

30-Oct-2019

Crocs, Inc. (CROX)

Q3 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Crocs, Inc. Third Quarter At this time all participants are in a listen-only mode. After the speaker's presentation, there will be a question-and-answer session. [Operator Instructions] Please be advised that today's conference is being recorded. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Marisa Jacobs, Global Head of Investor Relations. Thank you. Please go ahead.

Marisa Jacobs

Global Head of Investor Relations, Crocs, Inc.

Good morning, everyone, and thank you for joining us today for the Crocs third quarter 2019 earnings call. Earlier this morning, we announced our latest quarterly results and the copy of the press release can be found on our website at crocs.com.

We would like to remind you that some of the information provided on this call is forward-looking and accordingly is subject to the Safe Harbor provisions of the federal securities laws. These statements include, but are not limited to, statements regarding future revenues, gross margins, SG&A as a percent of revenues, operating margins, CapEx and our product pipeline. Crocs is not obligated to update these forward-looking statements to reflect the impact of future events. We caution you that all forward-looking statements are subject to risks and uncertainties described in the Risk Factors section of our Annual Report on Form 10-K.

Accordingly, actual results could differ materially from those described on this call. Please refer to Crocs Annual Report on Form 10-K, as well as other documents filed with the SEC for more information relating to these risk factors. Adjusted gross margin, SG&A, operating margin and earnings per diluted common share are non-GAAP measures. A reconciliation of these amounts to their GAAP counterparts is found in the press release we issued earlier this morning.

Joining us on the call today are; Andrew Rees, President and Chief Executive Officer; and Anne Mehlman, Executive Vice President and Chief Financial Officer. Following the prepared remarks, we will open the call for your questions.

At this time, I'll turn the call over to Andrew.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

Thank you, Marisa and good morning everyone. I'm really pleased with our third quarter results. We delivered revenues of \$313 million, a new third quarter record for Crocs. This represents 20% growth or 21% on a constant currency basis. Our operating income grew 187% to \$39.9 million or 13% of revenues; and our EPS rose to \$0.51 compared to \$0.07 in last year's third quarter. Wholesale, e-com and retail comps all grew nicely with the Americas delivering exceptional growth driven by another successful back to school season.

Our brand continues to resonate strongly with consumers as a result of our impactful marketing and our iconic products. Given these stellar results, we're once again increasing our 2019 guidance with revenues now anticipated to grow 11% to 12%. We expect our 2019 revenues to be the highest annual revenues in the company's history. Looking ahead to next fiscal year, we expect growth to continue to accelerate with 2020 revenues growing between 12% and 14%.

Focusing first on our brand; we have exciting new data to share. Earlier this month Piper Jaffray released the results of its fall 2019 Taking Stock with Teens Survey. We advanced in the all teen preferred footwear rankings to the number 7 spot up from number 13 last year and number 27 two years ago.

Results are also in from our own brand survey measuring participants' views about the Crocs brand. Our 2019 results were up double digits for each of our key metrics, brand desirability, brand relevance and brand consideration. We have now averaged double-digit growth across these same metrics over the past three years.

Since our last call we've continued to roll out exciting new marketing content and collaborations. We've done additional drops with Chinatown Market, Vivienne Tam and BEAMS along with a first time collaboration with Ruby Rose the newest Batwoman. We also launched our Crocs account on TikTok, a popular video sharing app. This included our #ThousandDollarCrocs challenge which had over 1.5 billion views in just the first two weeks.

It's also worth noting at Crocs, we don't recognize October it's all about Croctober. We organized celebrations throughout the month and on October 23, which is Croc Day, we dropped our latest shoe design for the occasion, it was Lit and our fans loved it.

There's much more to come. We have an amazing slate of brand ambassadors lined up for our fourth year of our Come As You Are campaign. We are excited to announce that we will be joined by award winning actor, activist and entrepreneur, Priyanka Chopra Jonas. Zoey Deschanel, Kim Sejeong and Suzu Hirose will return for 2020.

In addition to Priyanka's role as a brand ambassador, we're collaborating together on a series of donations through UNICEF to aid children around the world.

Next year we'll unveil the final edition to our 2020 lineup of brand ambassadors to address our China market. We'll also roll out another full slate of collaborations that expand the reach of our partnerships in fun and surprising ways. I'm confident our consumers will love our new offerings.

Returning to the present, our success has been driven by disciplined execution against our strategic priorities: growing revenues by prioritizing clogs, sandals, visible comfort technology and personalization. In our Fall/Holiday collection, we refreshed our core clog assortment with seasonally appropriate colors and prints and of course, layered in great offerings of lined clogs, which are perfect for cooler weather. We also introduced LiteRide for kids and rolled out new Jibbitz to keep our selection fresh. Our consumers responded with enthusiasm.

During Q3 clog revenues grew approximately 36% and made up 63% of our footwear sales, up from 55% during last year's third quarter. We increased clog sales in every region with exceptional growth in North America.

Clogs are obviously more in demand than sandals in the back half of the year. But that didn't prevent us from growing our sandal sales by 9% over last year's third quarter. Sandal revenues generated 19% of our footwear revenues, it's our 11th consecutive quarter of sandal revenue growth as we continue to increase global awareness of Crocs sandals.

