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YETI Holdings, Inc. (YETI)

Q3 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to YETI Holdings Third Quarter 2018 Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. Instructions will follow at that time. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to turn the conference over Jean Fontana of ICR. Thank you. You may begin.

Jean Fontana
Managing Director, ICR, Inc.

Thank you and good morning to everyone joining us on today's call to discuss YETI Holdings third quarter 2018 results. Participants on this call will make forward-looking statements including about our business plans and strategies, markets, products and investments as well as our guidance for fiscal 2018. These statements are based on our current expectations and are subject to numerous risks and uncertainties that could cause actual results to differ materially.

These risks and uncertainties are detailed in this morning's press release and under the caption Risk Factors and elsewhere in the document we filed regularly with the SEC, all of which can be found on our website at investors.yeti.com. We undertake no obligation to revise or update any forward-looking statements except as required by law.

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During our call we will also reference certain non-GAAP financial information including adjusted items. Reconciliations of GAAP to non-GAAP measures as well as a description of each and the limitations and rationale for each using such measures can be found in the supplement financial tables included in this morning's press release and in our filings with the SEC, all of which can be found on our website at investors.yeti.com.

We use non-GAAP measures as the lead in some of our discussions because we believe they more accurately represent the true operational performance and underlying results of our business. Hosting today's call will be Matt Reintjes, President and CEO of YETI and Paul Carbone, Chief Financial Officer. Following our prepared remarks, we'll open the call for questions.

With that, I will turn it over to Matt.

Matthew J. Reintjes

President, Chief Executive Officer & Director, YETI Holdings, Inc.

Thank you, Jean. Good morning, all. Welcome to the YETI's third quarter earnings call. It's great to be here today for our first earnings call as a public company. As you know, YETI a lifestyle brand that designs, builds, and markets premium outdoor equipment. That's what we do, and we believe we do it extremely well.

Let's start with a few highlights of our financial performance for the third quarter. We delivered net sales increase of 7%, Adjusted Operating Income growth of 29% and Adjusted Net Income growth of 81%. On a year-to-date basis, we drove net sales growth of 23%, Adjusted Operating Income growth of 64% and Adjusted Net Income growth of 166%. We're pleased with the strong performance of our DTC business and a continued demand from our wholesale business as we continue to balance our omni-channel strategy to be where consumers are shopping for our product.

Paul is going to spend more time in detail on our financial performance shortly. But I thought I'd give an update on some of the exciting milestones in Q3 and where the business is going. During the third quarter, we did have a number of significant milestones. We expanded our product line to include new items such as the Tundra Haul.

The Tundra Haul is our first wheeled hard cooler continues the evolution and innovation in YETI's hard coolers and our Tocayo everyday backpack. The Tundra Haul completed a successful run of YETI hard cooler innovation and the Tocayo backpack is the next step in the evolution of YETI bags, a product family that we introduced in 2017 with our Panga line of waterproof bags.

We also expanded our international presence in the Japan, launched our first national television and digital ad campaign and hit the road with our Ten Years of Tundra Film Tour, celebrating the YETI Tundra and the YETI Lifestyle. For the Tundra Tour, we had a fantastic attendance in reception across 11 cities in the U.S. from coast-to-coast from early September through the third week of November, culminating with 1,500 people in a theatre in our hometown of Austin, Texas.

As we think back over the past two years, as most of you know, we've been incredibly focused on creating a strong foundation for growth. We successfully implemented new infrastructure systems including SAP as our ERP, made people, process and technology improvements to our supply chain and demand forecasting. Replatformed our e-commerce website, drove our DTC business toward a balanced omni -channel approach, continue to build a strong brand momentum and a symbol to management team, I'm incredibly proud to work with.

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We know YETI is a special brand, and we believe the investments we put behind this business set us up to deliver strong, sustainable, and profitable growth over the long-term.

Today, our sales are balanced across two product families, with slightly more than 50% of our sales coming from Drinkware and slightly less than 50% coming from Coolers & Equipment.

Our customer base has evolved over the past three years. While our early adopters are in the hunting and fishing communities, we've become a go-to brand for both enthusiasts and casual campers, beachgoers, backyard barbecuers, tailgaters, daily commuters, and many more, further illustrating our broadening appeal, the percent of our female customers has grown from 9% in 2015 to 34% in 2018.

YETI's consumer base has also grown nationally. In 2015, approximately two-thirds of our consumer base was generated in our heritage markets from Texas across the Gulf Coast and the Southeast to Florida.

Today, more than 50% of our consumer demand is generated in our newer non-heritage markets. We believe we still have a large untapped opportunity in our heritage and our non-heritage markets for our current portfolio and new product innovation. The breadth of our current customer base relative to just three years ago tells us that there is significant growing demand for our products. With this as our foundation, we believe we have a long runway as we further broaden our customer base, extend our product offerings, and expand geographically.

Now, let's talk about why we believe YETI is rare and why we have an incredible opportunity in front of us. First, we're an influential, growing lifestyle brand with a passionate following. The YETI brand stands for innovation, performance, uncompromising quality, and durability. Our customers are passionate about YETI and act as brand advocates with 95% saying they have proactively recommended our products to their friends, family, and others.

Second, we have superior design capabilities and product development. We never compromise on product. We strategically invest in the product and we strategically invest in the brand. That's what allows us to deliver premium products and customer experiences. All of our products are built to stand up to whatever users do with it or do to it.

Third, we have a balanced omni-channel distribution strategy. Year-to-date wholesale represents 67% of our business with the balance of 33% being direct-to-consumer. When I joined YETI in 2015, 90% of our sales were wholesale based. We continue to value, support, and invest with our retail partners, but we also recognize we need to be where the consumer wants to shop, and we believe a powerful omni-channel approach supports that strategy.

