81,371,118 shares, as of November 3, 2018 and February 3, 2018, respectively	810	813
Paid-in capital	515,067	498,249
Retained earnings	1,072,988	1,132,173
Accumulated other comprehensive loss	(133,408)	(93,062)
Treasury stock, 61,334,745 and 60,252,569 shares as of November 3, 2018 and February 3, 2018, respectively	(638,559)	(621,354)
Guess?, Inc. stockholders' equity	816,898	916,819
Nonredeemable noncontrolling interests	13,657	16,656
Total stockholders' equity	830,555	933,475

Edgar Filing: GUESS INC - Form 10-Q

\$1,624,146 \$1,655,634

See accompanying notes to condensed consolidated financial statements.

1

Table of Contents

GUESS?, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF LOSS

(in thousands, except per share data)

(unaudited)

	Three Months Ended Nov 3, 2018	Oct 28, 2017	Nine Months Ended Nov 3, 2018	Oct 28, 2017
Product sales	\$583,121	\$528,209	\$1,710,788	\$1,518,323
Net royalties	22,286	20,744	61,779	53,267
Net revenue	605,407	548,953	1,772,567	1,571,590
Cost of product sales	385,264	357,844	1,139,055	1,037,812
Gross profit	220,143	191,109	633,512	533,778
Selling, general and administrative expenses	197,943	178,009	600,731	517,871
European Commission fine	42,428	—	42,428	—
Asset impairment charges	1,277	2,018	5,017	6,013
Net (gains) losses on lease terminations	—	11,494	(152)	11,494
Loss from operations	(21,505)	(412 )	) (14,512 )	) (1,600)
Other income (expense):				
Interest expense	(784)	(684 )	) (2,386 )	) (1,642)
Interest income	783	891	2,892	3,022
Other income (expense), net	(5,810)	2,216	(7,064)	1,935
	(5,811)	2,423	(6,558)	3,315
Earnings (loss) before income tax expense (benefit)	(27,316)	2,011	(21,070)	1,715
Income tax expense (benefit)	(14,500)	3,673	(13,001)	8,723
Net loss	(12,816)	(1,662 )	) (8,069 )	) (7,008)
Net earnings attributable to noncontrolling interests	626	1,198	1,064	1,926
Net loss attributable to Guess?, Inc.	\$ (13,442)	\$ (2,860)	\$ (9,133 )	) \$ (8,934)
Net loss per common share attributable to common stockholders (Note 3):				
Basic	\$ (0.17)	\$ (0.04)	\$ (0.12 )	) \$ (0.12)
Diluted	\$ (0.17)	\$ (0.04)	\$ (0.12 )	) \$ (0.12)
Weighted average common shares outstanding attributable to common stockholders (Note 3):				
Basic	80,189	82,390	80,067	82,599
Diluted	80,189	82,390	80,067	82,599
Dividends declared per common share	\$ 0.225	\$ 0.225	\$ 0.675	\$ 0.675

See accompanying notes to condensed consolidated financial statements.

Table of Contents

GUESS?, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF
COMPREHENSIVE INCOME (LOSS)
(in thousands)
(unaudited)

	Three Months Ended Nov 3, 2018	Oct 28, 2017	Nov 3, 2018	Oct 28, 2017	Nine Months Ended Nov 3, 2018
Net loss	\$12,816	\$(1,662)	\$(8,069)	\$(7,008)	\$(7,008)
Other comprehensive income (loss) (“OCI”):					
Foreign currency translation adjustment					
Gains (losses) arising during the period	(11,745)	(9,102)	(59,270)	47,770	47,770
Derivative financial instruments designated as cash flow hedges					
Gains (losses) arising during the period	1,833	3,387	14,000	(11,702)	(11,702)
Less income tax effect	(237)	(638)	(1,825)	1,482	1,482
Reclassification to net loss for (gains) losses realized	1,597	313	5,787	(997)	(997)
Less income tax effect	(178)	(78)	(720)	50	50
Defined benefit plans					
Foreign currency and other adjustments	42	106	345	2	2
Less income tax effect	(5)	(9)	(31)	—	—
Net actuarial loss amortization	150	116	453	344	344
Prior service credit amortization	(7)	(7)	(21)	(20)	(20)
Less income tax effect	(19)	(21)	(58)	(62)	(62)
Total comprehensive income (loss)	(21,385)	(7,595)	(49,409)	29,859	29,859
Less comprehensive income (loss) attributable to noncontrolling interests:					
Net earnings	626	1,198	1,064	1,926	1,926
Foreign currency translation adjustment	(1,181)	(918)	(994)	1,402	1,402
Amounts attributable to noncontrolling interests	(555)	280	70	3,328	3,328
Comprehensive income (loss) attributable to Guess?, Inc.	\$(20,830)	\$(7,875)	\$(49,479)	\$26,531	\$26,531

See accompanying notes to condensed consolidated financial statements.

Table of Contents

GUESS?, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Nine Months Ended	
	Nov 3, 2018	Oct 28, 2017
Cash flows from operating activities:		
Net loss	\$(8,069)	\$(7,008)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization of property and equipment	47,391	45,614
Amortization of other long-term and intangible assets	3,008	1,155
Share-based compensation expense	12,534	12,410
Unrealized forward contract (gains) losses	(1,884)	1,532
Net loss on disposition of property and equipment and long-term assets	5,663	4,548
Other items, net	12,937	(5,278)
Changes in operating assets and liabilities:		
Accounts receivable	(6,065)	2,527
Inventories	(159,463)	(93,337)
Prepaid expenses and other assets	(28,398)	(11,817)
Accounts payable and accrued expenses	87,857	21,411
Deferred rent and lease incentives	2,975	1,354
Other long-term liabilities	(15,401)	(7,313)
Net cash used in operating activities	(46,915)	(34,202)
Cash flows from investing activities:		
Purchases of property and equipment	(74,890)	(65,345)
Proceeds from sale of long-term assets	—	1,052
Changes in other assets	—	(553)
Acquisition of businesses, net of cash acquired	(6,404)	(2,929)
Net cash settlement of forward contracts	156	(354)
Purchases of investments	(2,093)	(497)
Net cash used in investing activities	(83,231)	(68,626)
Cash flows from financing activities:		
Proceeds from borrowings	—	166
Repayment of capital lease obligations and borrowings	(1,469)	(665)
Dividends paid	(54,858)	(56,527)
Noncontrolling interest capital contribution	—	962
Noncontrolling interest capital distribution	(3,069)	(1,358)
Issuance of common stock, net of tax withholdings on vesting of stock awards	4,737	(82)
Purchase of treasury stock	(23,620)	(24,812)
Net cash used in financing activities	(78,279)	(82,316)
Effect of exchange rates on cash, cash equivalents and restricted cash	(19,803)	20,808
Net change in cash, cash equivalents and restricted cash	(228,228)	(164,336)
Cash, cash equivalents and restricted cash at the beginning of the year	367,682	397,650
Cash, cash equivalents and restricted cash at the end of the period	\$139,454	\$233,314
Supplemental cash flow data:		
Interest paid	\$961	\$849
Income taxes paid	\$28,039	\$18,124

Edgar Filing: GUESS INC - Form 10-Q

Non-cash investing and financing activity:

Assets acquired under capital lease obligations	\$1,172	\$18,042
---	---------	----------

See accompanying notes to condensed consolidated financial statements.

Table of Contents

GUESS?, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

November 3, 2018

(unaudited)

(1) Basis of Presentation and New Accounting Guidance

Description of the Business

Guess?, Inc. (the “Company” or “GUESS?”) designs, markets, distributes and licenses a leading lifestyle collection of contemporary apparel and accessories for men, women and children that reflect the American lifestyle and European fashion sensibilities. The Company’s designs are sold in GUESS? owned stores, to a network of wholesale accounts that includes better department stores, selected specialty retailers and upscale boutiques and through the Internet.

GUESS? branded products, some of which are produced under license, are also sold internationally through a series of retail store licensees and wholesale distributors.

Basis of Presentation

In the opinion of management, the accompanying unaudited condensed consolidated financial statements of the Company contain all adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation of the condensed consolidated balance sheets as of November 3, 2018 and February 3, 2018, the condensed consolidated statements of loss and comprehensive income (loss) for the three and nine months ended November 3, 2018 and October 28, 2017 and the condensed consolidated statements of cash flows for the nine months ended November 3, 2018 and October 28, 2017. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (“GAAP”) for interim financial information and the instructions to Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (the “SEC”). Accordingly, they have been condensed and do not include all of the information and footnotes required by GAAP for complete financial statements. The results of operations for the three and nine months ended November 3, 2018 are not necessarily indicative of the results of operations to be expected for the full fiscal year. These financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended February 3, 2018.

The three and nine months ended November 3, 2018 had the same number of days as the three and nine months ended October 28, 2017. All references herein to “fiscal 2019,” “fiscal 2018” and “fiscal 2017” represent the results of the 52-week fiscal year ending February 2, 2019, the 53-week fiscal year ended February 3, 2018 and the 52-week fiscal year ended January 28, 2017, respectively.

Reclassifications

The Company has made certain reclassifications to prior year amounts to conform to the current period presentation within the accompanying notes to the condensed consolidated financial statements.

Net Gains (Losses) on Lease Terminations

During the nine months ended November 3, 2018, the Company recorded net gains on lease terminations of approximately \$0.2 million related primarily to the early termination of certain lease agreements in North America. The net gains on lease terminations were recorded during the three months ended May 5, 2018.

During the third quarter of fiscal 2018, the Company recorded net losses of \$11.5 million on lease terminations related primarily to the modification of certain lease agreements held with a common landlord in North America. In connection with this modification, the Company made up-front payments of approximately \$22.0 million, of which \$12.4 million was recognized as net losses on lease terminations and \$9.6 million was recorded as advance rent payments. During the third quarter of fiscal 2018, the Company also recorded net gains on lease terminations of approximately \$1.0 million related primarily to the early termination of certain lease agreements in Europe.

Table of Contents

New Accounting Guidance

Changes in Accounting Policies

In May 2014, the Financial Accounting Standards Board (“FASB”) issued a comprehensive new revenue recognition standard which superseded previous existing revenue recognition guidance. The standard is intended to clarify the principles of recognizing revenue and create common revenue recognition guidance between GAAP and International Financial Reporting Standards. The standard also requires expanded disclosures surrounding revenue recognition.

During fiscal 2017, the FASB issued additional clarification guidance on the new revenue recognition standard which also included certain scope improvements and practical expedients. The Company adopted this guidance (including clarification guidance issued) effective February 4, 2018 using the modified retrospective method and, as a result, recorded a cumulative adjustment to increase retained earnings by approximately \$5.8 million, net of taxes. The adjustment related primarily to changes in the presentation of advertising contributions received from the Company’s licensees and the related advertising expenditures incurred by the Company. Under previous guidance, the Company recorded advertising contributions received from its licensees and the related advertising expenditures incurred by the Company on a net basis in its consolidated balance sheet. To the extent that the advertising contributions exceeded the Company’s advertising expenditures for its licensees, the excess contribution was treated as a deferred liability and was included in accrued expenses in the Company’s consolidated balance sheet. Under the new revenue recognition standard, advertising contributions and related advertising expenditures related to the Company’s licensing business are recorded on a gross basis in the Company’s condensed consolidated statements of loss. This change resulted in an increase to net revenue and selling, general, and administrative (“SG&A”) expenses of \$2.7 million and \$2.5 million, respectively, during the three months ended November 3, 2018 compared to the same prior-year period. During the nine months ended November 3, 2018, this change resulted in an increase to net revenue and SG&A expenses of \$7.1 million and \$7.2 million, respectively, compared to the same prior-year period. Other minor differences related to the timing of revenue recognition from the Company’s e-commerce operations, which are now recognized when merchandise is transferred to a common carrier rather than upon receipt by the customer, and a minimal change in the valuation of the amount that is deferred related to points earned under the Company’s loyalty programs. Additionally, allowances for wholesale sales returns and wholesale markdowns are now presented as accrued expenses rather than as reductions to accounts receivable, and the estimated cost associated with the allowance for sales returns is presented within other current assets rather than included in inventories in the Company’s condensed consolidated balance sheet. Refer to Note 2 for the Company’s expanded disclosures on revenue recognition.

In January 2016, the FASB issued authoritative guidance which requires equity investments not accounted for under the equity method of accounting or consolidation accounting to be measured at fair value, with subsequent changes in fair value recognized in net income. In February 2018, the FASB issued additional clarification guidance which made targeted improvements to address certain aspects of recognition, measurement, presentation and disclosure requirements for financial instruments. The Company adopted this guidance (including the clarification guidance) effective February 4, 2018. The adoption of this guidance did not result in a cumulative-effect adjustment as of the beginning of the current year and did not have a material impact on the Company’s condensed consolidated financial statements or related disclosures.

In October 2016, the FASB issued authoritative guidance which amends the accounting for income taxes on intra-entity transfers of assets other than inventory. This guidance requires that entities recognize the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs. The income tax consequences on intra-entity transfers of inventory will continue to be deferred until the inventory has been sold to a third party. The Company adopted this guidance effective February 4, 2018. The adoption of this guidance did not have an impact on the Company’s condensed consolidated financial statements or related disclosures.

In March 2017, the FASB issued authoritative guidance related to the presentation of net periodic pension cost in the income statement. This guidance requires that the service cost component of net periodic pension cost be presented in the same line as other compensation costs arising from services rendered by the employees during the period. The other non-service components of net periodic pension cost are required to be presented in the

Table of Contents

income statement separately from the service cost component and outside of earnings from operations. This guidance also allows for the service cost component to be eligible for capitalization when applicable. The Company adopted this guidance effective February 4, 2018 on a retrospective basis for the presentation of the service cost component and other non-service components of net periodic pension cost in the income statement and on a prospective basis for capitalization of the service cost component. As a result, the Company reclassified \$0.5 million and \$1.6 million from SG&A expenses to other income (expense) during the three and nine months ended October 28, 2017, respectively, which resulted in a related improvement in operating loss during each of the respective periods. Other than the change in presentation of other non-service components of net periodic pension cost within the Company's condensed consolidated statements of loss, the adoption of this guidance did not have an impact on the Company's condensed consolidated financial statements and related disclosures.

In May 2017, the FASB issued authoritative guidance that provides clarification on accounting for modifications in share-based payment awards. The Company adopted this guidance effective February 4, 2018. The adoption of this guidance did not have an impact on the Company's condensed consolidated financial statements or related disclosures. In June 2018, the FASB issued authoritative guidance that expanded the scope of stock compensation to include non-employee share-based payment transactions. The Company early adopted this guidance during the second quarter of fiscal 2019. The adoption of this guidance did not have a material impact on the Company's condensed consolidated financial statements or related disclosures.

Recently Issued Accounting Guidance

In February 2016, the FASB issued a comprehensive new lease standard which will supersede previous lease guidance. The standard requires a lessee to recognize an asset related to the right to use the underlying asset and a liability that approximates the present value of the lease payments over the term of contracts that qualify as leases under the new guidance. The standard also requires expanded disclosures surrounding leases. The standard (including clarification guidance issued during fiscal 2019) is effective for fiscal periods beginning after December 15, 2018, which will be the Company's first quarter of fiscal 2020, with early adoption permitted. The Company has completed the design phase of its selected lease management system and is in the process of completing its inventory of its lease contracts, validating data migration, as well as implementing processes and controls to enable the preparation of the required financial information for this standard. In July 2018, the FASB issued authoritative guidance that provides entities with an additional transition method of applying the new lease standard at the adoption date and recognizing a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Upon adoption of the standard, the Company expects to report material right-of-use assets and material lease liabilities as well as enhanced disclosures.

In June 2016, the FASB issued authoritative guidance related to the measurement of credit losses on financial instruments. This guidance is effective for fiscal years beginning after December 15, 2019, which will be the Company's first quarter of fiscal 2021. Early adoption is permitted for fiscal periods beginning after December 15, 2018, which will be the Company's first quarter of fiscal 2020. The Company is currently evaluating the impact of the adoption of this standard on its condensed consolidated financial statements and related disclosures.

In January 2017, the FASB issued authoritative guidance to simplify the testing for goodwill impairment by removing step two from the goodwill testing. Under current guidance, if the fair value of a reporting unit is lower than its carrying amount (step one), an entity would calculate an impairment charge by comparing the implied fair value of goodwill with its carrying amount (step two). The implied fair value of goodwill was calculated by deducting the fair value of the assets and liabilities of the respective reporting unit from the reporting unit's fair value as determined under step one. This guidance instead provides that an impairment charge should be recognized based on the difference between a reporting unit's fair value and its carrying value. This guidance also does not require a qualitative test to be performed on reporting units with zero or negative carrying amounts. However, entities need to disclose any reporting units with zero or negative carrying amounts that have goodwill and the amount of goodwill allocated to each. This guidance is effective for fiscal years beginning after December 15, 2019, which will be the Company's first quarter of fiscal 2021, with early adoption permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The adoption of this guidance is not

Table of Contents

expected to have a material impact on the Company's condensed consolidated financial statements or related disclosures.

In August 2017, the FASB issued authoritative guidance to better align the results of hedge accounting with an entity's risk management activities. This guidance updates the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results in the financial statements. In October 2018, the FASB clarified the new hedge accounting guidance by allowing the Secured Overnight Financing Rate to be eligible as a U.S. benchmark interest rate for purposes of applying hedge accounting. This guidance is effective for fiscal years beginning after December 15, 2018, which will be the Company's first quarter of fiscal 2020, and requires a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption, with early adoption permitted. The updated presentation and disclosure guidance is required only on a prospective basis. The adoption of this guidance is not expected to have a material impact on the Company's condensed consolidated financial statements or related disclosures.

In August 2018, the FASB issued authoritative guidance to modify the disclosure requirements on fair value measurements. This guidance is effective for fiscal years beginning after December 15, 2019, which will be the Company's first quarter of fiscal 2021, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this standard on its related disclosures.

In August 2018, the FASB issued authoritative guidance to modify the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance is effective for fiscal years beginning after December 15, 2020, which will be the Company's first quarter of fiscal 2022, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this standard on its related disclosures.

In August 2018, the FASB issued authoritative guidance to align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The guidance provides criteria for determining which implementation costs to capitalize as an asset related to the service contract and which costs to expense. The capitalized implementation costs are required to be expensed over the term of the hosting arrangement. The guidance also clarifies the presentation requirements for reporting such costs in the entity's financial statements. This guidance is effective for fiscal years beginning after December 15, 2019, which will be the Company's first quarter of fiscal 2021, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this standard on its condensed consolidated financial statements and related disclosures.

(2) Revenue Recognition

Significant Accounting Policies and Practices

Products Transferred at a Point in Time

The Company recognizes the majority of its revenue from its direct-to-consumer (brick-and-mortar retail stores and concessions as well as e-commerce) and wholesale distribution channels at a point in time when it satisfies a performance obligation and transfers control of the product to the respective customer. For the Company's brick-and-mortar retail stores and concessions, revenue is typically recognized at the point of sale. The Company adopted the new revenue recognition standard effective as of the first quarter of fiscal 2019, and accordingly, revenue generated from the Company's e-commerce sites is recognized when merchandise is transferred to a common carrier. This is a change compared to the Company's treatment under previous guidance where revenue from the Company's e-commerce sites was recognized based on the estimated customer receipt date. This change had an immaterial impact on revenue for the three and nine months ended November 3, 2018. Revenue generated from the Company's wholesale distribution channel is recognized when control transfers to the customer, which generally occurs upon shipment. The amount of revenue that is recognized is based on the transaction price, which represents the invoiced amount and includes estimates of variable consideration such as allowances for sales returns, markdowns and loyalty award obligations, where applicable. The amount of variable

Table of Contents

consideration included in the transaction price may be constrained and is included only to the extent that it is probable that a significant reversal in the amount of the cumulative revenue recognized under the contract will not occur in a future period.

The Company accepts payments at its brick-and-mortar retail locations and its e-commerce sites in the form of cash, credit cards, gift cards and loyalty points, where applicable. Payment terms, typically less than one year, are offered to the Company's wholesale customers and do not include a significant financing component. The Company extends credit to wholesale customers based upon an evaluation of the customer's financial condition and credit history and generally requires no collateral but does obtain credit insurance when considered appropriate. As of November 3, 2018, approximately 49% of the Company's total net trade receivables and 62% of its European net trade receivables were subject to credit insurance coverage, certain bank guarantees or letters of credit for collection purposes. The Company's credit insurance coverage contains certain terms and conditions specifying deductibles and annual claim limits. The Company maintains allowances for doubtful accounts for estimated losses that result from the inability of its wholesale customers to make their required payments. The Company bases its allowances on analysis of the aging of accounts receivable at the date of the financial statements, assessments of historical and current collection trends, an evaluation of the impact of current economic conditions and whether the Company has obtained credit insurance or other guarantees. Management performs regular evaluations concerning the ability of its customers to satisfy their obligations and records a provision for doubtful accounts based on these evaluations. The Company's credit losses for the periods presented were not significant compared to sales and did not significantly exceed management's estimates. Refer to Note 5 for further information regarding the Company's allowance for doubtful accounts.

Shipping and handling costs associated with outbound freight incurred to transfer a product to a customer are accounted for as fulfillment costs and are included in SG&A expenses. Sales and usage-based taxes collected from customers and remitted directly to governmental authorities are excluded from net revenues. This is consistent with the presentation of such amounts in previous years.

The Company does not have significant contract balances related to its direct-to-consumer or wholesale distribution channels other than the allowance for sales returns and markdowns as well as liabilities related to its gift cards and loyalty programs. The Company also does not have significant contract acquisition costs related to its direct-to-consumer or wholesale distribution channels.

Sales Return Allowances

The Company accrues for estimated sales returns in the period in which the related revenue is recognized. To recognize the financial impact of sales returns, the Company estimates the amount of goods that will be returned based on historical experience and current trends and reduces sales and cost of sales accordingly. The Company's policy allows retail customers in certain regions a grace period to return merchandise following the date of sale. Substantially all of these returns are considered to be resalable at a price that exceeds the cost of the merchandise. The Company adopted the new revenue recognition standard effective as of the first quarter of fiscal 2019, and accordingly, has included the allowance for sales returns in accrued expenses and the estimated cost associated with such sales returns within other current assets in its condensed consolidated balance sheet. Prior to the adoption of the new revenue recognition standard, the Company recorded the allowance for wholesale sales returns against accounts receivable and the estimated cost of inventory associated with the allowance for sales returns in inventories. The allowance for retail sales returns was included in accrued expenses which is consistent with the current presentation. As of November 3, 2018, the Company included \$26.1 million in accrued expenses related to the allowance for sales returns and \$10.4 million in other current assets related to the estimated cost of such sales returns. As of February 3, 2018, the Company included \$25.0 million and \$2.9 million in accounts receivable and accrued expenses, respectively, related to the allowance for sales returns and \$11.9 million in inventories related to the estimated cost of such sales returns.

Table of Contents**Markdown Allowances**

Costs associated with customer markdowns are recorded as a reduction to revenues and any amounts unapplied to existing receivables are included in accrued expenses. These markdown allowances resulted from seasonal negotiations with the Company's wholesale customers, as well as historical trends and the evaluation of the impact of current economic conditions. The Company adopted the new revenue recognition standard effective as of the first quarter of fiscal 2019, and accordingly, has included the allowance for markdowns in accrued expenses in its condensed consolidated balance sheet. As of November 3, 2018, the Company included \$11.2 million in accrued expenses related to the allowance for markdowns. As of February 3, 2018, the Company included \$10.8 million in accounts receivable related to the allowance for markdowns.