With respect to visible comfort technology in Q3 we expanded our LiteRide franchise to incorporate kid's sizes and the response was very strong.

Jibbitz Charms, our unique offering for personalizing our footwear continue to grow at an accelerated pace. We're updating the assortment regularly to provide consumers with fresh offerings. We've also added a new personalization tool to our website that enables consumers to visualize their chosen Jibbitz on a clog and quickly move them into the checkout basket. Over the past few months, several wholesale accounts successfully tested Jibbitz in key locations and by year-end, they will be available in many more doors. Additional accounts will also introduce Jibbitz into their line-up in 2020.

Let me now turn briefly to our sales channels. Third quarter wholesale revenues grew dramatically, up 25% following last year's 9% growth as our wholesale customers are increasing their buys to meet rising consumer demand.

Our DTC comp which combines our retail and e-com results was up 16%, and our 2-year stack was up 34%.

E-commerce grew 28% on top of 23% growth during last year's third quarter. This represents our 10th consecutive quarter of double digit e-commerce growth. Increasing brand heat continues to drive more traffic to our own sites plus we're seeing good traction on global marketplaces with revenues growing accordingly.

Retail comps were up 12%, our ninth consecutive quarter of positive comps. Our 2-year stack was up 27%. Total retail sales grew 9% even as we continue to absorb the impact of last year's store closures.

Throughout the year, we have been executing against our growth strategy. Product acceptance and brand heat are rising, hence we are driving sustainable profitable revenue growth and effectively leveraging our cost base. We're on an exciting journey and one that's just getting started. I'm very optimistic about the path that lies ahead.

The progress we are making is the result of a team effort. I work with an extraordinary group of talented and dedicated colleagues and I want to thank them for everything that they do.

At this time, I'll turn the call over to Anne, to review our third quarter results and guidance.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

Thank you, Andrew, and good morning everyone. Let me begin by providing a short recap of our third quarter 2019 performance. For a reconciliation of non-GAAP amounts mentioned to their equivalent GAAP amounts, please refer to our press release.

As you've already heard, we had a record setting third quarter, exceeding our revenue, gross margin and SG&A guidance and significantly improving our EPS.

Third quarter revenues came in at \$312.8 million compared to \$261.1 million in the third quarter of 2018, a 19.8% increase, or 21% on a constant currency basis. Currency negatively impacted our revenues by approximately \$3 million, while store closures reduced revenues by approximately \$4 million; absent which our sales would have been up 22%. This is our 10th consecutive quarter of organic sales growth and the 5th consecutive quarter of double-digit organic sales growth.

We sold just under 16 million pairs of shoes, an increase of 19.3% over last year's third quarter. Our average selling price for footwear during Q3 increased slightly to \$18.99, with the increase attributable to less discounting and higher prices on certain product, which more than offset the impact of changes in our channel mix and the negative impact of currency.

The Americas had another phenomenal quarter. Revenues were up 35.2% to \$185.2 million with minimal impact from currency. Growth was robust across every channel. Following terrific work to increase capacity in order to keep up with rapidly rising demand, our Classic Clog inventories have been restored to appropriate levels. Additionally, the relocation of our Americas distribution center from L.A. to Dayton is on track and the L.A. facility will be closed by year-end.

We're excited about the great benefits we anticipate receiving from our Dayton facility including higher throughput, greater efficiency and an improved customer experience. We're evaluating investments into more projects next year and beyond, that would support our anticipated growth.

In Asia, third quarter revenues were \$74.3 million, down 1.2% from last year's third quarter. On a constant currency basis, revenues rose slightly. E-commerce was up significantly due to growth across our own dotcoms and our expanding marketplace presence. Lower wholesale revenues mainly reflect the timing of revenues between quarters and ongoing efforts to reposition our business in China. Retail comps declined primarily due to a continuing unrest in Hong Kong and weakness in our Korean shop-in-shops.

EMEA revenues rose 12.3% over the last year's third quarter to \$53.3 million. On a constant currency basis, revenues grew 16.1%. Our business is benefiting from steadily growing brand heat and our continued focus on digital commerce. Our third quarter adjusted gross margin was 53.6%, well above our guidance of 51.5%. Our adjusted gross margin rose 30 basis points compared to last year's third quarter.

Various headwinds including channel mix, higher distribution costs and 130 basis point drag from reduced purchasing power relating to currency, we're more than that by a variety of tailwinds including lower promotions and higher clog sales in the Americas plus savings associated with exiting our own manufacturing last year.

Adjusted SG&A improved by 640 basis points to 39.4% of revenues versus 45.8% in last year's third quarter. On a GAAP basis, SG&A came in at 39.6% of revenues versus 47.9%. The work done in 2017 and 2018 to reduce cost is now enabling us to drive significant leverage from revenue growth even as we continue to invest more in marketing.

Operating margins rose 750 basis points to 12.8% while our adjusted operating margin, at 14.2%, almost doubled.

Q3 tax expense was dramatically lower than last year. Higher than anticipated U.S. profits enabled us to use tax benefits accumulated during prior years.

Our diluted earnings per share rose to \$0.51 compared to \$0.07 in the third quarter of 2018, reflecting very strong business performance and a tax benefit of approximately \$0.03 associated with the lower tax expense.

Our adjusted diluted earnings per share tripled coming in at \$0.57 compared to \$0.19 in last year's third quarter.

