

Company Name: Logitech  
Company Ticker: LOGN SW  
Date: 2018-10-23  
Event Description: Q2 2019 Earnings Call

Market Cap: 6,127.97  
Current PX: 35.40  
YTD Change(\$): +2.50  
YTD Change(%): +7.599

Bloomberg Estimates - EPS  
Current Quarter: 0.667  
Current Year: 1.804  
Bloomberg Estimates - Sales  
Current Quarter: 877.200  
Current Year: 2839.750

## Q2 2019 Earnings Call

### Company Participants

- Benjamin Lu
- Bracken P. Darrell
- Vincent Pilette

### Other Participants

- Joern Iffert
- Alexander Duval
- Asiya Merchant
- Thomas Ferris Forte
- Michael Foeth
- Paul J. Chung
- Jürgen Wagner
- Ananda Baruah

## MANAGEMENT DISCUSSION SECTION

### Operator

Good day, and welcome to the Logitech's Second Quarter Fiscal 2019 Financial Results Conference Call. At this time, all participants are in a listen-only mode. We will be conducting a question-and-answer session and instructions will follow at that time. [Operator Instructions] This call is being recorded for replay purposes and may not be reproduced in whole or in part without written authorization from Logitech.

I would like to introduce your host for today's call, Mr. Benjamin Lu, Head of Investor Relations.

### Benjamin Lu

Hi. Thank you, and welcome to the Logitech conference call to discuss the company's financial results for the second quarter of fiscal year 2019. The press release, the prepared remarks and slides, as well as a live webcast of this call are available online at the Investor Relations page of our website, [ir.logitech.com](http://ir.logitech.com).

During the course of this call, we may make forward-looking statements, including with respect to future operating results that are made under the Safe Harbor of the Securities Litigation Reform Act of 1995. The forward-looking statements involve risks and uncertainties, and actual results could differ materially as noted in our quarterly and other filings with SEC. The company undertakes no obligation to update or revise any forward-looking statements as a result of new developments or otherwise.

Please note that today's call will include results reported on a non-GAAP basis except as otherwise noted. Non-GAAP reporting is provided to help you better understand our business. However, non-GAAP financial results are not meant to be considered in isolation from or as a substitute for or superior to GAAP results.

Non-GAAP measures have inherent limitations and should be used only in conjunction with Logitech's consolidated financial statements prepared in accordance with GAAP. Our press release and slides provide a reconciliation between

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GAAP and non-GAAP numbers and are posted on our IR website. We encourage listeners to review these items.

Unless noted otherwise, comparisons between periods are year-over-year and in constant currency. This call is being recorded, and will be available for replay on the Investor Relations page of the IR website.

Joining us today from California are Bracken Darrell, President and Chief Executive Officer, and Vincent Pilette, Chief Financial Officer.

I'll now turn the call over to Bracken.

## Bracken P. Darrell

Thanks, Ben, and thanks all of you for joining us. Over the past few years, we've built our business as a portfolio of categories, across the steadily increasing number of brands. That's the way we've talked about it with you. But today I want to shine a light on a slightly different aspect of our portfolio, category leadership. Everyone knows category leadership is an advantage but some might think that category leadership is almost automatic as an advantage, but we know better. If you don't put in place a powerhouse innovation engine, your strength is wasted. We know that very well. When Vincent and I started here, Logitech was a perfect example. We were the leader in about five categories, but our innovation was failing us.

Over the past six years, we've not only gained share in all those categories we led before, [ph] where we've had (00:02:53) about doubled the number of category leading franchises that we have to 11. Today those leadership categories represent nearly 70% of our net sales. We did that by deeply understanding consumers and using design as our central approach. This unlocks the power we always had in engineering. And for those where we are not a clear leader, we view them all as works in progress. We're working to either innovate and grow toward leadership like we are in Bluetooth speakers or redefine the category to create a new subcategory, where we believe we can satisfy a true consumer need and lead like Jaybird.

But we always attain leadership, maybe not. But you can see by our record, we're having some strong success so far and we will serially enter a new category that we believe we can lead. Our ambition is to be a vibrant portfolio category leading product groups combined with a strategic set of product groups striving to lead their category. How can you see that in our business today and how can you see it this quarter? The category leadership ambition, ambition and vision is behind our results. Our sales are growing consistently. Our gross margins are strong. And our operating income is leveraged with that growth. That's enabled by disproportionate growth in the category over time and strong value creation in the category, reflected by our gross margins.

Growing market share and growing gross margins. Those are the ultimate measures. Gross margin is the ultimate truth. Subpar innovation sees compression relative to the category in gross margin. But if your innovation is good and you're building your brand and serving your customers' needs, your gross margins improve relative to the category. Is this universally true? No, but it normally is and it's certainly been for us.

In Q2, our overall sales grew 10% to our highest ever for a September quarter and our gross margin improved strongly. Our operating profits increased much more than sales of better than expected, 18%. Our Gaming franchise delivered another powerful quarter with sales up 43%. Today, Gaming is our single largest product category. But in Gaming you can see an example of our striving for leadership.