Gift Cards

Gift card breakage is income recognized due to the non-redemption of a portion of gift cards sold by the Company for which a liability was recorded in prior periods. Gifts cards are mainly used in the U.S. and Canada. The Company issues its gift cards in the U.S. and Canada through one of its subsidiaries and is not required by law to escheat the value of unredeemed gift cards to the state in which the subsidiary is domiciled. Estimated breakage amounts are accounted for under the redemption recognition method and are classified as additional net revenues as the gift cards are redeemed. The Company's gift card breakage rate is approximately 5.5% and 5.3% for the U.S. retail business and Canadian retail business, respectively, based upon historical redemption patterns, which represents the cumulative estimated amount of gift card breakage from the inception of the electronic gift card program in late 2002. Based upon historical redemption trends, the Company recognizes estimated gift card breakage as a component of net revenue in proportion to actual gift card redemptions, over the period that remaining gift card values are redeemed. Any future revisions to the estimated breakage rate may result in changes in the amount of breakage income recognized in future periods. There have been no changes to the Company's accounting for gift card breakage upon adoption of the new revenue recognition standard effective as of the first quarter of fiscal 2019. During the three and nine months ended November 3, 2018, the Company recognized \$0.3 million and \$0.5 million, respectively, of gift card breakage to revenue. During the three and nine months ended October 28, 2017, the Company recognized \$0.4 million and \$0.6 million, respectively, of gift card breakage to revenue. As of November 3, 2018 and February 3, 2018, the Company included \$4.4 million and \$5.2 million in accrued expenses related to its gift card liability, respectively.

Loyalty Programs

The Company has customer loyalty programs in North America, Europe and Asia which cover all of its brands. Under certain of the programs, primarily in the U.S. and Canada, customers accumulate points based on purchase activity. Once a loyalty program member achieves a certain point level, the member earns awards that may only be redeemed for merchandise. Unredeemed points generally expire after six months without additional purchase activity and unredeemed awards generally expire after two months. Where applicable, the Company allocates a portion of the transaction price from sales in its direct-to-consumer channel to its loyalty program by using historical redemption rates to estimate the value of future award redemptions. This amount is accrued in current liabilities and recorded as a reduction of net revenue in the period which the related revenue is recognized. During the three and nine months ended November 3, 2018, activity related to the Company's loyalty programs decreased net revenue by \$0.1 million and \$0.5 million, respectively. During the three months ended October 28, 2017, activity related to the Company's loyalty programs had a minimal impact on the net revenues. During the nine months ended October 28, 2017, activity related to the Company's loyalty programs increased net revenue by \$0.4 million. The aggregate dollar value of the loyalty program accruals included accrued expense was \$4.5 million and \$3.8 million as of November 3, 2018 and February 3, 2018, respectively. Future revisions to the estimated liability may result in changes to net revenue.

Intellectual Property Transferred Over Time

The Company's trademark license agreements represent symbolic licenses that are dependent on the Company's continued support over the term of the license agreement. The amount of revenue that is recognized

Table of Contents

from the licensing arrangements is based on sales-based royalty and advertising fund contributions as well as specific fixed payments, where applicable.

The typical license agreement requires that the licensee pay the Company the greater of a royalty based on a percentage of the licensee's net sales of licensed products or a guaranteed annual minimum royalty that typically increases over the term of the license agreement. Generally, licensees are also required to make contributions to advertising funds, as a percentage of their sales, over the term of the licensing agreement, and may elect to make additional contributions to support specific brand-building initiatives. The Company recognizes revenue from sales-based royalty and advertising fund contributions when the related sales occur, which is consistent with the timing of when the performance obligation is satisfied. The Company adopted the new revenue recognition standard effective as of the first quarter of fiscal 2019, and accordingly, has recorded advertising contributions in revenue on a gross basis separate from any related advertising expenditures made by the Company which are recorded in SG&A expenses in the Company's condensed consolidated statements of income (loss). Prior to the adoption of the new revenue recognition standard, the Company recorded advertising contributions received from its licensees and the related advertising expenditures incurred by the Company on a net basis in its consolidated balance sheet. Under previous guidance, to the extent that the advertising contributions exceed the Company's advertising expenditures for its licensees, the excess contribution was treated as a deferred liability and was included in accrued expenses in the Company's condensed consolidated balance sheet. Refer to Note 1 for detail regarding the impact of this change on the Company's condensed consolidated balance sheet and its condensed consolidated statements of income (loss) as a result of the adoption of the new revenue recognition standard. The Company records royalty and advertising payments received on the Company's purchases of licensed product as a reduction of the cost of the licensed product. The Company's trademark license agreements customarily provide for a multi-year initial term ranging from three to ten years, and may contain options to renew prior to expiration for an additional multi-year period. Several of the Company's key license agreements provide for specified, fixed payments over and above the normal, ongoing royalty payments in consideration of the grant of the license rights. These payments are recognized ratably as revenue over the term of the license agreement and do not include a significant financing component. The unrecognized portion of upfront payments is included in deferred royalties in accrued expenses and other long-term liabilities depending on the short or long-term nature of the payments to be recognized. As of November 3, 2018, the Company had \$6.7 million and \$15.0 million of deferred royalties related to these upfront payments included in accrued expenses and other long-term liabilities, respectively. This compares to \$6.8 million and \$12.8 million of deferred royalties related to these upfront payments included in accrued expenses and other long-term liabilities, respectively, at February 3, 2018. During the three and nine months ended November 3, 2018, the Company recognized \$3.6 million and \$10.5 million in net royalties related to the amortization of the deferred royalties, respectively. During the three and nine months ended October 28, 2017, the Company recognized \$3.0 million and \$9.0 million in net royalties related to the amortization of the deferred royalties, respectively.

Contract balances related to the Company's licensing distribution channel consist primarily of royalty receivables and liabilities related to deferred royalties. Refer to Note 5 for further information on royalty receivables. The Company does not have significant contract acquisition costs related to its licensing operations.

Refer to Note 8 for further information on disaggregation of revenue by segment and country.

(3) Earnings (Loss) per Share

Basic earnings (loss) per share represents net earnings (loss) attributable to common stockholders divided by the weighted average number of common shares outstanding during the period. The Company considers any restricted stock units with forfeitable dividend rights that are issued and outstanding, but considered contingently returnable if certain service conditions are not met, as common equivalent shares outstanding. These restricted stock units are excluded from the weighted average number of common shares outstanding and basic earnings (loss) per share calculation until the respective service conditions have been met. Diluted earnings (loss) per share represents net earnings (loss) attributable to common stockholders divided by the weighted average number of

Table of Contents

common shares outstanding, inclusive of the dilutive impact of common equivalent shares outstanding during the period. The potentially dilutive impact of common equivalent shares outstanding is not included in the computation of diluted net loss per share as the impact of the shares would be antidilutive due to the net loss incurred for periods presented. Nonvested restricted stock awards (referred to as participating securities) are excluded from the dilutive impact of common equivalent shares outstanding in accordance with authoritative guidance under the two-class method since the nonvested restricted stockholders are entitled to participate in dividends declared on common stock as if the shares were fully vested and hence are deemed to be participating securities. Under the two-class method, distributed and undistributed earnings attributable to nonvested restricted stockholders are excluded from net earnings (loss) attributable to common stockholders for purposes of calculating basic and diluted earnings (loss) per common share. However, net losses are not allocated to nonvested restricted stockholders because they are not contractually obligated to share in the losses of the Company.

In addition, the Company has granted certain nonvested stock units that are subject to certain performance-based or market-based vesting conditions as well as continued service requirements through the respective vesting periods. These nonvested stock units are included in the computation of diluted net earnings (loss) per common share attributable to common stockholders only to the extent that the underlying performance-based or market-based vesting conditions are satisfied as of the end of the reporting period, or would be considered satisfied if the end of the reporting period was the end of the related contingency period, and the results would be dilutive under the treasury stock method.

The computation of basic and diluted net loss per common share attributable to common stockholders is as follows (in thousands, except per share data):

	Three Months Ended Nov 3, 2018	Oct 28, 2017	Nine Months Ended Nov 3, 2018	Oct 28, 2017
Net loss	\$(13,442)	\$(2,860)	\$(9,133)	\$(8,934)
Less net earnings attributable to nonvested restricted stockholders	187	186	577	581
Net loss attributable to common stockholders	\$(13,629)	\$(3,046)	\$(9,710)	\$(9,515)
Weighted average common shares used in basic computations	80,189	82,390	80,067	82,599
Effect of dilutive securities:				
Stock options and restricted stock units ¹	—	—	—	—
Weighted average common shares used in diluted computations	80,189	82,390	80,067	82,599
Net loss per common share attributable to common stockholders:				
Basic	\$(0.17)	\$(0.04)	\$(0.12)	\$(0.12)
Diluted	\$(0.17)	\$(0.04)	\$(0.12)	\$(0.12)

Notes:

For the three and nine months ended November 3, 2018, there were 1,499,247 and 1,312,054, respectively, of potentially dilutive shares that were not included in the computation of diluted weighted average common shares and common equivalent shares outstanding because their effect would have been antidilutive given the Company's net loss.

For the three months ended November 3, 2018 and October 28, 2017, equity awards granted for 1,310,933 and 2,901,025, respectively, of the Company's common shares and for the nine months ended November 3, 2018 and October 28, 2017, equity awards granted for 1,610,091 and 3,104,027, respectively, of the Company's common shares were outstanding but were excluded from the computation of diluted weighted average common shares and common equivalent shares outstanding because the assumed proceeds, as calculated under the treasury stock method, resulted in these awards being antidilutive. For the three and nine months ended November 3, 2018, the Company also excluded 1,336,679 nonvested stock units which are subject to the achievement of performance-based vesting

Edgar Filing: GUESS INC - Form 10-Q

conditions from the computation of diluted weighted average common shares and common equivalent shares outstanding because these conditions were not achieved as of November 3, 2018. For the three

Table of Contents

and nine months ended October 28, 2017, the Company excluded 1,145,080 nonvested stock units which were subject to the achievement of performance-based vesting conditions from the computation of diluted weighted average common shares and common equivalent shares outstanding because these conditions were not achieved as of October 28, 2017.

Share Repurchase Program

On June 26, 2012, the Company's Board of Directors authorized a program to repurchase, from time-to-time and as market and business conditions warrant, up to \$500 million of the Company's common stock. Repurchases under the program may be made on the open market or in privately negotiated transactions, pursuant to Rule 10b5-1 trading plans or other available means. There is no minimum or maximum number of shares to be repurchased under the program, which may be discontinued at any time, without prior notice. During the nine months ended November 3, 2018, the Company repurchased 1,118,808 shares under the program at an aggregate cost of \$17.6 million. The shares were repurchased during the three months ended May 5, 2018. During the nine months ended November 3, 2018, the Company also paid an additional \$6.0 million for shares that were repurchased during the fourth quarter of fiscal 2018 but were settled during the first quarter of fiscal 2019. During the nine months ended October 28, 2017, the Company repurchased 1,919,967 shares under the program at an aggregate cost of \$24.8 million. The Company repurchased 1,485,195 shares at an aggregate cost of \$17.8 million during the three months ended April 29, 2017 and an additional 434,772 shares at an aggregate cost of \$7.0 million during the three months ended October 28, 2017. As of November 3, 2018, the Company had remaining authority under the program to purchase \$374.6 million of its common stock.

Table of Contents

(4) Stockholders' Equity and Redeemable Noncontrolling Interests

A reconciliation of common stock outstanding, treasury stock and the total carrying amount of total stockholders' equity, Guess?, Inc. stockholders' equity and stockholders' equity attributable to nonredeemable noncontrolling interests for the fiscal year ended February 3, 2018 and nine months ended November 3, 2018 is as follows (in thousands, except share data):

	Shares		Stockholders' Equity			
	Common Stock	Treasury Stock	Guess?, Inc	Nonredeemable Stockholders' Noncontrolling Interests	Total	Redeemable Noncontrolling Interests
Balance at January 28, 2017	84,069,492	56,440,482	\$969,222	\$ 11,772	\$ 980,994	\$ 4,452
Net earnings (loss)	—	—	(7,894)	3,993	(3,901)	—
Foreign currency translation adjustment—	—	—	91,178	2,238	93,416	187
Loss on derivative financial instruments designated as cash flow hedges, net of income tax of \$2,738	—	—	(19,994)	—	(19,994)	—
Actuarial valuation loss and related amortization, prior service credit amortization and foreign currency and other adjustments on defined benefit plans, net of income tax of \$435	—	—	(1,647)	—	(1,647)	—
Issuance of common stock under stock compensation plans, net of tax effect	1,113,713	—	(1,257)	—	(1,257)	—
Issuance of stock under Employee Stock Purchase Plan	54,300	(54,300)	566	—	566	—
Share-based compensation	—	—	18,852	—	18,852	—
Dividends	—	—	(76,048)	—	(76,048)	—
Share repurchases	(3,866,387)	3,866,387	(56,159)	—	(56,159)	—
Noncontrolling interest capital contribution	—	—	—	11	11	951
Noncontrolling interest capital distribution	—	—	—	(1,358)	(1,358)	—
Balance at February 3, 2018	81,371,118	60,252,569	\$916,819	\$ 16,656	\$ 933,475	\$ 5,590
Cumulative adjustment from adoption of new accounting guidance	—	—	5,829	—	5,829	—
Net earnings (loss)	—	—	(9,133)	1,064	(8,069)	—
Foreign currency translation adjustment—	—	—	(58,276)	(994)	(59,270)	(786)
Gain on derivative financial instruments designated as cash flow hedges, net of income tax of (\$2,545)	—	—	17,242	—	17,242	—
Actuarial valuation and prior service credit amortization and foreign currency and other adjustments on defined benefit plans, net of income tax of (\$89)	—	—	688	—	688	—
Issuance of common stock under stock compensation plans, net of tax effect	718,583	—	4,124	—	4,124	—
Issuance of stock under Employee Stock Purchase Plan	36,632	(36,632)	613	—	613	—
Share-based compensation	—	—	12,534	—	12,534	—

Edgar Filing: GUESS INC - Form 10-Q

Dividends	—	—	(55,955) —	(55,955) —
Share repurchases	(1,118,808)	1,118,808	(17,587) —	(17,587) —
Noncontrolling interest capital distribution	—	—	—	(3,069) (3,069) —
Balance at November 3, 2018	81,007,525	61,334,745	\$ 816,898	\$ 13,657
				\$ 830,555 \$ 4,804

Table of Contents

Accumulated Other Comprehensive Income (Loss)

The changes in accumulated other comprehensive income (loss), net of related income taxes, for the three and nine months ended November 3, 2018 and October 28, 2017 are as follows (in thousands):

	Three Months Ended Nov 3, 2018				
	Foreign Currency Translation Adjustment	Instruments Designated as Cash	Derivative Financial Benefit	Defined Plans	Total
Balance at August 4, 2018		\$114,761	\$ (142 )	) \$11,117	\$126,020
Gains (losses) arising during the period		(10,564)	1,596	37	(8,931)
Reclassification to net loss for losses realized	—		1,419	124	1,543
Net other comprehensive income (loss)		(10,564)	3,015	161	(7,388)
Balance at November 3, 2018		\$125,325	\$ 2,873	\$ (10,956)	\$133,408
	Nine Months Ended Nov 3, 2018				
	Foreign Currency Translation Adjustment	Instruments Designated as Cash	Derivative Financial Benefit	Defined Plans	Total
Balance at February 3, 2018		\$67,049)	\$ (14,369 )	) \$11,644	\$93,062)
Gains (losses) arising during the period		(58,276)	12,175	314	(45,787)
Reclassification to net loss for losses realized	—		5,067	374	5,441
Net other comprehensive income (loss)		(58,276)	17,242	688	(40,346)
Balance at November 3, 2018		\$125,325	\$ 2,873	\$ (10,956)	\$133,408
	Three Months Ended Oct 28, 2017				
	Foreign Currency Translation Adjustment	Instruments Designated as Cash	Derivative Financial Benefit	Defined Plans	Total
Balance at July 29, 2017		\$103,675)	\$ (8,751 )	) \$8,483	\$120,909
Gains (losses) arising during the period		(8,184)	2,749	97	(5,338)
Reclassification to net loss for losses realized	—		235	88	323
Net other comprehensive income (loss)		(8,184)	2,984	185	(5,015)
Balance at October 28, 2017		\$111,859	\$ (5,767)	\$ (8,298)	\$125,924
	Nine Months Ended Oct 28, 2017				
	Foreign Currency Translation Adjustment	Instruments Designated as Cash	Derivative Financial Benefit	Defined Plans	Total

Edgar Filing: GUESS INC - Form 10-Q

	Hedges				
Balance at January 28, 2017	\$ (158,227)	\$ 5,400	\$ (8,562)	\$ (161,389)	
Gains (losses) arising during the period	46,368	(10,220)	2	36,150	
Reclassification to net loss for (gains) losses realized	—	(947)	262	(685)	
Net other comprehensive income (loss)	46,368	(11,167)	264	35,465	
Balance at October 28, 2017	\$ (111,859)	\$ (5,767)	\$ (8,298)	\$ (125,924)	

15

Table of Contents

Details on reclassifications out of accumulated other comprehensive income (loss) to net loss during the three and nine months ended November 3, 2018 and October 28, 2017 are as follows (in thousands):

	Three Months Ended	Nine Months Ended	Location of (Gain) Loss Reclassified from Accumulated OCI into Loss	
	Nov 3, 2018	Oct 28, 2017	Nov 3, 2018	Oct 28, 2017
Derivative financial instruments designated as cash flow hedges:				
Foreign exchange currency contracts	\$ 1,618	\$(81)	\$ 5,646	\$(1,360)
Foreign exchange currency contracts	—	337	201	244
Interest rate swap	(21)	57	(60)	119
Less income tax effect	(178)	(78)	(720)	50
	1,419	235	5,067	(947)
Defined benefit plans:				
Net actuarial loss amortization ¹	150	116	453	344
Prior service credit amortization ¹	(7)	(7)	(21)	(20)
Less income tax effect	(19)	(21)	(58)	(62)
	124	88	374	262
Total reclassifications during the period	\$ 1,543	\$ 323	\$ 5,441	\$(685)

Notes:

These accumulated other comprehensive income (loss) components are included in the computation of net periodic defined benefit pension cost. During the first quarter of fiscal 2019, the Company adopted new authoritative guidance which requires that the non-service components of net periodic defined benefit pension cost be presented outside of loss from operations. The Company adopted this guidance on a retrospective basis and, as a result, reclassified these components from SG&A expenses to other income (expense) for the three and nine months ended October 28, 2017. Refer to Note 13 for further information.

Redeemable Noncontrolling Interests

The Company is party to a put arrangement with respect to the common securities that represent the remaining noncontrolling interest for its majority-owned subsidiary, Guess Brasil Comércio e Distribuição S.A. (“Guess Brazil”), which was established through a majority-owned joint venture during fiscal 2014. The put arrangement for Guess Brazil, representing 40% of the total outstanding equity interest of that subsidiary, may be exercised at the discretion of the noncontrolling interest holder by providing written notice to the Company beginning in the sixth year of the agreement, or sooner in certain limited circumstances, and every third anniversary from the end of the sixth year thereafter subject to certain time restrictions. The redemption value of the Guess Brazil put arrangement is based on a multiple of Guess Brazil’s earnings before interest, taxes, depreciation and amortization subject to certain adjustments and is classified as a redeemable noncontrolling interest outside of permanent equity in the Company’s condensed consolidated balance sheet. The carrying value of the redeemable noncontrolling interest related to Guess Brazil was \$1.4 million and \$1.6 million as of November 3, 2018 and February 3, 2018, respectively.

The Company is also party to a put arrangement with respect to the common securities that represent the remaining noncontrolling interest for its majority-owned subsidiary, Guess? CIS, LLC (“Guess CIS”), which was established through a majority-owned joint venture during fiscal 2016. The put arrangement for Guess CIS, representing 30% of the total outstanding equity interest of that subsidiary, may be exercised at the discretion of the noncontrolling interest holder by providing written notice to the Company during the period beginning after the fifth anniversary of the agreement through December 31, 2025, or sooner in certain limited circumstances. The redemption value of the Guess CIS put arrangement is based on a multiple of Guess CIS’s earnings before interest, taxes, depreciation and

Edgar Filing: GUESS INC - Form 10-Q

amortization subject to certain adjustments and is classified as a redeemable noncontrolling interest outside of permanent equity in the Company's condensed consolidated balance sheet. During fiscal 2018, the Company and the noncontrolling interest holder made additional capital contribution

Table of Contents

totaling \$3.2 million, of which \$2.2 million was paid by the Company and the remaining amount was paid by the noncontrolling interest holder to retain the same pro-rata interest in Guess CIS. The carrying value of the redeemable noncontrolling interest related to Guess CIS was \$3.4 million and \$4.0 million as of November 3, 2018 and February 3, 2018, respectively.

(5) Accounts Receivable

Accounts receivable is summarized as follows (in thousands):

	Nov 3,	Feb 3,
	2018	2018
Trade	\$282,919	\$290,478
Royalty	8,437	5,504
Other	6,453	13,233
	297,809	309,215
Less allowances ¹	11,703	49,219
	\$286,106	\$259,996

Notes:

As of February 3, 2018, the accounts receivable allowance included allowances for doubtful accounts, wholesale sales returns and wholesale markdowns. During the first quarter of fiscal 2019, the Company adopted a new revenue recognition standard on a modified retrospective basis which changed the presentation of allowances for wholesale sales returns and wholesale markdowns to be classified within accrued expenses rather than as a reduction to accounts receivable. Accordingly, the Company has included allowances of \$26.1 million and \$11.2 million related to wholesale sales returns and wholesale markdowns, respectively, in accrued expenses as of November 3, 2018. As of November 3, 2018, the accounts receivable allowance was only related to allowances for doubtful accounts. Refer to Notes 1 and 2 for further information regarding the impact from the adoption of the new revenue recognition standard on the Company's condensed consolidated financial statements and related disclosures during the third quarter of fiscal 2019.

Accounts receivable consists of trade receivables relating primarily to the Company's wholesale business in Europe and, to a lesser extent, to its wholesale businesses in the Americas and Asia, royalty receivables relating to its licensing operations, credit card and retail concession receivables related to its retail businesses and certain other receivables. Other receivables generally relate to amounts due to the Company that result from activities that are not related to the direct sale of the Company's products or collection of royalties.

(6) Inventories

Inventories consist of the following (in thousands):

	Nov 3,	Feb 3,
	2018	2018
Raw materials	\$1,360	\$604
Work in progress	166	16
Finished goods ¹	546,991	427,684
	\$548,517	\$428,304

Notes:

During the first quarter of fiscal 2019, the Company adopted a new revenue recognition standard on a modified retrospective basis which changed the presentation of the estimated cost associated with the allowance for sales returns to be included within other current assets rather than included in inventories. Accordingly, the Company has included \$10.4 million related to the estimated cost associated with the allowance for sales returns in other current assets as of November 3, 2018. Refer to Notes 1 and 2 for further information regarding the impact from the adoption of the new revenue recognition standard on the Company's condensed consolidated financial statements and related disclosures during the third quarter of fiscal 2019.

Edgar Filing: GUESS INC - Form 10-Q

The above balances include an allowance to write down inventories to the lower of cost or net realizable value of \$26.7 million and \$29.9 million as of November 3, 2018 and February 3, 2018, respectively.

