

Zumiez Inc  
Form 10-Q  
September 10, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934  
FOR THE QUARTERLY PERIOD ENDED AUGUST 4, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934  
Commission file number 000-51300

ZUMIEZ INC.

(Exact name of registrant as specified in its charter)

|                                                                   |                                         |
|-------------------------------------------------------------------|-----------------------------------------|
| Washington                                                        | 91-1040022                              |
| (State or other jurisdiction of<br>incorporation or organization) | (I.R.S. Employer<br>Identification No.) |

4001 204<sup>th</sup> Street SW, Lynnwood, WA 98036

(Address of principal executive offices) (Zip Code)

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Registrant's telephone number, including area code: (425) 551-1500

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definition of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
Yes No

At September 5, 2018, there were 25,519,164 shares outstanding of common stock.

ZUMIEZ INC.

FORM 10-Q

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Signature

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## ZUMIEZ INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

|                                                                                                                                                                           | August 4,<br>2018<br>(Unaudited) | February<br>3, 2018 |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|---------------------|
| <b>Assets</b>                                                                                                                                                             |                                  |                     |
| Current assets                                                                                                                                                            |                                  |                     |
| Cash and cash equivalents                                                                                                                                                 | \$ 41,409                        | \$ 24,041           |
| Marketable securities                                                                                                                                                     | 91,500                           | 97,864              |
| Receivables                                                                                                                                                               | 20,554                           | 17,027              |
| Inventories                                                                                                                                                               | 149,656                          | 125,826             |
| Prepaid expenses and other current assets                                                                                                                                 | 16,169                           | 14,405              |
| Total current assets                                                                                                                                                      | 319,288                          | 279,163             |
| Fixed assets, net                                                                                                                                                         | 125,141                          | 128,852             |
| Goodwill                                                                                                                                                                  | 59,336                           | 62,912              |
| Intangible assets, net                                                                                                                                                    | 15,470                           | 16,696              |
| Deferred tax assets, net                                                                                                                                                  | 4,417                            | 4,174               |
| Other long-term assets                                                                                                                                                    | 6,815                            | 7,713               |
| Total long-term assets                                                                                                                                                    | 211,179                          | 220,347             |
| Total assets                                                                                                                                                              | \$ 530,467                       | \$ 499,510          |
| <b>Liabilities and Shareholders' Equity</b>                                                                                                                               |                                  |                     |
| Current liabilities                                                                                                                                                       |                                  |                     |
| Trade accounts payable                                                                                                                                                    | \$ 79,370                        | \$ 37,861           |
| Accrued payroll and payroll taxes                                                                                                                                         | 15,640                           | 20,650              |
| Income taxes payable                                                                                                                                                      | 2,580                            | 5,796               |
| Deferred rent and tenant allowances                                                                                                                                       | 7,895                            | 8,073               |
| Short term borrowings                                                                                                                                                     | 5,623                            | 943                 |
| Other liabilities                                                                                                                                                         | 21,274                           | 25,924              |
| Total current liabilities                                                                                                                                                 | 132,382                          | 99,247              |
| Long-term deferred rent and tenant allowances                                                                                                                             | 38,265                           | 39,275              |
| Other long-term liabilities                                                                                                                                               | 4,781                            | 5,073               |
| Total long-term liabilities                                                                                                                                               | 43,046                           | 44,348              |
| Total liabilities                                                                                                                                                         | 175,428                          | 143,595             |
| Commitments and contingencies (Note 4)                                                                                                                                    |                                  |                     |
| Shareholders' equity                                                                                                                                                      |                                  |                     |
| Preferred stock, no par value, 20,000 shares authorized; none issued and outstanding                                                                                      | —                                | —                   |
| Common stock, no par value, 50,000 shares authorized; 25,520 shares issued and outstanding at August 4, 2018 and 25,249 shares issued and outstanding at February 3, 2018 | 149,961                          | 146,523             |
| Accumulated other comprehensive (loss) income                                                                                                                             | (8,101)                          | 35                  |
| Retained earnings                                                                                                                                                         | 213,179                          | 209,357             |
| Total shareholders' equity                                                                                                                                                | 355,039                          | 355,915             |
| Total liabilities and shareholders' equity                                                                                                                                | \$ 530,467                       | \$ 499,510          |

See accompanying notes to condensed consolidated financial statements

ZUMIEZ INC.

