

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

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

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

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

This information should be read in conjunction with the unaudited interim consolidated financial statements and the notes included in Item 1 of Part I of this Quarterly Report on Form 10-Q and the audited consolidated financial statements and notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations, contained in our fiscal 2021 Annual Report on Form 10-K filed with the SEC on March 29, 2022. Fiscal 2022 and fiscal 2021 are referred to as "2022," and "2021," respectively. The first three quarters of 2022 and 2021 ended on October 30, 2022 and October 31, 2021, respectively. Components of management's discussion and analysis of financial condition and results of operations include:

- [Overview](#)
- [Financial Highlights and Market Conditions and Trends](#)
- [Quarter-to-Date Results of Operations](#)
- [Year-to-Date Results of Operations](#)
- [Comparable Store Sales and Total Comparable Sales](#)
- [Non-GAAP Financial Measures](#)
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- [Liquidity and Capital Resources](#)
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- [Operating Locations](#)

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

Overview

lululemon athletica inc. is principally a designer, distributor, and retailer of technical athletic apparel, footwear, and accessories. We have a vision to create transformative products and experiences that build meaningful connections, unlocking greater possibility and wellbeing for all. Since our inception, we have fostered a distinctive corporate culture; we promote a set of core values in our business which include taking personal responsibility, acting with courage, valuing connection and inclusion, and choosing to have fun. These core values attract passionate and motivated employees who are driven to achieve personal and professional goals, and share our purpose "to elevate human potential by helping people feel their best."

Our performance apparel and footwear are marketed under the lululemon brand. We offer a comprehensive line of apparel and accessories. Our apparel assortment includes items such as pants, shorts, tops, and jackets designed for a healthy

lifestyle including athletic activities such as yoga, running, training, and most other activities. We also offer apparel designed for being On the Move and fitness-related accessories. We expect to continue to broaden our merchandise offerings through expansion across these product areas. We also offer in-home connected fitness equipment and associated subscriptions through lululemon Studio, which evolved from our former business unit called MIRROR during the third quarter of 2022.

Financial Highlights

For the third quarter of 2022, compared to the third quarter of 2021:

- Net revenue increased 28% to \$1.9 billion. On a constant dollar basis, net revenue increased 31%.
- Total comparable sales increased 22%, or 25% on a constant dollar basis.
 - Comparable store sales increased 14%, or 17% on a constant dollar basis.
 - Direct to consumer net revenue increased 31%, or 34% on a constant dollar basis.
- Gross profit increased 25% to \$1.0 billion.
- Gross margin decreased 130 basis points to 55.9%.
- Income from operations increased 37% to \$352.4 million.
- Operating margin increased 120 basis points to 19.0%.
- Income tax expense increased 39% to \$97.3 million. Our effective tax rate for the third quarter of 2022 was 27.6% compared to 27.2% for the third quarter of 2021.
- Diluted earnings per share were \$2.00 compared to \$1.44 in the third quarter of 2021. The third quarter of 2021 includes \$23.5 million of after-tax costs related to the MIRROR acquisition, which reduced diluted earnings per share by \$0.18.

Refer to the non-GAAP reconciliation tables contained in the "Non-GAAP Financial Measures" section of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations" for reconciliations between constant dollar changes in net revenue, total comparable sales, comparable store sales, and direct to consumer net revenue and the most directly comparable measures calculated in accordance with GAAP.

Market Conditions and Trends

Macroeconomic conditions, COVID-19, and supply chain disruption continue to impact our business and operating costs, with the impact varying by market.

Macroeconomic Conditions

Macroeconomic conditions, including foreign currency fluctuations and inflationary pressures have impacted our financial results. This includes higher air freight costs and increased wage rates during the first three quarters of 2022 compared to 2021. We have not increased the retail prices on the significant proportion of our products. Inflation and other macroeconomic factors could also impact consumer purchasing behaviors and sustained increases in costs may have an adverse effect on our operating margins.

COVID-19 Pandemic

Most of our retail locations were open throughout the first three quarters of 2022 and 2021, with certain locations temporarily closed due to COVID-19 resurgences, including certain closures during 2022 in the People's Republic of China ("PRC").

Supply chain disruption

In 2021 and 2022 we have experienced supply chain disruption, including delays in inbound delivery of our products as well as in manufacturing. This supply chain disruption caused us to use higher cost modes of transport, including increasing our use of air freight. The supply chain disruption we have experienced has contributed to the 85% increase in our inventory balance compared to October 31, 2021. We expect that the growth rate in our inventory balance will moderate in the fourth

quarter of 2022 as a result of higher sales made during the holiday season, but expect the growth rate in our inventories to remain higher than the growth rate in our sales.

The use of air freight reduced our gross margin during the first three quarters of 2022, however we have begun to see improvement in the supply chain disruption and lower inbound freight costs.

Quarter-to-Date Results of Operations: Third Quarter Results

The following table summarizes key components of our results of operations for the periods indicated:

| | Third Quarter | | | |
|--|-----------------------|--------------|------------------------------------|---------|
| | 2022 | 2021 | 2022 | 2021 |
| | <i>(In thousands)</i> | | <i>(Percentage of net revenue)</i> | |
| Net revenue | \$ 1,856,889 | \$ 1,450,421 | 100.0 % | 100.0 % |
| Cost of goods sold | 818,037 | 621,028 | 44.1 | 42.8 |
| Gross profit | 1,038,852 | 829,393 | 55.9 | 57.2 |
| Selling, general and administrative expenses | 684,236 | 545,124 | 36.8 | 37.6 |
| Amortization of intangible assets | 2,189 | 2,195 | 0.1 | 0.2 |
| Acquisition-related expenses | — | 24,127 | — | 1.7 |
| Income from operations | 352,427 | 257,947 | 19.0 | 17.8 |
| Other income (expense), net | 331 | 15 | — | — |
| Income before income tax expense | 352,758 | 257,962 | 19.0 | 17.8 |
| Income tax expense | 97,288 | 70,174 | 5.2 | 4.8 |
| Net income | \$ 255,470 | \$ 187,788 | 13.8 % | 12.9 % |

Net Revenue

Net revenue increased \$406.5 million, or 28%, to \$1.9 billion for the third quarter of 2022 from \$1.5 billion for the third quarter of 2021. On a constant dollar basis, assuming the average foreign currency exchange rates for the third quarter of 2022 remained constant with the average foreign currency exchange rates for the third quarter of 2021, net revenue increased \$455.4 million, or 31%.