Table of Contents**(7) Income Taxes**

Income tax expense for the interim periods was computed using the tax rate estimated to be applicable for the full fiscal year, adjusted for discrete items. The Company's effective income tax rate was 61.7% for the nine months ended November 3, 2018, compared to 508.6% for the nine months ended October 28, 2017. The improvement in the effective income tax rate during the nine months ended November 3, 2018 was due primarily to the revision of provisional amounts recorded related to the impact of the 2017 Tax Cuts and Jobs Act in the U.S. (referred to herein as the "Tax Reform") as discussed further below, lower losses during the nine months ended November 3, 2018 in jurisdictions in which the Company has valuation allowances, the impact of discrete non-deductible expenses as compared to the same prior-year period and, to a lesser extent, the reversal of a valuation allowance on certain deferred taxes.

In December 2017, the U.S. government enacted the Tax Reform, which significantly changed the U.S. corporate income tax laws, including lowering the U.S. federal corporate income tax rate from 35% to 21% and requiring a one-time mandatory transition tax on accumulated foreign earnings. The Tax Reform also establishes new tax laws that are effective for calendar 2018, including but not limited to (i) a new provision designed to tax global intangible low-taxed income ("GILTI"), (ii) a general elimination of U.S. federal income taxes on dividends from foreign subsidiaries, (iii) a limitation on deductible interest expense and (iv) limitations on the deductibility of certain executive compensation. Any income tax payable related to the transition tax is due over an eight-year period beginning in calendar 2018. The SEC issued authoritative guidance which addresses accounting for the impact of the Tax Reform. This guidance provides a measurement period, which should not extend beyond one year from the enactment date, during which the Company may finalize the accounting for the impacts of the Tax Reform, and allows for the Company to record provisional estimates of such amounts. Based on the Company's interpretation of the Tax Reform, reasonable estimates were made to record provisional adjustments during the fourth quarter of fiscal 2018. During the third quarter of fiscal 2019, the Company completed the preparation of its U.S. federal tax return for the fiscal year 2018 and concluded, based on the additional information that has become available, that no transition tax is due. As a result, during the three months ended November 3, 2018, the Company revised its provisional amount initially recorded in the three months ended February 3, 2018 related to the Tax Reform and recognized a tax benefit of \$19.6 million. The Company will continue to refine such amounts within the measurement period allowed if and when additional interpretations are issued. On November 28, 2018, the U.S. Internal Revenue Service ("IRS") announced a proposed regulation to revise the section of the underlying IRS code which gave rise to the Company's change in the provisional calculation. In the event legislation is passed in the future to revise the relevant IRS code section, the Company could have additional tax expense and tax liabilities of approximately \$12.8 million. In accordance with current legislation, such charges would be payable over the next seven years.

The Company had no amounts recorded in the condensed consolidated balance sheet related to the transition tax in accrued expenses or other long-term liabilities as of November 3, 2018. The Company included \$1.9 million and \$17.7 million related to the transition tax in accrued expenses and other long-term liabilities in its condensed consolidated balance sheets as of February 3, 2018, respectively.

From time-to-time, the Company is subject to routine income tax audits on various tax matters around the world in the ordinary course of business. As of November 3, 2018, several income tax audits were underway for various periods in multiple jurisdictions. The Company accrues an amount for its estimate of additional income tax liability which the Company, more likely than not, will incur as a result of the ultimate resolution of income tax audits ("uncertain tax positions"). The Company reviews and updates the estimates used in the accrual for uncertain tax positions as more definitive information becomes available from taxing authorities, upon completion of tax audits, upon expiration of statutes of limitation, or upon occurrence of other events.

The Company had aggregate accruals for uncertain tax positions, including penalties and interest, of \$18.4 million and \$19.0 million as of November 3, 2018 and February 3, 2018, respectively.

Table of Contents

(8) Segment Information

The Company's businesses are grouped into five reportable segments for management and internal financial reporting purposes: Americas Retail, Americas Wholesale, Europe, Asia and Licensing. The Company's Americas Retail, Americas Wholesale, Europe and Licensing reportable segments are the same as their respective operating segments. Certain components of the Company's Asia operating segment are separate operating segments based on region, which have been aggregated into the Asia reportable segment for disclosure purposes. Management evaluates segment performance based primarily on revenues and earnings (loss) from operations before corporate performance-based compensation costs, net gains (losses) from lease terminations, asset impairment charges, restructuring charges, and other non-recurring charges, if any. The Company believes this segment reporting reflects how its business segments are managed and how each segment's performance is evaluated by the Company's chief operating decision maker to assess performance and make resource allocation decisions. The Americas Retail segment includes the Company's retail and e-commerce operations in North, South and Central America. The Americas Wholesale segment includes the Company's wholesale operations in the Americas. The Europe segment includes the Company's retail, e-commerce and wholesale operations in Europe and the Middle East. The Asia segment includes the Company's retail, e-commerce and wholesale operations in Asia and the Pacific. The Licensing segment includes the worldwide licensing operations of the Company. The business segment operating results exclude corporate overhead costs, which consist of shared costs of the organization, net gains (losses) on lease terminations, asset impairment charges and restructuring charges. Corporate overhead costs are presented separately and generally include, among other things, the following unallocated corporate costs: accounting and finance, executive compensation, corporate performance-based compensation, facilities, global advertising and marketing, human resources, information technology and legal.

Net revenue and loss from operations are summarized as follows for the three and nine months ended November 3, 2018 and October 28, 2017 (in thousands):

	Three Months Ended		Nine Months Ended	
	Nov 3, 2018	Oct 28, 2017	Nov 3, 2018	Oct 28, 2017
Net revenue:				
Americas Retail	\$186,925	\$187,021	\$555,390	\$561,903
Americas Wholesale	52,698	45,636	127,630	114,151
Europe	254,037	221,230	771,470	641,833
Asia	89,461	74,322	256,298	200,436
Licensing ^{1,2}	22,286	20,744	61,779	53,267
Total net revenue^{1,2}	\$605,407	\$548,953	\$1,772,567	\$1,571,590
Earnings (loss) from operations:				
Americas Retail ^{2,3}	\$3,799	\$(2,414)	\$3,701	\$(27,550)
Americas Wholesale ^{2,3}	10,392	8,562	21,743	20,783
Europe ^{3,4}	7,410	9,095	17,608	38,147
Asia ³	1,938	2,954	7,637	5,734
Licensing ^{2,3}	19,485	18,346	54,408	46,196
Total segment earnings from operations^{2,4}	43,024	36,543	105,097	83,310
Corporate overhead ^{2,4}	(20,824)	(23,443)	(72,316)	(67,403)
Net gains (losses) on lease terminations ⁵	—	(11,494)	152	(11,494)
Asset impairment charges ⁶	(1,277)	(2,018)	(5,017)	(6,013)
European Commission fine ⁷	(42,428)	—	(42,428)	—
Total loss from operations^{2,4}	\$(21,505)	\$(412)	\$(14,512)	\$(1,600)

Notes:

1

Edgar Filing: GUESS INC - Form 10-Q

During the fourth quarter of fiscal 2018, the Company reclassified net royalties received on the Company's inventory purchases of licensed product from net revenue to cost of product sales to reflect its treatment as a reduction of the cost of such licensed product. Accordingly, net revenue for the three and nine months ended October 28, 2017 has been adjusted to conform to the current period presentation. This reclassification had no impact on previously reported loss from operations.

During the first quarter of fiscal 2019, the Company adopted a comprehensive new revenue recognition standard² using a modified retrospective method that does not restate prior periods to be comparable to the current period presentation. The

Table of Contents

adoption of this guidance primarily impacted the presentation of advertising contributions received from the Company's licensees and the related advertising expenditures incurred by the Company. The adoption of this guidance resulted in an increase in net royalty revenue within the Company's Licensing segment of \$2.7 million, as well as an increase in SG&A expenses in our Americas Retail, Americas Wholesale and Licensing segments as well as corporate overhead of \$1.0 million, \$0.6 million, \$0.3 million and \$0.6 million, respectively, during the three months ended November 3, 2018 compared to the same prior-year period. The net favorable impact on loss from operations was approximately \$0.2 million during the three months ended November 3, 2018 compared to the same prior-year period. During the nine months ended November 3, 2018, the adoption of this guidance resulted in an increase in net royalty revenue within the Company's Licensing segment of \$7.1 million, as well as an increase in SG&A expenses in our Americas Retail, Americas Wholesale and Licensing segments as well as corporate overhead of \$3.3 million, \$1.5 million, \$0.7 million and \$1.7 million, respectively, during the nine months ended November 3, 2018 compared to the same prior-year period. The net unfavorable impact on loss from operations was approximately \$0.1 million during the nine months ended November 3, 2018 compared to the same prior-year period. Refer to Note 1 for more information regarding the impact from the adoption of this new standard.

During the first quarter of fiscal 2019, the Company changed the segment accountability for funds received from licensees on the Company's purchases of its licensed products. These amounts were treated as a reduction of cost of product sales within the Licensing segment but now are considered in the results of the segments that control the respective purchases for purposes of segment performance evaluation. Accordingly, segment results for the three and nine months ended October 28, 2017 have been adjusted to conform to the current period presentation.

During the first quarter of fiscal 2019, the Company adopted new authoritative guidance which requires that the non-service components of net periodic defined benefit pension cost be presented outside of earnings (loss) from operations. Accordingly, loss from operations and segment results for the three and nine months ended October 28, 2017 have been adjusted to conform to the current period presentation.

During the nine months ended November 3, 2018, the Company recorded net gains on lease terminations related primarily to the early termination of certain lease agreements in North America. The net gains on lease terminations were recorded during the three months ended May 5, 2018. During the nine months ended October 27, 2018, the Company recorded net losses on lease termination related primarily to the modification of certain lease agreements held with a common landlord in North America. Refer to Note 1 for more information regarding the net gains (losses) on lease terminations.

During each of the periods presented, the Company recognized asset impairment charges for certain retail locations resulting from under-performance and expected store closures. Refer to Note 14 for more information regarding these asset impairment charges.

During the third quarter of fiscal 2019, the Company recorded a charge of €37.0 million euro (\$42.4 million) related to an estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of European Union competition rules by the Company. Refer to Note 12 for further information.

The table below presents information regarding geographic areas in which the Company operated. Net revenue is classified primarily based on the country where the Company's customer is located (in thousands):

	Three Months Ended		Nine Months Ended	
	Nov 3, 2018	Oct 28, 2017	Nov 3, 2018	Oct 28, 2017
Net revenue:				
U.S.	\$181,113	\$170,068	\$519,547	\$507,239
Italy	65,050	67,561	213,336	195,955
Canada	49,961	53,381	136,296	142,905
South Korea	40,623	41,709	114,706	114,547
Other foreign countries	268,660	216,234	788,682	610,944
Total net revenue	\$605,407	\$548,953	\$1,772,567	\$1,571,590

Edgar Filing: GUESS INC - Form 10-Q

Due to the seasonal nature of the Company's business segments, the above net revenue and operating results are not necessarily indicative of the results that may be expected for the full fiscal year.

20

Table of Contents

(9) Borrowings and Capital Lease Obligations

Borrowings and capital lease obligations are summarized as follows (in thousands):

	Nov 3, 2018	Feb 3, 2018	
Mortgage debt, maturing monthly through January 2026	\$19,885	\$20,323	
Capital lease obligations	17,031	18,589	
Other	2,876	3,129	
	39,792	42,041	
Less current installments	3,538	2,845	
Long-term debt and capital lease obligations	\$36,254	\$39,196	

Mortgage Debt

On February 16, 2016, the Company entered into a ten-year \$21.5 million real estate secured loan (the “Mortgage Debt”). The Mortgage Debt is secured by the Company’s U.S. distribution center based in Louisville, Kentucky and provides for monthly principal and interest payments based on a 25-year amortization schedule, with the remaining principal balance and any accrued and unpaid interest due at maturity. Outstanding principal balances under the Mortgage Debt bear interest at the one-month LIBOR rate plus 1.5%. As of November 3, 2018, outstanding borrowings under the Mortgage Debt, net of debt issuance costs of \$0.1 million, were \$19.9 million. At February 3, 2018, outstanding borrowings under the Mortgage Debt, net of debt issuance costs of \$0.1 million, were \$20.3 million. The Mortgage Debt requires the Company to comply with a fixed charge coverage ratio on a trailing four-quarter basis if consolidated cash, cash equivalents, short-term investment balances and availability under borrowing arrangements fall below certain levels. In addition, the Mortgage Debt contains customary covenants, including covenants that limit or restrict the Company’s ability to incur liens on the mortgaged property and enter into certain contractual obligations. Upon the occurrence of an event of default under the Mortgage Debt, the lender may terminate the Mortgage Debt and declare all amounts outstanding to be immediately due and payable. The Mortgage Debt specifies a number of events of default (some of which are subject to applicable grace or cure periods), including, among other things, non-payment defaults, covenant defaults, cross-defaults to other material indebtedness, bankruptcy and insolvency defaults and material judgment defaults.

On February 16, 2016, the Company also entered into a separate interest rate swap agreement, designated as a cash flow hedge, that resulted in a swap fixed rate of approximately 3.06%. This interest rate swap agreement matures in January 2026 and converts the nature of the Mortgage Debt from LIBOR floating-rate debt to fixed-rate debt. The fair values of the interest rate swap asset as of November 3, 2018 and February 3, 2018 were approximately \$1.7 million and \$1.5 million, respectively.

Capital Lease Obligations

During fiscal 2018, the Company began the relocation of its European distribution center to the Netherlands. As a result, the Company entered into a capital lease of \$17.0 million for equipment used in the new facility. The capital lease primarily provides for monthly minimum lease payments through May 2027 with an effective interest rate of approximately 6%. As of November 3, 2018 and February 3, 2018, the capital lease obligation was \$14.9 million and \$17.3 million, respectively.

The Company also has smaller capital leases related primarily to computer hardware and software. As of November 3, 2018 and February 3, 2018, these capital lease obligations totaled \$2.1 million and \$1.3 million, respectively.

Credit Facilities

On June 23, 2015, the Company entered into a five-year senior secured asset-based revolving credit facility with Bank of America, N.A. and the other lenders party thereto (the “Credit Facility”). The Credit Facility provides for a borrowing capacity in an amount up to \$150 million, including a Canadian sub-facility up to \$50 million, subject to a borrowing base. Based on applicable accounts receivable, inventory, eligible cash balances and relevant covenant restrictions as of November 3, 2018, the Company could have borrowed up to \$134 million under the

Table of Contents

Credit Facility. The Credit Facility has an option to expand the borrowing capacity by up to \$150 million subject to certain terms and conditions, including the willingness of existing or new lenders to assume such increased amount. The Credit Facility is available for direct borrowings and the issuance of letters of credit, subject to certain letters of credit sublimits, and may be used for working capital and other general corporate purposes.

All obligations under the Credit Facility are unconditionally guaranteed by the Company and the Company's existing and future domestic and Canadian subsidiaries, subject to certain exceptions, and are secured by a first priority lien on substantially all of the assets of the Company and such domestic and Canadian subsidiaries, as applicable.

Direct borrowings under the Credit Facility made by the Company and its domestic subsidiaries shall bear interest at the U.S. base rate plus an applicable margin (varying from 0.25% to 0.75%) or at LIBOR plus an applicable margin (varying from 1.25% to 1.75%). The U.S. base rate is based on the greater of (i) the U.S. prime rate, (ii) the federal funds rate, plus 0.5%, and (iii) LIBOR for a 30-day interest period, plus 1.0%. Direct borrowings under the Credit Facility made by the Company's Canadian subsidiaries shall bear interest at the Canadian prime rate plus an applicable margin (varying from 0.25% to 0.75%) or at the Canadian BA rate plus an applicable margin (varying from 1.25% to 1.75%). The Canadian prime rate is based on the greater of (i) the Canadian prime rate, (ii) the Bank of Canada overnight rate, plus 0.5%, and (iii) the Canadian BA rate for a one-month interest period, plus 1.0%. The applicable margins are calculated quarterly and vary based on the average daily availability of the aggregate borrowing base. The Company is also obligated to pay certain commitment, letter of credit and other fees customary for a credit facility of this size and type. As of November 3, 2018, the Company had \$2.0 million in outstanding standby letters of credit, no outstanding documentary letters of credit and no outstanding borrowings under the Credit Facility.

The Credit Facility requires the Company to comply with a fixed charge coverage ratio on a trailing four-quarter basis if a default or an event of default occurs under the Credit Facility or generally if borrowings exceed 80% of the borrowing base. In addition, the Credit Facility contains customary covenants, including covenants that limit or restrict the Company and certain of its subsidiaries' ability to: incur liens, incur indebtedness, make investments, dispose of assets, make certain restricted payments, merge or consolidate and enter into certain transactions with affiliates. Upon the occurrence of an event of default under the Credit Facility, the lenders may cease making loans, terminate the Credit Facility and declare all amounts outstanding to be immediately due and payable. The Credit Facility specifies a number of events of default (some of which are subject to applicable grace or cure periods), including, among other things, non-payment defaults, covenant defaults, cross-defaults to other material indebtedness, bankruptcy and insolvency defaults and material judgment defaults. The Credit Facility allows for both secured and unsecured borrowings outside of the Credit Facility up to specified amounts.

The Company, through its European subsidiaries, maintains short-term committed and uncommitted borrowing agreements, primarily for working capital purposes, with various banks in Europe. As of November 3, 2018, the Company could have borrowed or entered into documentary letters of credit totaling up to \$87.1 million under these agreements. As of November 3, 2018, the Company had no outstanding borrowings or outstanding documentary letters of credit under these agreements. The agreements are denominated primarily in euros and provide for annual interest rates ranging from 1.1% to 5.0%. With the exception of one facility for up to \$39.9 million that has a minimum net equity requirement, there are no other financial ratio covenants.

Other

From time-to-time, the Company will obtain other financing in foreign countries for working capital to finance its local operations.

Table of Contents

(10) Share-Based Compensation

The following table summarizes the share-based compensation expense recognized under all of the Company's stock plans during the three and nine months ended November 3, 2018 and October 28, 2017 (in thousands):

	Three Months Ended		Nine Months Ended	
	Nov 3, 2018	Oct 28, 2017	Nov 3, 2018	Oct 28, 2017
Stock options	\$ 824	\$ 571	\$2,191	\$1,761
Stock awards/units	3,692	3,658	10,154	10,539
Employee Stock Purchase Plan	29	31	189	110
Total share-based compensation expense	\$ 4,545	\$ 4,260	\$12,534	\$12,410

Unrecognized compensation cost related to nonvested stock options and nonvested stock awards/units totaled approximately \$4.2 million and \$27.2 million, respectively, as of November 3, 2018. This cost is expected to be recognized over a weighted average period of 1.6 years. The weighted average grant date fair value of stock options granted was \$5.89 and \$1.57 during the nine months ended November 3, 2018 and October 28, 2017, respectively.

Grants

On June 25, 2018, the Company granted select key management 619,578 nonvested stock units which are subject to certain performance-based vesting or market-based vesting conditions. On April 28, 2017, the Company granted select key management 1,056,042 nonvested stock units which are subject to certain performance-based vesting or market-based vesting conditions.

Annual Grants

On March 30, 2018, the Company made an annual grant of 431,371 stock options and 490,528 nonvested stock awards/units to its employees. On March 29, 2017, the Company made an annual grant of 1,283,175 stock options and 707,675 nonvested stock awards/units to its employees.

Performance-Based Awards

The Company has granted certain nonvested stock units subject to performance-based vesting conditions to select executive officers. Each award of nonvested stock units generally has an initial vesting period from the date of the grant through either (i) the end of the first fiscal year or (ii) the first anniversary of the date of grant, followed by annual vesting periods which may range from two-to-three years.

The Company has also granted a target number of nonvested stock units to select key management, including certain executive officers. The number of shares that may ultimately vest with respect to each award may range from 0% up to 200% of the target number of shares, subject to the achievement of certain performance-based vesting conditions. Any shares that are ultimately issued are scheduled to vest at the end of the third fiscal year following the grant date. The following table summarizes the activity for nonvested performance-based units during the nine months ended November 3, 2018:

		Weighted Average
	Number of Units	Grant Date
		Fair Value
Nonvested at February 3, 2018	1,300,921	\$ 14.01
Granted	489,646	21.83
Vested	(141,625)	15.07
Forfeited	(52,312)	15.37
Nonvested at November 3, 2018	1,596,630	\$ 16.27

Table of Contents**Market-Based Awards**

The Company has granted certain nonvested stock units subject to market-based vesting conditions to select executive officers. The number of shares that may ultimately vest will equal 0% to 150% of the target number of shares, subject to the performance of the Company's total stockholder return ("TSR") relative to the TSR of a select group of peer companies over a three-year period. Vesting is also subject to continued service requirements through the vesting date. The following table summarizes the activity for nonvested market-based units during the nine months ended November 3, 2018:

	Number of Units	Weighted Average Grant Date	Fair Value
Nonvested at February 3, 2018	388,477	\$ 12.28	
Granted	129,932	20.28	
Vested	—	—	
Forfeited	—	—	
Nonvested at November 3, 2018	518,409	\$ 14.28	

(11)Related Party Transactions

The Company and its subsidiaries periodically enter into transactions with other entities or individuals that are considered related parties, including certain transactions with entities affiliated with trusts for the respective benefit of Paul Marciano, who is an executive and member of the Board of the Company, and Maurice Marciano, Chairman of the Board, and certain of their children (the "Marciano Trusts").

Leases

The Company leases warehouse and administrative facilities, including the Company's corporate headquarters in Los Angeles, California, from partnerships affiliated with the Marciano Trusts and certain of their affiliates. There were four of these leases in effect as of November 3, 2018 with expiration or option exercise dates ranging from calendar years 2018 to 2020.

Aggregate rent, common area maintenance charges and property tax expense recorded under these four related party leases were approximately \$3.7 million and \$3.6 million for the nine months ended November 3, 2018 and October 28, 2017, respectively. The Company believes that the terms of the related party leases have not been significantly affected by the fact that the Company and the lessors are related.

Aircraft Arrangements

The Company periodically charters aircraft owned by entities affiliated with the Marciano Trusts (the "Aircraft Entities"), through informal arrangements with the Aircraft Entities and independent third-party management companies contracted by the Aircraft Entities to manage their aircraft. The total fees paid under these arrangements for the nine months ended November 3, 2018 and October 28, 2017 were approximately \$1.0 million and \$0.7 million, respectively.

These related party disclosures should be read in conjunction with the disclosure concerning related party transactions in the Company's Annual Report on Form 10-K for the year ended February 3, 2018.

(12) Commitments and Contingencies**Leases**

The Company leases its showrooms, advertising, licensing, sales and merchandising offices, remote distribution and warehousing facilities and retail and factory outlet store locations under operating lease agreements expiring on various dates through December 2037. Some of these leases require the Company to make periodic payments for property taxes, utilities and common area operating expenses. Certain retail store leases provide for rents based upon the minimum annual rental amount and a percentage of annual sales volume,

Table of Contents

generally ranging from 4% to 20%, when specific sales volumes are exceeded. The Company's retail concession leases also provide for rents primarily based upon a percentage of annual sales volume which average approximately 35% of annual sales volume. Some leases include lease incentives, rent abatements and fixed rent escalations, which are amortized and recorded over the initial lease term on a straight-line basis. The Company also leases some of its equipment under operating lease agreements expiring at various dates through October 2023.

As discussed in further detail in Note 9, the Company leases equipment as well as computer hardware and software under capital lease obligations.

Investment Commitments

As of November 3, 2018, the Company had an unfunded commitment to invest €3.6 million (\$4.1 million) in a private equity fund. Refer to Note 14 for further information.