Fourth, we have a scalable infrastructure in place to support our growth. We've worked diligently to build our information technology capabilities in our business process effectiveness. Our infrastructure enables us to manage our global manufacturing base, optimize distribution logistics, and effectively serve our expanding customer base. Importantly, it also provides us with the capabilities necessary to support our future growth.

Fifth, we have a highly talented, experienced, and diverse management team. Our senior management team is comprised of experienced executives from large global product and services businesses with proven track records of scaling business, leading innovation, expanding distribution and managing expansive global operations.

To leverage the opportunity in front of YETI, we're executing against a clear set of growth drivers. Let me first talk about expanding brand awareness among new customers and in new geographies. We drive a brand – our brand

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awareness through multi-layered marketing programs, word-of-mouth referrals, experiential brand events, and YETI ambassadors.

What we know is that customers who know YETI, love YETI. While we have significantly expanded our brand reach throughout the United States, unaided brand awareness is approximately 10% reflecting mid-teens awareness in our heritage markets, but still mid-single-digit awareness in some non-heritage markets. Many of the most population dense parts of the U.S. remain underpenetrated from an unaided awareness perspective, which means introducing our brand and existing product portfolio into these markets creates great growth opportunity.

Second, our product is the heart of our business, and we have a strong track record of consistently expanding our product offering. By employing an uncompromising approach to product design, we've successfully expanded into innovative new products in hard coolers, soft coolers, Drinkware, travel bags, backpacks, and accessories. In 2017-2018, we launched a variety of award-winning new products and our future innovation pipeline is currently the highest in company's history.

We believe our product families, extensions, variations, and colorways, in addition to our new product launches, result in repeat purchase by existing customers and consistently attract new customers to YETI.

Turning to channel for distribution, DTC represents our fastest-growing sales channel. We believe our DTC channel will be another key component of our growth, when you have a passion-based lifestyle brand like YETI, people want to engage directly with you. DTC sales have grown from 8% of sales in 2015 to over 33% today. Year-to-date direct-to-consumer sales were up 49%, and we expect our growth momentum to continue.

We intend to continue to drive direct sales through our own website domestically and internationally. The Amazon Marketplace, our corporate sales initiatives, and by selectively increasing the number of our own retail stores. As a part of our DTC business, we sell through Amazon via Amazon FBA in order to maintain our minimally advertised pricing, manage inventory and plan assortment. We began selling through YETI Authorized on the Amazon Marketplace in late 2016, and we're optimistic about the continued expansion of this complementary distribution channel.

Turning to retail. We have one full price store in Austin, Texas, which launched in 2017. It would be classically defined as a flagship store; 8,500 square feet, it has a bar, it has a stage and true YETI fashion, it has an eight-foot tall bear, all the things you would expect at a YETI store. We created a brand experience. People come, hang out and buy YETI. Importantly, it's also profitable. We learned a lot from that store and believe we have the opportunity to add additional retail locations.

We've established a select retail strategy as a complementary part of our omni-channel approach to the market. We expect to open four to six stores per year in 2019 and 2020. We've identified our next two locations which we expect to open in mid-2019. We signed leases on King Street in Charleston, South Carolina and on North Milwaukee Avenue in Wicker Park, Chicago, Illinois. Both locations offer high visibility and a high level of foot traffic, in addition to a strong fit with our balanced approach to serving our heritage and non-heritage markets.

Now, turning to international. We're just scratching the surface and see significant opportunity to expand our international presence. We are seeing demand for YETI through our e-commerce and digital global monitoring and tracking. We also hear from our brand ambassadors about the product and brand reception when they're traveling to other parts of the world doing the incredible things that they do. In 2017, we entered Canada and

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Australia and in 2018, we saw strong growth in both of these countries. And as I said earlier, we just entered Japan in the third quarter of 2018.

We also believe there are meaningful growth opportunities in Europe and Asia, as many of the market dynamics and premium performance-based consumer desires and needs that we've successfully identified domestically are also highly valued in these markets. We plan to enter select international markets throughout 2019.

So, as you can probably tell, we're incredibly excited about the growth opportunities we see here at YETI. We fundamentally believe in the long-term sustainable growth of the YETI brand. I want to thank our customers and all of our YETI employees whose passion has built YETI into the brand it is today.

With that, I'll turn over to Paul to review our financial results.

Paul C. Carbone

Chief Financial Officer, YETI Holdings, Inc.

Great. Thanks, Matt, and good morning, everyone, and thank you for joining us. I'm excited to be part of the YETI team. We have a truly unique brand and an incredible team and a lot of white space to grow this premium brand. Additionally, we have an attractive asset-light financial model with strong sustainable sales and earnings growth potential.

I will begin with a review of our third quarter fiscal 2018 financial results followed by our full-year 2018 guidance and our long-term outlook.

So, starting with the third quarter. Net sales increased 7% to $196.1 million compared to $183 million in the third quarter last year. While 7% is lower than our long-term guidance, this was due to a one-time bulk sale last year during the third quarter as we transitioned into our second-generation of soft coolers.

Given our desire to get this new innovation associated with the second-generation coolers into the market as soon as possible, we decided to clear through our first-generation product which was actually purchased back in 2016. In the future, we do not expect to see the same level of excess prior gen inventory when we launch new products as we have revamped our demand planning and inventory management processes.

So, turning to sales by channel. Wholesale sales were roughly flat at $125 million with growth in Drinkware offset by a decline in Coolers & Equipment sales, mainly driven by the bulk sale of soft coolers I just mentioned.