When I arrived, we were number two in mice. Back then there were literally four people on our entire Gaming team. The tremendous growth we've achieved in Gaming since then was through the playbook you started to know us for. It all starts with great products. And with the product portfolio that we were proud of, we were able to align the Gaming group with a structural growth of the market that was just starting to celebrate five years ago. Now, we're number one in gaming mice.

While we worked on products, we also focused on the rise of eSports. We were early in positioning our portfolio around the burgeoning eSports phenomenon and the rise of mainstream gamers and this is paying off as we are seeing a

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new blockbuster gaming genres like the Battle Royale format, the Fortnite popularized transforming Gaming not just into a form of entertainment to play but also as a type of social expression. More and more gamers have broadcast themselves, playing their favorite games as a way of expressing who they are and interacting with other gamers on other social platforms and that's unlocking new opportunities for us. And so, with the Gaming becoming increasingly pervasive across the mainstream, we're doubling down and investing more to drive for continued momentum in our Gaming businesses.

Video Collaboration is a different example of striving for category leadership. Here, we had really no business five years ago and there was no category, but we are a leader in a developing category with an annual sales run rate of over \$200 million now; again for us, it all starts with great products. We've serially added products and now machine learning to further improve our offering. In this case, we also had to make investments in building out our direct enterprise sales force.

Because our products are outstanding, we've seen tremendous correlation between hiring an enterprise salesperson and a commensurate increase in our revenues. The limiting factor in growing Video Collaboration even bigger and faster is hiring the right people, the right sales people around the world. You can expect us to take the appropriate steps to ensure that we're investing in the right people, products and capabilities to support our powerful long-term growth outlook for VC. The growth trajectory, the cloud based video collaboration market continues unabated.

Zoom just hosted its third annual Zoomtopia Conference in San Jose nearby two weeks ago and they're seeing over 45 billion minutes a year of meetings conducted over [indiscernible] (00:07:35), and this was up 50% from the end of last year. We aren't surprised by that. In Q2, our Video Collaboration sales grew 25%. There's nothing wrong with 25% sales growth, but don't be deceived by it. The underlying sales out was over 50%, again a record high. And how about categories where we have a long and sustained category leadership record. PC Peripherals grew – sales grew 8% in Q2, its strongest growth in six quarters. Pointing Devices, Keyboards and Webcams all of which we lead all contributed to growth. And we haven't stopped innovating for users with all kinds of needs. There are still many, many opportunities here. We just released our MX VERTICAL mouse, which extends our focus on the importance of ergonomics in the workplace. MX VERTICAL had the strongest first quarter sales launch in the Americas of any pointing device product it launched in the last three years.

Stay tuned, because we'll continue to drive innovations and make every consumer more free to work and create whether it's home or in the office. Our tablets and other accessories had another robust quarter, with sales up 20%. And that's even more impressive when you consider that last year Q2 sales rose 50%, both new products such as Crayon, our first digital pencil for the 9.7 inch iPad, and Powered, our wireless charging dock for the iPhone, as well as existing products like our Slim Folio, drove the strong performance in Q2.

Now let me update everyone on our Mobile Speakers business. Our sales were still down this quarter. The underlying trends improved versus the prior two quarters. We've made great progress in transitioning out our older products to our newest ones. We updated our BOOM and MEGABOOM mobile speakers and made them better, much better. They have stronger base, improved sound and longer Bluetooth range, while still keeping their waterproof and drought-proof features that everybody loves. In fact they even now float.

Sales of BOOM 3 and MEGABOOM 3 are off to a good start and I can't wait to see how they do over the holidays. We got more attention from the media here than any launch since I've been here and probably any launch in our history. Audio & Wearable sales were flat in Q2. Blue Microphones sales distributed approximately one percentage point to our overall sales growth and offset the decline in desktop speakers and Jaybird. As we said previously, we're resetting our Jaybird portfolio and focusing the brand even more towards running and the channels that make sense for that focus. We launched two new Jaybird ear buds X4 and Tarah; and both just came out in late Q2. They retain Jaybird's reputation for ruggedness and comfort while being sweat proof and now for the first time even waterproof. We remain committed to building and positioning Jaybird for the niche worth segment of the market over the medium term. And with that let me turn the call over to Vincent, to walk you through our key financial metrics.

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## Vincent Pilette

Thanks, and good morning, everyone. As Bracken said our strong momentum continued this past quarter with sales up 10% in constant currency. We had strong growth momentum in Asia-Pacific, up 26%; solid growth in the Americas, up 9%; and the stabilizing business in Europe.

It was just over a year ago, when we acquired ASTRO Gaming since then the ASTRO business more than tripled in size, as we leverage a strong market growth reached into new channels and regions, and expanded the product portfolio through the launch of new headsets into lower price points. ASTRO is a great example of how we can take an acquired asset and build value by leveraging our core capabilities. This quarter, we closed the acquisition of Blue Microphones which added roughly one percentage point to our overall growth, and we're very optimistic about its future.

Also on an accounting note with regard to revenue, I mentioned last quarter that we implemented the new [ph] 606 revenue recognition (00:11:41) standard. This quarter our sales were impacted negatively by about 1 percentage points compared to Q2 last year, which was reported under the old standards. For the full year, we expect an immature impact from ASC 606.