During Q3 we repurchased approximately 1 million shares of our common stock on the open market for \$25 million at an average share price of \$23.99. Year-to-date we've repurchased approximately 5.7 million shares of our common stock for approximately \$133 million at an average cost of \$23.47 per share. Approximately \$520 million remains available under our plan for future share repurchases.

Our balance sheet continues to be very strong. We ended the quarter with \$87.9 million in cash. Our outstanding borrowings at the end of the quarter were \$185 million, down from \$215 million at the end of Q2. Inventory at the end of the third quarter increased 18.8% to approximately \$140 million. And our turnover ratio was 4.5 turns per year.

I'm extremely pleased with our performance during Q3. We executed well on all fronts leading to significant top and bottom line growth. As we turn to guidance, I want to remind you that our guidance is based on current currency rates.

With respect to the fourth quarter, we expect revenues to be between \$245 million and \$255 million compared to \$216 million in last year's fourth quarter. Our guidance incorporates approximately \$2 million from negative currency impacts as well as another \$2 million reduction from revenues associated with our lower store count. At the midpoint of our guidance, this represents growth of approximately 16% or 18% on an organic basis.

Adjusted gross margin will be approximately 50%. We expect gains from increased pricing, higher clog sales and leveraging our fixed supply chain costs to more than offset a headwind of approximately 100 basis points associated with reduced purchasing power related to currency and changes in channel mix.

Our GAAP gross margin, which includes 100 basis points of non-recurring charges associated with our new distribution center will be approximately 49%.

SG&A is expected to be approximately 47% of revenues compared to 52.7% in last year's fourth quarter. We are continuing to leverage our cost base even as we invest more in marketing activities to drive future growth.

Our forecast calls for us to make a profit in Q4 for the first time in eight years. This speaks to the growing relevance of clogs which are clearly in demand year-round, as well as to the operational improvements we've put in place to successfully improve our bottom line.

For full year 2019, we have once again updated our guidance and laid out all the specifics in our press release. The highlights include, revenue growth between 11% and 12%, which would result in record high revenues; an adjusted gross margin of approximately 51%, SG&A of approximately 40% of revenues; an adjusted operating margin of approximately 11% meeting our near-term target of returning to a double-digit operating margin.

As Andrew noted, with respect to 2020, we currently expect revenues to grow between 12% and 14%. This estimate assumes currency will have a negative impact of approximately \$10 million in 2020.

We're anticipating a strong finish to the year with record revenues and a return to a double-digit operating margin. This sets us up nicely for another terrific year in 2020.

At this time, I'll turn the call back over to Andrew for his final thoughts.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

Thank you, Anne. With three quarters of the year behind us, we've seen great success from adhering to our focus on clogs, sandals, visible comfort technology and Jibbitz. Our great product offerings are being amplified by impactful marketing and operational improvements are enabling us to flow a greater percentage of our revenues to the bottom line. We've made tremendous progress over the past few years and have established a clear strategy that we are confident will result in continued revenue growth and increased profitability for years to come.

Operator, please open the call for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from Mitch Kummetz from Pivotal Research Group. Your line is open. Please go ahead.

Mitch Kummetz

Analyst, Pivotal Research Group LLC

Yes. Thanks for taking my questions and congratulations on the quarter. Andrew on the 2020 guide, I'm just curious how much visibility do you have at this point? I would imagine you've got in your spring order book, I don't know if you could speak to that. But then how are you thinking about that versus other drivers of revenue growth for next year?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

Yeah. Thank you, Mitch. So let me talk more broadly around the drivers of revenue growth the next year and then I'll come back to visibility. So as we look forward into next year, I think the vast majority of what's underpinning our guidance is our strategy is working, right. We can see it working this year, we can see it accelerating through the

year into next year and that's really backed by a lot of the things we talked about in our prepared remarks and have talked about consistently: our product focus on clogs, sandals, visible comfort technology and Jibbitz, we can see the growth of each of those product category is accelerating. Our marketing is clearly working both from a CAYA perspective, our ambassadors that we've used this year and we're really excited about next year and it's also our social and digital cadence and collaborations.

From a regional perspective, Americas has been incredibly strong this year. We see it being strong next year, but we also see very solid growth from both EMEA and Asia next year. And then from a channel perspective as you know, we focus very heavily on digital. We focus very heavily on our e-commerce, and e-commerce marketplaces, new marketplaces we've gone into. E-tailers are an important part of reaching our core consumer. And so we feel really good about our strategy and we see our strategy accelerating.

In terms of visibility, yes, so obviously we don't comment on our order book or give pre-book numbers. But we look at our Spring/Summer product line I would say it has been very well received as we've visited wholesale accounts in this country and around the globe. So we feel really good about the visibility we have and it underpins the guidance that we were able to provide.

Mitch Kummetz

Analyst, Pivotal Research Group LLC

Q

Okay. Great. And then Anne, you mentioned that you had 11% operating margin, you've achieved your intermediate term target of double-digit margin. I'm just wondering when you guys are going to give us a new intermediate term operating margin target. When you think about what may be the operating margin opportunities are long-term, is there anything that you can address today in terms of where that might go? Especially I think when I look at the SG&A, you talked about the 40% of sales this year, which is obviously a huge improvement over last year and the year before. But on the surface, that number still seems like it's a little high and maybe there's some room for opportunity there. How do you think about that?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah. Hi, Mitch. Thanks for the question. So from a long-term operating margin perspective, we wanted to give an early revenue preview. So, for our outlook for next year, we will come back out and when we do our Q4 call and give a full P&L results. What we've said previously is obviously to get to a double-digit operating margin, our gross margin would be in the low-50s and our SG&A would be in the low-40s. And we will achieve that this year and then next year, we'll give more visibility for 2020.