The increase in net revenue was primarily due to increased company-operated store net revenue, including from new company-operated stores and increased comparable store sales, as well as due to increased direct to consumer net revenue. Other net revenue also increased.

Total comparable sales, which includes comparable store sales and direct to consumer net revenue, increased 22% for the third quarter of 2022 compared to the third quarter of 2021. Total comparable sales increased 25% on a constant dollar basis.

Net revenue for the third quarter of 2022 and 2021 is summarized below.

| | Third Quarter | | | | | |
|-------------------------|-----------------------|--------------|----------------------|---------|-----------------------|----------------------|
| | 2022 | 2021 | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(Percentages)</i> | | <i>(In thousands)</i> | <i>(Percentages)</i> |
| Company-operated stores | \$ 903,060 | \$ 707,160 | 48.6 % | 48.8 % | \$ 195,900 | 27.7 % |
| Direct to consumer | 767,351 | 586,525 | 41.3 | 40.4 | 180,826 | 30.8 |
| Other | 186,478 | 156,736 | 10.0 | 10.8 | 29,742 | 19.0 |
| Net revenue | \$ 1,856,889 | \$ 1,450,421 | 100.0 % | 100.0 % | \$ 406,468 | 28.0 % |

Company-Operated Stores. The increase in net revenue from our company-operated stores was driven by net revenue from company-operated stores that we opened or significantly expanded since the third quarter of 2021 which contributed \$112.8 million to the increase. We have opened 71 net new company-operated stores since the third quarter of 2021, including 43 stores in Asia Pacific, 19 stores in North America, and nine stores in Europe. The increase in net revenue from our company-operated stores was also driven by increased comparable store sales. Comparable store sales increased 14%, or 17% on a constant dollar basis. The increase in comparable store sales was primarily a result of increased store traffic and increased dollar value per transaction, partially offset by a decrease in conversion rates.

Direct to Consumer. Direct to consumer net revenue increased 31%, or 34% on a constant dollar basis. The increase in net revenue from our direct to consumer segment was primarily a result of increased traffic, partially offset by a decrease in conversion rates and a lower dollar value per transaction.

Other. The increase in other net revenue was primarily due to increased outlet sales, sales to wholesale accounts, recommerce revenue, license and supply arrangement revenue, and revenue from our pop up locations. The increase in net revenue was partially offset by a decrease in net revenue from lululemon Studio.

Gross Profit

| | Third Quarter | | | Year over year change |
|--------------|-----------------------|------------|-----------------------|-----------------------|
| | 2022 | 2021 | | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> | <i>(Percentage)</i> |
| Gross profit | \$ 1,038,852 | \$ 829,393 | \$ 209,459 | 25.3 % |
| Gross margin | 55.9 % | 57.2 % | (130) basis points | |

The decrease in gross margin was primarily the result of:

- an increase in costs related to our product departments and distribution centers as a percentage of net revenue of 70 basis points;
- an unfavorable impact of foreign currency exchange rates of 60 basis points; and
- a net decrease in product margin of 40 basis points, primarily due to higher markdowns as well as higher damages, shrink and a reduction in inventory provisions in the prior year. This was partially offset by lower air freight costs from rate reductions and reduced usage.

The decrease in gross margin was partially offset by a decrease in occupancy and depreciation costs as a percentage of net revenue of 40 basis points, driven primarily by the increase in net revenue.

Selling, General and Administrative Expenses

| | Third Quarter | | | Year over year change |
|---|-----------------------|------------|-----------------------|-----------------------|
| | 2022 | 2021 | | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> | <i>(Percentage)</i> |
| Selling, general and administrative expenses | \$ 684,236 | \$ 545,124 | \$ 139,112 | 25.5 % |
| Selling, general and administrative expenses as a percentage of net revenue | 36.8 % | 37.6 % | (80) basis points | |

The increase in selling, general and administrative expenses was primarily due to:

- an increase in costs related to our operating channels of \$72.0 million, comprised of:
 - an increase in variable costs of \$27.6 million primarily due to an increase in distribution costs and credit card fees, as a result of increased net revenue;
 - an increase in employee costs of \$26.9 million primarily due to an increase in salaries and wages expense and incentive compensation in our company-operated stores and direct to consumer channels, primarily from the growth in our business as well as increased wage rates;

- an increase in brand and community costs of \$12.8 million primarily due to an increase in digital marketing expenses related to our direct to consumer channel, partially offset by a decrease in marketing expenses related to lululemon Studio; and
- an increase in other operating costs of \$4.7 million primarily due to increased repairs and maintenance costs, depreciation, and technology costs, partially offset by a decrease in professional fees.
- an increase in head office costs of \$62.6 million, comprised of:
 - an increase in employee costs of \$33.9 million primarily due to an increase in salaries and wages and incentive compensation, primarily as a result of headcount growth and increased wage rates, and due to increased travel costs; and
 - an increase in other costs of \$28.7 million primarily due to an increase in depreciation, technology costs, and professional fees, partially offset by lower charitable donations as a result of timing.
- an increase in net foreign currency exchange and derivative revaluation losses of \$4.5 million.

Amortization of Intangible Assets

| | Third Quarter | | | |
|-----------------------------------|-----------------------|----------|-----------------------|---------------------|
| | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> | <i>(Percentage)</i> |
| Amortization of intangible assets | \$ 2,189 | \$ 2,195 | \$ (6) | (0.3)% |

The amortization of intangible assets was primarily the result of the amortization of intangible assets recognized upon the acquisition of MIRROR.

Acquisition-Related Expenses

| | Third Quarter | | | |
|------------------------------|-----------------------|-----------|-----------------------|---------------------|
| | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> | <i>(Percentage)</i> |
| Acquisition-related expenses | \$ — | \$ 24,127 | \$ (24,127) | (100.0)% |

In connection with our acquisition of MIRROR, we recognized acquisition-related compensation expenses of \$23.8 million and integration related costs of \$0.3 million in the third quarter of 2021. There were no acquisition-related expenses in the third quarter of 2022.