Legal and Other Proceedings

The Company is involved in legal proceedings, arising both in the ordinary course of business and otherwise, including the proceedings described below as well as various other claims and other matters incidental to the Company's business. Unless otherwise stated, the resolution of any particular proceeding is not currently expected to have a material adverse impact on the Company's financial position or results of operations. Even if such an impact could be material, we may not be able to estimate the reasonably possible loss or range of loss until developments in the proceedings have provided sufficient information to support an assessment.

On May 6, 2009, Gucci America, Inc. filed a complaint in the U.S. District Court for the Southern District of New York against Guess?, Inc. and certain third-party licensees for the Company asserting, among other things, trademark and trade dress law violations and unfair competition. The complaint sought injunctive relief, compensatory damages, including treble damages, and certain other relief. Complaints similar to those in the above action were subsequently filed by Gucci entities against the Company and certain of its subsidiaries in the Court of Milan, Italy, the Intermediate People's Court of Nanjing, China and the Court of Paris, France. The three-week bench trial in the U.S. matter concluded on April 19, 2012, with the court issuing a preliminary ruling on May 21, 2012 and a final ruling on July 19, 2012. Although the plaintiff was seeking compensation in the U.S. matter in the form of damages of \$26 million and an accounting of profits of \$99 million, the final ruling provided for monetary damages of \$2.3 million against the Company and \$2.3 million against certain of its licensees. The court also granted narrow injunctions in favor of the plaintiff for certain of the claimed infringements. On August 20, 2012, the appeal period expired without any party having filed an appeal, rendering the judgment final. On May 2, 2013, the Court of Milan ruled in favor of the Company in the Milan, Italy matter. In the ruling, the Court rejected all of the plaintiff's claims and ordered the cancellation of three of the plaintiff's Italian and four of the plaintiff's European Community trademark registrations. On June 10, 2013, the plaintiff appealed the Court's ruling in the Milan matter. On September 15, 2014, the Court of Appeal of Milan affirmed the majority of the lower Court's ruling in favor of the Company, but overturned the lower Court's finding with respect to an unfair competition claim. That portion of the matter moved to a damages phase based on the ruling. On October 16, 2015, the plaintiff appealed the remainder of the Court of Appeal of Milan's ruling in favor of the Company to the Italian Supreme Court of Cassation. In the China matter, the Intermediate People's Court of Nanjing, China issued a ruling on November 8, 2013 granting an injunction in favor of the plaintiff for certain of the claimed infringements on handbags and small leather goods and awarding the plaintiff statutory damages in the amount of approximately \$80,000. The Company strongly disagreed with the Court's decision and appealed the ruling. On August 31, 2016, the Court of Appeal for the China matter issued a decision in favor of the Company, rejecting all of the plaintiff's claims. In March 2017, the plaintiff petitioned the China Supreme Court for a retrial of the matter. On January 30, 2015, the Court of Paris ruled in favor of the Company in the France matter, rejecting all of the plaintiff's claims and partially canceling two of the plaintiff's community trademark registrations and one of the plaintiff's international trademark registrations. On February 17, 2015, the plaintiff appealed the Court of Paris' ruling. In April 2018, the parties entered into an agreement to settle all pending worldwide intellectual property litigation and trademark office matters between the parties and their subsidiaries, including the previously active litigation matters in Italy, China and France. As part of the settlement, the parties agreed on the use of

Table of Contents

various design elements by each party on a go-forward basis. The settlement did not have a significant impact on the Company's financial results, and the terms of the settlement are not expected to have a negative impact on the Company's business operations going forward.

The Company has received customs tax assessment notices from the Italian Customs Agency ("ICA") regarding its customs tax audit of one of the Company's European subsidiaries for the period from July 2010 through December 2012. Such assessments totaled €9.8 million (\$11.4 million), including potential penalties and interest. The Company strongly disagreed with the ICA's positions and therefore filed appeals with the Milan First Degree Tax Court ("MFDTC"). Those appeals were split into a number of different cases that were then heard by different sections of the MFDTC. The MFDTC ruled in favor of the Company on all of these appeals. The ICA subsequently appealed €9.7 million (\$11.0 million) of these favorable MFDTC judgments with the Appeals Court. To date, €6.3 million (\$7.2 million) have been decided in favor of the Company, €1.3 million (\$1.4 million) have been decided in favor of the ICA, and €2.1 million (\$2.4 million) remain pending. The Company believes that the unfavorable Appeals Court ruling is incorrect and inconsistent with the prior rulings on similar matters by both the MFDTC and other judges within the Appeals Court, and plans to appeal the decision to the Supreme Court. The ICA has appealed the favorable Appeals Court rulings to the Supreme Court. There can be no assurances the Company will be successful in the remaining appeals. It also continues to be possible that the Company will receive similar or even larger assessments for periods subsequent to December 2012 or other claims or charges related to the matter in the future. Although the Company believes that it has a strong position and will continue to vigorously defend this matter, it is unable to predict with certainty whether or not these efforts will ultimately be successful or whether the outcome will have a material impact on the Company's financial position or results of operations.

On June 6, 2017, the European Commission notified the Company that it had initiated proceedings to investigate whether certain of the Company's practices and agreements concerning the distribution of apparel and accessories within the European Union breached European Union competition rules related to cross-border transactions, internet sales limitations and resale price restrictions. The Company has cooperated with the European Commission, including through responses to requests for information, through changes to certain business practices and agreements and by engaging in a settlement discussion process. Depending on the outcome of the proceedings, a broad range of remedies is available to the European Commission, including imposing a fine and/or injunctive relief prohibiting or restricting certain business practices. The Company has already made certain changes to its business practices and agreements in response to, and early in the course of, these proceedings, and the Company believes that such changes have not had, and will not have, a material impact on its ongoing business operations within the European Union. Based on the settlement discussion process, the Company now believes that it is likely to incur a fine in an amount between €37.0 million (\$42.4 million) and €40.6 million (\$46.6 million) with no further modifications of the Company's business practices and agreements beyond those already made. Accordingly, the Company accrued an estimated charge of €37.0 million (\$42.4 million) during the third quarter of fiscal 2019. A final outcome in this matter could occur as early as the fourth quarter of fiscal 2019, although any resolution may be delayed or different than current expectations due to the inherent unpredictability of the proceedings.

(13)Defined Benefit Plans

Supplemental Executive Retirement Plan

On August 23, 2005, the Board of Directors of the Company adopted a Supplemental Executive Retirement Plan ("SERP") which became effective January 1, 2006. The SERP provides select employees who satisfy certain eligibility requirements with certain benefits upon retirement, termination of employment, death, disability or a change in control of the Company, in certain prescribed circumstances.

As a non-qualified pension plan, no dedicated funding of the SERP is required; however, the Company has made periodic payments into insurance policies held in a rabbi trust to fund the expected obligations arising under the non-qualified SERP. The amount of any future payments into the insurance policies, if any, may vary depending on investment performance of the trust. The cash surrender values of the insurance policies were \$61.6 million and \$64.5 million as of November 3, 2018 and February 3, 2018, respectively, and were included in other assets

Table of Contents

in the Company's condensed consolidated balance sheets. As a result of changes in the value of the insurance policy investments, the Company recorded unrealized loss of \$2.3 million and \$1.6 million in other expense during the three and nine months ended November 3, 2018, respectively, and unrealized gains of \$1.6 million and \$5.5 million in other income during the three and nine months ended October 28, 2017, respectively. The projected benefit obligation was \$54.9 million and \$54.8 million as of November 3, 2018 and February 3, 2018, respectively, and was included in accrued expenses and other long-term liabilities in the Company's condensed consolidated balance sheets depending on the expected timing of payments. SERP benefit payments of \$0.4 million and \$1.3 million were made during the three and nine months ended November 3, 2018, respectively. SERP benefit payments of \$0.4 million and \$1.3 million were made during the three and nine months ended October 28, 2017, respectively.

Foreign Pension Plans

In certain foreign jurisdictions, primarily in Switzerland, the Company is required to guarantee the returns on Company-sponsored defined contribution plans in accordance with local regulations. These plans are typically government-mandated defined contribution plans that provide employees with a minimum investment return, and as such, are treated under pension accounting in accordance with authoritative guidance. Under the Swiss plan, both the Company and certain of its employees with annual earnings in excess of government determined amounts are required to make contributions into a fund managed by an independent investment fiduciary. The Company's contributions must be made in an amount at least equal to the employee's contribution. Minimum employee contributions are based on the respective employee's age, salary and gender.

As of November 3, 2018 and February 3, 2018, the foreign pension plans had a total projected benefit obligation of \$27.9 million and \$26.4 million, respectively, and plan assets held in independent investment fiduciaries of \$22.4 million and \$21.4 million, respectively. The net liability of \$5.5 million and \$5.0 million was included in other long-term liabilities in the Company's condensed consolidated balance sheets as of November 3, 2018 and February 3, 2018, respectively.

Table of Contents

The components of net periodic defined benefit pension cost for the three and nine months ended November 3, 2018 and October 28, 2017 related to the Company's defined benefit plans are as follows (in thousands):

	Three Months Ended		
	Nov 3, 2018		
	Foreign		
	SERP	Pension	Total
	Plans		
Service cost	\$—	\$ 730	\$730
Interest cost	471	54	525
Expected return on plan assets	—	(72)	(72)
Net amortization of unrecognized prior service credit	—	(7)	(7)
Net amortization of actuarial losses	47	103	150
Net periodic defined benefit pension cost	\$518	\$ 808	\$1,326
	Nine Months Ended		
	Nov 3, 2018		
	Foreign		
	SERP	Pension	Total
	Plans		
Service cost	\$—	\$ 2,224	\$2,224
Interest cost	1,415	164	1,579
Expected return on plan assets	—	(221)	(221)
Net amortization of unrecognized prior service credit	—	(21)	(21)
Net amortization of actuarial losses	140	313	453
Net periodic defined benefit pension cost	\$1,555	\$ 2,459	\$4,014
	Three Months Ended		
	Oct 28, 2017		
	Foreign		
	SERP	Pension	Total
	Plans		
Service cost	\$—	\$ 492	\$492
Interest cost	461	22	483
Expected return on plan assets	—	(48)	(48)
Net amortization of unrecognized prior service credit	—	(7)	(7)
Net amortization of actuarial losses	38	78	116
Net periodic defined benefit pension cost	\$499	\$ 537	\$1,036
	Nine Months Ended		
	Oct 28, 2017		
	Foreign		
	SERP	Pension	Total
	Plans		
Service cost	\$—	\$ 1,452	\$1,452
Interest cost	1,382	64	1,446
Expected return on plan assets	—	(143)	(143)
Net amortization of unrecognized prior service credit	—	(20)	(20)
Net amortization of actuarial losses	114	230	344
Net periodic defined benefit pension cost	\$1,496	\$ 1,583	\$3,079

During the first quarter of fiscal 2019, the Company adopted new authoritative guidance which requires that the non-service components of net periodic defined benefit pension cost be presented outside of loss from operations. The Company adopted this guidance on a retrospective basis and, as a result, reclassified approximately \$0.5 million and

Edgar Filing: GUESS INC - Form 10-Q

\$1.6 million from SG&A expenses to other income (expense) for the three and nine months ended October 28, 2017, respectively.

Table of Contents

(14) Fair Value Measurements

Authoritative guidance defines fair value 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. The guidance establishes a fair value hierarchy, which prioritizes the inputs used in measuring fair value into three broad levels as follows:

Level 1—Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that can be accessed at the measurement date.

Level 2—Inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (i.e. interest rates, yield curves, etc.) and inputs that are derived principally from or corroborated by observable market data by correlation or other means (market corroborated inputs).

Level 3—Unobservable inputs that reflect assumptions about what market participants would use in pricing the asset or liability. These inputs would be based on the best information available, including the Company's own data.

The following table presents the fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of November 3, 2018 and February 3, 2018 (in thousands):

Recurring Fair Value Measures	Fair Value Measurements at Nov 3, 2018			Fair Value Measurements at Feb 3, 2018		
	Level 2	Level 3	Total	Level 2	Level 3	Total
Assets:						
Foreign exchange currency contracts	\$-\$7,527	\$-\$7,527	\$-\$51	\$-\$51		
Interest rate swap	—1,707	—1,707	—1,460	—1,460		
Total	\$-\$9,234	\$-\$9,234	\$-\$1,511	\$-\$1,511		
Liabilities:						
Foreign exchange currency contracts	\$-\$7	\$-\$7	\$-\$18,089	\$-\$18,089		
Deferred compensation obligations	—14,197	—14,197	—13,476	—13,476		
Total	\$-\$14,204	\$-\$14,204	\$-\$31,565	\$-\$31,565		

There were no transfers of financial instruments between the three levels of fair value hierarchy during the nine months ended November 3, 2018 or during the year ended February 3, 2018.

Foreign exchange currency contracts are entered into by the Company principally to hedge the future payment of inventory and intercompany transactions by non-U.S. subsidiaries. Periodically, the Company may also use foreign exchange currency contracts to hedge the translation and economic exposures related to its net investments in certain of its international subsidiaries. The fair values of the Company's foreign exchange currency contracts are based on quoted foreign exchange forward rates at the reporting date. The fair values of the Company's interest rate swaps are based upon inputs corroborated by observable market data. Deferred compensation obligations to employees are adjusted based on changes in the fair value of the underlying employee-directed investments. Fair value of these obligations is based upon inputs corroborated by observable market data.

During fiscal 2018, the Company invested €0.5 million (\$0.5 million) in a private equity fund. During the nine months ended November 3, 2018, the Company made additional investments totaling €0.9 million (\$1.1 million). As permitted in accordance with authoritative guidance, the Company uses net asset value per share as a practical expedient to measure the fair value of this investment and has not included this investment in the fair value hierarchy as disclosed above. During the three months ended November 3, 2018, there were no changes in the value of the private equity investment. During the nine months ended November 3, 2018, the Company recorded an unrealized loss of €0.1 million (\$0.2 million) in other expense. As of November 3, 2018 and February 3, 2018, the Company included €1.3 million (\$1.4 million) and €0.5 million (\$0.6 million), respectively, in other assets in the Company's condensed consolidated balance sheet related to this investment. As of November 3, 2018, the Company had an unfunded commitment to invest an additional €3.6 million (\$4.1 million) in the private equity fund.

Table of Contents

The carrying amount of the Company's remaining financial instruments, which principally include cash and cash equivalents, trade receivables, accounts payable and accrued expenses, approximates fair value due to the relatively short maturity of such instruments. The fair values of the Company's debt instruments (see Note 9) are based on the amount of future cash flows associated with each instrument discounted using the Company's incremental borrowing rate. As of November 3, 2018 and February 3, 2018, the carrying value of all financial instruments was not materially different from fair value, as the interest rates on the Company's debt approximated rates currently available to the Company.

Long-Lived Assets

Long-lived assets, such as property and equipment, and purchased intangibles subject to amortization, are reviewed for impairment quarterly or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The majority of the Company's long-lived assets relate to its retail operations which consist primarily of regular retail and flagship locations. The Company considers each individual regular retail location as an asset group for impairment testing, which is the lowest level at which individual cash flows can be identified. The asset group includes leasehold improvements, furniture, fixtures and equipment, computer hardware and software and certain long-term security deposits and lease acquisition costs. The Company reviews regular retail locations in penetrated markets for impairment risk once the locations have been opened for at least one year in their current condition, or sooner as changes in circumstances require. The Company believes that waiting at least one year allows a location to reach a maturity level where a more comprehensive analysis of financial performance can be performed. The Company evaluates impairment risk for regular retail locations in new markets, where the Company is in the early stages of establishing its presence, once brand awareness has been established. The Company also evaluates impairment risk for retail locations that are expected to be closed in the foreseeable future. The Company has flagship locations which are used as a regional marketing tool to build brand awareness and promote the Company's current product. Impairment for these locations is tested at a reporting unit level similar to goodwill since they do not have separately identifiable cash flows.

An asset is considered to be impaired if the Company determines that the carrying value may not be recoverable based upon its assessment of the asset's ability to continue to generate earnings from operations and positive cash flow in future periods or if significant changes in the Company's strategic business objectives and utilization of the assets occurred. If the carrying amount of an asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the estimated fair value, which is determined based on discounted future cash flows. The impairment loss calculations require management to apply judgment in estimating future cash flows and the discount rates that reflect the risk inherent in future cash flows.

Future expected cash flows for assets in regular retail locations are based on management's estimates of future cash flows over the remaining lease period or expected life, if shorter. For expected location closures, the Company will evaluate whether it is necessary to shorten the useful life for any of the assets within the respective asset group. The Company will use this revised useful life when estimating the asset group's future cash flows. The Company considers historical trends, expected future business trends and other factors when estimating the future cash flow for each regular retail location. The Company also considers factors such as: the local environment for each regular retail location, including mall traffic and competition; the Company's ability to successfully implement strategic initiatives; and the ability to control variable costs such as cost of sales and payroll and, in some cases, renegotiate lease costs. The estimated cash flows used for this nonrecurring fair value measurement are considered a Level 3 input as defined above. If actual results are not consistent with the assumptions and judgments used in estimating future cash flows and asset fair values, there may be additional exposure to future impairment losses that could be material to the Company's results of operations.

The Company recorded asset impairment charges of \$1.3 million and \$5.0 million during the three and nine months ended November 3, 2018, respectively, and \$2.0 million and \$6.0 million during the three and nine months ended October 28, 2017, respectively. The asset impairment charges related primarily to the impairment of certain retail locations in Europe and North America resulting from under-performance and expected store closures.

Table of Contents

(15) Derivative Financial Instruments

Hedging Strategy

Foreign Exchange Currency Contracts

The Company operates in foreign countries, which exposes it to market risk associated with foreign currency exchange rate fluctuations. The Company has entered into certain forward contracts to hedge the risk of foreign currency rate fluctuations. The Company has elected to apply the hedge accounting rules in accordance with authoritative guidance for certain of these hedges.

The Company's primary objective is to hedge the variability in forecasted cash flows due to the foreign currency risk. Various transactions that occur primarily in Europe, Canada, South Korea, China and Mexico are denominated in U.S. dollars, British pounds and Russian roubles and thus are exposed to earnings risk as a result of exchange rate fluctuations when converted to their functional currencies. These types of transactions include U.S. dollar denominated purchases of merchandise and U.S. dollar and British pound denominated intercompany liabilities. In addition, certain operating expenses, tax liabilities and pension-related liabilities are denominated in Swiss francs and are exposed to earnings risk as a result of exchange rate fluctuations when converted to the functional currency. The Company enters into derivative financial instruments, including forward exchange currency contracts, to offset some, but not all, of the exchange risk on certain of these anticipated foreign currency transactions.

Periodically, the Company may also use foreign exchange currency contracts to hedge the translation and economic exposures related to its net investments in certain of its international subsidiaries.

Interest Rate Swap Agreements

The Company is exposed to interest rate risk on its floating-rate debt. The Company has entered into interest rate swap agreements to effectively convert its floating-rate debt to a fixed-rate basis. The principal objective of these contracts is to eliminate or reduce the variability of the cash flows in interest payments associated with the Company's floating-rate debt, thus reducing the impact of interest rate changes on future interest payment cash flows. The Company has elected to apply the hedge accounting rules in accordance with authoritative guidance for certain of these contracts. Refer to Note 9 for further information.

The impact of the credit risk of the counterparties to the derivative contracts is considered in determining the fair value of the foreign exchange currency contracts and interest rate swap agreements. As of November 3, 2018, credit risk has not had a significant effect on the fair value of the Company's foreign exchange currency contracts and interest rate swap agreements.

Hedge Accounting Policy

Foreign Exchange Currency Contracts

U.S. dollar forward contracts are used to hedge forecasted merchandise purchases over specific months. Changes in the fair value of these U.S. dollar forward contracts, designated as cash flow hedges, are recorded as a component of accumulated other comprehensive income (loss) within stockholders' equity and are recognized in cost of product sales in the period that approximates the time the hedged merchandise inventory is sold. The Company also hedges forecasted intercompany royalties over specific months. Changes in the fair value of these U.S. dollar forward contracts, designated as cash flow hedges, are recorded as a component of accumulated other comprehensive income (loss) within stockholders' equity and are recognized in other income (expense) in the period in which the royalty expense is incurred.

The Company has also used U.S. dollar forward contracts to hedge the net investments of certain of the Company's international subsidiaries over specific months. Changes in the fair value of these U.S. dollar forward contracts, designated as net investment hedges, are recorded in foreign currency translation adjustment as a component of accumulated other comprehensive income (loss) within stockholders' equity and are not recognized in earnings (loss) until the sale or liquidation of the hedged net investment.

Table of Contents

The Company also has foreign exchange currency contracts that are not designated as hedging instruments for accounting purposes. Changes in fair value of foreign exchange currency contracts not designated as hedging instruments are reported in net earnings (loss) as part of other income (expense).

Interest Rate Swap Agreements

Interest rate swap agreements are used to hedge the variability of the cash flows in interest payments associated with the Company's floating-rate debt. Changes in the fair value of interest rate swap agreements designated as cash flow hedges are recorded as a component of accumulated other comprehensive income (loss) within stockholders' equity and are amortized to interest expense over the term of the related debt.

Periodically, the Company may also enter into interest rate swap agreements that are not designated as hedging instruments for accounting purposes. Changes in the fair value of interest rate swap agreements not designated as hedging instruments are reported in net earnings (loss) as part of other income (expense).

Summary of Derivative Instruments

The fair value of derivative instruments in the condensed consolidated balance sheets as of November 3, 2018 and February 3, 2018 is as follows (in thousands):

Derivative Balance Sheet Location	Fair Value at Nov 3, 2018	Fair Value at Feb 3, 2018
ASSETS:		
Derivatives designated as hedging instruments:		
Cash flow hedges:		
Foreign exchange currency contracts	Other current assets/ Other assets	\$5,254 \$41
Interest rate swap	Other assets	1,707 1,460
Total derivatives designated as hedging instruments	6,961	1,501
Derivatives not designated as hedging instruments:		
Foreign exchange currency contracts	Other current assets	2,273 10
Total	\$9,234	\$1,511
LIABILITIES:		
Derivatives designated as hedging instruments:		
Cash flow hedges:		
Foreign exchange currency contracts	Accrued expenses/ Other long-term liabilities	\$5 \$13,789
Derivatives not designated as hedging instruments:		
Foreign exchange currency contracts	Accrued expenses	2 4,300
Total	\$7	\$18,089

Derivatives Designated as Hedging Instruments**Foreign Exchange Currency Contracts Designated as Cash Flow Hedges**

During the nine months ended November 3, 2018, the Company purchased U.S. dollar forward contracts in Europe totaling US\$39.3 million that were designated as cash flow hedges. As of November 3, 2018, the Company had forward contracts outstanding for its European and Canadian operations of US\$93.7 million and US\$8.8 million, respectively, to hedge forecasted merchandise purchases, which are expected to mature over the next 10 months. As of November 3, 2018, accumulated other comprehensive income (loss) related to foreign exchange currency contracts included a net unrealized gain of approximately \$1.6 million, net of tax, which \$0.8 million

Table of Contents

will be recognized in cost of product sales over the following 12 months, at the then current values on a pre-tax basis, which can be different than the current quarter-end values.

At February 3, 2018, the Company had forward contracts outstanding for its European and Canadian operations of US\$145.8 million and US\$38.7 million, respectively, that were designated as cash flow hedges.