Mitch Kummetz

Analyst, Pivotal Research Group LLC

Q

Okay. All right. Thanks. Good luck.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Thank you.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Thank you.

Operator: Your next question comes from Erinn Murphy from Piper Jaffray. Your line is open. Please go ahead.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Great. Thanks. Good morning and congrats on a really strong quarter. I guess maybe Andrew first for you on the Americas wholesale businesses, that's incredibly strong in the quarter, almost 70%. Can you just walk through what you're seeing. Is that re-orders, is it new accounts you are going into? And you've mentioned with the Jibbitz business, you're starting to just test that within wholesale. Maybe share what you're seeing here in the North American market with that business?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. And we're absolutely thrilled with the performance in the Americas, so it's really a number of things. I would say through the – over the last 12 to 18 months, we have added accounts we've penetrated key accounts that we thought were important to our brand or reaching our core consumers. I think the biggest increase in terms of dollars was sell-through – with the increased placement, accelerated sell-through at our core accounts; that was really the biggest impact, combined with some addition of new accounts.

Jibbitz I think is important. We see it as very, very important in our DTC channels, where we can see it dramatically changing the emotional connectivity that the consumer has to our product, it really changes a generic purchase into a completely personal purchase, and they get an awful lot more excited about it. They tweet about it. They Instagram about it. So, it's a really important factor. We were able to land Jibbitz with a number of key, large wholesale accounts this quarter. I can say it tested very well. It will get rolled out in those chains and we'll add new chains next year.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Okay. That's helpful. And then maybe just going back to Asia, obviously that region is still collectively negative. Can you share a little bit more about what you're doing in China to reposition that market for growth? And then any insights on what – how Japan trended in the quarter just given the VAT increase as we rounded into October?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. Yeah, so maybe I'll comment on Asia generally, then pick up China and Japan. So in terms of Asia in general, I would say Asia it was flat for the quarter, but frankly met our expectations. That's what we were expecting it. And there were a few things going on. One was in the wholesale business, there are certainly some shifts from quarter-to-quarter and we're expecting a strong quarter from Asia next quarter, in the fourth quarter. And in the retail business, we were impacted by a couple of things.

One is frankly, the out of stock in our Korea shop-in-shops. But we've now resolved that, and so that was sort of faster sell-through than we anticipated. And then obviously we have a small number of stores in Hong Kong that were significantly impacted by everything that's going on there. E-commerce was very strong in Asia and we think that will continue to be strong. So it was where we expected it, but we do see a stronger quarter from Asia in next quarter. And obviously as we talked about earlier in terms of 2020, we see Asia producing a solid growth.

China, we talked I think last quarter about the board committee that we've put in place and the strategic plans we've put in place to reignite the growth in that country. I would say those are all tracking to plan and we feel really good about those. And as we think about the future of China definitely returning to growth next year, but the major acceleration in China is probably in 2021. And Japan I think we had solid performance in Japan. And I don't think there's anything really significant to comment on there.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Okay. And then just a question for Anne as I round out. Two things Anne, one on just the 2020 algorithm, obviously you've referenced and Andrew kind of gave some of the drivers for the 2020 revenue acceleration, but just based on that, is there any reason why you wouldn't see SG&A leverage at least similar to the level you saw this year or are there reinvestments I'm not thinking about that we just need to be mindful of resetting our model for the next year? And then just a housekeeping question Anne on the tax rate for fourth quarter? Thanks

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah. Hi, Erinn, good morning. So I'll actually start with the tax rate for the fourth quarter. So we expect our tax rate for the full year to be 12%. So you can back into the fourth quarter of what that tax rate is. So our tax rate for Q3 was 6.4% and that'll take us to an overall tax rate of 12% and that's how we think about our underlying tax rate for this year.

And then, to answer your second question, as far as the mechanics for next year, again, we wanted to give an early revenue preview and we will provide more color on the call in Q4, the Q4 call. One thing I would say just around gross margins, the pieces we have given as you think through the P&L, is that we will have, as we've talked about previously, 100 basis points of improvement all other things being neutral, from our Americas DC, that went live this quarter. And then we'll also – and then on the other side of that we'll continue to experience at these level of currency rates, we will continue to experience headwinds that we've had all year.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Got it. Thank you guys and Happy Croctober.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Thank you.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Thank you.

Operator: Your next question comes from Steve Marotta from C.L. King & Associates. Your line is open. Please go ahead.

Steven L. Marotta

Analyst, C.L. King & Associates, Inc.

Q

Good morning Andrew, Anne and Marisa. I want to just follow-up on the first question that was asked regarding the order book and I know that you don't give specifics on that, but could you tell me – tell us how much of that Spring/Summer order book is currently complete? In other words, if it's just 10% or if it's 90% or when will it be complete? And you would have that clearer outlook of what wholesale sales will grow in the first half of next year?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. I mean, I don't really want to get into too much stats, but if you just on the on the cadence of our business I would say the spring order book is probably – certainly north of 50% complete, probably close to 70% in that range.