Income from Operations

On a segment basis, we determine income from operations without taking into account our general corporate expenses. Segmented income from operations is summarized below.

| | Third Quarter | | | | | |
|-----------------------------------|----------------|------------|---|--------|-----------------------|--------------|
| | 2022 | | 2021 | | Year over year change | |
| | (In thousands) | | (Percentage of net revenue of respective operating segment) | | (In thousands) | (Percentage) |
| Segmented income from operations: | | | | | | |
| Company-operated stores | \$ 242,733 | \$ 180,700 | 26.9 % | 25.6 % | \$ 62,033 | 34.3 % |
| Direct to consumer | 321,742 | 257,050 | 41.9 | 43.8 | 64,692 | 25.2 |
| Other | 24,911 | 27,450 | 13.4 | 17.5 | (2,539) | (9.2) |
| | \$ 589,386 | \$ 465,200 | | | \$ 124,186 | 26.7 % |
| General corporate expense | 234,770 | 180,931 | | | 53,839 | 29.8 |
| Amortization of intangible assets | 2,189 | 2,195 | | | (6) | — |
| Acquisition-related expenses | — | 24,127 | | | (24,127) | (100.0) |
| Income from operations | \$ 352,427 | \$ 257,947 | | | \$ 94,480 | 36.6 % |
| Operating margin | 19.0 % | 17.8 % | | | 120 basis points | |

Company-Operated Stores. The increase in income from operations from our company-operated stores was primarily the result of increased gross profit of \$99.7 million, driven by increased net revenue and higher gross margin. The increase in gross margin was primarily due to leverage on occupancy and depreciation costs as a result of increased net revenue, partially offset by deleverage in costs from our distribution centers and product teams and by an unfavorable impact of foreign currency exchange rates. The increase in gross profit was partially offset by an increase in selling, general and administrative expenses, primarily due to higher employee and operating costs. Employee costs increased primarily due to higher salaries and wages expense and higher incentive compensation as a result of the growth in our business and increased wage rates. Store operating costs increased primarily due to increases in credit card fees and distribution costs, as a result of higher net revenue, as well as increased repairs and maintenance. Income from operations as a percentage of company-operated stores net revenue increased due to leverage on selling, general and administrative expenses and higher gross margin.

Direct to Consumer. The increase in income from operations from our direct to consumer segment was primarily the result of increased gross profit of \$108.5 million, driven by increased net revenue, partially offset by lower gross margin. The decrease in gross margin was primarily due to lower product margin driven by higher markdowns and an unfavorable impact of foreign currency exchange rates. The increase in gross profit was partially offset by an increase in selling, general and administrative expenses, primarily due to higher variable operating costs including distribution costs and credit card fees, as a result of higher net revenue, as well as higher digital marketing expenses, employee costs from the growth in our business and increased wage rates, technology costs, and depreciation. Income from operations as a percentage of direct to consumer net revenue decreased primarily due to lower gross margin and deleverage on selling, general and administrative expenses.

Other. The decrease in income from operations from our other channels was the result of increased selling, general and administrative expenses, primarily due to higher employee costs from the growth in our business and increased wage rates, partially offset by reduced lululemon Studio marketing expenses. The increase in selling, general and administrative expenses was partially offset by increased gross profit of \$1.3 million. Income from operations as a percentage of other net revenue decreased primarily due to lower gross margin, partially offset by leverage on selling, general and administrative expenses.

General Corporate Expense. The increase in general corporate expense was primarily due to increased employee costs, primarily from headcount growth and increased wage rates, as well as technology costs, and depreciation, partially offset by decreased charitable donations as a result of timing. The increase in general corporate expense was also due to an increase in net foreign currency exchange and derivative revaluation losses of \$4.5 million.

Other Income (Expense), Net

| | Third Quarter | | |
|-----------------------------|-----------------------|-------|-----------------------|
| | 2022 | 2021 | Year over year change |
| | <i>(In thousands)</i> | | <i>(Percentage)</i> |
| Other income (expense), net | \$ 331 | \$ 15 | \$ 316 2,106.7 % |

The increase in other income, net was primarily due to an increase in interest income from higher interest rates.

Income Tax Expense

| | Third Quarter | | |
|--------------------|-----------------------|-----------|-----------------------|
| | 2022 | 2021 | Year over year change |
| | <i>(In thousands)</i> | | <i>(Percentage)</i> |
| Income tax expense | \$ 97,288 | \$ 70,174 | \$ 27,114 38.6 % |
| Effective tax rate | 27.6 % | 27.2 % | 40 basis points |

Certain non-deductible expenses incurred in connection with the MIRROR acquisition increased the effective tax rate in the third quarter of 2021 by 210 basis points.

The effective tax rate for the third quarter of 2022 has increased compared to the third quarter of 2021 primarily due to the accrual of withholding taxes on unremitted foreign earnings and a decrease in deductions related to stock-based compensation. This was partially offset by favorable adjustments upon the filing of certain income tax returns.

Net Income

| | Third Quarter | | |
|------------|-----------------------|------------|-----------------------|
| | 2022 | 2021 | Year over year change |
| | <i>(In thousands)</i> | | <i>(Percentage)</i> |
| Net income | \$ 255,470 | \$ 187,788 | \$ 67,682 36.0 % |

The increase in net income was primarily due to an increase in gross profit of \$209.5 million, and a decrease in acquisition-related expenses of \$24.1 million, partially offset by an increase in selling, general and administrative expenses of \$139.1 million and an increase in income tax expense of \$27.1 million.

