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Q1 Fiscal 2021 Earnings Commentary

While most of our retail locations remained open throughout the first quarter of fiscal 2021, certain locations were temporarily closed based on government and health authority guidance in those markets, including in parts of Europe and Canada, as well as other markets. In accordance with relevant government and health authority guidance, we continue to operate our distribution centers and retail locations with restrictive and precautionary measures in place. These measures are market dependent and can include restricted occupancy levels, physical distancing, enhanced cleaning and sanitation, and reduced operating hours.

The financial measures discussed below include both GAAP and adjusted non-GAAP financial measures. Please see the section captioned "Reconciliation of Non-GAAP Financial Measures" included in the accompanying financial tables, which include more detail on the GAAP financial measures that are most directly comparable to the non-GAAP financial measures, and the related reconciliation between these financial measures.

This earnings commentary should be read in conjunction with the Company's quarterly report on Form 10-Q filed with the Securities and Exchange Commission ("SEC") on, or about, June 3, 2021 and the Company's annual report on Form 10-K filed with the SEC on March 30, 2021. These reports are available at www.sec.gov.

The below narrative compares the first quarter of fiscal 2021 to the first quarter of fiscal 2020, unless otherwise noted.

Sales

- **Total net revenue** increased 88% to $1.2 billion. The increase was primarily due to increased company-operated store and other net revenue. This was primarily due to net revenue from retail locations that were temporarily closed during Q1 2020, as a result of COVID-19. E-commerce revenue also increased, primarily due to increased traffic, as well as improved conversion rates and an increase in dollar value per transaction. The increase in traffic was partially due to a shift in the way guests are shopping as a result COVID-19. Net revenue increased by a two-year compound annual growth rate ("CAGR") of 25%.

- **Company-operated store revenue** totaled $536.6 million, or 43.8% of total revenue, compared to $260.0 million, or 39.9% of total revenue, in Q1 2020. Company-operated store revenue increased 3% on a two-year CAGR basis.

- **E-commerce revenue** totaled $545.1 million, or 44.4% of total revenue, compared to $352.0 million, or 54.0% of total revenue, in Q1 2020. E-commerce net revenue increased 55%, or increased 50% on a constant dollar basis, and increased 61% on a two-year CAGR basis.

- **Other revenue,** which includes net revenue from outlets, temporary locations, sales to wholesale accounts, license and supply arrangements, and the sales of in-home fitness equipment and associated content subscriptions, totaled $144.8 million, or 11.8% of total net revenue, compared to $40.0 million, or 6.1% of total net revenue, in Q1 2020. Other revenue increased 48% on a two-year CAGR basis.

Store Count

- **New stores**: We opened two net new company-operated stores in Q1 2021 in Asia Pacific.

- **Total company-operated stores**: At the end of Q1 2021, we had 523 total company-operated stores compared to 489 at the end of Q1 2020.

Gross Profit

- **Gross profit** was $700.3 million, or 57.1% of net revenue, compared to $334.4 million, or 51.3% of net revenue, in Q1 2020. Gross margin increased 580 basis points compared to Q1 2020.

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The increase in gross margin was primarily the result of:

- a decrease in depreciation and occupancy costs as a percentage of net revenue of 540 basis points, driven primarily by the increase in net revenue;
- a decrease in costs related to our product departments and our distribution centers as a percentage of net revenue of 100 basis points, primarily due to the increase in net revenue; and
- a favorable impact of foreign exchange rates of 50 basis points.

The increase in gross margin was partially offset by a decrease in product margin of 110 basis points, primarily due to higher air freight costs as a result of COVID-19 impacts on logistics availability and costs, partially offset by lower markdowns and inventory provision expenses.

- **Gross margin** increased 320 basis points compared to Q1 2019 primarily as a result of:
  - leverage on occupancy, depreciation, and our product departments of 220 basis points;
  - an increase in product margin of 80 basis points despite higher air freight costs related to COVID-19 and partly due to lower markdowns; and
  - a favorable impact of foreign exchange rates of 20 basis points.