Steven L. Marotta

Analyst, C.L. King & Associates, Inc.

Q

That's very helpful. And as far as the shifts you mentioned that there were some wholesale shifts in Asia towards the fourth quarter from the third quarter. Was there anything else material that would be impacting fourth quarter sales, are there other early deliveries that are expected anything like that?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

No, nothing as a material, Steve. As you know in some of our warm weather regions, so in Southeast Asia and places like that, we do deliver some of our Spring/Summer 20 product in the fourth quarter. As you'd expect, I would say the proportion and the cadence of that is entirely consistent with prior years.

Operator: Our next question comes from Jonathan Komp from Baird. Your line is open. Please go ahead.

Jonathan Robert Komp

Analyst, Robert W. Baird & Co., Inc.

Q

Yeah. Hi. Thank you. Andrew, I wanted to ask a bigger picture question on the strength you're seeing for the brand and clearly step up again in the second half and into 2020 in a number of different areas when you look at the reported metrics. So I'm just curious as you look at the strength today from a big picture standpoint, maybe any new thoughts about what's driving the broader trend? Anything new or any new elements that you've seen? And then maybe just more specifically on some of the efforts that you're taking to sustain the duration as you look forward.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. I wouldn't say there are a lot of new elements. I think the one I'll talk about a little bit is personalization, but I would say I think it's the combination. So it's a combination of very strong clog growth and re-igniting that, that core silhouette which is at the heart of our brand and resonates with a lot of consumers. And I would say it resonates with a newer younger consumer that's highlighted in the Teens Survey that we that we'd pointed to, but it also is incrementally resonating with our tried-and-tested core consumer. So we're seeing traction across the consumer platform which allows, I think the rate of acceleration we're seeing in clogs. On top of that, we continue to develop our sandal channel franchise with again strong growth in that and we're really excited about the sandal proposition that we're bringing to the market for 2020. I think you've got some really great products that are being well-received.

LiteRide as we've talked about, it's visible comfort technology in its second year in 2019, I think we also talked about those, we've talked about before but that has essentially doubled over the prior year. So that visible comfort technology is certainly resonating with consumers. And then personalization, so Jibbitz Charms have taken a big step forward in the Americas this year and we think the impact on the clog business has been very meaningful. As you all know, that is also quite a profitable business and we see that trend as a global trend. We see that desire for consumers to personalize as a key global megatrend and we are optimistic about the expansion of Jibbitz around the world. So I think each of the franchises is really, really working, that's really accelerating the brand. So, that's – I think that's really important.

Jonathan Robert Komp

Analyst, Robert W. Baird & Co., Inc.

Q

Great. And then presumably the strength you've seen in the order book is based on everything you mentioned plus really the backward-looking strength. But any of the new elements whether it's kind of the new social channels like TikTok or the new global brand ambassadors that you're looking forward to as you know potentially driving another leg going forward in terms of...

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yes.

Jonathan Robert Komp

Analyst, Robert W. Baird & Co., Inc.

Q

...brand awareness and brand heat?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. Look I think our social team and our social strategy are incredible. We did highlight in our prepared remarks the TikTok launch just earlier this month. And the incredible amount of views we had on the #ThousandDollarCrocs competition, so that was a huge amount of consumer engagement.

Our ambassadors next year I think are generally a step up over this year, I think we're really enthusiastic. I think Priyanka in particular is a global megastar. She resonates very strongly in the US and in Europe and frankly, also in Asia. So we think she is really – we are very excited to be partnering with her and also excited to be doing some of the work we're doing with her outside of just representing our brand in terms of the donations that we'll do with UNICEF. And we have one more significant ambassador that we will talk about next year that will be really key in China. So I think that's a very important part of our program, but it all works together. I would say all of these components are integrated and work together and I wouldn't like to break out and separate any one, it's the combination that is having the impact.

Jonathan Robert Komp

Analyst, Robert W. Baird & Co., Inc.

Q

Okay, great. And then maybe just last one for 2020, understanding you are not putting out an operating margin target yet, but I just wanted to follow-up and ask about the pricing to product cost outlook including the current view on tariffs and the price hike you took on a Classic Clogs and that will continue to flow through the channels, so any comments kind of broadly on those two pieces and what you see today?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah, sure. So, I think to close out the tariff commentary, at this point in time, it's not material for this year and it's really not material for next year either. What we see is that less than 10% of our products that are US products, will be sourced from China. So, we don't foresee at this level that tariffs will have an impact on our business, so that should be able to clear that up. I think overall just thinking through our dynamics of next year, we're really excited about our revenue growth and we will, as we get closer to next year, obviously provide a full P&L guidance similar to what we've provided in years past.

Jonathan Robert Komp

Analyst, Robert W. Baird & Co., Inc.

Q

Okay. Understood. All right. Thank you.

