

## Logitech Q1 Fiscal Year 2015 Preliminary Financial Results Management's Prepared Remarks (July 23, 2014)

Logitech is posting a copy of these prepared remarks, its press release and accompanying slides to its investor website. These prepared remarks will not be read on the call. We refer both to GAAP and to non-GAAP financial measures herein. For full GAAP to non-GAAP reconciliation information and cautionary information regarding the use of non-GAAP measures, please refer to "Supplemental Financial Information" in our earnings press release or "Financial Statements only" posted to our website under "Quarterly Results" at <http://ir.logitech.com>. The live webcast or replay of the question and answer session is also available on our website.

As previously disclosed, Logitech's Audit Committee, with the assistance of independent advisors, is conducting an independent investigation of certain accounting matters related to the Company's previously issued financial statements. Related to the Audit Committee's investigation, the Company is performing additional work associated with its Fiscal Year 2014 Annual Report on Form 10-K, which might result in adjustments to the financial statements previously issued. The Audit Committee has not reached any conclusion because the investigation is ongoing. In addition, preliminary financial information for the first quarter of Fiscal Year 2015 was compiled by the Company and has not yet been reviewed by the Company's independent registered public accounting firm. The financial information for the first quarter of Fiscal Year 2015 may be subject to adjustment depending on the outcome of the Audit Committee's investigation and changes in reserves and estimates resulting from subsequent events and other information available through the filing date of the Company's Quarterly Report on Form 10-Q for the first quarter of Fiscal Year 2015. Accordingly, the preliminary results for the first quarter of Fiscal Year 2015 and the results for the corresponding period of Fiscal Year 2014 contained in these prepared remarks may be subject to potentially material adjustment.

## **COMPANY COMMENTARY**

Following is a summary of the company's comments on key areas impacting preliminary, unaudited and unreviewed Q1 Fiscal Year 2015 performance. The growth percentages that follow are in comparison to same period of the prior year.

## **OVERVIEW**

Q1 sales were better than expected at \$484M, up 1%, with no impact from exchange rates on a global basis. Retail sales continued to increase, up by 3%. Non-GAAP operating income was \$44M and 9.1% of sales, a 660 basis point improvement and the highest for a Q1 in at least six years. Non-GAAP earnings per share more than tripled to \$0.23. Through efficient working capital management, we generated approximately \$28M in cash flow from operations in the quarter and approximately \$230M in the last twelve months.

## **RETAIL SALES BY PRODUCT CATEGORY**

For Q1, our retail sales increased by 3% to \$425M. Units increased by 4% while overall retail average selling price (ASP) declined by 1%.

We classify our retail sales into three high-level groupings: Growth, Profit Maximization and Non-Strategic.

## **GROWTH**

Our retail Growth category, which includes PC Gaming, Tablet & Other Accessories, and Mobile Speakers, delivered 17% sales growth in Q1, with units up by 29%.

## **PC GAMING**

Q1 sales in our PC Gaming category increased by 17%, with units up by 26%. Gaming mice, headsets, steering wheels, and gamepads drove the increase. The growth in mice sales was primarily driven by the new G502 Tunable Gaming Mouse, while the G930 Surround Sound Gaming Headset was a key contributor to the growth in headsets. The

faster unit growth in our PC Gaming category reflects strong shipments in headsets and mice.

#### TABLET & OTHER ACCESSORIES

In Q1, our sales declined by 15%, with units up 12%. The decline in sales reflects a 26% drop in sales of our tablet keyboards. The drop in sales was due to the combination of a weak market for iPad shipments and the impact of our decision to reduce inventory across our supply chain to better align with the slowdown in market growth.

Sales and unit shipments of our protective cases for the iPad, which we introduced in Q1 of the prior year, more than tripled from a relatively small base.

We continue to create and launch new iPad accessories, but we have broadened our focus and expanded our offerings to actively target the Samsung opportunity.

#### MOBILE SPEAKERS

Sales and units in Q1 in our Mobile Speaker category, which is made up entirely of wireless speakers, more than doubled for the fifth consecutive quarter. The strong performance in this category continues to be driven primarily by UE BOOM, winner of multiple distinguished design awards, and our best-selling product across all categories. Mobile Speaker sales increased significantly across our three regions due to strong demand and expanded distribution.

## **PROFIT MAXIMIZATION**

Sales in our Profit Maximization category increased by 1%, with units up by 2%.

### POINTING DEVICES

In Q1, our sales decreased by 1%, with units up by 4%. Sales were down slightly at the low-end and mid-range of the category, with growth at the high-end. Unit shipments increased across all price bands.

### PC KEYBOARDS & DESKTOPS

Q1 sales increased by 8%, with units up by 7%. Sales in the Americas and EMEA increased by double digits. The category growth was driven by continued strong sales of our living room keyboards as well as sales of the Desktop MK120 keyboard & mouse combo. Growth was achieved across all price bands, with double-digit improvement in the high-end.