In Q2, our non-GAAP gross margin improved by 110 basis points to 37.6% due to our continued cost reduction efforts, favorable mix and currency tailwind partially offset by investments in customer sales programs to support our growth. It's worth noting that we also benefited from a one-time \$7 million tax duty refund, which favorably impacted our gross margin. The net impact of the two one-timers this quarter, the headwind of the ASC 606 accounting standard and the tailwind from the duty refund is a favorable half a point benefit on gross margin.

Nonetheless it was just great execution from our operations team that enabled us to deliver a gross margin slightly above our long-term target and have to balance investments in our business in the face of various cost headwinds such as logistics and component cost, exchange rate volatility and more recently tariffs. Now I know there has been a lot of interest and questions in what is going on with tariffs and more specifically tariffs on imports into the U.S. from China. As we had mentioned last quarter, the first one of tariff had no material impact on our business, as only a few of our products were on the tariff list.

The second round of U.S. tariff that just went into effect on September 24, impacted more of our products, but through various mitigation efforts such as product reclassifications, tactical inventory pooling, supply chain or production shift and potential pricing adjustments in the future, we believe that we can manage the overall impact of tariffs this year within our previously announced profit guidance range. As some mitigation actions take time to implement, the net impact is estimated to be about half a point of gross margin in the second half which we can absorb in our full year outlook.

Our non-GAAP operating expenses increased 10% this past quarter. We invested in R&D, up 7%. And sales and marketing expenses were 13% to support the expected strong top line growth in the year and also impacted by the acquisition of Blue.

At the same time, we continue to drive G&A efficiencies with G&A spend down 3% year-over-year. The one thing you can expect from us as always is very tight control of our OpEx, creating efficiencies but also investing in resources to support long-term growth opportunities which are funded by gross margin expansion. That discipline and leverage is on display with our Q2 non-GAAP operating income which increased 18% to \$85 million and resulted in a 12.2% operating profit margin. Non-GAAP EPS grew 26% to \$0.49.

Cash from operations year-to-date is \$97 million, up \$30 million or 44% from the same period last year. In the quarter, we spent \$134 million in total consideration for the acquisition of Blue Microphones. We also paid \$114 million in dividends and \$10 million in share buyback, leading to a total cash balance of \$426 million at the end of September. Excluding the non-cash impact of ASC 606, working capital metrics and related balance sheet items, inventory, AR, AP were all in line to historical trends for September quarter.

I'm very excited about how we are positioned for the rest of the year. As Bracken had mentioned earlier, we'll keep applying our methodology of resetting, positioning and investing in each category depending on their respective life

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cycle in order to build over time a portfolio of category leadership and capture the long-term growth opportunities.

And with that Bracken, I'll pass it back to you.

## Bracken P. Darrell

Thanks, Vincent. It's great to start the year. It's a great start to the year, but there's still so much more to come. I really love this time of the year. In most of our categories, those who are looking for gifts, and probably like most of you, for their loved ones or maybe just for themselves, I have more to give you this – we have more to give this year than ever, ASTRO headsets, BOOM microphones, Jaybird Tarah earphones, MEGABOOM 3, MX VERTICAL, and I could go on and on. But they're really for everyone, whether you're a player at home or you are at work, but anyone who you wants to stay connected and maybe you can even give a Video Collaboration equipment with AI built into it to your loved one, might be an odd gift but we're promoting that.

And I'm even more excited about the other new things that we're working on right now, but they won't be available for this Christmas but maybe for the next. Now tariffs [indiscernible] (00:16:48) on everyone's mind, but we view it as another reality. You should just expect us to adjust to and we are. We'll confirm our outlook for fiscal year 2019 for both net sales growth of 9% to 11% and for non-GAAP operating income of \$325 million to \$335 million

And with that, Vincent and I are ready to take your questions.

## Q&A

### Operator

[Operator Instructions] Your first question comes from the line of Joern Iffert from UBS. Go ahead.

<Q - Joern Iffert>: Thanks for taking my questions and hi.

<A - Bracken P. Darrell>: Hey, Joern.

<Q - Joern Iffert>: And the first one would be please on the tariffs, you stated that there will be a negative impact on the gross profit margin of 50 basis points in the second half. Can you help me to reengineer the math and what percentage of revenues is impacted by this? So how many products are on the list?

And second question would be please again to clarify the gross-profit margin and you stated that as a net 50 basis points benefit from the duty refund and accounting changes. Can you also please highlight what was the benefit of the FX? And as a third question please, I mean your supply chain set up, I mean how are you reacting to the tariff risk? Are you already considering to diversify your whole supply chain in the next two to three years and if yes, what do you think will be the cost in the P&L and the CapEx? Thanks.

<A - Vincent Pilette>: Great, Joern. Let me take first the number question out of the way and then Bracken will address some of the risk and how we see the diversification of our risk here. So, in terms of over-tariff, I say that for the second half, we're going to have about half a point of mitigated impact. Obviously, over the long-term we have mitigation plan, but some take a little bit longer to implement than others. We do not quantify per each product. There's a bunch of chords that are impacted, some that are not. As you know, it goes below the category. It's not one full category that's impacted and half a point you can easily if you want play a reverse engineer, but I wouldn't focus on that. I would just say that for the second half, building to our guidance, we have half a point built from tariffs and that will continue to go down as we progress with our mitigation effort. So, that's number one.