Operator: Your next question comes from Sam Poser from Susquehanna. Your line is open. Please go ahead.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

Good morning. Thank you for taking my questions. I have a couple, just some housekeeping and then in some other stuff. Can you tell us what's the normalized tax rate, how we should think about the normalized tax rate on an annual basis?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah. Hi, Sam. So the way I would think about normalized tax rate for this year is 12%.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

No, I understand. But I mean like just longer term, you had this – you had the – you had some savings in Q3 which is non-recurring. So if we think about it, it's like 15% to 16% annually, is that a good number to use?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

We haven't come out with longer term tax rate. I would say that as we produce more profits in the US, we've been able to use previously accumulated tax benefits, so I wouldn't consider those to be one-time in nature, and that's why we're seeing our underlying tax rate this year came from down from 15% to 12%. And we'll obviously – we will give a tax rate guide when we guide full year for next year.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

Okay. And then – thank you. And then within the guidance you've provided on revenue both for the fourth quarter and next year, just in the general picture of things, how should we think about revenue by geography or by channel and geography? I mean how are you thinking about where this momentum is going to come from, where do you see the biggest growth so and so forth?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah, then maybe – I think the way to think about it Sam is and as we've talked about, we think Americans will continue to grow very strongly, right. So that's obviously been a big driver this year and we see that continue into next year. And EMEA has also done well this year and we also see that continue into next year. So maybe the difference is we see Asia strengthening into next year from a regional perspective.

From a channel perspective, it's what we've talked about over a long period of time which is number one digital, right. That digital is going to be our fastest growth environment both on our own sites, both on the marketplaces that we've penetrated and also through e-tailers which gets booked in our wholesale number. Number two brick-and-mortar and I would say the rest of wholesale. We have seen strong growth in brick-and-mortar in Americas and also in EMEA, and distributors continue to be solid contributors to growth. So I would say the profile and the variance between the different components is broadly similar into 2020 with the addition of Asia strengthening.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

So just to clarify the momentum in wholesale generally should continue nicely into at least the first half of next year, because then you come in with the big compares out of the US or the Americas. And then – and then digital just – e-commerce revenue just increased – you're expecting e-commerce revenue to accelerate next year over this year? Is that a fair statement as far as the growth? Or is this ...

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

I wouldn't say accelerated. I think it's grown extremely...

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

...it's growing fast.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. It's growing very strongly this year. I think I'm not – we're not guiding to an acceleration of digital commerce, but it's growing extremely well this year.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

Okay. Got you. And then, can you talk about some of the collaborations that you've done this year? I just noticed a couple of other ones came out. Can you talk about, if you want to be specific, love it, but I doubt you will, are you going to scale up some of them as part of your plans? Because a lot of them have been, I think probably, your brand that was probably the largest.

[indiscernible] (00:40:29)

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. So, as you indicated, we don't give specifics. A couple of things I would say, Sam. So, we have a number – at least two very significant collaborations planned for the remainder of this year. So we're really excited about those, so we've got two additional big collaborations for this year. I would say the calendar and the cadence of collaborations is basically full for next year. Right. So, we're working with – and I would say it's a very broad variety of individuals, influencers, brands that we really feel very good about the variety; and the impact that we'll have next year.

Some of the quantity and the size of the collaborations have certainly increased, one thing that I could tell you is our Croc Day shoe that we did on October 23rd, which I don't know whether you saw it, was a Classic, but fully loaded with Jibbitz and also glowed in the dark, so we were really thrilled by that. Great item for Halloween. That was – that sold six times the number of units than our Croc Day shoe sold last year. So...

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

And did it sell out?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

It sold, it achieved everything that we hoped it was going to achieve, so it sold six times the number of units, so we're really thrilled with its performance.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

I think I got it. Thank you very much and continue the success.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Okay.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Thank you.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Thanks, Sam.

Operator: Your next question comes from Jim Duffy from Stifel. Your line is open. Please go ahead.

James Vincent Duffy

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Thanks. Good morning. Congratulations to you all on the momentum in the business. Two questions from me, just trying to better understand some of the drivers. I believe you guys said clogs were 63% of revenue in the quarter. I'm curious how much variance there is in that number by region?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah. So I think we've definitely seen the strongest clog growth in the Americas region. We've seen clog growth overall, but particularly in the Americas region.

James Vincent Duffy

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. And then Andrew, you'd mentioned some commentary about strength with younger consumers, but also with your core set, do you have any data on the demographic mix of purchase volume, particularly in the Americas where the gross spend is so strong?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah. We don't break out sales by cohort, but I can say as we look at our brand study, so we do a very comprehensive brand study every year that looks at across our five major markets, it looks at changes in brand relevance, consideration, desirability with different cohorts. We can see those key metrics which we think are drivers of our underlying business, that we know are drivers of our underlying business. We can see those metrics accelerate double-digit rates with teens or with younger consumers, but we can also see them accelerate at pretty much similar rates with our core all of the consumers. So maybe a suburban mom.

And so we can see these changes across the board. So I think the new consumer that's come strongly into the brand over the last 12 months is that younger consumer. But it's really important to us that we see a balanced acceleration across the overall consumer set, because I think that drives underlying strength in the brand. And we think the younger consumer is really important because they influence a lot of people, right. If you look at the average household there, brothers and sisters are influenced by that consumer. Parents are influenced by that consumer and it's a very important pivot point for brands to attract that consumer, retain them and have them be a real vehicle for acceleration.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah, and Jim also just to add a little bit on to that because we haven't really talked about this, but EMEA is actually – really pleased with their results, they're up 16% year-to-date on a constant currency basis. So we talk a lot about the US and the back-to-school business, but EMEA gets a little bit overlooked because of the currency piece. If you look at the underlying growth, it's very strong and it's a different demographic than we're seeing driving some of the growth in the US. So it's very balanced growth.