### AUDIO – PC & WEARABLES

Q1 sales in our Audio category declined by 11%, with units down by 7%. The primary driver of the decline was weak sales of PC speakers, reflecting a market that appears to be in structural decline as music consumption continues to migrate to mobile platforms.

### VIDEO

Q1 sales in Video increased by 10%, with units down by 17%. Sales and units of consumer webcams declined by 23%, consistent with the ongoing structural decline of the consumer webcam market. Sales of our video collaboration offerings targeted at small and midsize conference rooms more than offset the decline in webcams. The primary contributor to this growth was the Logitech ConferenceCam CC3000e, a mobile video conferencing solution that delivers 1080p HD video and enterprise-quality audio for under \$1000. This well-received product, which was launched in Q4 of Fiscal 2014, was the main contributor to the sales growth as well as to the 33% increase in the average selling price for the Video category.

## REMOTES

In Q1, our Harmony Remotes sales decreased by 15%, with units up by 11%. The decline in sales was experienced in all regions. The increase in unit shipments reflects strong sales of the Harmony 350 Control. Even with the decline in sales, our streamlined remotes portfolio delivered a positive profit contribution in the quarter.

Our strategy for the category is to continue to evolve the portfolio to address more control points within the connected home market, such as our recent announcements that the Harmony Ultimate is now compatible with the Nest Learning Thermostat and with Sonos systems.

## **NON-STRATEGIC CATEGORIES**

### **OTHER**

This category is made up of products that we are in the process of discontinuing as we continually assess the strategic fit of the products in our portfolio. As planned, sales and units declined steeply in Q1, with sales just exceeding the \$1M mark.

## **RETAIL SALES BY REGION**

### **RETAIL SALES – AMERICAS REGION**

Q1 sales in the Americas grew by 9%, with units up by 12%. The increase in sales was primarily driven by strong performance in the Growth category, led by Mobile Speakers and PC Gaming. The sales growth was complemented by a single-digit gain in the Profit Maximization category.

### **RETAIL SALES – EMEA REGION**

Q1 sales in EMEA were flat in USD and down by 4% in local currency. Unit shipments declined by 6%. EMEA sales were impacted by weaker emerging markets. Excluding our sales in emerging markets, EMEA grew by 6%. Sales of our Mobile Speakers were

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particularly strong in the quarter and we achieved double-digit growth in Video and PC Keyboards & Desktops.

### **RETAIL SALES – ASIA PACIFIC REGION**

Sales in Q1 in Asia Pacific were down by 3% in USD and by 1% in local currency, with units up by 6%. Excluding our sales in emerging markets, Asia Pacific grew by 3%.

Consistent with the Americas and EMEA, we delivered strong sales growth for Mobile Speakers in Asia Pacific.

### **OEM SALES**

Our Q1 OEM sales decreased by 6%, primarily due to weak mice sales that were only partially offset by growth in Keyboards & Desktops.

### **LIFESIZE**

Lifesize sales declined by 15% in Q1. The decline reflects a combination of weak market conditions for endpoints and the transition toward the recently announced Lifesize Cloud, a software-as-a-service (SaaS) offering that provides an affordable, simple and scalable video conferencing solution with little to no need for IT involvement.

### **GROSS MARGIN**

Our Q1 non-GAAP gross margin increased by 240 basis points to a record high of 38.3%, a level we do not expect to sustain as we move through the remainder of Fiscal Year 2015.

Approximately one percentage point of the improvement is due to the unusual situation of our books still being open for Q4 of Fiscal 2014, which has resulted in changes that impact our Q1 Fiscal 2015 results. Reserves made in Q4 Fiscal 2014 reflected estimates about future periods. Those estimates were re-evaluated based on our actual performance in Q1. As a result, some of the related reserves booked in Q4 Fiscal 2014 were changed, which created a positive impact on our Q1 Fiscal 2015 income statement.

The remainder of the increase reflects the combination of a significant improvement in our Profit Maximization category, driven largely by product cost reductions, and margin improvements in our Growth category as we benefit from increased scale.

### **OPERATING EXPENSES**

Demonstrating continued discipline in managing our spending, our Q1 non-GAAP operating expenses were \$141M, down by \$18M, or 11%. This was the fifth consecutive quarter of year-over-year reductions. The decline, which was partially offset by new investments to drive future growth, includes savings resulting from the rationalization of infrastructure and indirect procurement activities. Non-GAAP operating expenses were 29.2% of sales, down by 420 basis points. Note that our Non-GAAP operating expenses in Q1 of the current year exclude \$8.7M in G&A costs related to the ongoing Audit Committee investigation.

### **OPERATING INCOME**

Our non-GAAP operating income in Q1 was \$44M, an improvement of \$32M, significantly outpacing the growth in sales and reflecting increased operating leverage. Our non-GAAP operating margin reached 9.1%, up by 660 basis points.

### **NET INCOME**

Non-GAAP net income was \$38M in Q1, up by \$28M and benefitting from our 12.9% non-GAAP effective tax rate.