Year-to-Date Results of Operations: First Three Quarters Results

The following table summarizes key components of our results of operations for the periods indicated:

| | First Three Quarters | | | |
|--|-----------------------|--------------|----------------------|---------|
| | 2022 | 2021 | 2022 | 2021 |
| | <i>(In thousands)</i> | | <i>(Percentages)</i> | |
| Net revenue | \$ 5,338,680 | \$ 4,127,504 | 100.0 % | 100.0 % |
| Cost of goods sold | 2,373,959 | 1,755,111 | 44.5 | 42.5 |
| Gross profit | 2,964,721 | 2,372,393 | 55.5 | 57.5 |
| Selling, general and administrative expenses | 1,954,340 | 1,583,075 | 36.6 | 38.4 |
| Amortization of intangible assets | 6,579 | 6,585 | 0.1 | 0.2 |
| Acquisition-related expenses | — | 39,934 | — | 1.0 |
| Gain on disposal of assets | (10,180) | — | (0.2) | — |
| Income from operations | 1,013,982 | 742,799 | 19.0 | 18.0 |
| Other income (expense), net | 454 | 338 | — | — |
| Income before income tax expense | 1,014,436 | 743,137 | 19.0 | 18.0 |
| Income tax expense | 279,447 | 202,319 | 5.2 | 4.9 |
| Net income | \$ 734,989 | \$ 540,818 | 13.8 % | 13.1 % |

Net Revenue

Net revenue increased \$1.2 billion, or 29%, to \$5.3 billion for the first three quarters of 2022 from \$4.1 billion for the first three quarters of 2021. On a constant dollar basis, assuming the average foreign currency exchange rates for the first three quarters of 2022 remained constant with the average foreign currency exchange rates for the first three quarters of 2021, net revenue increased \$1.3 billion, or 32%.

The increase in net revenue was primarily due to increased company-operated store net revenue, including from new company-operated stores and increased comparable store sales, as well as due to increased direct to consumer net revenue. Other net revenue also increased.

Total comparable sales, which includes comparable store sales and direct to consumer net revenue, increased 24% for the first three quarters of 2022 compared to the first three quarters of 2021. Total comparable sales increased 26% on a constant dollar basis.

Net revenue for the first three quarters of 2022 and 2021 is summarized below.

| | First Three Quarters | | | | | |
|-------------------------|-----------------------|--------------|----------------------|---------|-----------------------|---------------------|
| | 2022 | 2021 | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(Percentages)</i> | | <i>(In thousands)</i> | <i>(Percentage)</i> |
| Company-operated stores | \$ 2,537,741 | \$ 1,938,864 | 47.5 % | 47.0 % | \$ 598,877 | 30.9 % |
| Direct to consumer | 2,264,029 | 1,729,040 | 42.4 | 41.9 | 534,989 | 31.0 |
| Other | 536,910 | 459,600 | 10.1 | 11.1 | 77,310 | 16.8 |
| Net revenue | \$ 5,338,680 | \$ 4,127,504 | 100.0 % | 100.0 % | \$ 1,211,176 | 29.3 % |

Company-Operated Stores. The increase in net revenue from our company-operated stores was driven by net revenue from company-operated stores that we opened or significantly expanded since the third quarter of 2021 which contributed \$322.7 million to the increase. We have opened 71 net new company-operated stores since the third quarter of 2021, including 43 stores in Asia Pacific, 19 stores in North America, and nine stores in Europe. The increase in net revenue from our company-operated stores was also driven by increased comparable store sales. Comparable store sales increased 17%, or 19% on a constant dollar basis. The increase in comparable store sales was primarily a result of increased store traffic, partially offset by a decrease in conversion rates. Dollar value per transaction was consistent year over year.

Direct to Consumer. Direct to consumer net revenue increased 31%, or 33% on a constant dollar basis. The increase in net revenue from our direct to consumer segment was primarily a result of increased traffic, partially offset by a decrease in conversion rates and a lower dollar value per transaction.

Other. The increase in other net revenue was primarily due to increased outlet sales, sales to wholesale accounts, license and supply arrangement revenue, recommerce revenue, and revenue from our pop up locations. The increase in net revenue was partially offset by a decrease in net revenue from lululemon Studio.

Gross Profit

| | First Three Quarters | | |
|--------------|----------------------|----------------|-----------------------|
| | 2022 | 2021 | Year over year change |
| | (In thousands) | (In thousands) | (Percentage) |
| Gross profit | \$ 2,964,721 | \$ 2,372,393 | \$ 592,328 25.0 % |
| Gross margin | 55.5 % | 57.5 % | (200) basis points |

The decrease in gross margin was primarily the result of:

- a decrease in product margin of 180 basis points, primarily due to higher markdowns and higher air freight costs as a result of global supply chain disruption;
- an increase in costs related to our product departments and distribution centers as a percentage of net revenue of 40 basis points; and
- an unfavorable impact of foreign currency exchange rates of 40 basis points.

The decrease in gross margin was partially offset by a decrease in occupancy and depreciation costs as a percentage of net revenue of 60 basis points, driven primarily by the increase in net revenue.

Selling, General and Administrative Expenses

| | First Three Quarters | | |
|---|----------------------|----------------|-----------------------|
| | 2022 | 2021 | Year over year change |
| | (In thousands) | (In thousands) | (Percentage) |
| Selling, general and administrative expenses | \$ 1,954,340 | \$ 1,583,075 | \$ 371,265 23.5 % |
| Selling, general and administrative expenses as a percentage of net revenue | 36.6 % | 38.4 % | (180) basis points |

The increase in selling, general and administrative expenses was primarily due to:

- an increase in head office costs of \$199.1 million, comprised of:
 - an increase in employee costs of \$101.3 million primarily due to an increase in salaries and wages expense, incentive compensation, and stock-based compensation expense, primarily as a result of headcount growth and increased wage rates, as well as increased travel costs; and
 - an increase in costs of \$97.8 million primarily due to an increase in depreciation, technology costs, brand and community costs, and professional fees.
- an increase in costs related to our operating channels of \$166.9 million, comprised of:
 - an increase in variable costs of \$73.9 million primarily due to an increase in distribution costs and credit card fees, as a result of increased net revenue;
 - an increase in employee costs of \$73.4 million primarily due to an increase in salaries and wages expense and incentive compensation in our company-operated store and direct to consumer channels, primarily due to growth in our business and increased wage rates;
 - an increase in other operating costs of \$17.1 million primarily due to an increase in depreciation, repairs and maintenance costs, and technology costs, partially offset by a decrease in professional fees; and
 - an increase in brand and community costs of \$2.6 million primarily due to an increase in digital marketing expenses related to our direct to consumer channel, partially offset by a decrease in marketing expenses related to lululemon Studio.

- an increase in net foreign currency exchange and derivative revaluation losses of \$5.2 million.

