lululemon

Q3 Fiscal 2022 Earnings Commentary

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, December 8, 2022 and the Company's annual report on Form 10-K filed with the SEC on March 29, 2022. These reports are available at www.sec.gov.

The below narrative compares the third quarter of fiscal 2022 to the third quarter of fiscal 2021, unless otherwise noted.

Sales

- **Total net revenue** increased 28% to $1.9 billion, primarily due to increased company-operated store net revenue, including from increased comparable store sales and new company-operated stores, as well as due to increased direct to consumer net revenue. Other net revenue also increased. Net revenue increased 26% in North America, and increased 41% internationally. Total comparable sales increased 22%, or 25% on a constant dollar basis. Net revenue increased by a three-year compound annual growth rate ("CAGR") of 27%.

- **Company-operated store revenue** totaled $903.1 million, or 48.6% of total net revenue, compared to $707.2 million, or 48.8% of total net revenue, in Q3 2021. Comparable store sales increased 14%, or 17% on a constant dollar basis, primarily due to increased store traffic and increased dollar value per transaction, partially offset by a decrease in conversion rates. Company-operated store revenue increased 16% on a three-year CAGR basis.

- **E-commerce revenue** totaled $767.4 million, or 41.3% of total net revenue, compared to $586.5 million, or 40.4% of total net revenue, in Q3 2021. E-commerce net revenue increased 31%, or 34% on a constant dollar basis, primarily due to increased traffic, partially offset by a decrease in conversion rates and lower dollar value per transaction. E-commerce revenue increased 46% on a three-year CAGR basis.

- **Other revenue,** which includes net revenue from outlets, temporary locations, lululemon Studio, sales to wholesale accounts, license and supply arrangements, and recommerce, totaled $186.5 million, or 10.0% of total net revenue, compared to $156.7 million, or 10.8% of total net revenue, in Q3 2021.

Store Count

- **New stores**: We opened 12 net new company-operated stores in Asia Pacific, seven in North America, and four in Europe in Q3 2022.

- **Total company-operated stores**: At the end of Q3 2022, we had 623 total company-operated stores compared to 552 at the end of Q3 2021.

Gross Profit

- **Gross profit** was $1.0 billion, or 55.9% of net revenue, compared to $829.4 million, or 57.2% of net revenue, in Q3 2021. Gross margin decreased 130 basis points compared to Q3 2021.

lululemon

The decrease in gross margin was primarily the result of:

- an unfavorable impact of foreign currency exchange rates of 60 basis points;
- 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; and
- deleverage of 30 basis points on fixed costs, primarily due to an increase in costs related to our product departments and distribution centers, partially offset by leverage on occupancy and depreciation costs.

Selling, General and Administrative Expenses

- **SG&A expenses** were $684.2 million, or 36.8% of net revenue, compared to $545.1 million, or 37.6% of net revenue, in Q3 2021. The leverage of 80 basis points was driven by 70 basis points of net leverage from our operating channels primarily driven by company-operated stores and other, 60 basis points leverage on our head office costs, and 20 basis points leverage from foreign exchange translation. This was partially offset by 70 basis points deleverage from depreciation and amortization.

Operating Income

- **Operating income** was $352.4 million, or 19.0% of net revenue, compared to $257.9 million, or 17.8% of net revenue, in Q3 2021. Adjusted operating income, which excludes acquisition-related expenses, was $282.1 million or 19.4% in Q3 2021.

Income Tax Expense

- **Income tax expense** was $97.3 million compared to $70.2 million in Q3 2021 and the effective tax rate was 27.6%, compared to 27.2% in Q3 2021. The adjusted effective tax rate was 25.1% in Q3 2021.

Net Income

- **Net income** was $255.5 million, or $2.00 per diluted share, compared to $1.44 per diluted share in Q3 2021. Adjusted diluted earnings per share were $1.62 in Q3 2021.

Share Count

- Our diluted share count for the quarter was 127.8 million compared to 130.2 million in Q3 2021.
- In Q3 2022, we repurchased 54.6 thousand shares at an average price of $311.21 per share for a total cost of $17.0 million.

Capital Expenditures

- **Capital expenditures** were $175.6 million in Q3 2022 compared to $122.5 million in Q3 2021. The Q3 2022 capital expenditures were primarily related to investments that support our business growth, including technology investments and our multi-year distribution center project, as well as store capital for new locations, relocations, and renovations.

Balance Sheet Highlights

- **Cash and cash equivalents** were $352.6 million at the end of Q3 2022 and the available capacity under our committed revolving credit facility was $394.8 million.
- **Inventories** increased 85% to $1.7 billion at the end of Q3 2022 compared to Q3 2021.

lululemon

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; changes in consumer shopping preferences and shifts in distribution channels; the acceptability of our products to guests; our highly competitive market and increasing competition; increasing costs and decreasing selling prices; our ability to achieve the synergies and benefits sought through the acquisition of MIRROR (now known as lululemon Studio); the ability of lululemon Studio to generate near and long term expected cash flows which if not achieved could result in a material impairment of goodwill or other assets; our ability to anticipate consumer preferences and successfully develop and introduce new, innovative and updated products; our ability to accurately forecast guest demand for our products; our ability to expand in light of our limited operating experience and limited brand recognition in new international markets and new product categories; 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; disruptions of our supply chain; our reliance on a relatively small number of vendors to supply and manufacture a significant portion of our products; 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 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; the current COVID-19 coronavirus pandemic and related government, private sector, and individual consumer responsive actions; 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 patents 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 disclosure 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.

lululemon

Reconciliation of Non-GAAP Financial Measures

Unaudited; Expressed in thousands, except per share amounts

Constant dollar changes

The below changes show the change for Q3 2022 compared to Q3 2021.

	Net Revenue	Total Comparable Sales[1,2]	Comparable Store Sales[2]	Direct to Consumer Net Revenue
Change	28 %	22 %	14 %	31 %
Adjustments due to foreign currency exchange rate changes	3	3	3	3
Change in constant dollars	31 %	25 %	17 %	34 %

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

Adjusted financial measures

The following table reconciles adjusted financial measures with the most directly comparable measures calculated in accordance with GAAP. The adjustments relate to the acquisition of MIRROR, including accelerated compensation expense related to the transition of the former MIRROR Chief Executive Officer to a temporary advisory role with the Company, and its related tax effects. Please refer to Note 3. Acquisition-Related Expenses included in Item 1 of Part I of our Report on Form 10-Q to be filed with the SEC on or about December 8, 2022 for further information on these adjustments. There were no acquisition-related expenses in the third quarter of 2022.

	Q3 2021					
	Income from Operations	Operating Margin	Income Tax Expense	Effective Tax Rate	Net Income	Diluted Earnings Per Share
GAAP results	$ 257,947	17.8 %	$ 70,174	27.2 %	$ 187,788	$ 1.44
Transaction and integration costs	328	—			328	—
Acquisition-related compensation	23,799	1.6			23,799	0.18
Tax effect of the above			611	(2.1)	(611)	—
Adjusted results (non-GAAP)	$ 282,074	19.4 %	$ 70,785	25.1 %	$ 211,304	$ 1.62