Direct-to-consumer sales increased 23% to $71.2 million with strong performance in both categories particularly Drinkware. Direct-to-consumer growth was driven by increased purchases on YETI.com, Amazon as well as increased consumer in corporate customized Drinkware. As a reminder, we sell YETI products through the Amazon Marketplace not to Amazon.

By category, Drinkware sales increased 37% to $104 million, driven by the expansion of our Drinkware line, new Drinkware accessories, and the introduction of new Drinkware colorways.

Coolers & Equipment decreased 16% to $86.7 million. This decrease was largely driven by the bulk sale of soft coolers last year. Gross profit in the third quarter increased 19% to $97.5 million, and the rate expanded 480 basis points to 49.7% of net sales. This margin expansion was due to cost improvements across our portfolio, the lapping of the bulk sale which I mentioned earlier combined – accounted for more than half the increase.

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Gross margin also benefited from fixed cost leverage, the non-reoccurrence of reserves taken last year and the benefit from the sales mix shift towards direct-to-consumer. These were partially offset by price reductions on select hard and soft coolers that we took this past January as we plan for new product introductions.

Adjusted SG&A was 33.6% of net sales as compared to 31.5% in the same period last year, as we continue to invest in our business in support of our long-term growth objectives.

The increase was driven by increased head count and higher compensation – incentive compensation, increased facility, utility, and outbound freight expenses, professional fees, as well as credit card processing fees. These increases were partially offset by a reduction in marketing expenses.

Adjusted Operating Income increased 29% to $31.7 million or a 280-basis point improvement to 16.2% of net sales.

Our effective tax rate was 16% during the quarter compared to 32% in last year's third quarter due to the reduction in the U.S. corporate income tax rate enacted as part of the Tax Cuts and Jobs Act and the revaluation of deferred tax assets for state income taxes.

Adjusted Net Income increased 81% to $20.2 million or $0.24 per diluted share. Adjusted EBITDA increased 26% to $38.4 million from $30.5 million in the prior year period and represented approximately 19.6% of net sales in the third quarter this year compared to 16.7% in the same quarter last year.

Now, let's turn to our balance sheet. As of September 29, 2018, we had cash and cash equivalents of $52.1 million as compared to $34.7 million at the end of the third quarter last year. We ended the quarter with $157.7 million in inventory as compared to the $227.2 million last year. The 31% decline in inventory as compared to last year is the result of improved demand forecasting and better inventory control across all product categories.

We ended the quarter with $387.8 million in outstanding borrowings under our credit facility, which reflecting mandatory payments of $44 million and additional voluntary debt payments of $30 million during the third quarter. At the end of the quarter, our net debt-to-adjusted EBITDA leverage ratio was 2.6 times.

Additionally, this month, we intend to use the net IPO proceeds along with additional cash on hand to make a $50 million voluntary debt payment which will fully retire our term loan B. After this voluntary payment, we will have approximately $337.8 million of debt outstanding.

Now, I'd like to turn to our full year fiscal 2018 outlook. We expect net sales to increase between 19% and 20% compared to fiscal 2017 with higher sales growth in the direct-to-consumer channel relative to the wholesale channel. We expect adjusted operating margin of between 15.2% and 15.5%, primarily driven by higher gross margin.

We expect earnings per diluted share of between $0.60 and $0.64. This assumes a tax rate of approximately 22.5% and approximately 83 million shares outstanding. We expect adjusted earnings per diluted share of between $0.79 and $0.82 compared to $0.28 last year.

Adjusted EBITDA is expected to be between $141 million and $144 million, as compared to $97.5 million last year.

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Capital expenditures are expected to be between $24 million – $21 million and $24 million for the full year. We ended 2017 at 4.4 times levered and expect to end this year around 2.1 times, and we expect to continue to delever the business about half a turn per year based on both EBITDA growth and debt pay down.

Now, let's talk longer term. Longer term, we expect annual sales – net sales growth of approximately 10% to 15%. We expect our wholesale segment to grow in the low- to mid-single-digit range and our DTC business to grow in the mid-20% range, and that's evenly balanced across YETI.com, Amazon and corporate sales.

International will grow faster than the U.S., but off a small base today. By product category, we expect similar growth rates from Coolers & Equipment and from Drinkware.

Gross margin is expected to reach between 50% to 52% long-term. We get that from a few levers. First, we are working to reduce product cost primarily through negotiations with our vendors. Quality has always been and always will be number one for us. So, this isn't about taking quality out of the product. It is based on the volume we are purchasing from our vendors and their ability to leverage their fixed costs. We're growing our key manufacturing partners while eliminating our underperformers.

We also now have should cost models across all of our products. So when we go into negotiation with vendors and manufacturers, we're actually armed with information to leverage and drive down cost. So, we're doing a lot of work in our supply chain to reduce product cost.

Secondly, the continued growth of our direct-to-consumer business with its higher gross margins. And lastly, we gain leverage on fixed costs which is about 5% of our COGS today.

Adjusted EBITDA is expected to reach 19% to 22%, driven by the gross margin expansion. We plan to invest in SG&A over the next couple of years as we build out our direct-to-consumer team and increase marketing spend as we focus on demand creation. As a result, we expect the increased SG&A will offset a little bit of the gross margin expansion.

We expect CapEx in the range of $35 million to $48 million. We are a capital-light business. We use contract manufacturers and third-party logistics. So our overall general run rate has been approximately $30 million to $35 million with about half for IT and half for new business development, which primarily includes molds and tooling for new products.

Going forward, we will spend additional capital above that run rate as we build out a few retail stores. But again, as you've heard us say before, we are not looking to become a retailer. We are talking about opening a handful of stores per year.