Amortization of Intangible Assets

| | First Three Quarters | | | |
|-----------------------------------|-----------------------|----------|---|--------|
| | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> <i>(Percentage)</i> | |
| Amortization of intangible assets | \$ 6,579 | \$ 6,585 | \$ (6) | (0.1)% |

The amortization of intangible assets was primarily the result of the amortization of intangible assets recognized upon the acquisition of MIRROR.

Acquisition-Related Expenses

| | First Three Quarters | | | |
|------------------------------|-----------------------|-----------|---|----------|
| | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> <i>(Percentage)</i> | |
| Acquisition-related expenses | \$ — | \$ 39,934 | \$ (39,934) | (100.0)% |

In connection with our acquisition of MIRROR, we recognized acquisition-related compensation expenses of \$38.1 million and integration related costs of \$1.9 million in the first three quarters of 2021. There were no acquisition-related expenses in the first three quarters of 2022.

Gain on Disposal of Assets

| | First Three Quarters | | | |
|----------------------------|-----------------------|------|---|-----|
| | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> <i>(Percentage)</i> | |
| Gain on disposal of assets | \$ (10,180) | \$ — | \$ 10,180 | n/a |

During the second quarter of 2022, we completed the sale of an administrative office building, which resulted in a pre-tax gain of \$10.2 million.

Income from Operations

On a segment basis, we determine income from operations without taking into account our general corporate expenses. Segmented income from operations is summarized below.

| | First Three Quarters | | | | | |
|-----------------------------------|-----------------------|--------------|--|--------|---|---------|
| | 2022 | 2021 | 2022 | 2021 | Year over year change | |
| | <i>(In thousands)</i> | | <i>(Percentage of net revenue of respective operating segment)</i> | | <i>(In thousands)</i> <i>(Percentage)</i> | |
| Segmented income from operations: | | | | | | |
| Company-operated stores | \$ 660,246 | \$ 464,844 | 26.0 % | 24.0 % | \$ 195,402 | 42.0 % |
| Direct to consumer | 933,272 | 754,231 | 41.2 | 43.6 | 179,041 | 23.7 |
| Other | 74,064 | 64,196 | 13.8 | 14.0 | 9,868 | 15.4 |
| | \$ 1,667,582 | \$ 1,283,271 | | | \$ 384,311 | 29.9 % |
| General corporate expense | 657,201 | 493,953 | | | 163,248 | 33.0 |
| Amortization of intangible assets | 6,579 | 6,585 | | | (6) | — |
| Acquisition-related expenses | — | 39,934 | | | (39,934) | (100.0) |
| Gain on disposal of assets | (10,180) | — | | | 10,180 | n/a |
| Income from operations | \$ 1,013,982 | \$ 742,799 | | | \$ 271,183 | 36.5 % |
| Operating margin | 19.0 % | 18.0 % | | | 100 basis points | |

Company-Operated Stores. The increase in income from operations from our company-operated stores was primarily the result of increased gross profit of \$298.1 million, driven by increased net revenue. The increase in gross profit was

partially offset by an increase in selling, general and administrative expenses, primarily due to higher employee and operating costs. Employee costs increased primarily due to higher salaries and wages expense and higher incentive compensation as a result of the growth in our business and increased wage rates. Store operating costs increased primarily due to increases in credit card fees and distribution costs as a result of higher net revenue, as well as increased repairs and maintenance. Income from operations as a percentage of company-operated stores net revenue increased due to leverage on selling, general and administrative expenses.

Direct to Consumer. The increase in income from operations from our direct to consumer segment was primarily the result of increased gross profit of \$290.1 million, driven by increased net revenue, partially offset by lower gross margin. The decrease in gross margin was primarily due to lower product margin driven by higher markdowns, increased air freight costs, and an unfavorable impact of foreign currency exchange rates. The increase in gross profit was partially offset by an increase in selling, general and administrative expenses primarily due to higher variable costs including distribution costs and credit card fees as a result of higher net revenue, as well as higher digital marketing expenses, employee costs from the growth in our business and increased wage rates, depreciation and technology costs. Income from operations as a percentage of direct to consumer net revenue decreased for the first three quarters of 2022, compared to the first three quarters of 2021, primarily due to decreased gross margin, partially offset by leverage on selling, general and administrative expenses.

Other. The increase in income from operations from our other channels was primarily the result of decreased selling, general and administrative expenses driven by reduced lululemon Studio marketing expenses. The increase in income from operations from our other channels was also due to increased gross profit of \$4.2 million, driven by increased net revenue, partially offset by lower gross margin. Income from operations as a percentage of other net revenue decreased primarily due to lower gross margin, partially offset by lower selling, general and administrative expenses.

General Corporate Expense. The increase in general corporate expense was primarily due to increased employee costs, primarily from headcount growth and increased wage rates, as well as increased technology costs, brand and community costs, professional fees, and depreciation. The increase in general corporate expense was also due to an increase in net foreign currency exchange and derivative revaluation losses of \$5.2 million.

Other Income (Expense), Net

| | First Three Quarters | | |
|-----------------------------|-----------------------|--------|---|
| | 2022 | 2021 | Year over year change |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> <i>(Percentage)</i> |
| Other income (expense), net | \$ 454 | \$ 338 | \$ 116 34.3 % |

The increase in other income, net was primarily due to an increase in interest income from higher interest rates, partially offset by an increase in other expenses.

Income Tax Expense

| | First Three Quarters | | |
|--------------------|-----------------------|------------|---|
| | 2022 | 2021 | Year over year change |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> <i>(Percentage)</i> |
| Income tax expense | \$ 279,447 | \$ 202,319 | \$ 77,128 38.1 % |
| Effective tax rate | 27.5 % | 27.2 % | 30 basis points |

Certain non-deductible expenses incurred in connection with the MIRROR acquisition increased the effective tax rate in the first three quarters of 2021 by 120 basis points.

A lower tax rate on the capital gain on the sale of an administrative building reduced our effective tax rate in the first three quarters of 2022 by 20 basis points

The increase in the effective tax rate was primarily due to the accrual of withholding taxes on unremitted foreign earnings and a decrease in deductions related to stock-based compensation. This was partially offset by a reduction in non-deductible expenses in international jurisdictions and favorable adjustments upon the filing of certain income tax returns.