Interest Rate Swap Agreement Designated as Cash Flow Hedge

During fiscal 2017, the Company entered into an interest rate swap agreement with a notional amount of \$21.5 million, designated as a cash flow hedge, to hedge the variability of cash flows in interest payments associated with the Company's floating-rate debt. This interest rate swap agreement matures in January 2026 and converts the nature of the Company's real estate secured term loan from LIBOR floating-rate debt to fixed-rate debt, resulting in a swap fixed rate of approximately 3.06%.

As of November 3, 2018, accumulated other comprehensive income related to the interest rate swap agreement included a net unrealized gain of approximately \$1.3 million, net of tax, which will be recognized in interest expense after the following 12 months, at the then current values on a pre-tax basis, which can be different than the current quarter-end values.

The following table summarizes the gains (losses) before taxes recognized on the derivative instruments designated as cash flow hedges in OCI and net loss for the three and nine months ended November 3, 2018 and October 28, 2017 (in thousands):

		Gains Recognized in OCI	Location of Gain (Loss) Reclassified from Three Months Ended	Accumulated OCI into Loss ¹	Gain (Loss) Reclassified from Accumulated OCI into Loss	Three Months Ended
		Nov 3, 2018	Oct 28, 2017		Nov 3, 2018	Oct 28, 2017
Derivatives designated as cash flow hedges:						
Foreign exchange currency contracts	\$ 1,630	\$ 3,215	Cost of product sales		\$ (1,618)	\$ 81
Foreign exchange currency contracts—	38		Other income (expense)		—	(337)
Interest rate swap	203	134	Interest expense		21	(57)
		Gains Recognized in OCI	Location of Gain (Loss) Reclassified from Nine months ended	Accumulated OCI into Loss ¹	Gain (Loss) Reclassified from Accumulated OCI into Loss	Nine months ended
		Nov 3, 2018	Oct 28, 2017		Nov 3, 2018	Oct 28, 2017
Derivatives designated as cash flow hedges:						
Foreign exchange currency contracts	\$ 13,690	\$ (10,601)	Cost of product sales		\$ (5,646)	\$ 1,360
Foreign exchange currency contracts	2	(958)	Other income (expense)		(201)	(244)
Interest rate swap	308	(143)	Interest expense		60	(119)

Notes:

The Company recognized gains of \$0.6 million and \$2.0 million resulting from the ineffective portion related to foreign exchange currency contracts in interest income during the three and nine months ended November 3, 2018, respectively. The Company recognized gains of \$0.5 million and \$2.0 million resulting from the ineffective portion related to foreign exchange currency contracts in interest income during the three and nine months ended October 28, 2017, respectively. There was no ineffectiveness recognized related to the interest rate swap during the three and nine months ended November 3, 2018 and October 28, 2017.

Table of Contents

The following table summarizes net after-tax derivative activity recorded in accumulated other comprehensive income (loss) (in thousands):

	Three Months Ended Nov 3, 2018	Oct 28, 2017	Nine Months Ended Nov 3, 2018	Oct 28, 2017
Beginning balance gain (loss)	\$ (142)	\$ (8,751)	\$ (14,369)	\$ 5,400
Net gains (losses) from changes in cash flow hedges	1,596	2,749	12,175	(10,220)
Net (gains) losses reclassified into loss	1,419	235	5,067	(947)
Ending balance gain (loss)	\$ 2,873	\$ (5,767)	\$ 2,873	\$ (5,767)

Foreign Exchange Currency Contracts Not Designated as Hedging Instruments

As of November 3, 2018, the Company had euro foreign exchange currency contracts to purchase US\$28.0 million expected to mature over the next 6 months and Canadian dollar foreign exchange currency contracts to purchase US\$1.8 million expected to mature over the next 2 months.

The following table summarizes the gains (losses) before taxes recognized on the derivative instruments not designated as hedging instruments in other income (expense) for the three and nine months ended November 3, 2018 and October 28, 2017 (in thousands):

Location of Gain (Loss) Recognized in Loss	Gain (Loss) Recognized in Loss
Three Months Ended	Nine Months Ended
Nov 3 2018	Oct 28, 2017
	Nov 3 Oct 28, Nov 3, Oct 28, 2018 2017 2018 2017

Derivatives not designated as hedging instruments:

Foreign exchange currency contracts	Other income (expense)	\$ 794	\$ 1,645	\$ 6,700	\$ (5,688)
-------------------------------------	------------------------	--------	----------	----------	------------

At February 3, 2018, the Company had euro foreign exchange currency contracts to purchase US\$68.2 million and Canadian dollar foreign exchange currency contracts to purchase US\$17.6 million.

(16) Subsequent Events**Dividends**

On November 28, 2018, the Company announced a regular quarterly cash dividend of \$0.225 per share on the Company's common stock. The cash dividend will be paid on January 2, 2019 to shareholders of record as of the close of business on December 12, 2018.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**General**

Unless the context indicates otherwise, when we refer to "we," "us," "our" or the "Company" in this Form 10-Q, we are referring to Guess?, Inc. ("GUESS?") and its subsidiaries on a consolidated basis.

Important Factors Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q, including documents incorporated by reference herein, contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements may also be contained in the Company's other reports filed under the Securities Exchange Act of 1934, as amended, in its press releases and in other documents. In addition, from time-to-time, the Company, through its management, may make oral forward-looking statements. These statements relate to expectations, analyses and other information based on current plans, forecasts of future results and estimates of amounts not yet determinable. These statements also relate to our goals, future prospects, global cost reduction opportunities and profitability efforts, capital allocation plans, cash needs and current business strategies and strategic initiatives. These forward-looking statements are identified by their use of terms and phrases such as "anticipate," "believe," "continue," "could," "estimate," "expect," "goal," "intend," "may," "outlook," "pending," "plan," "predict,"

Table of Contents

“project,” “see,” “should,” “strategy,” “will,” “would,” and other similar terms and phrases, including references to assumption. Although we believe that the expectations reflected in any of our forward-looking statements are reasonable, actual results could differ materially from those projected or assumed. These forward-looking statements may include, among other things, statements or assumptions relating to: our expected results of operations; the accuracy of data relating to, and anticipated levels of, future inventory and gross margins; anticipated cash requirements and sources; cost containment efforts; estimated charges (including the estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of certain European Union competition rules by the Company); plans regarding store openings, closings, remodels and lease negotiations; plans regarding the opening or relocation of our distribution centers; plans regarding business growth, international expansion and capital allocation; plans regarding supply chain efficiencies and global planning and allocation; e-commerce, digital and omni-channel initiatives; business seasonality; results and risks of current and future legal proceedings, industry trends; consumer demands and preferences; competition; currency fluctuations and related impacts; estimated tax rates, including the impact of the 2017 Tax Cuts and Jobs Act in the U.S. (referred to herein as the “Tax Reform”) and changes to provisional estimates; results of tax audits and other regulatory proceedings; the impact of recent accounting pronouncements; raw material and other inflationary cost pressures; consumer confidence; and general economic conditions. We do not intend, and undertake no obligation, to update our forward-looking statements to reflect future events or circumstances. Such statements involve risks and uncertainties, which may cause actual results to differ materially from those set forth in these statements. Important factors that could cause or contribute to such differences include those discussed under “Part I, Item 1A. Risk Factors” contained in the Company’s most recent Annual Report on Form 10-K for the fiscal year ended February 3, 2018 and in our other filings made from time-to-time with the Securities and Exchange Commission (“SEC”) after the date of this report.

Business Segments

The Company’s businesses are grouped into five reportable segments for management and internal financial reporting purposes: Americas Retail, Americas Wholesale, Europe, Asia and Licensing. Management evaluates segment performance based primarily on revenues and earnings (loss) from operations before corporate performance-based compensation costs, net gains (losses) from lease terminations, asset impairment charges, restructuring charges, and other non-recurring charges, if any. The Americas Retail segment includes the Company’s retail and e-commerce operations in North, South and Central America. The Americas Wholesale segment includes the Company’s wholesale operations in the Americas. The Europe segment includes the Company’s retail, e-commerce and wholesale operations in Europe and the Middle East. The Asia segment includes the Company’s retail, e-commerce and wholesale operations in Asia and the Pacific. The Licensing segment includes the worldwide licensing operations of the Company. The business segment operating results exclude corporate overhead costs, which consist of shared costs of the organization, net gains (losses) on lease terminations, asset impairment charges and restructuring charges. Corporate overhead costs are presented separately and generally include, among other things, the following unallocated corporate costs: accounting and finance, executive compensation, corporate performance-based compensation, facilities, global advertising and marketing, human resources, information technology and legal. Information regarding these segments is summarized in “Part I, Item 1. Financial Statements — Note 8 — Segment Information.”

Products

We derive our net revenue from the sale of GUESS?, G by GUESS, GUESS Kids and MARCIANO apparel and our licensees’ products through our worldwide network of directly operated and licensed retail stores, wholesale customers and distributors, as well as our online sites. We also derive royalty revenue from worldwide licensing activities.

Foreign Currency Volatility

Since the majority of our international operations are conducted in currencies other than the U.S. dollar (primarily the Canadian dollar, Chinese yuan, euro, Japanese yen, Korean won, Mexican peso and Russian rouble),

Table of Contents

currency fluctuations can have a significant impact on the translation of our international revenues and earnings (loss) into U.S. dollar amounts.

In addition, some of our transactions that occur primarily in Europe, Canada, South Korea, China and Mexico are denominated in U.S. dollars, Swiss francs, British pounds and Russian roubles, exposing them to exchange rate fluctuations when these transactions (such as inventory purchases) are converted to their functional currencies. As a result, fluctuations in exchange rates can impact the operating margins of our foreign operations and reported earnings (loss), and are largely dependent on the transaction timing and magnitude during the period that the currency fluctuates. When these foreign exchange rates weaken versus the U.S. dollar at the time U.S. dollar denominated inventory is purchased relative to the purchases of the comparable period, our product margins could be unfavorably impacted if the relative sales prices do not change.

During the first nine months of fiscal 2019, the average U.S. dollar rate was weaker against the Canadian dollar, Chinese yuan, euro, Japanese yen and Korean won, and stronger against the Mexican peso, Russian rouble and Turkish Lira compared to the average rate in the same prior-year period. This had an overall favorable impact on the translation of our international revenues and an unfavorable impact on earnings from operations for the nine months ended November 3, 2018 compared to the same prior-year period.

If the U.S. dollar strengthens relative to the respective fiscal 2018 foreign exchange rates, foreign exchange could negatively impact our revenues and operating results as well as our international cash and other balance sheet items during the remainder of fiscal 2019, particularly in Canada, Europe and Mexico. Alternatively, if the U.S. dollar weakens relative to the respective fiscal 2018 foreign exchange rates, our revenues and operating results as well as our other cash balance sheet items could be positively impacted by foreign currency fluctuations during the remainder of fiscal 2019, particularly in these regions.

The Company enters into derivative financial instruments to offset some, but not all, of the exchange risk on foreign currency transactions. For additional discussion regarding our exposure to foreign currency risk, forward contracts designated as hedging instruments and forward contracts not designated as hedging instruments, refer to “Item 3. Quantitative and Qualitative Disclosures About Market Risk.”

Strategy

The Company continues to remain focused on its five top strategic initiatives aimed at driving shareholder value, including: (i) elevating the quality of our sales organization and merchandising strategy to match the quality of our product and marketing; (ii) building a major business in Asia by unlocking the potential of the GUESS? brand in the region; (iii) creating a culture of purpose and accountability throughout the entire Company by implementing a more centralized organizational structure that reinforces our focus on sales and profitability; (iv) improving our cost structure (including supply chain and overhead); and (v) stabilizing and revitalizing our wholesale business. The following provides further details on the progress of these initiatives:

Sales Organization and Merchandising Strategy. We are executing on our plan to elevate the quality of our sales organization and merchandising strategy which includes: (1) elevating the product knowledge of our sales force; (2) building a more strategic and operational online organization in order to increase millennials' engagement with our brand through digital marketing and social media; (3) taking steps such as investing in key stores and developing stronger replenishment, visual, stockroom and cost-control standards in order to improve our overall field and store structure; (4) implementing a more effective yearly retail calendar to better enable each store to fully capture local opportunities; (5) using feedback from our sales force to improve our collections and increase the number and effectiveness of our SKU's; and (6) implementing a global pricing system with greater clarity and simplicity.

Building our Asia Business. We believe there continues to be significant potential in this region and plan to continue to allocate sufficient resources to fuel future growth.

Transforming our Company's Culture. In order to generate global synergies, major decisions (including supply chain, technology, finance, stock allocation and communications) are becoming more centralized in the Company's management team in Los Angeles. This centralized approach reinforces our focus on sales and

Table of Contents

profitability and fosters an environment of accountability and execution measured through key performance metrics. Improving our Cost Structure. We plan to continue improving our cost structure by identifying synergies among departments and strengthening our supply chain. We are executing on the following supply chain initiatives to drive improvements in product costs: (i) developing a sourcing network in new territories that can offer better costs; (ii) consolidating and building strategic partnerships with high-quality suppliers to gain scale efficiencies; and (iii) implementing a fabric platforming process for each of the regional design offices to develop and utilize common fabrics across multiple styles creating a consistently high quality global offer for our wholesale and retail customers. We are also working to shorten our lead times through partnering with our suppliers, exercising agility in the production process and continuously searching for new suppliers and sourcing opportunities in reaction to the latest trends.

We are also focused on improving the profitability of our retail business in the Americas. As almost two-thirds of our leases in the U.S. and Canada are up for renewal or have lease exit options over the next three years, we continue to have the flexibility to further optimize our retail footprint, or renegotiate lower rents, as appropriate, in the coming years. However, we are not restricting ourselves to waiting for these dates to close stores or renegotiate rents.

Stabilizing our Wholesale Business. We are partnering with our wholesale customers to emphasize a retail-oriented mindset and encourage the adoption of best practices, including high quality visual merchandising, frequent rotation of products and maximization of inventory turns.

Capital Allocation

The Company's investments in capital for the full fiscal year 2019 are planned between \$95 million and \$100 million. The planned investments in capital are related primarily to retail and e-commerce expansion in Europe and Asia as well as continued investments in technology to support our long-term growth plans.

Comparable Sales

The Company reports National Retail Federation calendar comparable sales on a quarterly basis for our retail businesses which include the combined results from our brick-and-mortar retail stores and our e-commerce sites. We also separately report the impact of e-commerce sales on our comparable sales metric. As a result of our omni-channel strategy, our e-commerce business has become strongly intertwined with our brick-and-mortar retail store business. Therefore, we believe that the inclusion of e-commerce sales in our comparable sales metric provides a more meaningful representation of our retail results.

Sales from our brick-and-mortar retail stores include purchases that are initiated, paid for and fulfilled at our retail stores and directly operated concessions as well as merchandise that is reserved online but paid for and picked-up at our retail stores. Sales from our e-commerce sites include purchases that are initiated and paid for online and shipped from either our distribution centers or our retail stores as well as purchases that are initiated in a retail store, but due to inventory availability at the retail store, are ordered and paid for online and shipped from our distribution centers or picked-up from a different retail store.

Store sales are considered comparable after the store has been open for 13 full months. If a store remodel results in a square footage change of more than 15%, or involves a relocation or a change in store concept, the store sales are removed from the comparable store base until the store has been opened at its new size, in its new location or under its new concept for 13 full months. E-commerce sales are considered comparable after the online site has been operational in a country for 13 full months and exclude any related revenue from shipping fees.

Definitions and calculations of comparable sales used by the Company may differ from similarly titled measures reported by other companies.

Other

The Company operates on a 52/53-week fiscal year calendar, which ends on the Saturday nearest to January 31 of each year. The nine months ended November 3, 2018 had the same number of days as the nine months ended October 28, 2017.

Table of Contents

Executive Summary

Overview

Net loss attributable to Guess?, Inc. increased 370.0% to \$13.4 million, or diluted loss of \$0.17 per common share, for the quarter ended November 3, 2018, compared to \$2.9 million, or diluted loss of \$0.04 per common share, for the quarter ended October 28, 2017.

During the quarter ended November 3, 2018, the Company recognized asset impairment charges of \$1.3 million, certain professional services and legal fees and related costs of \$0.1 million, income tax benefits of \$19.6 million related to changes in the provisional amounts recorded related to the Tax Reform, and charges of €37.0 million euros (\$42.4 million) related to the estimated European Commission fine (or a combined \$24.0 million after considering the related tax benefit of these adjustments of \$0.2 million), or an unfavorable \$0.30 per share impact. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. were \$10.6 million and adjusted diluted earnings were \$0.13 per common share for the quarter ended November 3, 2018. During the quarter ended October 28, 2017, the Company recognized net losses on lease terminations of \$11.5 million and asset impairment charges of \$2.0 million. Combined, these items had a \$13.3 million negative impact after considering the related tax benefit of these adjustments of \$0.3 million, or an unfavorable \$0.16 per share impact. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. were \$10.4 million and adjusted diluted earnings were \$0.12 per common share for the quarter ended October 28, 2017. References to financial results excluding the impact of these items are non-GAAP measures and are addressed below under “Non-GAAP Measures.”

Highlights of the Company’s performance for the quarter ended November 3, 2018 compared to the same prior-year period are presented below, followed by a more comprehensive discussion under “Results of Operations”:

Operations

- Total net revenue increased 10.3% to \$605.4 million for the quarter ended November 3, 2018, compared to \$549.0 million in the same prior-year quarter. In constant currency, net revenue increased by 13.1%.
- Gross margin (gross profit as a percentage of total net revenue) increased 160 basis points to 36.4% for the quarter ended November 3, 2018, compared to 34.8% in the same prior-year period.
- Selling, general and administrative (“SG&A”) expenses as a percentage of total net revenue (“SG&A rate”) increased 40 basis points to 32.8% for the quarter ended November 3, 2018, compared to 32.4% in the same prior-year period.
- SG&A expenses increased 11.2% to \$197.9 million for the quarter ended November 3, 2018, compared to \$178.0 million in the same prior-year period.
- During the quarter ended November 3, 2018, the Company recognized asset impairment charges of \$1.3 million, compared to \$2.0 million in the same prior-year period.
- During the quarter ended November 3, 2018, the Company recognized charges of €37.0 million (\$42.4 million) related to an estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of certain European Union competition rules by the Company.
- Operating margin decreased 350 basis points to negative 3.6% for the quarter ended November 3, 2018, compared to negative 0.1% in the same prior-year period. For the quarter ended November 3, 2018 as compared to the same prior-year period, the charges related to the estimated European Commission fine negatively impacted operating margin by 700 basis points, lower losses on lease terminations positively impacted operating margin by 210 basis points and lower asset impairment charges positively impacted operating margin by 20 basis points.
- Loss from operations increased 5,120% to \$21.5 million for the quarter ended November 3, 2018, compared to \$0.4 million in the same prior-year period.

Table of Contents

Other expense, net (including interest income and expense), totaled \$5.8 million for the quarter ended November 3, 2018, compared to other income, net, of \$2.4 million in the same prior-year period. The effective income tax rate improved to 53.1% for the quarter ended November 3, 2018, compared to 182.6% in the same prior-year period. During the quarter ended November 3, 2018, the Company revised the provisional amounts previously recorded related to impact of the Tax Reform, and recorded income tax benefits of \$19.6 million.

Key Balance Sheet Accounts

The Company had \$138.9 million in cash and cash equivalents and \$0.5 million in restricted cash as of November 3, 2018, compared to \$233.1 million in cash and cash equivalents and \$0.2 million in restricted cash at October 28, 2017.

The Company invested \$17.6 million to repurchase 1,118,808 of its common shares during the nine months ended November 3, 2018. During the nine months ended November 3, 2018, the Company also paid an additional \$6.0 million for shares that were repurchased during the fourth quarter of fiscal 2018 but were settled during the first quarter of fiscal 2019.

Accounts receivable consists of trade receivables relating primarily to the Company's wholesale business in Europe and, to a lesser extent, to its wholesale businesses in the Americas and Asia, royalty receivables relating to its licensing operations, credit card and retail concession receivables related to its retail businesses and certain other receivables. Accounts receivable increased by \$49.4 million, or 20.9%, to \$286.1 million as of November 3, 2018, compared to \$236.7 million at October 28, 2017, and includes the impact of the reclassifications related to the adoption of the new revenue recognition standard in the first quarter of fiscal 2019. On a constant currency basis, accounts receivable increased by \$55.9 million, or 23.6%, when compared to October 28, 2017.

Inventory increased by \$71.3 million, or 15.0%, to \$548.5 million as of November 3, 2018, compared to \$477.2 million at October 28, 2017, and includes the impact of the reclassifications related to the adoption of the new revenue recognition standard in the first quarter of fiscal 2019. On a constant currency basis, inventory increased by \$83.9 million, or 17.6%, when compared to October 28, 2017.

Global Store Count

In the third quarter of fiscal 2019, together with our partners, we opened 65 new stores worldwide, consisting of 22 stores in Europe and the Middle East, 30 stores in Asia and the Pacific, six stores in Central and South America, four stores in the U.S., and three stores in Canada. Together with our partners, we closed 35 stores worldwide, consisting of 18 stores in Asia and the Pacific, one store in the U.S., seven stores in Central and South America, no stores in Canada and nine stores in Europe and the Middle East.

We ended the third quarter of fiscal 2019 with 1,692 stores and 432 concessions worldwide, comprised as follows:

Region	Stores			Concessions		
	Total	Directly Operated	Partner Operated	Total	Directly Operated	Partner Operated
United States	298	296	2	1	—	1
Canada	89	89	—	—	—	—
Central and South America	103	65	38	27	27	—
Total Americas	490	450	40	28	27	1
Europe and the Middle East	687	460	227	39	39	—
Asia and the Pacific	515	198	317	365	174	191
Total	1,692	1,108	584	432	240	192

Of the total 1,692 stores, 1355 were GUESS? stores, 218 were GUESS? Accessories stores, 70 were G by GUESS stores and 49 were MARCIANO stores.

Table of Contents

Results of Operations

Three Months Ended November 3, 2018 and October 28, 2017

Consolidated Results

Net Revenue. Net revenue increased by \$56.5 million, or 10.3%, to \$605.4 million for the quarter ended November 3, 2018, compared to \$549.0 million for the quarter ended October 28, 2017. In constant currency, net revenue increased by 13.1% as currency translation fluctuations relating to our foreign operations unfavorably impacted net revenue by \$15.5 million compared to the same prior-year period. The increase was driven primarily by retail expansion in our international markets and, to a lesser extent, the impact of positive comparable sales in all regions and higher wholesale shipments in Europe and the Americas.

Gross Margin. Gross margin increased 160 basis points to 36.4% for the quarter ended November 3, 2018, compared to 34.8% in the same prior-year period, of which 100 basis points was due to higher overall product margins and 60 basis points was due to a lower occupancy rate. The higher overall product margins were driven primarily by lower markdowns in Americas Retail and higher initial markups, partially offset by higher duties and freight costs in Europe. The lower occupancy rate was driven primarily by overall leveraging of expenses due mainly to higher European wholesale shipments and positive comparable sales and negotiated rent reductions in Americas Retail, partially offset by higher distribution costs related to the relocation of the Company's European distribution center.

Gross Profit. Gross profit increased by \$29.0 million, or 15.2%, to \$220.1 million for the quarter ended November 3, 2018, compared to \$191.1 million in the same prior-year period. The increase in gross profit, which included the unfavorable impact of currency translation, was due primarily to the favorable impact on gross profit from higher revenue and, to a lesser extent, the higher gross margins. Currency translation fluctuations relating to our foreign operations unfavorably impacted gross profit by \$5.6 million.