James Vincent Duffy

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay interesting. My next question I want to ask about pricing strategy. Can you give us an update there? Is there more room for pricing in North America, do you have any expectations for pricing actions in other regions? And I guess, as long as we're on that topic, what are – what's kind of contemplated in that 2020 view that you guys provided as it relates to pricing?

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

So, in terms of pricing, I think, yeah, we've taken some price action on clog Classic through the back end of this year in North America. I would also say that we've adjusted pricing in many other parts of the world in EMEA and in key Asian countries as well as we've gone through the year. As we look forward, we'll decide pricing on a style by style, region by region basis; and I really have two key guide points. One, we want to continue to make sure we're giving incredible value to our consumers, which we, even at these increased price levels, the consumer is essentially telling us, we've given them great value, as well as making sure that we capture the right value for the brand and for our shareholders.

So, we have those two – and obviously they are in competition. So, we have those two guideposts in mind and we will continue to adjust on a region by region, style by style basis as we look forward and as we see opportunities both up and down, frankly, to make sure that we're positioned in the way that we want to be positioned. And I would say absolutely the adjustments that we've made and the impact we think those adjustments will have are embedded in the indications we've given for growth in 2020.

James Vincent Duffy

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Great. And last one from me is just on that 2020 view, a lot of companies have a hard time guiding a single quarter ahead. Why did you guys think it important to go out with the 2020 view this morning here in October?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Jim so we've provided a revenue preview the last two years, so this will be our third consecutive year of providing a revenue preview. So we're just being consistent with our prior practices and we want to give as much as visibility as we have and we feel comfortable providing.

James Vincent Duffy

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Understood. Thanks so much.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Thank you.

Operator: Your next question comes from Erinn Murphy from Piper Jaffray. Your line is open. Please go ahead.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Great. Hey, guys. Just a couple of follow-ups from me. Just going back to the price increases that Duffy was talking about. You've taken the Classic to \$44.99 here in the North American market. Any feedback from consumers thus far on that? Have they even noticed that it's increased? And then how does this rollout into wholesale as we go into spring 2020? Are the wholesale order books that you're referencing that you have good visibility in, are they at the \$44.99 or just maybe help us think about the mechanics there?

And then just my second follow-up is back on the Jibbitz business. Is it really predominantly teens that are buying Jibbitz from a personalization perspective or are there examples that you see in your business where you're seeing a kind of broader demographic adopting that? Thank you.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

All right, Erinn a lot of questions there. So in terms of consumer acceptance of the price increase, we think that's gone well. We're pleased with how that's gone both on e-com, in-store and with wholesalers. So I think we feel pretty confident about that. In terms of how that rolls into next year, so selling for Spring/Summer 2020 is at the new prices or at the wholesale price consistent with our adjusted MSRP. And if you look in the marketplace there are some wholesale customers they've already taken price to that new price.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Okay.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Right. So they haven't all done that, but some have done that for sure. And then the third piece around Jibbitz, yeah, I would say the strong acceleration is with that younger consumer. Yeah, that teen customer that is looking to – as you know Jibbitz has already been – historically has been very kid focused and that continues. But the big acceleration has been more with a teen customer. I would say that continues to be some traction with the elder customer, but Jibbitz I is definitely younger in terms of its demographic.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Got it. Thank you, guys.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Thank you.

Operator: Your next question comes from Jim Chartier from Monness, Crespi, Hardt. Your line is open. Please go ahead.

Jim A. Chartier

Analyst, Monness, Crespi, Hardt & Co., Inc.

Q

Good morning. Thanks for taking my question and nice quarter. You guys have talked about exporting the brand heat from the US overseas. I'm just curious Asia e-commerce at 55%, what are you seeing within that that gives you confidence that the strategies are working. And then Korea shop-in-shops, I think, you mentioned were out of stock. Is Korea the furthest along in terms of building brand heat within Asia? Thanks.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

A

Yeah, so I think we're definitely seeing brand heat spreading around the world, in fact more than seeing – well, obviously that's a key part of what we're trying to do, right. I think you can see that in Europe. I think Anne highlighted 16% constant currency growth year-to-date in Europe. So certainly some of that is brand heat orientated. One of the metrics that we do look at as a real guidepost of brand heat is natural search to our e-commerce site. So not the paid search, but the natural search and the growth in that and we can see natural search growing really across the globe on our own sites.

I would say the very significant acceleration in Asia e-commerce is probably less a reflection, we certainly do see brand heat coming in to Asia. But there was lot of blocking and tackling on operational components that we improved or we have been improving through the year in Asia that I think came to fruition in third quarter. So I think there is underlying growth in Asia plus we fixed some things that were not working very well and they've had a big impact in terms of e-commerce.

In terms of places where the brand heat would be most visible in Asia, absolutely I think Korea is important, but Japan is also important. Those countries do tend to lead in terms of leveraging maybe Western or US trends and understanding what those trends are and then accepting and accelerating those trends.

Jim A. Chartier

Analyst, Monness, Crespi, Hardt & Co., Inc.