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)

(In thousands, except per share amounts)

(Unaudited)

|                                                                           | Three Months Ended |                  | Six Months Ended  |                  |
|---------------------------------------------------------------------------|--------------------|------------------|-------------------|------------------|
|                                                                           | August 4,<br>2018  | July 29,<br>2017 | August 4,<br>2018 | July 29,<br>2017 |
| Net sales                                                                 | \$ 218,971         | \$ 192,245       | \$ 425,257        | 373,399          |
| Cost of goods sold                                                        | 146,436            | 132,449          | 290,136           | 261,555          |
| Gross profit                                                              | 72,535             | 59,796           | 135,121           | 111,844          |
| Selling, general and administrative expenses                              | 65,837             | 60,558           | 130,133           | 118,841          |
| Operating profit (loss)                                                   | 6,698              | (762 )           | 4,988             | (6,997 )         |
| Interest income, net                                                      | 238                | 92               | 521               | 174              |
| Other income (expense), net                                               | 248                | (23 )            | (233 )            | (472 )           |
| Earnings (loss) before income taxes                                       | 7,184              | (693 )           | 5,276             | (7,295 )         |
| Provision (benefit) for income taxes                                      | 2,807              | (85 )            | 3,506             | (2,239 )         |
| Net income (loss)                                                         | \$ 4,377           | \$ (608 )        | \$ 1,770          | (5,056 )         |
| Basic earnings (loss) per share                                           | \$ 0.18            | \$ (0.02 )       | \$ 0.07           | (0.21 )          |
| Diluted earnings (loss) per share                                         | \$ 0.17            | \$ (0.02 )       | \$ 0.07           | (0.21 )          |
| Weighted average shares used in computation of earnings (loss) per share: |                    |                  |                   |                  |
| Basic                                                                     | 24,955             | 24,689           | 24,894            | 24,635           |
| Diluted                                                                   | 25,188             | 24,689           | 25,211            | 24,635           |

See accompanying notes to condensed consolidated financial statements

ZUMIEZ INC.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

(In thousands)

(Unaudited)

|                                                                                 | Three<br>Months Ended<br>July |             | Six Months<br>Ended |                  |
|---------------------------------------------------------------------------------|-------------------------------|-------------|---------------------|------------------|
|                                                                                 | August<br>4, 2018             | 29,<br>2017 | August<br>4, 2018   | July 29,<br>2017 |
| Net income (loss)                                                               | \$4,377                       | \$(608 )    | \$1,770             | \$(5,056)        |
| Other comprehensive (loss) income, net of tax and reclassification adjustments: |                               |             |                     |                  |
| Foreign currency translation                                                    | (3,293)                       | 8,305       | (8,168)             | 9,784            |
| Net change in unrealized gain on available-for-sale debt securities             | 100                           | 17          | 32                  | 28               |
| Other comprehensive (loss) income, net                                          | (3,193)                       | 8,322       | (8,136)             | 9,812            |
| Comprehensive income (loss)                                                     | \$1,184                       | \$7,714     | \$(6,366)           | \$4,756          |

See accompanying notes to condensed consolidated financial statements

ZUMIEZ INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(In thousands)