The Company includes inbound freight charges, purchasing costs and related overhead, retail store occupancy costs, including rent and depreciation, and a portion of the Company's distribution costs related to its retail business in cost of product sales. The Company also includes net royalties received on the Company's inventory purchases of licensed product as a reduction to cost of product sales. The Company's gross margin may not be comparable to that of other entities since some entities include all of the costs related to their distribution in cost of product sales and others, like the Company, generally exclude wholesale-related distribution costs from gross margin, including them instead in SG&A expenses. Additionally, some entities include retail store occupancy costs in SG&A expenses and others, like the Company, include retail store occupancy costs in cost of product sales.

SG&A Rate. The Company's SG&A rate increased 40 basis points to 32.8% for the quarter ended November 3, 2018, compared to 32.4% in the same prior-year period driven primarily by higher distribution costs related to the relocation of the Company's European distribution center.

SG&A Expenses. SG&A expenses increased by \$19.9 million, or 11.2%, to \$197.9 million for the quarter ended November 3, 2018, compared to \$178.0 million in the same prior-year period. The increase, which included the unfavorable impact of currency translation, was driven primarily by higher selling and merchandising expenses, higher advertising expenses (in part due to classification changes under the new revenue recognition standard) and distribution costs related to the relocation of the Company's European distribution center. Currency translation fluctuations relating to our foreign operations unfavorably impacted SG&A expenses by \$4.3 million.

European Commission Fine. During the quarter ended November 3, 2018, the Company recognized charges of €37.0 million (\$42.4 million) related to an estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of certain European Union competition rules by the Company. Refer to "Part I, Item 1. Financial Statements — Note 12 — Commitments and Contingencies — Legal and Other Proceedings" for more information regarding this matter.

Table of Contents

Asset Impairment Charges. During the quarter ended November 3, 2018, the Company recognized asset impairment charges of \$1.3 million, compared to \$2.0 million in the same prior-year period.

Operating Margin. Operating margin decreased 350 basis points to negative 3.6% for the quarter ended November 3, 2018, compared to negative 0.1% in the same prior-year period. For the quarter ended November 3, 2018 as compared to the same prior-year period, the charges related to the estimated European Commission fine negatively impacted operating margin by 700 basis points, lower losses on lease terminations positively impacted operating margins by 210 basis points and lower asset impairment charges positively impacted operating margin by 20 basis points.

Excluding the impact of these items, operating margin increased by 130 basis points compared to the same prior-year period. The positive impact of currency on operating margin for the quarter ended November 3, 2018 was approximately 20 basis points.

Loss from Operations. Loss from operations increased by \$21.1 million, or 5,119.7%, to \$21.5 million for the quarter ended November 3, 2018, compared to \$0.4 million in the same prior-year period. Currency translation fluctuations relating to our foreign operations unfavorably impacted loss from operations by \$1.3 million.

Interest Income, Net. Interest income, net, was minimal for the quarter ended November 3, 2018, compared to \$0.2 million for the quarter ended October 28, 2017 and includes the impact of hedge ineffectiveness of foreign exchange currency contracts designated as cash flow hedges.

Other Income (Expense), Net. Other expense, net, was \$5.8 million for the quarter ended November 3, 2018, compared to other income, net, of \$2.2 million in the same prior-year period. Other expense, net, in the quarter ended November 3, 2018 consisted primarily of unrealized losses on non-operating assets and net realized mark-to-market revaluation losses on foreign currency balances, partially offset by realized mark-to-market revaluation gains on foreign exchange currency contracts. Other income, net, in the quarter ended October 28, 2017 consisted primarily of unrealized gains on non-operating assets and net unrealized and realized mark-to-market revaluation gains on foreign exchange currency contracts.

Income Tax Expense (Benefit). The income tax benefit for the quarter ended November 3, 2018 was \$14.5 million, or a 53.1% effective tax rate, compared to income tax expense of \$3.7 million, or a 182.6% effective tax rate, in the same prior-year period. Generally, income taxes for the interim periods are computed using the tax rate estimated to be applicable for the full fiscal year, adjusted for discrete items, which is subject to ongoing review and evaluation by management. During the three months ended November 3, 2018, the Company revised provisional amounts initially recorded in the three months ended February 3, 2018 related to the Tax Reform and recognized a tax benefit of \$19.6 million. This benefit increased the effective tax rate by approximately 72%. The remaining change in the effective income tax rate during the quarter ended November 3, 2018 compared to the same prior-year period was due primarily to the impact of discrete non-deductible expenses during the quarter ended November 3, 2018, and to a lesser extent, the mix of earnings in jurisdictions with different statutory tax rates and valuation allowances (including the lower U.S. tax rate due to the Tax Reform).

Net Earnings Attributable to Noncontrolling Interests. Net earnings attributable to noncontrolling interests were \$0.6 million, net of taxes, for the quarter ended November 3, 2018, compared to \$1.2 million, net of taxes, for the quarter ended October 28, 2017.

Net Earnings (Loss) Attributable to Guess?, Inc. Net loss attributable to Guess?, Inc. increased by \$10.6 million, or 370.0%, to \$13.4 million for the quarter ended November 3, 2018, compared to \$2.9 million in the same prior-year period. Diluted loss per share increased to \$0.17 for the quarter ended November 3, 2018, compared to \$0.04 for the quarter ended October 28, 2017. During the quarter ended November 3, 2018, the Company recognized asset impairment charges of \$1.3 million, certain professional services and legal fees and related costs of \$0.1 million, income tax benefits of \$19.6 million related to changes in the provisional amounts recorded related to the Tax Reform, and charges of €37.0 million (\$42.4 million) related to the estimated European Commission fine (or a combined \$24.0 million after considering the related tax benefit of \$0.2 million), or an unfavorable \$0.30

Table of Contents

per share impact. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. were \$10.6 million and adjusted diluted earnings were \$0.13 per common share for the quarter ended November 3, 2018. We estimate that the negative impact of currency on diluted earnings per share for the quarter ended November 3, 2018 was approximately \$0.02 per share. During the quarter ended October 28, 2017, the Company recognized asset impairment charges of \$2.0 million and lease termination charges of \$11.5 million (or \$13.3 million after considering the related tax benefit of these adjustments of \$0.3 million), or an unfavorable \$0.16 per share impact. Excluding the impact of these amounts and the related tax effect, adjusted net earnings attributable to Guess?, Inc. were \$10.4 million and adjusted diluted earnings were \$0.12 per common share for the quarter ended October 28, 2017.

References to financial results excluding the impact of these items are non-GAAP measures and are addressed below under "Non-GAAP Measures."

Information by Business Segment

The following table presents our net revenue and earnings (loss) from operations by segment for the three months ended November 3, 2018 and October 28, 2017 (dollars in thousands):

	Three Months Ended		Change	% Change
	Nov 3, 2018	Oct 28, 2017		
Net revenue:				
Americas Retail	\$186,925	\$187,021	\$(-96)	(0.1 %)
Americas Wholesale	52,698	45,636	7,062	15.5
Europe	254,037	221,230	32,807	14.8
Asia	89,461	74,322	15,139	20.4
Licensing ^{1,2}	22,286	20,744	1,542	7.4
Total net revenue ^{1,2}	\$605,407	\$548,953	\$56,454	10.3 %
Earnings (loss) from operations:				
Americas Retail ^{2,3}	\$3,799	\$(2,414)	\$6,213	257.4 %
Americas Wholesale ^{2,3}	10,392	8,562	1,830	21.4
Europe ^{3,4}	7,410	9,095	(1,685)	(18.5)
Asia ³	1,938	2,954	(1,016)	(34.4)
Licensing ^{2,3}	19,485	18,346	1,139	6.2
Total segment earnings from operations ^{2,4}	43,024	36,543	6,481	17.7
Corporate overhead ^{2,4}	(20,824)	(23,443)	2,619	11.2
Estimated European Commission fine ⁵	(42,428)	—	(42,428)	
Net gains on lease terminations	—	\$(11,494)	11,494	
Asset impairment charges ⁶	(1,277)	(2,018)	741	
Total loss from operations ^{2,4,5,6}	\$21,505)	\$(412)	\$21,093)	5,119.7%
Operating margins:				
Americas Retail ^{2,3}	2.0	% (1.3	%)	
Americas Wholesale ^{2,3}	19.7	% 18.8	%	
Europe ^{3,4}	2.9	% 4.1	%	
Asia ³	2.2	% 4.0	%	
Licensing ^{1,2,3}	87.4	% 88.4	%	
Total Company ^{1,2,4,5,6}	(3.6	)% (0.1)%	

Notes:

- ¹ During the fourth quarter of fiscal 2018, the Company reclassified net royalties received on the Company's inventory purchases of licensed product from net revenue to cost of product sales to reflect its treatment as a reduction of the cost of such licensed product. Accordingly, net revenue for the three months ended October 28, 2017 has been adjusted to conform to the current period presentation. This reclassification had no impact on previously reported

loss from operations.

During the first quarter of fiscal 2019, the Company adopted a comprehensive new revenue recognition standard using a modified retrospective method that does not restate prior periods to be comparable to the current period presentation. The adoption of this guidance primarily impacted the presentation of advertising contributions received from the Company's licensees and the related advertising expenditures incurred by the Company. The adoption of this guidance resulted in an increase in net royalty revenue within the Company's Licensing segment of \$2.7 million, as well as an increase in SG&A

Table of Contents

expenses in our Americas Retail, Americas Wholesale and Licensing segments as well as corporate overhead of \$1.0 million, \$0.6 million, \$0.3 million and \$0.6 million, respectively, during the three months ended November 3, 2018 compared to the same prior-year period. The net favorable impact on earnings from operations was approximately \$0.2 million during the three months ended November 3, 2018 compared to the same prior-year period. Refer to Note 1 to the Condensed Consolidated Financial Statements for more information regarding the impact from the adoption of this new standard.

During the first quarter of fiscal 2019, the Company changed the segment accountability for funds received from licensees on the Company's purchases of its licensed products. These amounts were treated as a reduction of cost of product sales within the Licensing segment but now are considered in the results of the segments that control the respective purchases for purposes of segment performance evaluation. Accordingly, segment results for the three months ended October 28, 2017 have been adjusted to conform to the current period presentation.

During the first quarter of fiscal 2019, the Company adopted new authoritative guidance which requires that the non-service components of net periodic defined benefit pension cost be presented outside of earnings (loss) from operations. Accordingly, loss from operations and segment results for the three months ended October 28, 2017 have been adjusted to conform to the current period presentation.

During the quarter ended November 3, 2018, the Company recognized charges of €37.0 million (\$42.4 million) related to an estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of certain European Union competition rules by the Company.

During each of the periods presented, the Company recognized asset impairment charges for certain retail locations resulting from under-performance and expected store closures. Refer to Note 14 for more information regarding these asset impairment charges.

Americas Retail

Net revenue from our Americas Retail segment decreased by \$0.1 million, or 0.1%, to \$186.9 million for the quarter ended November 3, 2018, from \$187.0 million in the same prior-year period. In constant currency, net revenue increased by 1.1%, driven primarily by positive comparable sales, partially offset by store closures. The store base for the U.S. and Canada decreased by an average of 35 net stores during the quarter ended November 3, 2018 compared to the same prior-year period, resulting in an 8.4% net decrease in average square footage. Comparable sales (including e-commerce) increased 3% in U.S. dollars and 4% in constant currency. The inclusion of our e-commerce sales had a minimal impact on the comparable sales percentage in U.S. dollars and constant currency. Currency translation fluctuations relating to our non-U.S. retail stores and e-commerce sites had a negative impact of \$2.2 million on net revenue during the quarter ended November 3, 2018.

Operating margin improved 330 basis points to 2.0% for the quarter ended November 3, 2018, compared to negative 1.3% in the same prior-year period, due to higher gross margins, partially offset by a higher SG&A rate. The higher gross margins were driven primarily by lower markdowns and, to a lesser extent, cost reductions due primarily to negotiated rent reductions. The higher SG&A rate was driven primarily by higher store selling expenses.

Earnings from operations from our Americas Retail segment were \$3.8 million for the quarter ended November 3, 2018, compared to operating loss of \$2.4 million in the same prior-year period. The improvement reflects the favorable impact on earnings from the higher product margins, positive comparable store sales and, to a lesser extent, lower occupancy costs driven primarily by negotiated rent reductions.

Americas Wholesale

Net revenue from our Americas Wholesale segment increased by \$7.1 million, or 15.5%, to \$52.7 million for the quarter ended November 3, 2018, compared to \$45.6 million in the same prior-year period. In constant currency, net revenue increased by 18.2%, driven primarily by higher shipments in our U.S. wholesale business. Currency translation fluctuations relating to our non-U.S. wholesale businesses unfavorably impacted net revenue by \$1.2 million.

Operating margin improved 90 basis points to 19.7% for the quarter ended November 3, 2018, from 18.8% in the same prior-year period, due primarily to higher gross margins.

Table of Contents

Earnings from operations from our Americas Wholesale segment increased by \$1.8 million, or 21.4%, to \$10.4 million for the quarter ended November 3, 2018, compared to \$8.6 million in the same prior-year period.

Europe

Net revenue from our Europe segment increased by \$32.8 million, or 14.8%, to \$254.0 million for the quarter ended November 3, 2018, compared to \$221.2 million in the same prior-year period. In constant currency, net revenue increased by 19.8%, driven primarily by retail expansion, higher shipments in our European wholesale business and positive comparable sales. As of November 3, 2018, we directly operated 460 stores in Europe compared to 385 stores at October 28, 2017, excluding concessions, which represents a 19.5% increase over the same prior-year period.

Comparable sales (including e-commerce) increased 8% in U.S. dollars and 12% in constant currency compared to the same prior-year period. The inclusion of our e-commerce sales increased the comparable sales percentage by 5% in U.S. dollars and constant currency. Currency translation fluctuations relating to our European operations unfavorably impacted net revenue by \$11.1 million.

Operating margin decreased 120 basis points to 2.9% for the quarter ended November 3, 2018, from 4.1% in the same prior-year period, driven primarily by lower gross margins and a higher SG&A rate. The lower gross margins were due primarily to higher distribution costs related to the relocation of the Company's European distribution center. The higher SG&A rate was driven primarily by higher distribution costs related to the relocation of the Company's European distribution center, partially offset by overall leveraging of expenses resulting from higher revenues. Earnings from operations from our Europe segment decreased by \$1.7 million, or 18.5%, to \$7.4 million for the quarter ended November 3, 2018, compared to \$9.1 million in the same prior-year period, driven primarily by higher distribution costs related to the relocation of the Company's European distribution center, partially offset by the favorable impact on earnings from higher revenue. Currency translation fluctuations relating to our European operations unfavorably impacted earnings from operations by \$1.0 million.

Asia

Net revenue from our Asia segment increased by \$15.1 million, or 20.4%, to \$89.5 million for the quarter ended November 3, 2018, compared to \$74.3 million in the same prior-year period. In constant currency, net revenue increased by 21.8%, driven primarily by retail expansion and, to a lesser extent, positive comparable sales. As of November 3, 2018, we and our partners operated 515 stores and 365 concessions in Asia, compared to 482 stores and 371 concessions at October 28, 2017. As of November 3, 2018, we directly operated 198 stores and 174 concessions in Asia, compared to 132 directly operated stores and 183 concessions at October 28, 2017. Comparable sales (including e-commerce) increased 8% in U.S. dollars and 9% in constant currency. The inclusion of our e-commerce sales increased the comparable sales percentage by 3% in U.S. dollars and constant currency. Currency translation fluctuations relating to our Asian operations unfavorably impacted net revenue by \$1.1 million.

Operating margin decreased 180 basis points to 2.2% for the quarter ended November 3, 2018, from 4% in the same prior-year period, due to a higher SG&A rate, and to a lesser extent, lower gross margins. The higher SG&A rate was driven by higher expenses due primarily to retail expansion. The lower gross margins were driven primarily by the unfavorable impact of country mix on product margins.

Earnings from operations from our Asia segment decreased by \$1.0 million, or 34.4%, to \$1.9 million for the quarter ended November 3, 2018, from \$3.0 million in the same prior-year period, driven primarily by the unfavorable impact on earnings from higher SG&A expenses and lower product margins, partially offset by the favorable impact on earnings from revenue.

Table of Contents

Licensing

Net royalty revenue from our Licensing segment increased by \$1.5 million, or 7.4%, to \$22.3 million for the quarter ended November 3, 2018, compared to \$20.7 million in the same prior-year period. This increase was driven by the impact from the adoption of new accounting guidance for revenue recognition which increased net royalty revenue by \$2.7 million, or 13.0%, during the quarter ended November 3, 2018 compared to the same prior-year period.

Earnings from operations from our Licensing segment increased by \$1.1 million, or 6.2%, to \$19.5 million for the quarter ended November 3, 2018, compared to \$18.3 million in the same prior-year period. The increase was driven by the favorable impact to earnings from higher revenue.

Corporate Overhead

Unallocated corporate overhead decreased by \$2.6 million to \$20.8 million for the quarter ended November 3, 2018, compared to \$23.4 million in the same prior-year period, driven primarily by lower general legal related expenses and performance-based compensation, partially offset by an increase in advertising expenses.

Nine Months Ended November 3, 2018 and October 28, 2017

Consolidated Results

Net Revenue. Net revenue increased by \$201.0 million, or 12.8%, to \$1.8 billion for the nine months ended November 3, 2018, compared to \$1.6 billion for the nine months ended October 28, 2017. In constant currency, net revenue increased by 11.2% as currency translation fluctuations relating to our foreign operations favorably impacted net revenue by \$24.8 million compared to the same prior-year period. The increase was driven primarily by retail expansion in our international markets, higher wholesale shipments in the U.S and Europe and positive comparable sales.

Gross Margin. Gross margin increased 170 basis points to 35.7% for the nine months ended November 3, 2018, compared to 34.0% in the same prior-year period, of which 140 basis points was due to higher overall product margins and 30 basis points was due to a lower occupancy rate. The higher overall product margins were driven primarily by lower markdowns in Americas Retail and higher initial markups. The lower occupancy rate was driven primarily by overall global leveraging of expenses and cost reductions due primarily to negotiated rent reductions in Americas Retail, partially offset by higher distribution costs related to the relocation of the Company's European distribution center.

Gross Profit. Gross profit increased by \$99.7 million, or 18.7%, to \$633.5 million for the nine months ended November 3, 2018, compared to \$533.8 million in the same prior-year period. The increase in gross profit, which included the favorable impact of currency translation, was due primarily to the favorable impact on gross profit from higher revenue and, to a lesser extent, the improved gross margin. Currency translation fluctuations relating to our foreign operations favorably impacted gross profit by \$6.4 million.

SG&A Rate. The Company's SG&A rate increased 80 basis points to 33.8% for the nine months ended November 3, 2018, compared to 33.0% in the same prior-year period. The Company's SG&A rate included the negative impact of 30 basis points from certain professional service and legal fees and related costs, which the Company otherwise would not have incurred as part of its business operations. Excluding these amounts, the Company's SG&A rate would have increased 50 basis points driven primarily by higher distribution costs related to the relocation of the Company's European distribution center.

SG&A Expenses. SG&A expenses increased by \$82.9 million, or 16.0%, to \$600.7 million for the nine months ended November 3, 2018, compared to \$517.9 million in the same prior-year period. The increase, which included the favorable impact of currency translation, was driven primarily by higher distribution costs related to the relocation of the Company's European distribution center and, to a lesser extent, higher selling and merchandising expenses. Currency translation fluctuations relating to our foreign operations favorably impacted SG&A expenses by \$11.9 million.

Table of Contents

European Commission Fine. During the nine months ended November 3, 2018, the Company recognized charges of €37.0 million (\$42.4 million) related to an estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of certain European Union competition rules by the Company. Refer to “Part I, Item 1. Financial Statements — Note 12 — Commitments and Contingencies” for more information regarding this matter.

Net Gains (Losses) on Lease Terminations. During the nine months ended November 3, 2018, the Company recognized net gains on lease terminations of \$0.2 million related primarily to the early termination of certain lease agreements in North America. There were net losses on lease terminations of \$11.5 million during the nine months ended October 28, 2017.

Asset Impairment Charges. During the nine months ended November 3, 2018, the Company recognized asset impairment charges of \$5.0 million, compared to \$6.0 million in the same prior-year period.

Operating Margin. Operating margin decreased 70 basis points to negative 0.8% for the nine months ended November 3, 2018, compared to negative 0.1% in the same prior-year period. The charges related to the estimated European Commission fine negatively impacted operating margin by 240 points and certain professional service and legal fees and related costs negatively impacted operating margin by 30 basis points. This was partially offset by the favorable impact on operating margin from lower asset impairment charges of 10 basis points during the nine months ended November 3, 2018 compared to the same prior-year period. Lower losses on lease terminations of \$11.6 million had a positive impact of 70 basis points on operating margin for the nine months ended November 3, 2018. Excluding the impact of these items, operating margin would have improved by 120 basis points compared to the same prior-year period. The negative impact of currency on operating margin for the nine months ended November 3, 2018 was approximately 10 basis points.

Operating loss. Operating loss was \$14.5 million for the nine months ended November 3, 2018, compared to an operating loss of \$1.6 million in the same prior-year period. Currency translation fluctuations relating to our foreign operations unfavorably impacted earnings from operations by \$5.6 million.

Interest Income, Net. Interest income, net, was \$0.5 million for the nine months ended November 3, 2018, compared to \$1.4 million for the nine months ended October 28, 2017 and includes the impact of hedge ineffectiveness of foreign exchange currency contracts designated as cash flow hedges.

Other Income (Expense), Net. Other expense, net, was \$7.1 million for the nine months ended November 3, 2018, compared to other income, net, of \$1.9 million in the same prior-year period. Other expense, net, in the nine months ended November 3, 2018 consisted primarily of net unrealized and realized mark-to-market revaluation losses on foreign currency balances and unrealized losses on non-operating assets, partially offset by net unrealized and realized mark-to-market revaluation gains on foreign exchange currency contracts. Other income, net, in the nine months ended October 28, 2017 consisted primarily of unrealized gains on non-operating assets and net unrealized mark-to-market revaluation gains on foreign currency balances, partially offset by net realized and unrealized mark-to-market revaluation losses on foreign exchange currency contracts.

Income Tax Expense (Benefit). The income tax benefit for the nine months ended November 3, 2018 was \$13.0 million, or a 61.7% effective tax rate, compared to income tax expense of \$8.7 million, or a 508.6% effective tax rate, in the same prior-year period. Generally, income taxes for the interim periods are computed using the tax rate estimated to be applicable for the full fiscal year, adjusted for discrete items, which is subject to ongoing review and evaluation by management. During the three months ended November 3, 2018, the Company revised provisional amounts initially recorded in the three months ended February 3, 2018 related to the Tax Reform and recognized a tax benefit of \$19.6 million. This resulted in an increase in the effective tax rate for the nine months ended November 3, 2018 of approximately 93.0%. The remaining change in the adjusted effective tax rate was due primarily to higher losses incurred in certain foreign jurisdictions where the Company has valuation allowances in the same prior-year period, the impact of the mix of earnings in different taxable jurisdictions (including the

Table of Contents

lower U.S. tax rate due to the Tax Reform), the impact of discrete non-deductible expenses during the quarter ended November 3, 2018, and the reversal of a valuation allowance.

Net Earnings Attributable to Noncontrolling Interests. Net earnings attributable to noncontrolling interests were \$1.1 million, net of taxes, for the nine months ended November 3, 2018, compared to \$1.9 million, net of taxes, for the nine months ended October 28, 2017.