Secondly, on the gross margin impact from the one timer this quarter, as you mentioned and I'll repeat, we have about half a point a mix of unfavorable and favorable. This quarter if you take the euro, we trended for which is the main exchange rate, we traded at above the way it was last year. It's a little bit of a tailwind still. As you know, we commit to a growth in constant currency. That's how we focus developing the business, but everything below into our P&L we

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manage in U.S. dollars. And when we have a little bit of favorable tailwind from currency, then we may use it in various ways as long as we need our profit commitment which is in U.S. dollars. That currency effect, as you know, if it stays at \$1.15 for the euro exchange rate as one example me moving to a tailwind by Q4 but one quarter at a time.

<A - **Bracken P. Darrell**>: Vincent already talked about some of the short-term impacts, but you also asked about the longer term impacts over the next two years or three years of the effect of a new world of with whether tariffs coming from China. We have a manufacturing strategy in place and we're always updating that and as far as we view tariffs is just another impact on our manufacturing strategy. So certainly we are looking at the supply chain changes in the context of where we are today and where we might be tomorrow. Do I expect that to have a big impact on OpEx? No.

<Q - **Joern Iffert**>: All right. Thanks very much.

<A - **Bracken P. Darrell**>: Thank you.

<Q - **Joern Iffert**>: And Vincent, just a follow up here, I mean, sorry to follow up on the gross profit margin 50 basis points, was this including the FX benefits or was it excluding the FX benefits, the plus 50 basis points you were saying for Q2?

<A - **Vincent Pilette**>: Yeah. For Q2 excluding the currency benefit we do not isolate or report the specific currency benefit on the gross margin. As you know, we manage differently and some of that benefit maybe capitalizing our inventory, there is hedging, there's many different dimensions if you want that really lead us to drive the gross margin on U.S. dollars. So to answer your question was excluding the currency there.

<Q - **Joern Iffert**>: But, Vince, have you think about the gross profit margin as you also indicated to be one of the key KPIs? Should we expect this to fall back to the midpoint of your guidance between 35% to 37% for the second half or can it stay around 37% for the next two quarters. How should we think about it?

<A - **Vincent Pilette**>: Now, that's a very good question. So we managed the business in the long-term, still in the long-term range of 35% to 37%. Operationally in the first half, we've been on the high end of that range and as you know normal in Q3 and Q4 your margins tend historically a little bit lower, so it would be prudent if you muddle at the midpoint of that gross margin. Now, of course, we don't guide the gross margin per se, we manage the business on the bottom line and the top line perspective.

<Q - **Joern Iffert**>: All right. Thank you.

<A - **Bracken P. Darrell**>: Thank you.

## Operator

Your next question comes from the line of Alexander Duval from Goldman Sachs. Please go ahead. Your line is open.

<Q - **Alexander Duval**>: Yes. Hi, everyone. Many thanks for the question.

<A - **Bracken P. Darrell**>: Hey, Alex.

<Q - **Alexander Duval**>: It's Alex from Goldman Sachs. Just a couple of quick ones, first of all on the music side of things, it seemed instead of the recent – or the last quarter if there had been potential need to reset the channel a bit given some lower price offerings from digital assistant players. But you actually stated today that you're seeing some underlying improvements in trend. So I wondered if you could give a bit more color on what you're seeing and how confident you are that growth could return?

And secondly just on this China tariffs point, you did obviously mention that you're able to manage these impacts within your prior full year guidance range. I wondered if you could just clarify to what extent you're confident that you're baking in all the potential impacts. Obviously, there's a lot of complex moving parts. So I'm just trying to understand to what degree you've been conservative on that? Many thanks.

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<A - **Bracken P. Darrell**>: Okay. Let me take the music question and Vince will take the tariff question. Yeah, I would say the – yeah, you've seen, I think we were pretty clear over the last two quarters, we've been pretty aggressively selling out the old product out of the channel to make sure it's very clean or as clean as we can make it as we bring in the new product and that's traditional for us. And we did that. And as we've done that now we've started to and we did that. And as we've done that now we've started to shipping the new product. And it's a little too early to say exactly what that will do but we're confident that the new products are very compelling, they're priced well, they are good value, and the feedback has been tremendous.

So I think, this is one of the big quarters for Bluetooth speakers. Q4 is also big because we go into the summer season when a lot of our speakers really valuable. So I'd say so far so good. I think certainly you'll see improvement versus the last two quarters. And will it go back to growth or strong growth, we don't know yet. We're not banking on that, but we certainly expect a significant improvement.

<A - **Vincent Pilette**>: Good. On tariff, so we started very early. Actually, Alex. We've been working on it since May and working on the first list and on the second one. At this point in time, we know all of the skews that are being impacted in our portfolio. We also know the tariff increase in September 24; it's by about 10%, moving January 1 at 25% and all of that is known. For that, we have our forecast at the skew level. I can say, we have a certain degree of variability there that could impact the number, and then we have our mitigation plan that's pretty well known.