### **EARNINGS PER SHARE**

Non-GAAP earnings per share in Q1 more than tripled to \$0.23, up from \$0.07.

## **CASH**

Increased efficiency in working capital management led to the generation of approximately \$28M in cash flow from operations in Q1, the most for a Q1 in the last five years. Our cash conversion cycle in the quarter was approximately 27 days, our best ever for a Q1, with about a 14 day improvement over the prior year driven by our inventory efficiency initiatives. We ended Q1 with about \$485M in cash, up by \$166M.

## **SHARE COUNT & REPURCHASES**

Our diluted share count in Q1 was 165.8M shares. We have a \$250M share repurchase plan available for opportunistic usage once our SEC filings are current.

## **FISCAL YEAR 2015 OUTLOOK**

We are confirming our Fiscal Year 2015 outlook of \$2.16 billion in sales and increasing our outlook for non-GAAP operating income from \$145 million to approximately \$170M, a 17% increase reflecting the expected strength of our gross margin.

## **FORWARD LOOKING STATEMENTS**

These remarks contain forward-looking statements within the meaning of the federal securities laws, including, without limitation, statements regarding: our Audio category market, the consumer webcam market, our margin level, future growth, products and product categories out of which we intend to transition, and Fiscal Year 2015 revenue, gross margin and operating income. The forward-looking statements in these remarks involve risks and uncertainties that could cause Logitech's actual results and events to differ materially from those anticipated in these forward-looking statements, including, without limitation: the results of the Audit Committee's investigation and the completion of the additional work related to the Company's Fiscal Year 2014 Annual Report on Form 10-K and the Fiscal Year 2015 First Quarter Quarterly Report on Form 10-Q; any adjustments resulting from the review of the preliminary financial results for the first

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quarter of Fiscal Year 2015 by the Company's independent registered public accounting firm or from the review of subsequent events, including reserves and estimates, through the date of filing the Fiscal Year 2015 First Quarter Quarterly Report on Form 10-Q; if our product offerings, marketing activities and investment prioritization decisions do not result in the sales, profitability or profitability growth we expect, or when we expect it; the demand of our customers and our consumers for our products and our ability to accurately forecast it; if we fail to innovate and develop new products in a timely and cost-effective manner for our new and existing product categories; if we do not successfully execute on our growth opportunities in our new product categories or our growth opportunities are more limited than we expect; if sales of PC peripherals are less than we expect; the effect of pricing, product, marketing and other initiatives by our competitors; if our products and marketing strategies fail to separate our products from competitors' products; if we do not fully realize our goals to lower our costs and improve our operating leverage; if there is a deterioration of business and economic conditions in one or more of our sales regions or operating segments, or significant fluctuations in exchange rates; the effect of changes to our effective income tax rates. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included in Logitech's periodic filings with the Securities and Exchange Commission, including our Quarterly Report on Form 10-Q for the fiscal quarter ended December 31, 2013 and our Amended Annual Report on Form 10-K/A for the fiscal year ended March 31, 2013, available at [www.sec.gov](http://www.sec.gov), under the caption Risk Factors and elsewhere. Logitech does not undertake any obligation to update any forward-looking statements to reflect new information or events or circumstances occurring after the date of these remarks.

### USE OF NON-GAAP FINANCIAL INFORMATION

To facilitate comparisons to Logitech's historical results, Logitech has included non-GAAP adjusted measures which exclude share-based compensation expense, amortization of other intangible assets, restructuring charges (credits), other

restructuring-related charges, investment impairment (recovery) and other items detailed under "Supplemental Financial Information" in our earnings press release or "Financial Statements only" posted to our website under "Quarterly Results" at <http://ir.logitech.com>. Logitech believes this information, used together with the GAAP financial information, will help investors to evaluate its current period performance and trends in its business.

#### CHANNEL INVENTORY DATA

Estimates the inventory levels of our products held by or in-transit to our retailer and distributor customers. Includes data compiled by Logitech from data supplied by our customers, and our estimates of inventory in transit to our customers. Customers supplying data vary by geographic region and from period to period, but typically represent a majority of our retail sales. Data and our estimates are subject to limitations and possible error sources and may not be an entirely accurate indicator of actual customer channel inventory. Limitations and possible error sources include the following:

- Data supplied by our customers may not be indicative of inventory held by our customers as a whole
- Reliability of the data depends on accuracy and timeliness of information supplied to us by our customers, and the processes by which they collect their data are largely outside our control
- In the U.S., Canada, and to a lesser extent Asia Pacific, and a still lesser extent, EMEA, data is based on Point of Sale (POS) electronic data. Where POS data is not available, the data is collected largely through manual processes, including the exchange of spreadsheets or other non-automated methods of data transmission, which are subject to typical human errors, including errors in data entry, transmission and interpretation
- Our interpretation of the data, and our estimates of in-transit inventory, may be subject to errors in assumptions, calculations or other errors.