Net Income

| | First Three Quarters | | | | |
|------------|-----------------------|------------|-----------------------|--------|---------------------|
| | 2022 | 2021 | Year over year change | | |
| | <i>(In thousands)</i> | | <i>(In thousands)</i> | | <i>(Percentage)</i> |
| Net income | \$ 734,989 | \$ 540,818 | \$ 194,171 | 35.9 % | |

The increase in net income was primarily due to an increase in gross profit of \$592.3 million, a decrease in acquisition-related expenses of \$39.9 million, and a gain on disposal of assets of \$10.2 million in the current year, partially offset by an increase in selling, general and administrative expenses of \$371.3 million, an increase in income tax expense of \$77.1 million, and an increase in other income (expense), net of \$0.1 million.

Comparable Store Sales and Total Comparable Sales

We use comparable store sales to assess the performance of our existing stores as it allows us to monitor the performance of our business without the impact of recently opened or expanded stores. We use total comparable sales to evaluate the performance of our business from an omni-channel perspective. We believe investors would similarly find these metrics useful in assessing the performance of our business.

Comparable store sales reflect net revenue from company-operated stores that have been open, or open after being significantly expanded, for at least 12 full fiscal months. Net revenue from a store is included in comparable store sales beginning with the first fiscal month for which the store has a full fiscal month of sales in the prior year. Comparable store sales exclude sales from new stores that have not been open for at least 12 full fiscal months, from stores which have not been in their significantly expanded space for at least 12 full fiscal months, and from stores which have been temporarily relocated for renovations or temporarily closed. Comparable store sales also exclude sales from direct to consumer and our other operations, as well as sales from company-operated stores that have closed.

Total comparable sales combines comparable store sales and direct to consumer net revenue.

In fiscal years with 53 weeks, the 53rd week of net revenue is excluded from the calculation of comparable sales. In the year following a 53 week year, the prior year period is shifted by one week to compare similar calendar weeks.

Opening new stores and expanding existing stores is an important part of our growth strategy. Accordingly, total comparable sales is just one way of assessing the success of our growth strategy insofar as comparable sales do not reflect the performance of stores opened, or significantly expanded, within the last 12 full fiscal months. The comparable sales measures we report may not be equivalent to similarly titled measures reported by other companies.

Non-GAAP Financial Measures

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

A constant dollar basis assumes the average foreign currency exchange rates for the period remained constant with the average foreign currency exchange rates for the same period of the prior year. We provide constant dollar changes in our results to help investors understand the underlying growth rate of net revenue excluding the impact of changes in foreign currency exchange rates.

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

Constant Dollar Changes in Net Revenue

The below changes in net revenue show the change compared to the corresponding period in the prior year.

| | Third Quarter 2022 | | First Three Quarters 2022 | |
|---|--------------------|---------------|---------------------------|---------------|
| | Net Revenue | | Net Revenue | |
| | (In thousands) | (Percentages) | (In thousands) | (Percentages) |
| Change | \$ 406,468 | 28 % | \$ 1,211,176 | 29 % |
| Adjustments due to foreign currency exchange rate changes | 48,946 | 3 | 91,338 | 3 % |
| Change in constant dollars | \$ 455,414 | 31 % | \$ 1,302,514 | 32 % |

Constant Dollar Changes in Total Comparable Sales, Comparable Store Sales, and Direct to Consumer Net Revenue

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

| | Third Quarter 2022 | | | First Three Quarters 2022 | | |
|---|---------------------------------------|-------------------------------------|--------------------------------|---------------------------------------|-------------------------------------|--------------------------------|
| | Total Comparable Sales ^{1,2} | Comparable Store Sales ² | Direct to Consumer Net Revenue | Total Comparable Sales ^{1,2} | Comparable Store Sales ² | Direct to Consumer Net Revenue |
| Change | 22 % | 14 % | 31 % | 24 % | 17 % | 31 % |
| Adjustments due to foreign currency exchange rate changes | 3 | 3 | 3 | 2 | 2 | 2 |
| Change in constant dollars | 25 % | 17 % | 34 % | 26 % | 19 % | 33 % |

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

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

Seasonality

Our business is affected by the general seasonal trends common to the retail apparel industry. Our annual net revenue is weighted more heavily toward our fourth fiscal quarter, reflecting our historical strength in sales during the holiday season, while our operating expenses are more equally distributed throughout the year. As a result, a substantial portion of our operating profits are generated in the fourth quarter of our fiscal year. For example, we generated approximately 44% and 56% of our full year operating profit during the fourth quarters of 2021 and 2020, respectively. Due to a significant number of our company-operated stores being temporarily closed due to COVID-19 during the first two quarters of 2020, we earned a higher proportion of our operating profit during the last two quarters of 2020 compared to 2021.

Liquidity and Capital Resources

Our primary sources of liquidity are our current balances of cash and cash equivalents, cash flows from operations, and capacity under our committed revolving credit facility, including to fund short-term working capital requirements. Our primary cash needs are capital expenditures for opening new stores and remodeling or relocating existing stores, investing in our distribution centers, investing in technology and making system enhancements, funding working capital requirements, and making other strategic capital investments both in North America and internationally. We may also use cash to repurchase shares of our common stock. Cash and cash equivalents in excess of our needs are held in interest bearing accounts with financial institutions, as well as in money market funds and term deposits.

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

| | First Three Quarters | | |
|--|-----------------------|--------------|-----------------------|
| | 2022 | 2021 | Year over year change |
| | <i>(In thousands)</i> | | |
| Total cash provided by (used in): | | | |
| Operating activities | \$ (79,801) | \$ 658,124 | \$ (737,925) |
| Investing activities | (386,862) | (313,438) | (73,424) |
| Financing activities | (399,428) | (523,197) | 123,769 |
| Effect of foreign currency exchange rate changes on cash | (41,156) | 21,585 | (62,741) |
| Increase (decrease) in cash and cash equivalents | \$ (907,247) | \$ (156,926) | \$ (750,321) |

Operating Activities

The increase in cash used in operating activities was primarily as a result of:

- a decrease in cash flows from the changes in operating assets and liabilities of \$929.4 million. This decrease was primarily driven by \$543.2 million from inventories, as well as changes in income taxes, accrued compensation, accrued liabilities and other, and prepaid expenses and other current assets; and
- changes in adjusting items of \$2.7 million, primarily driven by lower cash inflows related to derivatives not designated in a hedging relationship and the gain on disposal of assets, partially offset by increased depreciation and stock-based compensation expenses.