Net Loss Attributable to Guess?, Inc. Net loss attributable to Guess?, Inc. was \$9.1 million for the nine months ended November 3, 2018, compared to \$8.9 million in the same prior-year period. Diluted loss per share was \$0.12 for the nine months ended November 3, 2018, compared to \$0.12 for the nine months ended October 28, 2017. During the nine months ended November 3, 2018, the Company recognized net gains on lease terminations of \$0.2 million, asset impairment charges of \$5.0 million, certain professional services and legal fees and related costs of \$5.9 million, income tax benefits of \$19.6 million related to changes in provisional amounts recorded due to the Tax Reform, and charges of \$42.4 million (€37.0 million) related to the estimated European Commission fine (or a combined \$31.3 million after considering the related tax benefit of \$2.3 million), or a negative impact of \$0.39 per share. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. were \$22.2 million and adjusted diluted earnings were \$0.27 per common share during the nine months ended November 3, 2018. We estimate there was no significant impact of currency on diluted earnings per share for the nine months ended November 3, 2018. During the nine months ended October 28, 2017, the Company recognized asset impairment charges of \$6.0 million and net losses on lease terminations of \$11.5 million (or \$16.0 million after considering the related tax benefit of these adjustments of \$1.5 million), or an unfavorable \$0.20 per share impact. Excluding the impact of these items and the related tax effects, adjusted net earnings attributable to Guess?, Inc. were \$7.1 million and adjusted diluted earnings per share were \$0.08 per common share during the nine months ended October 28, 2017. References to financial results excluding the impact of these items are non-GAAP measures and are addressed below under “Non-GAAP Measures.”

Table of Contents

Information by Business Segment

The following table presents our net revenue and earnings (loss) from operations by segment for the nine months ended November 3, 2018 and October 28, 2017 (dollars in thousands):

	Nine Months Ended			% Change
	Nov 3, 2018	Oct 28, 2017	Change	Change
Net revenue:				
Americas Retail	\$555,390	\$561,903	\$ (6,513)	(1.2 %)
Americas Wholesale	127,630	114,151	13,479	11.8
Europe	771,470	641,833	129,637	20.2
Asia	256,298	200,436	55,862	27.9
Licensing ^{1,2}	61,779	53,267	8,512	16.0
Total net revenue ^{1,2}	\$1,772,567	\$1,571,590	\$200,977	12.8 %
Earnings (loss) from operations:				
Americas Retail ^{2,3}	\$3,701	\$ (27,550)	\$31,251	113.4 %
Americas Wholesale ^{2,3}	21,743	20,783	960	4.6
Europe ^{3,4}	17,608	38,147	(20,539)	(53.8)
Asia ³	7,637	5,734	1,903	33.2
Licensing ^{2,3}	54,408	46,196	8,212	17.8
Total segment earnings from operations ^{2,4}	105,097	83,310	21,787	26.2
Corporate overhead ^{2,4}	(72,316)	(67,403)	(4,913)	(7.3)
Estimated European Commission fine ⁵	(42,428)	—	(42,428)	
Net gains on lease terminations	152	(11,494)	11,646	
Asset impairment charges ⁶	(5,017)	(6,013)	996	
Total loss from operations ^{2,4,5,6}	\$ (14,512)	\$ (1,600)	\$ (12,912)	(807.0 %)
Operating margins:				
Americas Retail ^{2,3}	0.7	% (4.9	%)	
Americas Wholesale ^{2,3}	17.0	% 18.2	%	
Europe ^{3,4}	2.3	% 5.9	%	
Asia ³	3.0	% 2.9	%	
Licensing ^{1,2,3,4}	88.1	% 86.7	%	
Total Company ^{1,2,4,5,6}	(0.8	%) (0.1	%)	

Notes:

During the fourth quarter of fiscal 2018, the Company reclassified net royalties received on the Company's inventory purchases of licensed product from net revenue to cost of product sales to reflect its treatment as a reduction of the cost of such licensed product. Accordingly, net revenue for the nine months ended October 28, 2017 has been adjusted to conform to the current period presentation. This reclassification had no impact on previously reported loss from operations.

During the first quarter of fiscal 2019, the Company adopted a comprehensive new revenue recognition standard using a modified retrospective method that does not restate prior periods to be comparable to the current period presentation. The adoption of this guidance primarily impacted the presentation of advertising contributions received from the Company's licensees and the related advertising expenditures incurred by the Company. The adoption of this guidance resulted in an increase in net royalty revenue within the Company's Licensing segment of \$7.1 million, as well as an increase in SG&A expenses in our Americas Retail, Americas Wholesale and Licensing segments as well as corporate overhead of \$3.3 million, \$1.5 million, \$0.7 million and \$1.7 million, respectively, during the nine months ended November 3, 2018 compared to the same prior-year period. The net unfavorable impact on earnings from operations was approximately \$0.1 million during the nine months ended November 3, 2018 compared to the same prior-year period. Refer to Note 1 to the Condensed Consolidated Financial Statements

Edgar Filing: GUESS INC - Form 10-Q

for more information regarding the impact from the adoption of this new standard. During the first quarter of fiscal 2019, the Company changed the segment accountability for funds received from licensees on the Company's purchases of its licensed products. These amounts were treated as a reduction of cost of product sales within the Licensing segment but now are considered in the results of the segments that control the respective purchases for purposes of segment performance evaluation. Accordingly, segment results for the nine months ended October 28, 2017 have been adjusted to conform to the current period presentation.³

Table of Contents

During the first quarter of fiscal 2019, the Company adopted new authoritative guidance which requires that the non-service components of net periodic defined benefit pension cost be presented outside of earnings (loss) from operations. Accordingly, loss from operations and segment results for the nine months ended October 28, 2017 have been adjusted to conform to the current period presentation.

During the quarter ended November 3, 2018, the Company recognized charges of €37.0 million (\$42.4 million) related to an estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of certain European Union competition rules by the Company.

During each of the periods presented, the Company recognized asset impairment charges for certain retail locations resulting from under-performance and expected store closures. Refer to Note 14 for more information regarding these asset impairment charges.

Americas Retail

Net revenue from our Americas Retail segment decreased by \$6.5 million, or 1.2%, to \$555.4 million for the nine months ended November 3, 2018, from \$561.9 million in the same prior-year period. In constant currency, net revenue decreased by 1.0%, driven primarily by store closures, partially offset by positive comparable sales. The store base for the U.S. and Canada decreased by an average of 46 net stores during the nine months ended November 3, 2018 compared to the same prior-year period, resulting in a 10.7% net decrease in average square footage.

Comparable sales (including e-commerce) increased 3% in U.S. dollars and constant currency. The inclusion of our e-commerce sales had a 0.2% positive impact on the comparable sales percentage in U.S. dollars and constant currency. Currency translation fluctuations relating to our non-U.S. retail stores and e-commerce sites unfavorably impacted net revenue by \$0.8 million.

Operating margin improved 560 basis points to 0.7% for the nine months ended November 3, 2018, compared to negative 4.9% in the same prior-year period. This improvement was driven primarily by higher product margins due to lower markdowns and lower occupancy costs due primarily to negotiated rent reductions.

Earnings from operations from our Americas Retail segment improved by \$31.3 million, or 113.4%, to \$3.7 million for the nine months ended November 3, 2018, compared to loss from operations of \$27.6 million in the same prior-year period. The improvement reflects the favorable impact on earnings from improved gross margin.

Americas Wholesale

Net revenue from our Americas Wholesale segment increased by \$13.5 million, or 11.8%, to \$127.6 million for the nine months ended November 3, 2018, compared to \$114.2 million in the same prior-year period. In constant currency, net revenue increased by 12.8%, driven primarily by higher shipments in our U.S. wholesale business, and to a lesser extent, our Mexican and Canadian wholesale businesses. Currency translation fluctuations relating to our non-U.S. wholesale businesses unfavorably impacted net revenue by \$1.1 million.

Operating margin decreased 120 basis points to 17.0% for the nine months ended November 3, 2018, from 18.2% in the same prior-year period, due primarily to lower gross margins driven primarily by the liquidation of aged inventory in the first half of the year.

Earnings from operations from our Americas Wholesale segment increased by \$1.0 million, or 4.6%, to \$21.7 million for the nine months ended November 3, 2018, from \$20.8 million in the same prior-year period, driven primarily by the favorable impact on earnings from increased sales, partially offset by the unfavorable impact on earnings from lower gross margins.

Europe

Net revenue from our Europe segment increased by \$129.6 million, or 20.2%, to \$771.5 million for the nine months ended November 3, 2018, compared to \$641.8 million in the same prior-year period. In constant currency, net revenue increased by 16.9%, driven primarily by the favorable impact from retail expansion, higher shipments in our European wholesale business and to a lesser extent, positive comparable sales. Comparable sales (including e-commerce) increased 9% in U.S. dollars and 5% in constant currency compared to the same prior-year period. The inclusion of our e-commerce sales increased the comparable sales percentage by 5% in U.S. dollars and

Table of Contents

constant currency. Currency translation fluctuations relating to our European operations favorably impacted net revenue by \$21.2 million.

Operating margin decreased 360 basis points to 2.3% for the nine months ended November 3, 2018, from 5.9% in the same prior-year period, driven primarily by lower gross margins and, to a lesser extent, a higher SG&A rate. The lower gross margins were due primarily to higher distribution costs related to the relocation of the Company's European distribution center. The higher SG&A rate was driven by higher distribution costs related to the relocation of the Company's European distribution center, partially offset by overall leveraging of expenses resulting from higher revenues.

Earnings from operations from our Europe segment decreased by \$20.5 million, or 53.8%, to \$17.6 million for the nine months ended November 3, 2018, compared to \$38.1 million in the same prior-year period. The decrease was driven primarily by the higher distribution costs related to the relocation of the Company's European distribution center, partially offset by the favorable impact on earnings from revenue increases. Currency translation fluctuations relating to our European operations unfavorably impacted earnings from operations by \$5.6 million.

Asia

Net revenue from our Asia segment increased by \$55.9 million, or 27.9%, to \$256.3 million for the nine months ended November 3, 2018, compared to \$200.4 million in the same prior-year period. In constant currency, net revenue increased by 25.1%, driven primarily by retail expansion and, to a lesser extent, positive comparable sales.

Comparable sales (including e-commerce) increased 16% in U.S. dollars and 13% in constant currency compared to the same prior-year period. The inclusion of our e-commerce sales increased the comparable sales percentage by 4.4% in U.S. dollars and constant currency. Currency translation fluctuations relating to our Asian operations favorably impacted net revenue by \$5.5 million.

Operating margin improved 10 basis points to 3.0% for the nine months ended November 3, 2018, compared to 2.9% in the same prior-year period, due to higher gross margins, offset by a higher SG&A rate. The higher gross margins were due primarily to overall leveraging of occupancy costs. The higher SG&A rate was driven by higher expenses due primarily to retail expansion and country mix.

Earnings from operations from our Asia segment increased by \$1.9 million, or 33.2%, to \$7.6 million for the nine months ended November 3, 2018, compared to \$5.7 million in the same prior-year period, driven primarily by the favorable impact on earnings from higher revenue, partially offset by higher SG&A expenses.

Licensing

Net royalty revenue from our Licensing segment increased by \$8.5 million, or 16.0%, to \$61.8 million for the nine months ended November 3, 2018, compared to \$53.3 million in the same prior-year period. This increase was driven primarily by the impact from the adoption of new accounting guidance for revenue recognition which increased net royalty revenue by \$7.1 million, or 13.3%, during the nine months ended November 3, 2018 compared to the same prior-year period.

Earnings from operations from our Licensing segment increased by \$8.2 million, or 17.8%, to \$54.4 million for the nine months ended November 3, 2018, compared to \$46.2 million in the same prior-year period. The increase was driven by the favorable impact to earnings from higher revenue.

Corporate Overhead

Unallocated corporate overhead increased by \$4.9 million to \$72.3 million for the nine months ended November 3, 2018, compared to \$67.4 million in the same prior-year period, driven primarily by \$5.9 million in certain professional service and legal fees and related costs, which the Company otherwise would not have incurred as part of its business operations, and increased advertising expenses, partially offset by lower general legal expenses and performance-based compensation.

Table of Contents**Non-GAAP Measures**

The Company's reported financial results are presented in accordance with GAAP. The reported net loss attributable to Guess?, Inc. and diluted loss per share for the three and nine months ended November 3, 2018 reflect the impact of net gains (losses) on lease terminations, asset impairment charges, certain professional service and legal fees and related costs, estimated charges related to the expected European Commission fine, the tax effects of these adjustments, and revisions to provisional amounts previously recorded related to the Tax Reform, where applicable. The reported net loss attributable to Guess?, Inc. and diluted loss per share for the three and nine months ended October 28, 2017 reflect the impact of net losses on lease terminations, asset impairment charges and the tax effects of these adjustments. These items affect the comparability of the Company's reported results. The financial results are also presented on a non-GAAP basis, as defined in Section 10(e) of Regulation S-K of the SEC, to exclude the effect of these items. The Company believes that these items are not indicative of the underlying performance of its business and that the "non-GAAP" or "adjusted" information provided is useful for investors to evaluate the comparability of the Company's operating results and its future outlook when reviewed in conjunction with the Company's GAAP financial statements. The non-GAAP measures are provided in addition to, and not as alternatives for, the Company's reported GAAP results.

The adjusted measures for the three months ended November 3, 2018 exclude the impact of asset impairment charges of \$1.3 million, certain professional services and legal fees and related costs of \$0.1 million, estimated charges of \$42.4 million related to the expected European Commission fine, and the tax benefit related to changes in provisional amounts recorded related to the Tax Reform of \$19.6 million. The asset impairment charges related primarily to the impairment of certain retail locations in Europe and North America resulting from under-performance and expected store closures. These items resulted in a combined \$24.0 million impact (after considering the related tax benefit of \$0.2 million), or an unfavorable \$0.30 per share impact during the three months ended November 3, 2018. Net loss attributable to Guess?, Inc. was \$13.4 million and diluted loss was \$0.17 per common share for the three months ended November 3, 2018. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. were \$10.6 million and adjusted diluted earnings were \$0.13 per common share for the three months ended November 3, 2018.

The adjusted measures for the nine months ended November 3, 2018 exclude the impact of net gains on lease terminations of \$0.2 million, asset impairment charges of \$5.0 million, certain professional services and legal fees and related costs of \$5.9 million, estimated charges of \$42.4 million related to the expected European Commission fine, and the net tax benefit related to the above non-GAAP adjustments, if any, and changes in provisional amounts recorded related to the Tax Reform of \$19.6 million. The net gains on lease terminations related primarily to the early termination of certain lease agreements in North America. The asset impairment charges related primarily to the impairment of certain retail locations in Europe and North America resulting from under-performance and expected store closures. These items resulted in a combined \$31.3 million impact (after considering the related tax benefit of \$2.3 million), or an unfavorable \$0.39 per share impact during the nine months ended November 3, 2018. Net loss attributable to Guess?, Inc. was \$9.1 million and diluted loss was \$0.12 per common share for the nine months ended November 3, 2018. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. were \$22.2 million and adjusted diluted earnings were \$0.27 per common share for the nine months ended November 3, 2018.

The adjusted measures for the three months ended October 28, 2017 excluded the impact of net losses on lease terminations of \$11.5 million and asset impairment charges of \$2.0 million. The net losses on lease terminations related primarily to the modification of certain lease agreements held with a common landlord in North America. The asset impairment charges related primarily to the impairment of certain retail locations in North America resulting from under-performance and expected store closures. These items resulted in a \$13.3 million impact (after considering the related tax benefit of \$0.3 million), or an unfavorable \$0.16 per share impact during the three months ended October 28, 2017. Net loss attributable to Guess?, Inc. was \$2.9 million and diluted loss was \$0.04 per common share for the three months ended October 28, 2017. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. were \$10.4 million and adjusted diluted earnings were \$0.12 per common share for the three months ended October 28, 2017.

Table of Contents

The adjusted measures for the nine months ended October 28, 2017 exclude the impact of net losses on lease terminations of \$11.5 million and asset impairment charges of \$6.0 million. During the nine months ended October 28, 2017, these items resulted in a combined \$16.0 million impact (after considering the related tax benefit of \$1.5 million), or an unfavorable \$0.20 per share impact during the nine months ended October 28, 2017. Net loss attributable to Guess?, Inc. was \$8.9 million and diluted loss was \$0.12 per share for the nine months ended October 28, 2017. Excluding the impact of these items, adjusted net earnings attributable to Guess?, Inc. was \$7.1 million and adjusted diluted earnings were \$0.08 per common share for the nine months ended October 28, 2017.

Our discussion and analysis herein also includes certain constant currency financial information. Foreign currency exchange rate fluctuations affect the amount reported from translating the Company's foreign revenue, expenses and balance sheet amounts into U.S. dollars. These rate fluctuations can have a significant effect on reported operating results under GAAP. The Company provides constant currency information to enhance the visibility of underlying business trends, excluding the effects of changes in foreign currency translation rates. To calculate net revenue, comparable sales and earnings (loss) from operations on a constant currency basis, operating results for the current-year period are translated into U.S. dollars at the average exchange rates in effect during the comparable period of the prior year. To calculate balance sheet amounts on a constant currency basis, the current period balance sheet amount is translated into U.S. dollars at the exchange rate in effect at the comparable prior-year period end. The constant currency calculations do not adjust for the impact of revaluing specific transactions denominated in a currency that is different to the functional currency of that entity when exchange rates fluctuate. The constant currency information presented may not be comparable to similarly titled measures reported by other companies.

In calculating the estimated impact of currency fluctuations (including translational and transactional impacts) on other measures such as earnings (loss) per share, the Company estimates gross margin (including the impact of foreign exchange currency contracts designated as cash flow hedges for anticipated merchandise purchases) and expenses using the appropriate prior-year rates, translates the estimated foreign earnings (loss) at the comparable prior-year rates and excludes the year-over-year earnings impact of gains or losses arising from balance sheet remeasurement and foreign exchange currency contracts not designated as cash flow hedges for merchandise purchases.

Liquidity and Capital Resources

We need liquidity globally primarily to fund our working capital, occupancy costs, expansion plans, remodeling and rationalization of our retail stores, shop-in-shop programs, concessions, systems, infrastructure, other existing operations, international growth and potential acquisitions and investments. In addition, in the U.S. we need liquidity to fund share repurchases and payment of dividends to our stockholders. Generally, our working capital needs are highest during the late summer and fall as our inventories increase before the holiday selling period. During the nine months ended November 3, 2018, we relied primarily on trade credit, available cash, real estate and other operating leases, capital leases, proceeds from short-term lines of credit and internally generated funds to finance our operations, payment of dividends, share repurchases and expansion. We anticipate that we will be able to satisfy our ongoing cash requirements during the next twelve months for working capital, capital expenditures, payments on our debt, capital leases and operating leases as well as lease termination payments, potential acquisitions and investments, share repurchases and dividend payments to stockholders, primarily with cash flow from operations and existing cash balances as supplemented by borrowings under our existing Credit Facility in the U.S. and Canada as well as bank facilities in Europe as needed. Such facilities are described further below under "—Borrowings and Capital Lease Obligations." Due to the seasonality of our business and cash needs, including to help fund our continuing retail expansion plans, we expect to increase borrowings under our established credit facilities from time to time, during the next twelve months.

In December 2017, the U.S. government enacted the Tax Reform, which significantly changed the U.S. corporate income tax laws, including moving from a global taxation regime to a territorial regime and lowering the future U.S. federal tax rate from 35% to 21%. The Company is also required to pay a transition tax on all historical earnings of foreign subsidiaries that have not been repatriated to the U.S. Any income tax payable

Table of Contents

related to the transition tax is due over an eight-year period beginning in calendar 2018. The Company included \$1.9 million and \$17.7 million amounts recorded in the condensed consolidated balance sheet related to the transition tax in accrued expenses or other long-term liabilities as of February 3, 2018, respectively. During the third quarter of fiscal 2019, the Company completed the preparation of its U.S. federal tax return for fiscal 2018 and concluded, based on the additional information that has become available, that no transition tax is due with respect to the Tax Reform. As a result, during the three months ended November 3, 2018, the Company reversed provisional amounts initially recorded during the three months ended February 3, 2018 and recorded a benefit of \$19.6 million. Therefore, the Company had no amounts recorded in the condensed consolidated balance sheet related to the transition tax in accrued expenses or other long-term liabilities as of November 3, 2018.

The Company has provided for tax liabilities on amounts that are estimated to be repatriated from foreign operations as a result of the Tax Reform. We have not provided for other income taxes on undistributed foreign earnings expected to be reinvested outside the U.S. If in the future we decide to repatriate such earnings, we would incur other incremental taxes. Our current plans do not indicate a need to repatriate them to fund our U.S. cash requirements. As of November 3, 2018, the Company had cash and cash equivalents of \$138.9 million, of which approximately \$25.4 million was held in the U.S.

Excess cash and cash equivalents, which represent the majority of our outstanding cash and cash equivalents balance, are held primarily in overnight deposit and short-term time deposit accounts. Please see “—Important Factors Regarding Forward-Looking Statements” and “Part I, Item 1A. Risk Factors” contained in the Company’s most recent Annual Report on Form 10-K for the fiscal year ended February 3, 2018 for a discussion of risk factors which could reasonably be likely to result in a decrease of internally generated funds available to finance capital expenditures and working capital requirements.

The Company has presented below the cash flow performance comparison of the nine months ended November 3, 2018, compared to the nine months ended October 28, 2017.

Operating Activities

Net cash used in operating activities was \$46.9 million for the nine months ended November 3, 2018, compared to \$34.2 million for the nine months ended October 28, 2017, or a decrease of \$12.7 million. This decrease was driven primarily by changes in working capital due mainly to higher inventory and payables resulting from retail expansion, partially offset by higher cash flows generated from net earnings for the nine months ended November 3, 2018 compared to the same prior-year period.

Investing Activities

Net cash used in investing activities was \$83.2 million for the nine months ended November 3, 2018, compared to \$68.6 million for the nine months ended October 28, 2017. Net cash used in investing activities for the nine months ended November 3, 2018 related primarily to capital expenditures incurred on retail expansion, investments in technology infrastructure and existing store remodeling programs. In addition, the cost of any business acquisitions, purchases of investments and other assets and the settlement of forward exchange currency contracts are also included in cash flows used in investing activities.

The increase in cash used in investing activities was driven primarily by higher spending on retail expansion during the nine months ended November 3, 2018 compared to the same prior-year period. During the nine months ended November 3, 2018, the Company opened 133 directly operated stores compared to 92 directly operated stores that were opened in the same prior-year period.

Financing Activities

Net cash used in financing activities was \$78.3 million for the nine months ended November 3, 2018, compared to \$82.3 million for the nine months ended October 28, 2017. Net cash used in financing activities for the nine months ended November 3, 2018 related primarily to the payment of dividends and repurchases of shares of the Company’s common stock. In addition, payments related to capital lease obligations and borrowings and proceeds from issuance of common stock under our equity plan, capital contributions from noncontrolling interests and borrowings are also included in cash flows used in financing activities.

Table of Contents

The decrease in cash used in financing activities was driven primarily by higher proceeds from issuance of common stock under our equity plan, decrease in payments for repurchases of shares of the Company's common stock and dividends paid to stockholders, partially offset by an increase in distributions to noncontrolling interests during the nine months ended November 3, 2018 compared to the same prior-year period.