The two things that are less known is A, the forecast and secondly, whether or not we are going to act on increased price. So, we have a forecast; that's based on what we know and that always try to leave room for the unknown.

We have a good track record of meeting our forecast. It doesn't mean that it's 100% guaranteed, but we feel pretty good about the model and all of the moving parts in that.

The last one I would want to add, you may have heard at times that politician say that maybe the whole imports from China into the U.S. would be under tariff. Of course, that is not currently our working assumption we work on what we know from an over scope perspective.

<Q - **Alexander Duval**>: Very helpful. Many thanks.

<A - **Bracken P. Darrell**>: Thanks, Alex.

## Operator

Your next question comes from the line of Asiya Merchant from Citigroup. Please go ahead. Your line is open.

<Q - **Asiya Merchant**>: Hi, everyone.

<A - **Bracken P. Darrell**>: Hey, there.

<A - **Vincent Pilette**>: Hi, Asiya.

<Q - **Asiya Merchant**>: Hi. Congratulations on the results. Quick question, as you think about seasonality into the back half of your fiscal year or into even the holiday season ahead, how do you think about that relative to seasonal norms that you've had? And then, secondly, EMEA still seems like it's stabilizing but not really growing. When should we expect that region to also post growth? And then lastly, related to the seasonal question, macro within China lots of demand indicators coming through. Clearly you had a very strong sell-through in Asia Pac. But then as you look ahead into the quarter and into the back half of the fiscal 2019, how are you thinking about the demand indicators in China? Thank you.

<A - **Vincent Pilette**>: Let me first take the modeling linearity kind of question out of the way and then Bracken will take the second two questions. In term of sequential seasonality which I'm assuming is what you're looking at right now. Historically we've been growing about 20% up from Q2 going into our Q3, right, our calendar Q4. And when you look at our forecast for the rest of the year, we are somewhat in line with that seasonality. The two things you need to

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keep in mind is last year in Q2 we had bought ASTRO. This time in Q2 again, we bought Blue Microphone. Those two may skew your historical seasonality. So historical seasonality plus the acquisition of Blue this time is what make our guidance going forward.

**<A - Bracken P. Darrell>**: And the two regional questions, as you mentioned EMEA is stabilizing and I feel really good about the moves we're making there. So, we've made a lot of changes structurally and we're changing some process and we're also really moving to a lower promotion, higher marketing spending environment, which we were super excited about. Very similar to what we've done in Asia Pacific. This will probably take a year or two years to really fully implement, but I feel very good about it. I think you'll see improvement there. And I wouldn't want to – we don't guide on the quarter, so I wouldn't want to say. But yeah, I think you'll certainly see improvement there and we're excited about it.

China, everybody is talking about the macro environment in China and we have a great China business. We had a great China business this quarter. We're very excited about the team we have there, the approach we're executing there. Our indicators in China continue to be good, but I would say it's true that the overall the currency has weakened in China and we all know that and we read the same things you do. But I guess I'd just say I'm super excited about the team and the operating excellence that we have in China. So, I think we're going to get the most out of China you could possibly get. And so far so good, we don't see any doom and gloom on the horizon.

**<A - Vincent Pilette>**: And for those of you who are modeling here, listening to Bracken, China sales is about 10% of our overall sales. So, that gives you some magnitude of...

**<A - Bracken P. Darrell>**: I would just add one of the things that you asked in regional question. Just like we're a portfolio of categories with different categories performing at different levels, different times same thing for the regions and we are very aware of that. So, we actually like that because as we're resetting EMEA, we've got a really strong AP. AMR is doing fine. And I think you'll see the mix does change from time to time. I imagined a lot period where EMEA will come back stronger and Asia-Pacific will be a little softer than it is, although probably still very strong.

**<Q - Asiya Merchant>**: Great. Thank you. And then one if I may follow up. Like looking longer term into your fiscal 2020 I know you guys have a \$2 EPS out there that you put out at your Analyst Day earlier this year and things sounded really good. How do you guys think about whether it's China, whether it's just tariff, GDP growth forecasting lower, all that and yet you guys continue to execute really well. How do you think about all that as it relates to kind of like a guidance that you provided for \$2 in EPS for 2020? Any changes there?

**<A - Vincent Pilette>**: No. I think there was no change, right. Every time we deliver a good quarter and Q2 is another one. I'm having many of you asking, can we deliver \$2 EPS a little bit earlier? And as you know, we're very conservative. We have an operating plan. We march towards that and we feel after all the good calls, we've had very strong in term of delivering the long-term value. There may be in and out that may change and some assumption will change, but that's part of the portfolio with so many levers that we have in that.

**<A - Bracken P. Darrell>**: Yeah, I would also add, I mean, we're – as we've talked about many times and we talked about in the opening today, we're a portfolio of businesses, portfolio of countries around the world of course and we have a lot of tools to play. And so, I don't believe we are really hypersensitive to modest changes in the economic environments around the world. We're much more control of our own destiny, especially with our growth plan where we can serially enter new categories and we have opportunities, and we do have opportunities to do that. So, I don't think we're going to be – I mean, of course, if there's a massive slowdown around the world, that will affect everybody, but generally speaking it, we control our own destiny.