(Unaudited)

|                                                 |              |            | Accumulated   |            |            |
|-------------------------------------------------|--------------|------------|---------------|------------|------------|
|                                                 |              |            | Other         |            |            |
|                                                 | Common Stock |            | Comprehensive | Retained   |            |
|                                                 | Shares       | Amount     | Income (Loss) | Earnings   | Total      |
| Balance at February 3, 2018                     | 25,249       | \$ 146,523 | \$ 35         | \$ 209,357 | \$ 355,915 |
| Net income                                      | —            | —          | —             | 1,770      | 1,770      |
| Other comprehensive loss, net                   | —            | —          | (8,136 )      | —          | (8,136 )   |
| Issuance and exercise of stock-based awards     | 271          | 426        | —             | —          | 426        |
| Stock-based compensation expense                | —            | 3,012      | —             | —          | 3,012      |
| Cumulative effect of accounting change (Note 1) | —            | —          | —             | 2,052      | 2,052      |
| Balance at August 4, 2018                       | 25,520       | \$ 149,961 | \$ (8,101 )   | \$ 213,179 | \$ 355,039 |

|                                             |              |            | Accumulated   |            |            |
|---------------------------------------------|--------------|------------|---------------|------------|------------|
|                                             |              |            | Other         |            |            |
|                                             | Common Stock |            | Comprehensive | Retained   |            |
|                                             | Shares       | Amount     | Loss          | Earnings   | Total      |
| Balance at January 28, 2017                 | 24,945       | \$ 140,984 | \$ (16,488 )  | \$ 182,555 | \$ 307,051 |
| Net loss                                    | —            | —          | —             | (5,056 )   | (5,056 )   |
| Other comprehensive income, net             | —            | —          | 9,812         | —          | 9,812      |
| Issuance and exercise of stock-based awards | 286          | 198        | —             | —          | 198        |
| Stock-based compensation expense            | —            | 2,500      | —             | —          | 2,500      |
| Balance at July 29, 2017                    | 25,231       | \$ 143,682 | \$ (6,676 )   | \$ 177,499 | \$ 314,505 |

See accompanying notes to condensed consolidated financial statements

ZUMIEZ INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

|                                                                                          | Six Months Ended  |                  |
|------------------------------------------------------------------------------------------|-------------------|------------------|
|                                                                                          | August<br>4, 2018 | July 29,<br>2017 |
| Cash flows from operating activities:                                                    |                   |                  |
| Net income (loss)                                                                        | \$ 1,770          | \$(5,056 )       |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |                   |                  |
| Depreciation, amortization and accretion                                                 | 13,920            | 13,520           |
| Deferred taxes                                                                           | (990 )            | (2,456 )         |
| Stock-based compensation expense                                                         | 3,012             | 2,500            |
| Other                                                                                    | 310               | 621              |
| Changes in operating assets and liabilities:                                             |                   |                  |
| Receivables                                                                              | (4,099 )          | (2,092 )         |
| Inventories                                                                              | (25,993)          | (32,553)         |
| Prepaid expenses and other current assets                                                | (1,570 )          | (995 )           |
| Trade accounts payable                                                                   | 40,815            | 34,627           |
| Accrued payroll and payroll taxes                                                        | (4,785 )          | 561              |
| Income taxes payable                                                                     | (2,973 )          | (3,372 )         |
| Deferred rent and tenant allowances                                                      | (872 )            | (521 )           |
| Other liabilities                                                                        | (2,997 )          | (1,016 )         |
| Net cash provided by operating activities                                                | 15,548            | 3,768            |
| Cash flows from investing activities:                                                    |                   |                  |
| Additions to fixed assets                                                                | (9,061 )          | (12,461)         |
| Purchases of marketable securities and other investments                                 | (35,046)          | (37,586)         |
| Sales and maturities of marketable securities and other investments                      | 41,200            | 42,615           |
| Net cash used in investing activities                                                    | (2,907 )          | (7,432 )         |
| Cash flows from financing activities:                                                    |                   |                  |
| Proceeds from revolving credit facilities                                                | 29,227            | 1,791            |
| Payments on revolving credit facilities                                                  | (24,233)          | (1,791 )         |
| Proceeds from issuance and exercise of stock-based awards                                | 621               | 370              |
| Payments for tax withholdings on equity awards                                           | (195 )            | (172 )           |
| Net cash provided by financing activities                                                | 5,420             | 198              |
| Effect of exchange rate changes on cash and cash equivalents                             | (693 )            | 510              |
| Net increase (decrease) in cash and cash equivalents                                     | 17,368            | (2,956 )         |
| Cash and cash equivalents, beginning of period                                           | 24,041            | 20,247           |
| Cash and cash equivalents, end of period                                                 | \$41,409          | \$ 17,291        |
| Supplemental disclosure on cash flow information:                                        |                   |                  |
| Cash paid during the period for income taxes                                             | \$7,362           | \$3,660          |
| Accrual for purchases of fixed assets                                                    | 3,496             | 2,550            |