In summary, we are very pleased with our third quarter results. We are very excited about our future potential and we look forward to reporting our progress in the quarters to come. And with that, I'd like to turn the call over – open the call for questions.

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QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question is from Robert Ohmes with Bank of America Merrill Lynch. Please proceed with your question.

Alexander Perry
Analyst, Bank of America Merrill Lynch

Q

Hi. This is Alex Perry on for Robbie. Congrats on a strong start.

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Thanks, Alex.

Alexander Perry
Analyst, Bank of America Merrill Lynch

Q

My first question is, can you talk through any success you're seeing in your new product families? And how much of your future growth do you expect to be driven by new products?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah. Thanks, Alex. This is Matt. We don't talk about the future growth of new products and break it out by category and overall, it's not something that we've disclosed in the past and don't plan to break it out that way. What I can say is, we've been pleased with the success in the uptake of our new products. As we think about our philosophy on launching new products, we want to layer growth upon growth. So we look to our historical products and legacy products to drive growth, and then bring layers and planks growth with the new products on top of it and look at our overall long horizon. We don't have kind of seasonal in-and-out product launches outside of our colorways. So we're pleased with how the new products are performing.

Alexander Perry
Analyst, Bank of America Merrill Lynch

Q

Great. That's very helpful. And then just a follow-up, can you talk to your geographic expansion strategy, and how are you planning to penetrate some of the white space opportunities that you mentioned out there, such as the Northeast?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah, there's a couple ways we do it, Alex, and we talk about our depth and breadth strategy when we talk about brand expansion and we apply the same geographically, which is, we want to find markets and consumers that are existing in heritage YETI pursuits in, hunting, fishing, outdoor speak to, and continue to bring new pursuits on those, and that drives the breadth.

So if you look at our business over the last three years how it's evolved from hunting and fishing, to including more broad outdoors, to including the sailing communities and climbing communities, that's how we build relevance into those new markets. We also add overarching, as you've heard in our global brand awareness

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research, but also in our national advertising campaign driving more broad-based awareness into those markets. We're running right now our national ad which started in the second half of this year and [ph] we're likely going to success that (00:25:57).

Alexander Perry
Analyst, Bank of America Merrill Lynch

Q

Great. Thanks a lot. Good luck to your holiday.

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Thank you.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Thanks, Alex. Next question.

Operator: Our next question is from Kimberly Greenberger with Morgan Stanley. Please proceed.

Kimberly Conroy Greenberger
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thank you so much. I was wondering if you could talk about any early insights that you have on the corporate sales. I think you were hiring some dedicated corporate sales people here in the third quarter, and I'm wondering if there are any early observations there? And then if we could look at the cooler business, could you comment on the performance in coolers outside of the bulk sales last year. So, if you exclude, let's say, those soft cooler sales, how is the rest of the category performing? Thanks so much.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yeah. Thanks, Kimberly. It's Paul. So, on corporate sales, so as you said, we talked as we are on the road show about hiring additional people into that group actually to start making outbound calls which we started that process and we have one or two people currently doing that.

I can say for the third quarter, our corporate sales performance was excellent and performed in line with the whole direct-to-consumer comps. So, if you think about that, it was in line, so it performed very, very nicely. And that's a really interesting and exciting business for us to continue to grow.

So on – and then on the coolers, if you back out the one-time sale last year, overall, coolers were still slightly down year-over-year, in that there's a couple of things into play. So first, we saw a good consumer demand throughout the quarter. So we watch it at retail, so we saw good demands throughout the quarter. And then there are a couple of things that play; one is as we introduced the Tundra, we slowly – we ramped that in the wholesale channel a little bit slower than we originally expected to, just to make sure we build inventory in advance. So that was the second thing.

And then we were rolling over several exciting launches from last year. So that was kind of the performance in the Coolers & Equipment.

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And then, the last thing I would say is, if you look to our full year guidance, topline guidance, 19% to 20% and what that implies for the fourth quarter, you'll all do the math there. But we expect strong positive growth out of both Coolers & Equipment and Drinkware for the fourth quarter. So, I think that third quarter has rollover items, as you mentioned, but that still is a growth category for us.

Kimberly Conroy Greenberger
Analyst, Morgan Stanley & Co. LLC

Q

Fantastic. Thanks so much. Can I just follow-up on your Drinkware comments, Paul. They were – Drinkware, very nicely exceeded our expectations here this quarter. Was there something driving that better than expected outcome? Any new products or more effective marketing? We're just wondering the driver there. Thanks.

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah. This is Matt. We continue to see as we bring colorway innovation, as we expand into new geographies, Drinkware is a really nice introduction product into those markets.

We saw some mix shift late in the quarter of buying between hard coolers and or excuse me, Coolers & Equipment and Drinkware. But really, it's the continued vitality in the Drinkware line. No kind of specific or unique product launch that drove it. It's – we're continuing to see good momentum in that category.

Kimberly Conroy Greenberger
Analyst, Morgan Stanley & Co. LLC

Q

Thanks so much.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Thanks, Kimberly. Next question please.

Operator: Our next question is from Peter Benedict with Robert W. Baird. Please proceed with your question.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.

Q

Hey, guys, thanks for taking the question. Starting with the topline 10% to 15% longer term, Paul as you said the fourth quarter guide consistent with that. As we kind of look out beyond this year just for modeling purposes, are there any other kind of unique items that we need to think about from a quarterly basis that might create some volatility. I think there was some excess sales maybe in the first quarter of this year of end-of-life products? So, that's just my first question. Anything that we need to be aware of from a cycling standpoint over the next handful of quarters?