The increase in cash used in operating activities was partially offset by increased net income of \$194.2 million.

Investing Activities

The increase in cash used in investing activities was primarily due to increased capital expenditures, partially offset by the settlement of net investment hedges and other investing activities. The increase in capital expenditures was primarily due to corporate expenditures driven by investment in technology and business systems and increased expenditures on corporate office renovations. There has also been an increase in company-operated store expenditures driven by opening new stores and remodeling existing stores as well as increased investment in our new and existing distribution facilities. This was partially offset by decreased capital expenditures for our direct to consumer segment. The proceeds of the sale of an administrative office building during the second quarter of 2022 are included in other investing activities.

Financing Activities

The decrease in cash used in financing activities was primarily the result of a decrease in stock repurchases. Cash used in financing activities for the first three quarters of 2022 included \$375.0 million to repurchase 1.2 million shares of our common stock compared to \$491.3 million to repurchase 1.4 million shares for the first three quarters of 2021. The common stock was repurchased in the open market at prevailing market prices, including under plans complying with the provisions of Rule 10b5-1 and Rule 10b-18 of the Securities Exchange Act of 1934, with the timing and actual number of shares repurchased depending upon market conditions, eligibility to trade, and other factors.

Liquidity Outlook

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

The following table includes certain measures of our liquidity:

| | October 30, 2022 |
|--|-----------------------|
| | <i>(In thousands)</i> |
| Cash and cash equivalents | \$ 352,624 |
| Working capital excluding cash and cash equivalents ⁽¹⁾ | 958,722 |
| Capacity under committed revolving credit facility | 394,821 |

(1) Working capital is calculated as current assets of \$2.6 billion less current liabilities of \$1.3 billion.

We enter into standby letters of credit to secure certain of our obligations, including leases, taxes, and duties. As of October 30, 2022, letters of credit and letters of guarantee totaling \$6.7 million had been issued, including \$5.2 million under our committed revolving credit facility.

Our committed North America credit facility provides for \$400.0 million in commitments under an unsecured five-year revolving credit facility. The credit facility has a maturity date of December 14, 2026, subject to extension under certain circumstances. As of October 30, 2022, aside from letters of credit of \$5.2 million, we had no other borrowings outstanding under this credit facility. Further information regarding our credit facilities and associated covenants is outlined in Note 5. Revolving Credit Facilities included in Item 1 of Part I of this report.

The timing and cost of our inventory purchases will vary depending on a variety of factors such as revenue growth, assortment and purchasing decisions, product costs including freight and duty, and the availability of production capacity and speed. Our inventory balance as of October 30, 2022 was \$1.7 billion, an increase of 85% from October 31, 2021. On a number of units basis, our inventory increased 80% compared to October 31, 2021.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions. Predicting future events is inherently an imprecise activity and, as such, requires the use of judgment. Actual results may vary from our estimates in amounts that may be material to the financial statements. An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact our consolidated financial statements.

Our critical accounting policies and estimates are discussed within "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" of our 2021 Annual Report on Form 10-K filed with the SEC on March 29, 2022.

Goodwill Impairment Assessment

Goodwill is tested annually for impairment on the first day of the fourth quarter, or more frequently if events or circumstances indicate it is more likely than not that an impairment may have occurred.

There is \$362.5 million of goodwill allocated to the MIRROR reporting unit, which was renamed the "lululemon Studio" reporting unit during the third quarter of 2022. As of October 30, 2022, we concluded that the deterioration in macroeconomic conditions and trends in the digital fitness industry indicated a potentially adverse change in the fair value of the lululemon Studio reporting unit, and therefore we performed a quantitative impairment analysis. The result of the analysis concluded that the fair value of the lululemon Studio reporting unit exceeded its carrying value, and no impairment has been recognized.

We used a discounted cash flow model to estimate the fair value, supplemented by market analysis, which indicated the fair value of lululemon Studio was approximately 4% higher than its carrying value. The key assumptions of the fair value of the lululemon Studio reporting unit are the revenue growth rates, operating profit margins, and the discount rate. Our ability to generate expected cash flows is dependent on several factors including, but not limited to, customer demand and trends in the connected fitness industry including the level of desire to exercise at home, our ability to attract new subscribers to grow the community, and our ability to maintain a loyal subscriber base. The fair value of lululemon Studio is also dependent on the ability of lululemon Studio to achieve long term profitability.

Failure to increase the growth rate of new subscribers in the near term, or if we are unable to reduce customer acquisition costs, or other internal or external factors, could cause a material impairment of goodwill.

Operating Locations

Our company-operated stores by country as of October 30, 2022 and January 30, 2022 are summarized in the table below.

| Number of company-operated stores by country | October 30, 2022 | January 30, 2022 |
|--|------------------|------------------|
| United States | 337 | 324 |
| People's Republic of China ⁽¹⁾ | 105 | 86 |
| Canada | 66 | 63 |
| Australia | 31 | 31 |
| United Kingdom | 20 | 17 |
| South Korea | 16 | 12 |
| Germany | 10 | 9 |
| New Zealand | 8 | 7 |
| Singapore | 8 | 6 |
| Japan | 6 | 6 |
| Ireland | 4 | 3 |
| France | 3 | 3 |
| Malaysia | 2 | 2 |
| Spain | 2 | — |
| Sweden | 2 | 2 |
| Netherlands | 1 | 1 |
| Norway | 1 | 1 |
| Switzerland | 1 | 1 |
| Total company-operated stores | 623 | 574 |

⁽¹⁾ Included within PRC as of October 30, 2022, were nine stores in Hong Kong Special Administrative Region, six stores in Taiwan, and two stores in Macao Special Administration Region. As of January 30, 2022, there were nine stores in Hong Kong Special Administrative Region, five stores in Taiwan, and two stores in Macao Special Administration Region.