See accompanying notes to condensed consolidated financial statements



ZUMIEZ INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

### 1. Nature of Business and Basis of Presentation

**Nature of Business**—Zumiez Inc., including its wholly owned subsidiaries, (the “Company,” “we,” “us,” “its” and “our”) is a leading specialty retailer of apparel, footwear, accessories and hardgoods for young men and women who want to express their individuality through the fashion, music, art and culture of action sports, streetwear, and other unique lifestyles. At August 4, 2018, we operated 703 stores; 611 in the United States (“U.S.”), 50 in Canada, 35 in Europe, and 7 in Australia. We operate under the names Zumiez, Blue Tomato and Fast Times. Additionally, we operate ecommerce websites at ~~zumiez.com~~, ~~blue-tomato.com~~ and fasttimes.com.au.

**Fiscal Year**—We use a fiscal calendar widely used by the retail industry that results in a fiscal year consisting of a 52- or 53-week period ending on the Saturday closest to January 31. Each fiscal year consists of four 13-week quarters, with an extra week added to the fourth quarter every five or six years. The three months ended August 4, 2018 and July 29, 2017 were 13-week periods. The six months ended August 4, 2018 and July 29, 2017 were 26-week periods.

**Basis of Presentation**—The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (“U.S. GAAP”) for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial reporting. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The unaudited condensed consolidated financial statements include the accounts of Zumiez Inc. and its wholly-owned subsidiaries. All significant intercompany transactions and balances are eliminated in consolidation.

In our opinion, the unaudited condensed consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the condensed consolidated balance sheets, operating results and cash flows for the periods presented.

The financial data at February 3, 2018 is derived from audited consolidated financial statements, which are included in our Annual Report on Form 10-K for the year ended February 3, 2018, and should be read in conjunction with the audited consolidated financial statements and notes thereto. Interim results are not necessarily indicative of results for the full fiscal year due to seasonality and other factors.

**Use of Estimates**—The preparation of financial statements in conformity with U.S. GAAP requires estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements as well as the reported amounts of revenues and expenses during the reporting period. These estimates can also affect supplemental information disclosed by us, including information about contingencies, risk and financial condition. Actual results could differ from these estimates and assumptions.

**Significant Accounting Policies**—Our significant accounting policies are detailed in Note 2, “Summary of Significant Accounting Policies” within Part IV Item 15 of the Annual Report on Form 10-K for the year ended February 3, 2018. There have been no significant changes in accounting policies, with exception of the adoption of Accounting

Standards Codification Topic 606, Revenue from Contracts with Customers (“ASC 606”). Our significant accounting policies impacted by the adoption of ASC 606 are discussed below.

**Revenue Recognition**—Revenue is recognized upon purchase at our retail store locations. For our ecommerce sales, revenue is recognized when control passes to the customer upon shipment. Taxes collected from our customers are recorded on a net basis. We accrue for estimated sales returns by customers based on historical return experience. The allowance for sales returns was \$2.9 million at August 4, 2018 and \$2.6 million at February 3, 2018. We record the sale of gift cards as a current liability and recognize revenue when a customer redeems a gift card. The current liability for gift cards was \$2.6 million at August 4, 2018 and \$6.4 million at February 3, 2018. Additionally, the portion of gift cards that will not be redeemed (“gift card breakage”) is recognized in proportion of the patterns used by the customer based on our historical redemption patterns. We recognized net sales related to gift card breakage of \$0.1 million for the three months ended August 4, 2018 and July 29, 2017 and \$0.2 million for the six months ended August 4, 2018 and July 29, 2017.