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yes, so – good morning, Peter. So, from a end-of-life, there's nothing material in the out quarters as we look into 2019, and nothing to the magnitude of the third quarter of 2017. The one thing as you think about next year and we'll talk more about this in February when we report fourth quarter earnings and we talk about guidance for next year is, in the second quarter of last year, we changed our revenue recognition for our Amazon sales as we redid

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our contract with firm that or the company that manages the marketplace for us. And we now recognize that on sell-through versus sell-in. So – and we made that change in the second quarter of 2018.

So in the first quarter of 2019, as we look at that, we will be comparing Amazon sell-through to Amazon sell-in, and that will create a little bit of a nuance in the first quarter of next year. And we'll talk more fully about that as we report fourth quarter earnings. But that was the only real significant item as we think about next year.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.

Q

Okay. That's helpful. Thanks for that. As we look at the fourth quarter, I mean is there anything that's changed in your view maybe relative to 60 days ago or so, just on the fourth quarter, we're now getting into the holiday season here, so just kind of your latest thinking there? It looks like things are pretty consistent, but just wanted to see if anything had changed with the margin?

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yes, so let me start and then Matt may want to make a comment. So as this is being our first call with all of you and investors, so as a matter of practice, this call and going forward, we're not going to specifically comment on anything in quarter. So we'll talk always prior quarter and then any guidance or updates we're doing, but nothing in quarter. And with that though, to your question, has anything changed in our view, I think as you see in our long-term guidance, we feel very confident in the fourth quarter.

But Matt, anything else?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

No, I mean – good morning, Peter, we continue to focus on in the fourth quarter, driving the brand awareness, getting a reach into new geographies, the success of the products that we launched this year going in. We expect our direct-to-consumer business which as you know we talk a lot about and invested heavily in to continue to perform well. And we're running the playbook that we had – that we had talked about and excited about getting through 2018 into 2019.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.

Q

Okay. Great. Last question for me, and then I'll move on. Just any latest thinking here on the tariffs. I know that you guys are prepared for that. Any update on progress maybe with working with some of your vendors in China, just your latest thoughts there? Thanks so much.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yeah, thanks. So, let me take that one. So – and let me specifically talk to current known tariffs. So, we will be able to completely offset List 3 tariffs at s 25% rate in 2019. So – and just as a reminder, the List 3 tariffs touch or incorporate our soft coolers, our bag category, and then a couple of other smaller products like the chair in our Coolers & Equipment. It does not impact hard coolers, because those are not made in China.

So, we'll be able to offset that completely in 2019. The size of those tariffs, if those – at 25% for the full-year 2019 against those categories is approximately $15 million impact to us.

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And again, we can offset that completely. So, how are we doing that? The first is, we have FX tailwinds as we pay for products in U.S. dollars. The second, we are accelerating the strategic project to move sourcing of many of these items out of China. We have both ongoing cost negotiations, so just general across the product's portfolio that we charge our procurement team with. And then also specific cost negotiations on the impacted items.

So since we are able to offset the entire impact, we have made the decision and we've talked about this not to take price in those items covered by List 3. That's kind of as we dimensionalize what is impact in List 3 for 2019.

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.
A

And Peter, the only thing I would add to put a fine point on that is, we have an operational team setup, they're executing against a plan. We've got this project fully resourced and they're making good progress towards everything, Paul said.

Peter S. Benedict
Analyst, Robert W. Baird & Co., Inc.
Q

Okay. Terrific. Thanks so much, guys.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.
A

Great. Thanks, Peter.

Operator: Our next question is from Randy Konik with Jefferies. Please proceed with your question.

Randal J. Konik
Analyst, Jefferies LLC
Q

Yeah, thanks a lot. I guess, Matt or Paul, I wanted to ask about some data analytics. If you – has there been – have you noticed any order flow differences or composition of products ordered when you look between what's being ordered on Amazon.com versus YETI.com? I'm just curious because it seems to me like Amazon would be a good place for people that are just discovering the brand, but people like me that know the brand very well, I tend to order my products through YETI.com. So, I'm just curious if there's any data learnings within the direct-to-consumer channel distribution that you're kind of coming – that are kind of coming at you to give you a sense of the future?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.
A

Yeah, Randy, this is Matt, thanks for the question. We look very closely at that as we've talked about in the past, we've been in the direct-to-consumer game in a meaningful way really only going back to 2016. So, we're building out our data analytics database of kind of knowledge and capability. We see some differences, but I would call them sort of early indications, not significant differences. I think your thesis is one that we're working to see if that proves out. But we do like the reach of the Amazon platform, and we like the reach of YETI.com and the opportunity to kind of drive the full basket through both of those. But I would say it still would be early to kind of call a significant mix shift between those two or a significant basket shift between those two.

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Randal J. Konik
Analyst, Jefferies LLC

Q

Understood. And then I guess another follow-up on learnings is, one thing I've done with YETI purchase is that I've never done for other products and I don't know why I do it but I do it, that is register the product, so you can see, if you pull me up, you'll see that I order a Hondo chair or custom cups whatever I've done. Have you kind of looked at that data and try to get a sense of what your consumers are doing, repeat purchases, building their kind of closet out with YETI products, what are you learning from the registration part of the business as consumer buys the product and then registers that product?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah. Great question, Randy. And thank you for registering your product. We appreciate it. I think that the part of the reason we have that registry is, one, we want to be able to communicate effectively with our customers. We – as we've talked about in the past – this past summer, we hired a new head of e-commerce who is incredibly talented and comes from a database of marketing and analytics background for exactly the reasons of your last two questions is to continue to build out the insights and the actionable insights we have from the data that we're gathering.