**<Q - Asiya Merchant>**: Great. Thank you. Congratulations again.

**<A - Bracken P. Darrell>**: Thank you.

**Operator**



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Your next question comes from the line of Thomas Forte from D.A. Davidson. Please go ahead. Your line is open.

<A - Bracken P. Darrell>: Hey, Thomas.

<Q - Thomas Ferris Forte>: Great, thanks. So, wanted to ask two questions; one on tariffs and one on eSports M&A.

<A - Bracken P. Darrell>: Sure.

<Q - Thomas Ferris Forte>: So, on the tariffs front, given your leadership position in the categories that you operate in, we would imagine you'd have the ability to adjust price if necessary. I use that as one of the levers to us that potential pressure.

And then on eSports, definitely seems like it's becoming more mainstream. You can see Ninja on Samsung ads and [ph] something like (00:31:47) football and you've made two what we think are excellent acquisitions with ASTRO and Blue Microphones. How should we think about your M&A strategy going forward for gaming?

<A - Bracken P. Darrell>: Okay. I'll answer both of those. Yeah, I think from – yeah, you're right. I mean, when I open this category leadership and if you're a category leader, you should have the opportunity to have some pricing leverage and we think we do. Now, we're not going to be responsible with that either. We're about creating value for consumers. So, we're going to – we'll do that in the right way and we have experienced driving pricing around the world. We've priced many times, re-priced, raised price in both Asia Pacific and EMEA, not as often in the U.S. But yeah, we should have pricing leverage where we need to.

From an eSports standpoint, thank you for the comments on the two acquisitions. We're obviously super excited about both of those. And we completely believe in the rise of the eSports and feel it's really at the very beginning. Our M&A plans, we of course don't share anything, but we're looking across. We're always looking at many things and we're looking at many things right now.

<Q - Thomas Ferris Forte>: Great. Thank you for taking my questions.

<A - Bracken P. Darrell>: Thank you.

## Operator

Your next question comes from the line of Michael Foeth from Vontobel. Please go ahead. Your line is open.

<A - Bracken P. Darrell>: Hi, Michael.

<A - Vincent Pilette>: Hey, Michael.

<Q - Michael Foeth>: Yes, hi. Hi, how are you?

<A - Bracken P. Darrell>: Good.

<Q - Michael Foeth>: Just two questions on – Smart Home is obviously a small category, but you've been talking about category leadership and I was wondering that the sharp decline there, what is the source of that, possibly the Circle cameras. And so, how do you react to a situation where you sort of are losing out and maybe not the leader in the category? That would be the first question. And the second question is regarding EMEA again. If you can be more specific what is really behind the relative weakness or which categories are behind relative weakness, that would be helpful. And if you're seeing any changes in consumer behavior in the large European countries. Thank you.

<A - Bracken P. Darrell>: Okay. On the Smart Home, there are two different things going on there. You mentioned Circle camera, it's tiny for us. And as I opened, I said we only want to be either the – we want to be the leader in the category at large or we want to be a leader in the thing that we think of as the category at small, which is a subset of the category that we feel like we can really lead. And we're working on that. And I can't disclose more than that except to say that we'll see. It's really small, so I wouldn't get too excited about what – wherever Circle is. From a Harmony standpoint, which is the remote control business, that one is a good example of what you do in a category leadership

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context when the category itself continues to go down.

So, what are we doing there? We're consolidating. So, we're really reducing the number of skews that we have, we're reducing our overall OpEx spend there so we can reallocate it to where we think there's growth, and we'll have a good profitable business there for whatever it is and we – it'll be resized by the time we get to the other end.

You may remember when Vincent and I first started working together, we did this a couple different times and this is part of the deal here and it's part of our strategy. In EMEA, I wouldn't point to a single category. I think this is really across the board. We are really changing our approach to Europe, looking ahead two or three years, and we're really taking a lot of the playbook that we took from Asia Pacific, which moved very strongly online and is a good combination of great online marketing and good offline marketing and we're applying the same model into EMEA and I think it's going to take a few years to really see the benefits of that, but I think the growth will come back faster than that, but the real benefits that will come later, but I'm excited about it. So, I couldn't point to a single category and I'm not concerned about Europe. I feel like we're really doing the right things and I feel very good about the steps we're taking and I think the results will come relatively soon.

<Q - Michael Foeth>: Thanks.

<A - Bracken P. Darrell>: Okay. Thanks.

## Operator

Your next question comes from the line of Paul Chung from JPMorgan. Please go ahead, sir. Your line is open.

<A - Bracken P. Darrell>: Hey, Paul.

<A - Vincent Pilette>: Hey, Paul.

<Q - Paul J. Chung>: Hey. How's it going? Thanks for taking my question. So, first up on keyboards. You've been driving pretty impressive growth over the past three quarters. Can you just expand on what's driving the strength there, [ph] SMB (00:36:22) – the MX lines are listing overall ASP somewhat, but could you just talk about unit shipment trends, market share dynamics, channel strategy, that would be helpful?