**Loyalty Program**—We have a customer loyalty program, the Zumiez STASH, which allows members to earn points for purchases or performance of certain activities. The points can be redeemed for a broad range of rewards, including product and experiential rewards. Points earned for purchases are recorded as a current liability and a reduction of net sales based on the relative fair value of the points at the time the points are earned and estimated redemption rates. Revenue is recognized upon redemption of points for rewards. Points earned for the performance of activities are recorded as a current liability based on the estimated cost of the points and as marketing expense when redeemed. Deferred revenue related to our customer loyalty program was \$1.9 million at August 4, 2018 and \$1.6 million at February 3, 2018.

**Recent Accounting Standards**—In February 2016, the Financial Accounting Standards Board (“FASB”) issued a comprehensive standard related to lease accounting to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. Most significantly, the new guidance requires lessees to recognize operating leases with a term of more than 12 months as lease assets and lease liabilities. The adoption will require a modified retrospective approach at the beginning of the earliest period presented. The new standard is effective for the fiscal year beginning after December 15, 2018. We will adopt for the fiscal year beginning February 3, 2019. All of our retail store locations are subject to operating lease arrangements. While we expect this standard to result in a material increase to the assets and liabilities on our Consolidated Balance Sheet, we are continuing to evaluate the impact of this standard on our consolidated financial statements and related disclosures. Our minimum lease commitments at August 4, 2018 are disclosed in Note 4, “Commitments and Contingencies”.

In January 2016, the FASB issued a new standard related primarily to accounting for equity investments, financial liabilities where the fair value option has been elected, and the presentation and disclosure requirements for financial instruments. There will no longer be an available-for-sale classification for equity securities and therefore, no changes in fair value will be reported in other comprehensive income for equity securities with readily determinable fair values. We adopted this standard beginning February 4, 2018 and it did not have a material impact to our condensed consolidated financial statements.

In May 2014, the FASB issued a comprehensive new revenue recognition standard codified under ASC 606. The new standard allows for a full retrospective approach to transition or a modified retrospective approach. This guidance was effective for fiscal years beginning after December 15, 2017. On February 4, 2018, we adopted this standard using the modified retrospective approach. Results at August 4, 2018 and for the three and six months ended August 4, 2018 are presented under ASC 606, while results at July 29, 2017 and for the three and six months ended July 29, 2017 continue to be reported in accordance with our historical accounting under ASC Topic 605, Revenue Recognition.

The adoption of ASC 606 resulted in a change to the timing of revenue recognition on ecommerce sales from delivery to shipment and the timing of revenue recognition on gift card breakage from remote to in proportion to the patterns of rights exercised by our customers. We recorded an increase to retained earnings of \$2.1 million, net of \$0.6 million in taxes, as of February 4, 2018 due to the cumulative effect of adopting ASC 606. The cumulative effect resulted in a decrease in other liabilities of \$3.1 million and inventory of \$0.4 million, as well as \$0.4 million decrease in our deferred tax assets and \$0.2 million increase in income taxes payable. The impact of adopting ASC 606 was not material to the condensed consolidated financial statements for the three and six months ended August 4, 2018.

We elected to use the practical expedients to account for shipping and handling costs that occur after the customer obtains control of the goods as fulfillment costs. We accrue the expense of shipping and handling costs when product is shipped. We also elected to exclude from net sales the tax amounts collected from our customers to be remitted to governmental authorities.