Great. And so...

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

Yeah, I think one other piece to add in Asia from an e-commerce standpoint is we had – we have now 13 marketplaces globally. A lot of those are in Asia and we've done a lot of expansion there and we feel really good about that and you can see that in the difference between the comp growth in Asia and the year-over-year growth in Asia in e-commerce. So we're really excited about that momentum. It's still early days, but it's been really great.

Jim A. Chartier

Analyst, Monness, Crespi, Hardt & Co., Inc.

And so, it looks like you start to lap easy e-commerce comparisons in Asia in the next three quarters and is it reasonable to expect 50% e-commerce growth in Asia as the blocking and tackling continues to drive the business?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

I think we feel confident in overall e-commerce being our fastest growing channel. I don't think we're willing to give color on individual markets.

Jim A. Chartier

Analyst, Monness, Crespi, Hardt & Co., Inc.

All right. Thanks and best of luck.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

Thank you.

Operator: Our next question comes from Sam Poser from Susquehanna. Your line is open, please go ahead.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

Thank you. Just a quick follow-up on the price increase. How much of that price increase – to what degree is that price increase both in the first quarter and into next year going to offset the FX headwind for the – I mean, when we think about that because that's a fairly large increase. How much do you foresee that offsetting that the FX headwind?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Yeah. Let me start with a little bit of dynamics, Sam, on our third quarter. So if you think about our third quarter, we had 130 basis points of FX. And then also we had channel mix, so as we shift more to wholesale, we see a channel mix impact. Wholesale is overall accretive on the bottom line, but from a gross margin standpoint, it's lower and we saw that impact Q3 by 80 basis points, which was obviously offset by underlying strength in overall margins.

When you think about that for Q4, you can see FX mitigate a little bit. We're expecting about 100 basis points of FX in Q4 and then we do have some channel mix again. So we expect those same dynamics to continue to next year. And as Andrew mentioned, we took price increases in August on e-com, so we did have some price increases in this quarter and then retail will be in Q4, and is anticipated in our guidance.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

I understand that, but I mean just like when we think in the next year and so on, I mean like whether you think about the headwind of currency that you talked about next year on the margin, I know you're not guiding, but are you thinking that this price increase could offset, I mean just take those two elements, the price increase if it's at wholesale or retail could offset the impact of currency. Could that be just those two things be a wash with each other?

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

I think it's too early to say which is why we are not guiding for next year from a full P&L standpoint. Obviously pricing is one of the dynamics that will help support margins next year.

Sam Poser

Analyst, Susquehanna Financial Group LLLP

Q

Great. And thank you very much, Anne.

Anne Mehlman

Chief Financial Officer & Executive Vice President, Crocs, Inc.

A

Thank you, Sam.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

Thanks, Sam.

A

Operator: Your next question is from Mitch Kummetz from Pivotal Research Group. Your line is open. Please go ahead.

Mitch Kummetz

Analyst, Pivotal Research Group LLC

Yeah. Just a couple of quick follow ups, so Andrew, I know you guys have given some decent color on Asia by country. I am wondering on Europe, you talked about growing brand heat. Has that been pretty consistent across countries? And if not, could you maybe drill down a little bit on where you've seen more strength versus less strength? And then my second question is on clogs, if I recall correctly, you had some supply constraints on clogs in the first half of this year, is there any way to quantify the impact of that? I mean, was it – did it take down your sales by \$10 million, \$20 million more or less? I don't know if there's any way you can put a number around that in terms of what that supply constraint impact was on this year that I would assume is unlikely next year?

Q

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

Yeah. So, EMEA, I would say the strength in our business is relatively consistent across EMEA. So EMEA is obviously, Western Europe, Eastern Europe, but also the Middle East and a little bit in North Africa; Middle East and North Africa being distributors; and Eastern Europe being distributors. So, I would say, direct countries have grown strongly as well as our distributor business.

A

So, I think it's pretty consistent, I wouldn't really call out any highlights. Obviously, we do break out by channel; and you can see that digital commerce – e-commerce has performed well throughout the year. That's been a really good driver. But that actually is across the whole business. So I wouldn't – I don't think there's really highlights or low lights in EMEA, it's pretty solid. And obviously impacted by the euro pretty significantly the currency compression.

In terms of the second piece really – what was it – sorry, what was your second question again?

Mitch Kummetz

Analyst, Pivotal Research Group LLC

On the clogs the supply constraint?

Q

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

Supply constraint, yeah, sorry. Didn't write it down. Supply constraint, yeah, I think we've solved this in North America. You can see our inventory was up nicely, which was important to us and it gives us some of our confidence going forward. So we've really solved those supply constraints and that was really strongly around the Classic Clog. We haven't really gone back and quantified, but I'm sure it helped in our order book, right. So I'm sure if you're a major wholesaler account and you felt like you were not getting all the supply you wanted this year, you've ordered more strongly for next year.

A

Mitch Kummetz
Analyst, Pivotal Research Group LLC



Great. Thanks again.

Operator: There are no further questions at this time. I turn the call back over to the presenters.

Andrew Rees

President, Chief Executive Officer and Director, Crocs, Inc.

Thank you. Thank you. Appreciate everybody's questions today and their continued interest in the company. So we look forward to talking to you again at the end of Q4.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

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