Randal J. Konik
Analyst, Jefferies LLC

Q

Got it. And one thing on the Custom Shop side, it seems like there's a three-week turnaround time which would argue for significant demand from the Custom Shop. So maybe walk us through what you're seeing in that part of the business? It seems like a real opportunity obviously over time and also seems like an opportunity to build capacity for that side of the business. So just give us some thoughts there?

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yeah, so we have seen great demand and we think about this on two sides of it. So first, let me talk about the demand side and then let me talk about the capacity as you mentioned. So on the demand side, this is both YETI Custom Shop, so the consumer-facing and then also corporate sales, because they're doing a lot of marked Drinkware as well.

So, beginning next year, we're deep into a project that will actually combine the two websites, and combine the consumer journey into one. So you will go to YETI.com and be able to order custom Drinkware throughout your journey if you're buying a cooler or just Drinkware. So we think that will absolutely drive demand.

The second thing, and I think it was in response to Kimberly's question, we added outbound – people here to do outbound corporate sales. So up until the first half of this year we were just answering the phone and answering e-mails and now we're actually proactive. So on the demand side, we're driving it both with the consumer by combining the websites, and then also on the corporate side by actually proactively going out sourcing business.

On the capacity side, so – and then how do you feed all that? On the capacity side, we have continued to add capacity at our factories actually based here in Austin. And we'll continue to do that and we're obviously looking at options of how do we keep that capacity growing as we grow demand, and that's something that Mike Kienitz, our Head of Operations, I might be exaggerating saying we talk about every day, but probably every three days if nothing else. But, yeah, those are two big, so overall, the customization is a big driver for us, both through consumer and corporate, and then also building that capacity.

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Randal J. Konik
Analyst, Jefferies LLC

Q

Understood. One last question.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yeah.

Randal J. Konik
Analyst, Jefferies LLC

Q

One thing I've noticed on TV is the TV ads that have kind of started to kind of pop through whether it be watching a football game, whatever I've been watching. But how are you thinking about building awareness in the young markets of International Canada, Japan, and Australia. What's the strategy there to build awareness in those regions? Thanks.

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah, great. It's not – I would say the playbook that we're running in some of the under aware areas of the U.S. is not fundamentally different than the playbook that we're running and will run in the international markets. It's a multi-layered marketing strategy that includes finding local ambassadors and references for it. We've successfully done that in Australia and in Canada.

We're in the process of doing that in Japan, so you get the strong reference point of the best in the best in the [ph] pro's pros in there either a (00:42:57) selective area or a pursuit, driving strong merchandising at retail, training the retail partners so that they can represent the product well at the retail, participating actively from an event perspective in community. So we've run events in Australia, we've run events in Canada, we've run events in parts of the U.S. where we're underpenetrated today, and we'll continue to kind of run that multi-layered strategy. We believe that the mix between broad-based awareness like the ad campaign that you see on TV and the kind of person-to-person, event-driven activation is incredibly important. So that playbook that we've built over 12 years in the U.S., we're seeing a similar playbook work and the fruits of it internationally.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Great. Thanks, Randy.

Operator: Our next question is from Peter Keith with Piper Jaffray. Please proceed with your question.

Peter Jacob Keith
Analyst, Piper Jaffray & Co.

Q

Hey. Good morning, everyone. Congrats on your first release here. I wanted to follow-up on Randy's question, just looking at usability of the products and how that maybe has evolved over time. I guess what I'm looking at specifically is, with your user studies, do you have a sense on how many YETI products, some of your enthusiasts own now versus maybe three years ago, and that would help us maybe get some verification on how receptive people are to the new product launches?

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Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah, Peter, thanks, this is Matt for the question. We do, we have some early data. The annual owner study that we do and with multiple time a year brand study, we are asking those questions and we've been doing the brand studies and owner studies kind of going back to 2015, but when you really think about the expansion in the product portfolio, it really took hold in the last call it 24 months.

So we're trending that and seeing both depth within a category that an owner has, and then breadth in adoption. The other thing we do is we get analytics through purchases on YETI.com and what the basket people have bought, and if we have – as Randy said, the registration data, and we can compare those things. So, we are actively looking at that to both see what the uptake is of new products with existing owners and the uptake with new customers.

Peter Jacob Keith
Analyst, Piper Jaffray & Co.

Q

Okay. Thank you. And then with the abundance of new products that have been coming out here in the last couple of months at retail, we've seen the wine tumblers, and we've seen the new Tundra Haul. I guess, could you give us a sense on which products do you think have seen very good uptick from wholesale and will be displayed on retail floors over the holiday season?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah, I think the two that you mentioned are both good examples of that. There are products that we are not fully distributed yet. We've continued to ramp those. We just brought the wine tumblers into the channel in the fourth quarter. The Haul we announced in the wholesale or announced publicly and then rolled in the wholesale in late Q3.

And so, it's still getting out into the market. And I would say both those are good examples of how we think about product launches and not the one-time capture of opportunity, but the build over time. And I think you're going to see the success of the Haul and the wine tumblers both in the fourth quarter and as we go into 2019.

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Great. Thanks, Peter. Sorry, go ahead operator.

Operator: That's okay. Our next question is from Brett Andress with KeyBanc Capital Markets. Please proceed.

Brett Andress
Analyst, KeyBanc Capital Markets, Inc.

Q

Hey. Good morning. Thanks for taking my questions. I wanted to dig a little bit more into your wholesale sell-through trends that you comment on in the press release. So, I guess in percentage terms, what kind of sell-through did you see in your national accounts, because I think presumably you had that visibility, so what the coolers look like, what the Drinkware look like. I'm just really trying to square your sell-in versus your sell-out a little bit better?