Retail locations operated by third parties under license and supply arrangements are not included in the above table. As of October 30, 2022, there were 22 licensed locations, including 11 in Mexico, seven in the United Arab Emirates, three in Qatar, and one in Kuwait.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Risk. The functional currency of our international subsidiaries is generally the applicable local currency. Our consolidated financial statements are presented in U.S. dollars. Therefore, the net revenue, expenses, assets, and liabilities of our international subsidiaries are translated from their functional currencies into U.S. dollars. Fluctuations in the value of the U.S. dollar affect the reported amounts of net revenue, expenses, assets, and liabilities. Foreign currency exchange differences which arise on translation of our international subsidiaries' balance sheets into U.S. dollars are recorded as other comprehensive income (loss), net of tax in accumulated other comprehensive income or loss within stockholders' equity.

We also have exposure to changes in foreign currency exchange rates associated with transactions which are undertaken by our subsidiaries in currencies other than their functional currency. Such transactions include intercompany transactions and inventory purchases denominated in currencies other than the functional currency of the purchasing entity. As a result, we have been impacted by changes in foreign currency exchange rates and may be impacted for the foreseeable future. The potential impact of currency fluctuation increases as our international expansion increases.

As of October 30, 2022, we had certain forward currency contracts outstanding in order to hedge a portion of the foreign currency exposure that arises on translation of a Canadian subsidiary into U.S. dollars. We also had certain forward currency contracts outstanding in an effort to reduce our exposure to the foreign currency exchange revaluation gains and losses that are recognized by our Canadian and Chinese subsidiaries on U.S. dollar denominated monetary assets and liabilities. Please refer to Note 8. Derivative Financial Instruments included in Item 1 of Part I of this report for further information, including details of the notional amounts outstanding.

In the future, in an effort to reduce foreign currency exchange risks, we may enter into further derivative financial instruments including hedging additional currency pairs. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

We currently generate a significant portion of our net revenue and incur a significant portion of our expenses in Canada. We also hold a significant portion of our net assets in Canada. The reporting currency for our consolidated financial statements is the U.S. dollar. A strengthening of the U.S. dollar against the Canadian dollar results in:

- the following impacts to the consolidated statements of operations:
 - a decrease in our net revenue upon translation of the sales made by our Canadian operations into U.S. dollars for the purposes of consolidation;
 - a decrease in our selling, general and administrative expenses incurred by our Canadian operations upon translation into U.S. dollars for the purposes of consolidation;
 - foreign currency exchange revaluation gains by our Canadian subsidiaries on U.S. dollar denominated monetary assets and liabilities; and
 - derivative valuation losses on forward currency contracts not designated in a hedging relationship;
- the following impacts to the consolidated balance sheets:
 - a decrease in the foreign currency translation adjustment which arises on the translation of our Canadian subsidiaries' balance sheets into U.S. dollars; and
 - net investment hedge losses from derivative valuation losses on forward currency contracts, entered into as net investment hedges of a Canadian subsidiary.

During the first three quarters of 2022, the change in the relative value of the U.S. dollar against the Canadian dollar resulted in a \$83.0 million increase in accumulated other comprehensive loss within stockholders' equity. During the first three quarters of 2021, the change in the relative value of the U.S. dollar against the Canadian dollar resulted in a \$35.6 million reduction in accumulated other comprehensive loss within stockholders' equity.

A 10% appreciation in the relative value of the U.S. dollar against the Canadian dollar compared to the foreign currency exchange rates in effect for the first three quarters of 2022 would have resulted in lower income from operations of approximately \$26.9 million. This assumes a consistent 10% appreciation in the U.S. dollar against the Canadian dollar over the first three quarters of 2022. The timing of changes in the relative value of the U.S. dollar combined with the seasonal nature of our business, can affect the magnitude of the impact that fluctuations in foreign currency exchange rates have on our income from operations.

Interest Rate Risk. Our committed revolving credit facility provides us with available borrowings in an amount up to \$400.0 million. Because our revolving credit facilities bear interest at a variable rate, we will be exposed to market risks relating to changes in interest rates, if we have a meaningful outstanding balance. As of October 30, 2022, aside from letters of credit of \$5.2 million, there were no borrowings outstanding under these credit facilities. We currently do not engage in any interest rate hedging activity and currently have no intention to do so. However, in the future, if we have a meaningful outstanding balance under our revolving facility, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. These may take the form of forward contracts, option contracts, or interest rate swaps. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Our cash and cash equivalent balances are held in the form of cash on hand, bank balances, and short-term deposits with original maturities of three months or less, and in money market funds. We do not believe these balances are subject to material interest rate risk.

Credit Risk. We have cash on deposit with various large, reputable financial institutions and have invested in AAA-rated money market funds. The amount of cash and cash equivalents held with certain financial institutions exceeds government-insured limits. We are also exposed to credit-related losses in the event of nonperformance by the financial institutions that are counterparties to our forward currency contracts. The credit risk amount is our unrealized gains on our derivative instruments, based on foreign currency rates at the time of nonperformance. We have not experienced any losses related to these items, and we believe credit risk to be minimal. We seek to minimize our credit risk by entering into transactions with credit worthy and reputable financial institutions and by monitoring the credit standing of the financial institutions with whom we transact. We seek to limit the amount of exposure with any one counterparty.

Inflation

Inflationary factors such as increases in the cost of our product, as well as overhead costs and capital expenditures may adversely affect our operating results. During 2021 and the first three quarters of 2022, our operating margin was impacted by higher air freight costs compared to fiscal 2021 and 2020 as a result of global supply chain disruption, as well as increased wage rates. Sustained increases in transportation costs, wages, and raw material costs, or other inflationary pressures in the future may have an adverse effect on our ability to maintain current levels of operating margin if the selling prices of our products do not increase with these increased costs, or we cannot identify cost efficiencies.

ITEM 4. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial and accounting officer, to allow timely decisions to be made regarding required disclosure. We have established a Disclosure Committee, consisting of certain members of management, to assist in this evaluation. The Disclosure Committee meets on a quarterly basis, and as needed.

Our management, including our principal executive officer and principal financial and accounting officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Exchange Act) as of October 30, 2022. Based on that evaluation, our principal executive officer and principal financial and accounting officer concluded that, as of October 30, 2022, our disclosure controls and procedures were effective.

There were no changes in our internal control over financial reporting during the quarter ended October 30, 2022 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.