Effect of Exchange Rates on Cash, Cash Equivalents and Restricted Cash

During the nine months ended November 3, 2018, changes in foreign currency translation rates decreased our reported cash, cash equivalents and restricted cash balance by \$19.8 million. This compares to an increase of \$20.8 million in cash, cash equivalents and restricted cash driven by changes in foreign currency translation rates during the nine months ended October 28, 2017.

Working Capital

As of November 3, 2018, the Company had net working capital (including cash and cash equivalents) of \$522.1 million, compared to \$640.9 million at February 3, 2018 and \$616.6 million at October 28, 2017. The Company's primary working capital needs are for accounts receivable and inventory.

Accounts receivable increased by \$49.4 million, or 20.9%, to \$286.1 million as of November 3, 2018, compared to \$236.7 million at October 28, 2017. On a constant currency basis, accounts receivable increased by \$55.9 million, or 23.6%, when compared to October 28, 2017. During the first quarter of fiscal 2019, the Company adopted a new revenue recognition standard on a modified retrospective basis which changed the presentation of allowances for wholesale sales returns and wholesale markdowns to be classified within accrued expenses rather than as a reduction to accounts receivable. Accordingly, the Company has included allowances of \$26.1 million and \$11.2 million related to wholesale sales returns and wholesale markdowns, respectively, in accrued expenses as of November 3, 2018. The increase was driven primarily by the reclassification of reserves to accrued expenses, and higher European wholesale shipments, partially offset by the favorable timing of collections during the nine months ended November 3, 2018 compared to the same prior-year period.

The accounts receivable balance consists of trade receivables relating primarily to the Company's wholesale business in Europe and, to a lesser extent, to its wholesale businesses in the Americas and Asia, royalty receivables relating to its licensing operations, credit card and retail concession receivables related to its retail businesses and certain other receivables. As of November 3, 2018, approximately 49% of our total net trade receivables and 62% of our European net trade receivables were subject to credit insurance coverage, certain bank guarantees or letters of credit for collection purposes. Our credit insurance coverage contains certain terms and conditions specifying deductibles and annual claim limits.

Inventory increased by \$71.3 million, or 15.0%, to \$548.5 million as of November 3, 2018, compared to \$477.2 million at October 28, 2017. On a constant currency basis, inventory increased by \$83.9 million, or 17.6%, when compared to October 28, 2017. The adoption of the new revenue recognition standard also impacted the presentation of the estimated cost associated with the allowance for sales returns to be included within other current assets rather than included in inventories. Accordingly, the Company has included \$10.4 million related to the estimated cost associated with the allowance for sales returns in other current assets as of November 3, 2018. The increase in inventory was driven primarily by retail expansion in our international markets, partially offset by the reclassification of costs associated with sales returns to other current assets.

Table of Contents**Special Payments**

During the quarter ended November 3, 2018, the Company recognized charges of €37.0 million (\$42.4 million) related to an estimated fine expected to be imposed on the Company by the European Commission related to its inquiry concerning possible violations of certain European Union competition rules by the Company. Refer to “Part I, Item 1. Financial Statements — Note 12 — Commitments and Contingencies — Legal and Other Proceedings” for more information regarding this matter. Although such fines are typically payable within 90 days of the assessment date, the Company intends to request an extended pay period, if and when a fine is assessed. However, there can be no assurances that the Company will be granted any extension. Therefore, as of November 3, 2018, such amounts are classified as current within accrued expenses on the condensed consolidated balance sheet. If the Company is not granted an extension, the Company fully expects to have sufficient availability under existing credit facilities and working capital for full payment during the first quarter of fiscal 2020 if such fine is levied in the fourth quarter of fiscal 2019.

As discussed in more detail above, during the quarter ended November 3, 2018, the Company revised provisional amounts initially recorded in the three months ended February 3, 2018 related to the Tax Reform and recognized a tax benefit of \$19.6 million during the three months ended November 3, 2018. On November 28, 2018, the U.S. Internal Revenue Service (“IRS”) announced a proposed regulation to revise the section of the underlying IRS code which gave rise to the Company’s change in the provisional calculation. In the event legislation is passed in the future to revise the relevant IRS code section, the Company could have additional tax expense and tax liabilities of approximately \$12.8 million. In accordance with current legislation, such charges would be payable over the next seven years.

Capital Expenditures

Gross capital expenditures totaled \$74.9 million, before deducting lease incentives of \$6.0 million, for the nine months ended November 3, 2018. This compares to gross capital expenditures of \$65.3 million, before deducting lease incentives of \$6.0 million for the nine months ended October 28, 2017.

The Company’s investments in capital for the full fiscal year 2019 are planned between \$95 million and \$100 million. The planned investments in capital are related primarily to retail and e-commerce expansion in Europe and Asia as well as continued investments in technology to support our long-term growth plans.

We will periodically evaluate strategic acquisitions and alliances and pursue those that we believe will support and contribute to our overall growth initiatives.

Dividends

During the first quarter of fiscal 2008, the Company announced the initiation of a quarterly cash dividend of \$0.06 per share of the Company’s common stock. Since that time, the Company has continued to pay a quarterly cash dividend, which has subsequently increased to \$0.225 per common share.

On November 28, 2018, the Company announced a regular quarterly cash dividend of \$0.225 per share on the Company’s common stock. The cash dividend will be paid on January 2, 2019 to shareholders of record as of the close of business on December 12, 2018.

The payment of cash dividends in the future will be at the discretion of our Board of Directors and will be based upon a number of business, legal and other considerations, including our cash flow from operations, capital expenditures, debt service and covenant requirements, cash paid for income taxes, earnings, share repurchases, economic conditions and U.S. and global liquidity.

Share Repurchases

On June 26, 2012, the Company’s Board of Directors authorized a program to repurchase, from time-to-time and as market and business conditions warrant, up to \$500 million of the Company’s common stock. Repurchases under the program may be made on the open market or in privately negotiated transactions, pursuant to Rule 10b5-1 trading plans or other available means. There is no minimum or maximum number of shares to be repurchased under the program, which may be discontinued at any time, without prior notice. During the nine months ended November 3, 2018, the Company repurchased 1,118,808 shares under the program at an aggregate cost of \$17.6

Table of Contents

million. The shares were repurchased during the three months ended May 5, 2018. During the nine months ended November 3, 2018, the Company also paid an additional \$6.0 million for shares that were repurchased during the fourth quarter of fiscal 2018 but were settled during the first quarter of fiscal 2019. During the nine months ended October 28, 2017, the Company repurchased 1,919,967 shares under the program at an aggregate cost of \$24.8 million. The Company repurchased 1,485,195 shares at an aggregate cost of \$17.8 million during the three months ended April 29, 2017 and an additional 434,772 shares at an aggregate cost of \$7.0 million during the three months ended October 28, 2017. As of November 3, 2018, the Company had remaining authority under the program to purchase \$374.6 million of its common stock.

Borrowings and Capital Lease Obligations

See “Part I, Item 1. Financial Statements — Note 9 — Borrowings and Capital Lease Obligations” in this Form 10-Q for disclosures about our borrowings and capital lease obligations.

Supplemental Executive Retirement Plan

On August 23, 2005, the Board of Directors of the Company adopted a Supplemental Executive Retirement Plan (“SERP”) which became effective January 1, 2006. The SERP provides select employees who satisfy certain eligibility requirements with certain benefits upon retirement, termination of employment, death, disability or a change in control of the Company, in certain prescribed circumstances.

As a non-qualified pension plan, no dedicated funding of the SERP is required; however, the Company has made periodic payments into insurance policies held in a rabbi trust to fund the expected obligations arising under the non-qualified SERP. The amount of any future payments into the insurance policies, if any, may vary depending on investment performance of the trust. The cash surrender values of the insurance policies were \$61.6 million and \$64.5 million as of November 3, 2018 and February 3, 2018, respectively, and were included in other assets in the Company’s condensed consolidated balance sheets. As a result of changes in the value of the insurance policy investments, the Company recorded unrealized loss of \$2.3 million and \$1.6 million in other expense during the three and nine months ended November 3, 2018, respectively, and unrealized gains of \$1.6 million and \$5.5 million in other income during the three and nine months ended October 28, 2017, respectively. The projected benefit obligation was \$54.9 million and \$54.8 million as of November 3, 2018 and February 3, 2018, respectively, and was included in accrued expenses and other long-term liabilities in the Company’s condensed consolidated balance sheets depending on the expected timing of payments. SERP benefit payments of \$0.4 million and \$1.3 million were made during the three and nine months ended November 3, 2018, respectively. SERP benefit payments of \$0.4 million and \$1.3 million were made during the three and nine months ended October 28, 2017, respectively.

Inflation

The Company does not believe that inflation trends in the U.S. and internationally over the last three years have had a significant effect on net revenue or profitability.

Wholesale Backlog

We generally receive orders for fashion apparel three to six months prior to the time the products are delivered to our customers’ stores. The backlog of wholesale orders at any given time is affected by various factors, including seasonality, cancellations, the scheduling of market weeks, the timing of the receipt of orders and the timing of the shipment of orders and may include orders for multiple seasons. Accordingly, a comparison of backlogs of wholesale orders from period-to-period is not necessarily meaningful and may not be indicative of eventual actual shipments.

U.S. and Canada Backlog. Our U.S. and Canadian wholesale backlog as of December 3, 2018, consisting primarily of orders for fashion apparel, was \$50.4 million in constant currency, compared to \$36.9 million at December 4, 2017.

Table of Contents

Europe Backlog. As of December 2, 2018, the European wholesale backlog was €247.0 million, compared to €224.8 million at December 3, 2017. The backlog as of December 2, 2018 is comprised of sales orders for the Fall/Winter 2018, Spring/Summer 2019 and Fall/Winter 2019 seasons.

Application of Critical Accounting Policies

Our critical accounting policies reflecting our estimates and judgments are described in “Part II, Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” in our Annual Report on Form 10-K for the year ended February 3, 2018 filed with the SEC on March 29, 2018. There have been no significant changes to our critical accounting policies during the nine months ended November 3, 2018.

Recently Issued Accounting Guidance

See “Part I, Item 1. Financial Statements — Note 1 — Basis of Presentation and New Accounting Guidance” in this Form 10-Q for disclosures about recently issued accounting guidance.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk.

Exchange Rate Risk

More than half of product sales and licensing revenue recorded for the nine months ended November 3, 2018 were denominated in currencies other than the U.S. dollar. The Company’s primary exchange rate risk relates to operations in Europe, Canada, South Korea, China and Mexico. Changes in currencies affect our earnings in various ways. For further discussion on currency-related risk, please refer to our risk factors under “Part I, Item 1A. Risk Factors” contained in the Company’s most recent Annual Report on Form 10-K for the fiscal year ended February 3, 2018.

Foreign Currency Translation Adjustment

The local selling currency is typically the functional currency for all of the Company’s significant international operations. In accordance with authoritative guidance, assets and liabilities of the Company’s foreign operations are translated from foreign currencies into U.S. dollars at period-end rates, while income and expenses are translated at the weighted average exchange rates for the period. The related translation adjustments are reflected as a foreign currency translation adjustment in accumulated other comprehensive income (loss) within stockholders’ equity. In addition, the Company records foreign currency translation adjustments related to its noncontrolling interests within stockholders’ equity. Accordingly, our reported other comprehensive income (loss) could be unfavorably impacted if the U.S. dollar strengthens, particularly against the British pound, Canadian dollar, Chinese yuan, euro, Japanese yen, Korean won, Mexican peso, Russian rouble and Turkish lira. Alternatively, if the U.S. dollar weakens relative to those currencies, our reported other comprehensive income (loss) could be favorably impacted. Our foreign currency translation adjustments recorded in other comprehensive income (loss) are significantly impacted by net assets denominated in euros.

Periodically, the Company may also use foreign exchange currency contracts to hedge the translation and economic exposures related to its net investments in certain of its international subsidiaries (see below). Changes in the fair values of these foreign exchange currency contracts, designated as net investment hedges, are recorded in foreign currency translation adjustment as a component of accumulated other comprehensive income (loss) within stockholders’ equity.

During the nine months ended November 3, 2018, the total foreign currency translation adjustment decreased stockholders’ equity by \$59.3 million, driven primarily by the weakening of the U.S. dollar against the euro.

Foreign Currency Transaction Gains and Losses

Transaction gains and losses that arise from exchange rate fluctuations on transactions denominated in a currency other than the functional currency, including gains and losses on foreign exchange currency contracts (see below), are included in the condensed consolidated statements of loss. Net foreign currency transaction losses included in the determination of net loss were \$8.7 million and \$1.6 million for the nine months ended November 3, 2018 and October 28, 2017, respectively.

Table of Contents**Foreign Exchange Currency Contracts**

The Company operates in foreign countries, which exposes it to market risk associated with foreign currency exchange rate fluctuations. Various transactions that occur primarily in Europe, Canada, South Korea, China and Mexico are denominated in U.S. dollars, British pounds and Russian roubles and thus are exposed to earnings risk as a result of exchange rate fluctuations when converted to their functional currencies. These types of transactions include U.S. dollar denominated purchases of merchandise and U.S. dollar and British pound denominated intercompany liabilities. In addition, certain operating expenses, tax liabilities and pension-related liabilities are denominated in Swiss francs and are exposed to earnings risk as a result of exchange rate fluctuations when converted to the functional currency. The Company is also subject to certain translation and economic exposures related to its net investment in certain of its international subsidiaries. The Company enters into derivative financial instruments to offset some, but not all, of its exchange risk. In addition, some of the derivative contracts in place will create volatility during the fiscal year as they are marked-to-market according to the accounting rules and may result in revaluation gains or losses in different periods from when the currency impact on the underlying transactions are realized.

Foreign Exchange Currency Contracts Designated as Cash Flow Hedges

During the nine months ended November 3, 2018, the Company purchased U.S. dollar forward contracts in Europe totaling US\$39.3 million that were designated as cash flow hedges. As of November 3, 2018, the Company had forward contracts outstanding for its European and Canadian operations of US\$93.7 million and US\$8.8 million, respectively, to hedge forecasted merchandise purchases, which are expected to mature over the next 10 months. The Company's foreign exchange currency contracts are recorded in its condensed consolidated balance sheet at fair value based on quoted market rates. Changes in the fair value of the U.S. dollar forward contracts, designated as cash flow hedges for forecasted merchandise purchases, are recorded as a component of accumulated other comprehensive income (loss) within stockholders' equity and are recognized in cost of product sales in the period that approximates the time the hedged merchandise inventory is sold. Changes in the fair value of the U.S. dollar forward contracts, designated as cash flow hedges for forecasted intercompany royalties, are recorded as a component of accumulated other comprehensive income (loss) within stockholders' equity and are recognized in other income (expense) in the period in which the royalty expense is incurred.

As of November 3, 2018, accumulated other comprehensive income (loss) related to foreign exchange currency contracts included a net unrealized gain of approximately \$1.6 million, net of tax, which \$0.8 million will be recognized in cost of product sales over the following 12 months, at the then current values on a pre-tax basis, which can be different than the current quarter-end values.

As of November 3, 2018, the net unrealized gain of the remaining open forward contracts recorded in the Company's condensed consolidated balance sheet was approximately \$5.2 million.

At February 3, 2018, the Company had forward contracts outstanding for its European and Canadian operations of US\$145.8 million and US\$38.7 million, respectively, that were designated as cash flow hedges. At February 3, 2018, the net unrealized loss of these open forward contracts recorded in the Company's condensed consolidated balance sheet was approximately \$13.7 million.

Foreign Exchange Currency Contracts Not Designated as Hedging Instruments

The Company also has foreign exchange currency contracts that are not designated as hedging instruments for accounting purposes. Changes in fair value of foreign exchange currency contracts not designated as hedging instruments are reported in net earnings (loss) as part of other income (expense). For the nine months ended November 3, 2018, the Company recorded a net gain of \$6.7 million for its euro and Canadian dollar foreign exchange currency contracts not designated as hedges, which has been included in other income. As of November 3, 2018, the Company had euro foreign exchange currency contracts to purchase US\$28.0 million expected to mature over the next 6 months and Canadian dollar foreign exchange currency contracts to purchase US\$1.8 million expected to mature over the next 2 months. As of November 3, 2018, the net unrealized gain of these open forward contracts recorded in the Company's condensed consolidated balance sheet was approximately \$2.3 million.

Table of Contents

At February 3, 2018, the Company had euro foreign exchange currency contracts to purchase US\$68.2 million and Canadian dollar foreign exchange currency contracts to purchase US\$17.6 million. At February 3, 2018, the net unrealized loss of these open forward contracts recorded in the Company's condensed consolidated balance sheet was approximately \$4.3 million.

Sensitivity Analysis

As of November 3, 2018, a sensitivity analysis of changes in foreign currencies when measured against the U.S. dollar indicates that, if the U.S. dollar had uniformly weakened by 10% against all of the U.S. dollar denominated foreign exchange derivatives totaling US\$132.3 million, the fair value of the instruments would have decreased by \$14.7 million. Conversely, if the U.S. dollar uniformly strengthened by 10% against all of the U.S. dollar denominated foreign exchange derivatives, the fair value of these instruments would have increased by \$12.0 million. Any resulting changes in the fair value of the hedged instruments may be partially offset by changes in the fair value of certain balance sheet positions (primarily U.S. dollar denominated liabilities in our foreign operations) impacted by the change in the foreign currency rate. The ability to reduce the exposure of currencies on earnings depends on the magnitude of the derivatives compared to the balance sheet positions during each reporting cycle.

Interest Rate Risk

The Company is exposed to interest rate risk on its floating-rate debt. The Company has entered into interest rate swap agreements to effectively convert its floating-rate debt to a fixed-rate basis. The principal objective of these contracts is to eliminate or reduce the variability of the cash flows in interest payments associated with the Company's floating-rate debt, thus reducing the impact of interest rate changes on future interest payment cash flows. The Company has elected to apply the hedge accounting rules in accordance with authoritative guidance for certain of these contracts.

Interest Rate Swap Agreement Designated as Cash Flow Hedge

During fiscal 2017, the Company entered into an interest rate swap agreement with a notional amount of \$21.5 million, designated as a cash flow hedge, to hedge the variability of cash flows in interest payments associated with the Company's floating-rate debt. This interest rate swap agreement matures in January 2026 and converts the nature of the Company's real estate secured term loan from LIBOR floating-rate debt to fixed-rate debt, resulting in a swap fixed rate of approximately 3.06%. The fair value of the interest rate swap agreement is based upon inputs corroborated by observable market data. Changes in the fair value of the interest rate swap agreement, designated as a cash flow hedge to hedge the variability of cash flows in interest payments associated with the Company's floating-rate debt, are recorded as a component of accumulated other comprehensive income (loss) within stockholders' equity and are amortized to interest expense over the term of the related debt.

As of November 3, 2018, accumulated other comprehensive income related to the interest rate swap agreement included a net unrealized gain of approximately \$1.3 million, net of tax, which will be recognized in interest expense after the following 12 months, at the then current values on a pre-tax basis, which can be different than the current quarter-end values. As of November 3, 2018 and February 3, 2018, the net unrealized gain of the interest rate swap recorded in the Company's condensed consolidated balance sheet was approximately \$1.7 million and \$1.5 million, respectively.

Sensitivity Analysis

As of November 3, 2018, approximately 93% of the Company's total indebtedness related to a real estate secured term loan and capital lease obligations. The real estate secured term loan is covered by a separate interest rate swap agreement with a swap fixed interest rate of approximately 3.06% that matures in January 2026. The interest rate swap agreement is designated as a cash flow hedge and converts the nature of the Company's real estate secured term loan from LIBOR floating-rate debt to fixed-rate debt. The capital lease obligations are based on fixed interest rates derived from the respective agreements.

The Company's remaining indebtedness is at variable rates of interest. Accordingly, changes in interest rates would impact the Company's results of operations in future periods. A 100 basis point increase in interest rates

Table of Contents

would have had an insignificant effect on interest expense for the nine months ended November 3, 2018. The fair value of the Company's debt instruments is based on the amount of future cash flows associated with each instrument discounted using the Company's incremental borrowing rate. As of November 3, 2018 and February 3, 2018, the carrying value of all financial instruments was not materially different from fair value, as the interest rates on the Company's debt approximated rates currently available to the Company.

ITEM 4. Controls and Procedures.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the quarterly period covered by this report.

There was no change in our internal control over financial reporting during the third quarter of fiscal 2019 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings.

See "Part I, Item 1. Financial Statements — Note 12 — Commitments and Contingencies — Legal and Other Proceedings" in this Form 10-Q for disclosures about our legal and other proceedings.

ITEM 1A. Risk Factors.

There have not been any material changes from the Risk Factors as previously disclosed in our Annual Report on Form 10-K for the year ended February 3, 2018, filed with the SEC on March 29, 2018.

Table of Contents

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds.

Items (a) and (b) are not applicable.

Item (c). Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares That May Yet Be Purchased Under the Plans or Programs
August 5, 2018 to September 1, 2018				
Repurchase program ¹	—	—	—	\$ 374,636,677
Employee transactions ²	418	\$ 22.43	—	
September 2, 2018 to October 6, 2018				
Repurchase program ¹	—	—	—	\$ 374,636,677
Employee transactions ²	1,627	\$ 22.51	—	
October 7, 2018 to November 3, 2018				
Repurchase program ¹	—	—	—	\$ 374,636,677
Employee transactions ²	246	\$ 21.24	—	
Total				
Repurchase program ¹	—	—	—	
Employee transactions ²	2,291	\$ 22.36	—	

Notes:

On June 26, 2012, the Company's Board of Directors authorized a program to repurchase, from time-to-time and as market and business conditions warrant, up to \$500 million of the Company's common stock. Repurchases under the ¹ program may be made on the open market or in privately negotiated transactions, pursuant to Rule 10b5-1 trading plans or other available means. There is no minimum or maximum number of shares to be repurchased under the program, which may be discontinued at any time, without prior notice.

² Consists of shares surrendered to, or withheld by, the Company in satisfaction of employee tax withholding obligations that occur upon vesting of restricted stock awards/units granted under the Company's 2004 Equity Incentive Plan, as amended.

Table of Contents

ITEM 6. Exhibits.

Exhibit Number	Description
3.1.	<u>Restated Certificate of Incorporation of the Registrant (incorporated by reference from Amendment No. 3 to the Registrant's Registration Statement on Form S-1 (Registration No. 333-4419) filed July 30, 1996).</u>
3.2.	<u>Third Amended and Restated Bylaws of the Registrant (incorporated by reference from the Registrant's Annual Report on Form 10-K for the year ended February 3, 2018).</u>
4.1.	<u>Specimen Stock Certificate (incorporated by reference from Amendment No. 3 to the Registrant's Registration Statement on Form S-1 (Registration No. 333-4419) filed July 30, 1996).</u>
†31.1.	<u>Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>
†31.2.	<u>Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>
††32.1.	<u>Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u>
††32.2.	<u>Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u>
†101.INS	XBRL Instance Document
†101.SCHXBRL	Taxonomy Extension Schema Document
†101.CALXBRL	Taxonomy Extension Calculation Linkbase Document
†101.DEFXBRL	Taxonomy Extension Definition Linkbase Document
†101.LABXBRL	Taxonomy Extension Label Linkbase Document
†101.PREXBRL	Taxonomy Extension Presentation Linkbase Document

Filed herewith

Furnished herewith

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Guess?, Inc.

Date: December 7, 2018 By:/s/ VICTOR HERRERO

Victor Herrero
Chief Executive Officer

Date: December 7, 2018 By:/s/ SANDEEP REDDY

Sandeep Reddy
Chief Financial Officer
(Principal Financial Officer)