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Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yeah, so thanks for the question, Brett. So, we receive POS data from our biggest customers in the wholesale channel. And while I'm not going to quote the exact numbers, we saw strong sell-through in units and dollars across both categories, across both Drinkware and Coolers & Equipment. I think I mentioned Coolers & Equipment in relation to a earlier question. But we saw a nice consistent positive sell-through in the third quarter, even though our sell-in in Coolers & Equipment and across both channels was down year-over-year.

Brett Andress
Analyst, KeyBanc Capital Markets, Inc.

Q

Got it. Okay. And then I guess [ph] dwelling out (00:48:07) that a little bit. I mean can you give us any early indications on the success of your holiday campaign. I mean, it seems it's coordinated with some national media buys. I mean just any early results or anecdotes that you're seeing from this past weekend or how you're measuring the success of that, I guess, as we go throughout the holiday season here?

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yeah, so let me talk broadly, and as I said, we're not going to comment in quarter, but sitting here and the 2018 full year guidance of topline, I mean, what that indicates for Q4, which is double-digit topline growth in the quarter, rolling over significant growth last year in Q4 actually. Please take that away as we feel very confident and comfortable and like what we see in the fourth quarter. I know the response to our advertising and the national campaign has been very positive from a feedback point of view.

And then before we take the next question, I want to just clarify, I may have misspoke in my prepared remarks. So, let me just clarify. And it was in relation to our payments that we made for debt. So, let me just repeat my prepared remarks to make sure we have this right.

So, we ended the quarter with $387.8 million in outstanding borrowings under our credit facility reflecting mandatory payments of $11 million and additional voluntary debt payments of $30 million, ending the quarter at a leverage ratio of 2.6 times. I think what I may have said in my – when I originally talked I said $44 million in additional voluntary payments during the quarter, but it was $11 million during the quarter. I just wanted to clarify that and make sure we have that transcript wise and for the larger group.

With that, we'll take the next question.

Operator: Our next question is from Dan Wewer with Raymond James. Please proceed.

Dan R. Wewer
Analyst, Raymond James & Associates, Inc.

Q

Yeah, thanks. Good morning, Matt. I wanted to ask you about the health of the wholesale channel. I mean, DICK'S was obviously incredibly complementary about YETI yesterday morning. But looking at the publicly-traded sporting goods retailers as a whole, comp sales have been weak, no one is really opening a meaningful number of stores, if that represents any type of challenge for YETI and it will make it even more important to grow your DTC channel?

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Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah. Thanks, Dan. It's a great question. I think a couple of things and start on the end of it. We truly believe in, and as you heard in our comments the omni-channel strategy and that consumer buying behavior shifting and we're seeing – we're prepared for and seeing the success of that and I think the growth of the DTC business. We also think the wholesale channel is very complementary and we expect to continue drive performance out of that.

I think one of the things that is unique about how YETI's positioned is, when you think about the breadth of our retail partnerships, it covers a broad range from sporting goods to hardware to outdoors, surf shop, skate shops. So, we have a pretty broad based retail group. And within that portfolio of retail partners there are some that are performing better and some that are lagging and part of our strategy in building out that reach both from an authenticity of the doors that we work with, but also gives us the ability in the wholesale channel to kind of [ph] whether (00:51:57) different parts of the market going up and down. We've also seen that retailers that focus on merchandising, presenting the product that put the product upfront are seeing a lot of success with it. And we continue to invest behind that.

Dan R. Wewer
Analyst, Raymond James & Associates, Inc.

Q

Okay. And then just a second question. The last couple of months since we've been involved, a comment question is on that 10% to 15% revenue growth target, how much of that is dependent on new product? I'm not sure if you're comfortable talking about the revenue growth from the existing product line and what you're expecting from new products going forward, but that is a very commonly asked question?

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yes. So, let me try to put it in context without giving you numbers. So, the 10% to 15% topline growth and let me first start at category, it's about equally balanced between categories as we think about this and we look at the out years.

As far as new product and as Matt said, we don't specifically look at the business this way even internally, because you talk about a new colorway and Drinkware, is that a new product, is that or not, we think of it as an extension. But what I would say is, as we look in the out years, new product introduction is important to us, but we don't need home runs to deliver the 10% to 15%. So you've heard us say this before our Tundra continues to grow after 10 years. We're going to – Coolers & Equipment, which a lot – hard coolers is a big piece of that as we talked about with our 2018 guidance, Coolers & Equipment will be significant double-digit growth in the fourth quarter as you do the math on our full year guidance.

So we don't necessarily look at it as new products, but what I would say to you and investors is that we're not banking on home runs, we are banking on developing and delivering great new products as we have in the past, and as they slide in, but we don't need the home runs to hit the 10% to 15%.

Operator: Our next question is from Sharon Zackfia with William Blair. Please proceed.

Sharon Zackfia
Analyst, William Blair & Co. LLC

Q

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Hi. Good morning. I didn't realize we were going in alphabetical order, so maybe next time, we can go in reverse. But I just had a few I guess clarifying questions. So I don't think you mentioned what growth was on heritage versus non-heritage either year-to-date or in a quarter. So, I'd be curious to hear about that? And then I guess secondarily, particularly as you've embarked on this new ad campaign, are you seeing anything innately with the consumer base or demographics that would preclude the portability of YETI to achieve the kind of success it has had in the Southeast in the heritage markets more broadly on a national basis?