Selling, General and Administrative Expenses

- **SG&A expenses** were $496.6 million, or 40.5% of net revenue, compared to $299.6 million, or 46.0% of net revenue, in Q1 2020. The leverage of 550 basis points was primarily due to the increase in net revenue, including 280 basis points of leverage from our operating channel costs driven by company-operated stores partially offset by the consolidation of MIRROR's results in 2021 but not 2020, 280 basis points of leverage from head office costs, and 80 basis points from depreciation and amortization. This was partially offset by 90 basis points from the unfavorable impact of foreign exchange rates.
- **SG&A expenses** as a percentage of net revenue increased 310 basis points compared to Q1 2019 primarily due to the consolidation of MIRROR's results in 2021 but not in 2019 as well as higher depreciation due to accelerated investments to support our e-commerce business and operating channel costs related to COVID-19.

Amortization of Intangible Assets and Acquisition-Related Expenses

- **Amortization of intangible assets** was $2.2 million in Q1 2021, an increase from less than $0.1 million in Q1 2020. The increase was the result of amortization of intangible assets recognized upon the acquisition of MIRROR in Q2 2020.
- **Acquisition-related expenses** of $7.7 million were recognized in Q1 2021, compared to $2.0 million in Q1 2020 related to our acquisition of MIRROR.

Operating Income

- **Operating income** was $193.8 million, or 15.8% of net revenue, compared to $32.8 million, or 5.0% of net revenue, in Q1 2020. Adjusted operating income, which excludes acquisition-related expenses, was $201.5 million, or 16.4%, compared to $34.8 million or 5.3% in Q1 2020.
- **Operating margin** decreased 70 basis points compared to Q1 2019. Adjusted operating margin decreased 10 basis points.

Income Tax Expense

- **Income tax expense** was $49.1 million compared to $5.3 million in Q1 2020 and the effective tax rate was 25.3% compared to 15.6% in Q1 2020. The adjusted effective tax rate was 24.5% compared to 14.7% in Q1 2020.

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Net Income

- **Net income** was $145.0 million, or $1.11 per diluted share, compared to $0.22 per diluted share in Q1 2020, and $0.74 in Q1 2019. Adjusted diluted earnings per share were $1.16, compared to $0.23 in Q1 2020.

Share Count

- Our diluted share count for the quarter was 131.0 million compared to 130.8 million in Q1 2020.
- In Q1 2021, we repurchased 0.3 million shares at a cost of $83.8 million.

Capital Expenditures

- **Capital expenditures** were $64.2 million in Q1 2021 compared to $52.1 million in Q1 2020. The increase was primarily the result of increased e-commerce channel capital expenditures driven by investment in our distribution centers.

Balance Sheet Highlights

- Cash and cash equivalents were $1.2 billion at the end of Q1 2021 and the available capacity under our committed revolving credit facility was $397.3 million.
- Inventories increased 17% to $732.9 million at the end of Q1 2021 compared to Q1 2020.

Forward-Looking Statements and Non-GAAP Reconciliations

Forward-Looking Statements:

This supplemental disclosure includes estimates, projections, statements relating to our business plans, objectives, and expected operating results that are "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. In many cases, you can identify forward-looking statements by terms such as "may," "will," "should," "expects," "plans," "anticipates," "outlook," "believes," "intends," "estimates," "predicts," "potential" or the negative of these terms or other comparable terminology. These forward-looking statements also include our guidance and outlook statements. These statements are based on management's current expectations but they involve a number of risks and uncertainties. Actual results and the timing of events could differ materially from those anticipated in the forward-looking statements as a result of risks and uncertainties, which include, without limitation: our ability to maintain the value and reputation of our brand; the current COVID-19 coronavirus pandemic and related government, private sector, and individual consumer responsive actions; our highly competitive market and increasing competition; increasing product costs and decreasing selling prices; our ability to anticipate consumer preferences and successfully develop and introduce new, innovative and updated products; the acceptability of our products to guests; our ability to accurately forecast guest demand for our products; changes in consumer shopping preferences and shifts in distribution channels; our ability to expand internationally in light of our limited operating experience and limited brand recognition in new international markets; our ability to realize the potential benefits and synergies sought with the acquisition of MIRROR; our ability to manage our growth and the increased complexity of our business effectively; our ability to successfully open new store locations in a timely manner; seasonality; our reliance on and limited control over third-party suppliers to provide fabrics for and to produce our products; the operations of many of our suppliers are subject to international and other risks; suppliers or manufacturers not complying with our Vendor Code of Ethics or applicable laws; our ability to deliver our products to the market and to meet guest expectations if we have problems with our distribution system; increasing labor costs and other factors associated with the production of our products in South Asia and South East Asia; our ability to safeguard against security breaches with respect to our information technology systems; our compliance with privacy and data protection laws; any material disruption of our information systems; our ability to have technology-based systems function effectively and grow our e-commerce business globally; climate change, and related legislative and regulatory responses; increased scrutiny regarding our environmental, social, and governance, or sustainability responsibilities; an economic recession, depression, or downturn or economic uncertainty in our key markets; global economic and political conditions and global events such as health pandemics; our ability to source and sell our merchandise profitably or at all if new trade restrictions are imposed or existing trade restrictions become more burdensome; changes in tax laws or unanticipated tax liabilities; our ability to comply with trade and other regulations; fluctuations in foreign currency exchange rates; imitation by our competitors; our ability to protect our intellectual property rights; conflicting trademarks and the prevention of sale of certain products; our exposure to various types of litigation; and other risks and uncertainties set out in filings made from time to time with the United States Securities and Exchange Commission and available at www.sec.gov, including, without limitation, our most recent reports on Form 10-K and Form 10-Q. You are urged to consider these factors carefully in evaluating the forward-looking statements contained herein and are cautioned not to place undue reliance on such forward-looking statements, which are qualified in their entirety by these cautionary statements. The forward-looking statements made herein speak only as of the date of this press release and we undertake no obligation to publicly update such forward-looking statements to reflect subsequent events or circumstances, except as may be required by law.

Reconciliation of Non-GAAP Financial Measures

Unaudited; In thousands, except per share amounts

Constant dollar changes

The below changes show the change for Q1 2021 compared to Q1 2020.

	Change in Net Revenue	Change in Direct to Consumer Net Revenue
Change	88 %	55 %
Adjustments due to foreign exchange rate changes	(5)%	(5)
Change in constant dollars	83 %	50 %

The below table shows comparable store productivity calculated as comparable store sales[1] for Q1 2021 as a percentage of the net revenue generated from these company-operated stores in the corresponding period two years prior, Q1 2019.

	Q1 2021 Compared to Q1 2019
Comparable store productivity	89 %
Adjustments due to foreign exchange rate changes	(1)%
Comparable store productivity in constant dollars	88 %

[1]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. Comparable store sales exclude sales from stores which have been temporarily relocated for renovations or have been temporarily closed.

Adjusted financial measures

The following tables reconcile adjusted financial measures with the most directly comparable measures calculated in accordance with GAAP. The adjustments relate to the acquisition of MIRROR and its related tax effects. Please refer to Note 3. Acquisition included in Item 1 of Part I of our Report on Form 10-Q to be filed with the SEC on or about June 3, 2021 for further information on these adjustments.

	Q1 2021					
	Income from Operations	Operating Margin	Income Tax Expense	Effective Tax Rate	Net Income	Diluted Earnings Per Share
GAAP results	$ 193,821	15.8 %	$ 49,092	25.3 %	$ 144,956	$ 1.11
Transaction and integration costs	496	—			496	—
Acquisition-related compensation	7,168	0.6			7,168	0.05
Tax effect of the above			372	(0.8)	(372)	—
Adjusted results (non-GAAP)	$ 201,485	16.4 %	$ 49,464	24.5 %	$ 152,248	$ 1.16

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	Q1 2020									
	Income from Operations		Operating Margin	Income Tax Expense		Effective Tax Rate	Net Income		Diluted Earnings Per Share	
GAAP results	$	32,751	5.0 %	$	5,293	15.6 %	$	28,632	$	0.22
Transaction and integration costs		2,045	0.3					2,045		0.01
Tax effect of the above					—	(0.9)		—		—
Adjusted results (non-GAAP)	$	34,796	5.3 %	$	5,293	14.7 %	$	30,677	$	0.23