<A - Bracken P. Darrell>: Sure. The Keyboard & Combo (sic) [Keyboards & Combos] (00:36:36) business for us has been a strength for years and it continues to be and we keep innovating there. We launched the new Living-Room Keyboard this quarter, as you probably know, and that's a great product. The MX products continue to do well. And then we've got the signature product, the very high end, which is CRAFT. I would just say, generally across the board, our innovation is doing well there. We continue to, generally speaking, hold our gain share in the major markets and we still have opportunities to gain share in all those PC categories, believe it or not. When I look at some of our share trends in some places, especially at the low end here and there, we should be doing better. So, yeah, I mean I think our Keyboard & Combo (sic) [Keyboards & Combos] (00:37:16) will continue to be good.

<Q - Paul J. Chung>: Okay. And then second question is on Blue Microphone (sic) [Blue Microphones] (00:37:24), which triggers you to kind of take action in this market, and any details on margins, channel overlap, that would be helpful as well?

<A - Bracken P. Darrell>: One of the things we've talked about before is that when we – we're always working on categories and usually secretly. So, we've got several categories in development all the time. One of those, I was pretty [ph] averted (00:37:46) about that I think in the last call. One of those was a microphone. So, we were very interested in this category. Now, when we start to work in a category, we have teams working on products and understanding the category and the category dynamics.

At the same time, we take a hard look from an M&A standpoint where we think we can either accelerate something we're doing or differentiate it or even replace it entirely. Blue Microphone (sic) [Blue Microphones] (00:38:07) was a wonderful example of being able to really completely replace what we are doing and take a big leap into the category, a

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category that we already felt like we started to understand well enough to play. So, that's the story there. And as I said, we're really excited about it.

<A - Vincent Pilette>: And we're seeing the same levers that apply to ASTRO will be at play here from launching new product, expanding into internationally new regions, expanding into new distribution channels and building up the portfolio overall. From a gross margin perspective, if we don't talk about gross margin by category, but it's accretive to our overall corporate gross margin.

<A - Bracken P. Darrell>: We would have gone into this – I guess the point I was trying to make is, we would have gone into this category regardless, just like we went into...

<A - Vincent Pilette>: Yeah.

<A - Bracken P. Darrell>: Just like we went into video conferencing or we went into Bluetooth speakers. We would have gone into this category regardless. This acquisition enable us to go faster, a lot faster.

<Q - Paul J. Chung>: Okay. Great. And then, my last question is I just want to hear your take on Google Project Stream. I assume Logi may benefit if the service does take off, if console gamers may migrate to PCs. So, curious to hear your take and then what was ASTRO's contribution in the quarter? Thank you.

<A - Bracken P. Darrell>: Well. First of all on Google, you could expand that to Google, Amazon, really all the big players. Anybody who's out there providing a platform for streaming or a platform for gaming [indiscernible] (00:39:42) and beyond just streaming in general, it's good for us because that's our business. We really view ourselves as enabling these large platforms and the users who love them and want to try them. And so it's great for us and we're super excited about it and [indiscernible] (00:39:57) has been fantastic for us and YouTube is actually fantastic for us too. So, I'd say it's just another good one.

<A - Vincent Pilette>: On ASTRO sites, we don't split the gaming. ASTRO is fully – this is the fifth quarter fully in our overall baseline. The only quantifying number I said is we tripled the size of the business and it's a good contributor of the overall gaming growth that we've reported.

<Q - Paul J. Chung>: Thank you so much.

<A - Bracken P. Darrell>: Thank you, Paul.

## Operator

Your next question comes from the line of Jürgen Wagner from MainFirst Bank. Please go ahead. Your line is open.

<A - Bracken P. Darrell>: Hey, Jürgen.

<Q - Jürgen Wagner>: Yeah, hi.

<A - Vincent Pilette>: Hey.

<Q - Jürgen Wagner>: Thank you for letting me on. I mean, you mentioned that PC Peripherals is a broad-based strength and you also mentioned that or explained to us [ph] my keyboard (00:40:44) is doing so well. But do you see any impact from the current processor shortage? And in previous calls, you indicated that PC Peripherals segment as a whole to be flattish, plus or minus now you have [indiscernible] (00:40:58). Should we then see somewhat a leveling off until year end? Thank you.

<A - Bracken P. Darrell>: Yeah. I'll respond to the first part. I'll let Vincent respond to the second since kind of a modeling question. The processor shortage has been talked about a lot and I'm just continually amazed by how well our team and operations has done to manage our business in the context of that. I do hear about other companies with big cost problems and it is costing us more by the way. But with big cost problems coming out of these various shortages of these very small components that never seemed particularly impactful for and suddenly are. We just have a great

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operations team who's managed that really well and hasn't been a big impact for us, and I don't think it will be.

<A - Vincent Pilette>: And in fact [ph] in companies (00:41:46) if you're rethinking about Intel shortages or other big shortages in term of impacting the PC units being shipped into the market, I want to just remind you that we look at the installed base as really the addressable market for us. And I don't think those shortages in the short term will impact the installed base to impact the peripheral indirectly. So, that's the main one. I don't remember, there's another question.