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.
A

Great, Sharon, good morning. So on heritage and non-heritage, we didn't talk about that, and it's not something we are going to specifically give growth numbers going for, but I tell you what happened in the third quarter and as we talked about in the first half of the year as well. Business or sales outside of the heritage markets have grown faster, so we're seeing that adoption, we're seeing our penetration into the white space. So they have grown faster and you see that Matt talked about the mix shift going from approximately two-thirds back in 2015 to now less than 50% in the heritage when he said it was over 50% in the non-heritage. So you're seeing it grow faster and that continued in the third quarter. Matt, you want to talk about...

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.
A

I would just say, Sharon, I think the best indicator we have of the portability is the speed with which we've been able to make that shift from our heritage markets to our non-heritage markets and we're seeing that in the results.

Sharon Zackfia
Analyst, William Blair & Co. LLC
Q

I guess with that though the demographics on the non-heritage markets, I mean are you seeing that [ph] skew (00:56:27) more female for you, younger, more urban, anything associated with that. It just seems like the brand is perceived a little bit differently outside of its hunting roots once you get outside of Texas and the Southeast?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.
A

Yeah, I think we've seen a couple of things in the demographics. We've seen relative consistency in our age bracket and we've seen relative consistency in our household income. We've seen the shift, the male to female shift, but I wouldn't call that the exclusive of the non-heritage market. So I think it is as we broadened our product portfolio, as we broadened our messaging, as we increase the number of pursuit communities and passion-based communities that we speak to and engage with, I think we're seeing that broad-based throughout the U.S.

Operator: Our next question is from Alexandra Walvis with Goldman Sachs. Please proceed.

Alexandra Walvis
Analyst, Goldman Sachs & Co. LLC
Q

Good morning, guys. Thanks for taking our questions here. My first question, Paul, you mentioned in your comments that you expect to see – expect to not see that prior generation current activity again going forward. Can you help us to understand why you're confident that we shouldn't expect that kind of activity again? Thank you.

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Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yes. So, let me start there and there's a couple of things. One, and I try to mention or I mentioned in my prepared remarks. So, specifically on the soft coolers, a lot of that inventory that we own – so, there's two pieces of how much inventory we have and then how do we transition into new products. So, on the soft coolers in particular, a lot of that inventory that we had at first-gen was back from the 2016 period where we were ordering supply chain product, everything that we've talked about and we had a lot of inventory. So, our demand signals are much better now and our ordering as we order products. So, that's kind of that piece of it and that first-gen was really back pre-2017, but we decided to clear it in the third quarter of 2017.

And then secondly, we plan this from a product road map longer term, right? So, we're looking further out into the future, so these transitions are now smoother. So, we don't have that lumpiness and we don't have all this inventory. And then we're also using – and this is more for colorways, which become end-of-life and Drinkware for instance. The last few we've actually done on YETI.com at full price. So as we wind down a color, we send out – we talk to our consumers and say last chance to buy X color, and that's actually at full price.

So we're more deliberate on the frontend as we're managing inventory and then more deliberate in the cycle as we look forward to know when we're going to wind down and transition. And then more deliberate at the end when similar to like I talked about at YETI.com, we actually go and we do it at full price, but we've put out this last chance type of message to our consumers.

Alexandra Walvis
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thank you. And then I had a second question on your promotional strategy. We noticed that you had some deals out there on Black Friday with the free Rambler Mug for example offered to customers spending over a certain threshold. I wonder if you could help us to think about how you guys are planning for promotional events going forward, how regularly would you expect to use those opportunities, and what types of things should we expect going forward?

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

A

Yeah. Alex, this is Matt. I would say we're very selective as we use things promotionally. The Black Rambler gift with purchase that you saw over the holiday – the Black Friday holiday was consistent with things we've done in the past couple years ago with the black Trucker Hat. We've used our YETI ICE complementary to our product. And so we have a very select promotional cadence, and we do it in a select way. We will continue to have that approach to how we think about promotional activity. And the breadth of our portfolio is actually not with not on promotion and not available. So, I think the – I think we feel good about it and how we've built that into our planning.

Operator: Our next question is from Jim Duffy with Stifel. Please proceed with your question.

James Vincent Duffy
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Thanks. Good morning. Two quick ones for me. The largest customer DICK'S has an impressive display of products. Can you help us think about that? Was sell-in for that a Q3 factor or is what we see on the shelves revenue to be recognized still in the fourth quarter?

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Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

Yes. So, Jim, thanks. So, that was sell-in during the third quarter. So, everything, we recognize the wholesale as we sell it to the wholesale partner. So, anything that you see in DICK'S store has been recognized by us and for just the quarterly break some of that was in Q3, some of it if they ordered in Q4 was in Q4. But certainly as we ship it to them, we recognize that and that is a nice floor set for sure.

James Vincent Duffy
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Great. And then, Paul, just quick thoughts on inventory year-end, will you bring in any inventory early to circumvent tariff increases?

Paul C. Carbone
Chief Financial Officer, YETI Holdings, Inc.

A

We've done some of that. So, it's a good question. So, we've done some of that and we'll continue to bring in inventory. It's not only for the tariff piece, but it's also just as everyone across the industry, across cross industries is doing that. We also may do that with other items that are even impacted by tariffs just to get them here for – make sure they're getting through ports, getting on ships. So, we have done some of that with both impacted items and non-impacted items just to make sure we have actually the inventory in our possession as we turn into the New Year.

Operator: We have reached the end of our question-and-answer session, I would like to turn the call back over to Matt Reintjes for closing remarks.

Matthew J. Reintjes
President, Chief Executive Officer & Director, YETI Holdings, Inc.

Thank you. Thanks for joining us on our Q3 2018 and our first earnings call as a public company. Wish everyone a wonderful Q4 and holiday.

Operator: Thank you. This concludes today's conference. You may disconnect your lines at this time and thank you for your participation.

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