<A - Bracken P. Darrell>: It was PC...

<A - Vincent Pilette>: And then overall guidance and absolutely it's an important one. As you know, right, we've provided an outlook for our PC Peripherals overall to be low-single digit. I wouldn't change that. Obviously, every quarter, we'll try to drive better. We'll introduce new products, we'll optimize our sales performance and we've delivered the results that you've seen. We'll continue with the prudent and conservative approach of planning this at what we see, which is a low-single digit and hopefully we'll continue to do better in that environment.

<Q - Jürgen Wagner>: Okay. Okay. Thank you.

<A - Bracken P. Darrell>: Thanks, Jürgen.

## Operator

Your next question comes from the line of Ananda Baruah from Loop Capital. Please go ahead. Your line is open.

<Q - Ananda Baruah>: Hey. Good morning, guys.

<A - Vincent Pilette>: Hey, Ananda.

<Q - Ananda Baruah>: How are you?

<A - Bracken P. Darrell>: Good morning.

<Q - Ananda Baruah>: I appreciate you guys taking the question. Yeah, congrats on solid results.

<A - Bracken P. Darrell>: Thank you.

<Q - Ananda Baruah>: Just a couple for me if I could. Just going back to tariffs, Bracken, you sounded like you were saying – communicating that you don't expect it to be sort of material based on your sort of current news. Any further detail you can give on – and Vincent you mentioned sort of the plan you guys are looking at. Any detail you can give with regards to how much of that is related to just sort of utilizing current supply chain as it is versus introducing new things in the supply chain that may not exist today or previously existed, just to get some sense of the structural nature of the impact? And then I have a followup on that too.

<A - Vincent Pilette>: Yeah. Hey, Ananda. So, the quantified amount we said is manageable within our current outlook. And then in the long term, I know you follow this at the time, right. It's like currency movement and other things. In the long term, those structural move will be built into the business model and we'll be able to absorb it. It does include moving some production location. We don't want to give too much detail. We're still working the plan, which started in May, and we'll continue all the way into the next calendar year. We have multiple activities that would change structurally the supply chain and build actually a more diversified supply chain and therefore making the company more robust. It does not call at this point in time any material change in CapEx in term of investments. And that's the extent of the plan, I guess, we'd like to.

<A - Bracken P. Darrell>: Yeah. And I would just add, Ananda, one of the core capabilities of Logitech from a supply chain perspective has always been the ability to move our manufacturing in and out of our own factory. And that includes in and out of other people's factories if we happen to be contract manufacturing with other people in China. And that's exactly what this is about. When and if we need to move a product line out, in this case out of China entirely, we're more than capable of doing that. We've got the teams to do it, staffing to do it and we have lots of experience

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doing it. We do it, in fact, all the time.

<Q - **Ananda Baruah**>: Bracken, this is what I would – I was sort of indirectly teasing at, is this the advantage of having, I think what you referred to in the past is a modularized manufacturing kind of structure, an interplant? Is that sort of a play here as well as a part of it?

<A - **Bracken P. Darrell**>: Well, I do think it's an advantage to have both of your own manufacturing and external manufacturing in your past, so that you have a lot of experience moving. And so we do have a lot of experience moving and even surprises me and it surprised me the first couple of years I was here how easily and how quickly we could move a manufacturing line out of our factory or out of somebody's factory into another one without any glitch at all. So, I think that is an advantage.

<Q - **Ananda Baruah**>: Okay, that's great. And then just quick followup. I may have missed this earlier, but the gaming revenue, it seems like gaming might be getting stronger. It's tough because the [indiscernible] (00:46:20) big and they do move a bit. But I think you put up mid-40s growth over the mid-40s compare or something like that, which is significantly higher than kind of run rate. So, do you – just context around that, are you – do you feel like you're continuing to see the category strengthen? And if not the category strengthen, do you think that you're continuing to see or your core positioning within the category strengthened, so that your sort of normalized growth is accelerating there? Thanks.

<A - **Bracken P. Darrell**>: Well, I think the category continues to be super strong. I think we're doing well in those categories. But the nice thing about our story is, boy, we could be doing better. There are areas in our business and they're not small. Two or three that I think, gosh, we should be really outperforming where we are. And so we're really doubling down the innovation there to see if we can put ourselves in place to do that. So, I don't know whether I would say it's accelerating or – certainly not decelerating, but I do think our opportunity there looks big and sustainable.

<Q - **Ananda Baruah**>: That's great. Thanks a lot. I'll [ph] cede (00:47:31) the floor. Thanks, guys.

<A - **Bracken P. Darrell**>: Thank you.

<A - **Vincent Pilette**>: Thanks, Ananda.

## Operator

And there are no further questions at this time. I will now turn the call over to Bracken Darrell, CEO, for closing remarks.

## Bracken P. Darrell

Okay, well, I want to thank all of you for joining us. Thanks for the call. Make sure to go out. The holidays are approaching, buy lots of our stuff. And we'll see you or we'll talk to you in January.

## Vincent Pilette

Thank you.

## Operator

This concludes today's conference call. You may now disconnect.

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