## 2. Revenue Recognition

The following table disaggregates net sales by geographic region (in thousands):

|               | Three Months Ended |                  | Six Months Ended  |                  |
|---------------|--------------------|------------------|-------------------|------------------|
|               | August 4,<br>2018  | July 29,<br>2017 | August 4,<br>2018 | July 29,<br>2017 |
| United States | \$ 188,648         | \$ 165,220       | \$ 359,188        | \$ 319,285       |
| Canada        | 12,465             | 11,333           | 23,171            | 19,787           |
| Europe        | 16,071             | 14,005           | 39,245            | 31,094           |
| Australia     | 1,787              | 1,687            | 3,653             | 3,233            |
| Net sales     | \$ 218,971         | \$ 192,245       | \$ 425,257        | \$ 373,399       |

### 3. Cash, Cash Equivalents and Marketable Securities

The following tables summarize the estimated fair value of our cash, cash equivalents and marketable securities and the gross unrealized holding gains and losses (in thousands):

|                                       | August 4, 2018 |         |            |  |           |
|---------------------------------------|----------------|---------|------------|--|-----------|
|                                       | Gross          |         | Gross      |  |           |
|                                       | Unrealized     |         | Unrealized |  | Estimated |
|                                       | Amortized      | Holding | Holding    |  | Fair      |
|                                       | Cost           | Gains   | Losses     |  | Value     |
| Cash and cash equivalents:            |                |         |            |  |           |
| Cash                                  | \$40,480       | \$ —    | \$ —       |  | \$ 40,480 |
| Money market funds                    | 929            | —       | —          |  | 929       |
| Total cash and cash equivalents       | 41,409         | —       | —          |  | 41,409    |
| Marketable securities:                |                |         |            |  |           |
| State and local government securities | 69,326         | 15      | (71 )      |  | 69,270    |
| Variable-rate demand notes            | 22,230         | —       | —          |  | 22,230    |
| Total marketable securities           | \$91,556       | \$ 15   | \$ (71 )   |  | \$ 91,500 |

|                                       | February 3, 2018 |         |            |  |           |
|---------------------------------------|------------------|---------|------------|--|-----------|
|                                       | Gross            |         | Gross      |  |           |
|                                       | Unrealized       |         | Unrealized |  | Estimated |
|                                       | Amortized        | Holding | Holding    |  | Fair      |
|                                       | Cost             | Gains   | Losses     |  | Value     |
| Cash and cash equivalents:            |                  |         |            |  |           |
| Cash                                  | \$21,911         | \$ —    | \$ —       |  | \$ 21,911 |
| Money market funds                    | 2,130            | —       | —          |  | 2,130     |
| Total cash and cash equivalents       | 24,041           | —       | —          |  | 24,041    |
| Marketable securities:                |                  |         |            |  |           |
| State and local government securities | 68,620           | 9       | (130 )     |  | 68,499    |
| Variable-rate demand notes            | 29,365           | —       | —          |  | 29,365    |
| Total marketable securities           | \$97,985         | \$ 9    | \$ (130 )  |  | \$ 97,864 |

All of our marketable securities have an effective maturity date of two years or less and may be liquidated, at our discretion, prior to maturity.

The following tables summarize the gross unrealized holding losses and fair value for investments in an unrealized loss position, and the length of time that individual securities have been in a continuous loss position (in thousands):

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|                                       | August 4, 2018      |          |                      |        | February 3, 2018    |          |                      |        |
|---------------------------------------|---------------------|----------|----------------------|--------|---------------------|----------|----------------------|--------|
|                                       | Less Than 12 Months |          | 12 Months or Greater |        | Less Than 12 Months |          | 12 Months or Greater |        |
|                                       | Unrealized          |          | Unrealized           |        | Unrealized          |          | Unrealized           |        |
|                                       | Fair Value          | Losses   | Fair Value           | Losses | Fair Value          | Losses   | Fair Value           | Losses |
| Marketable securities:                |                     |          |                      |        |                     |          |                      |        |
| State and local government securities | 51,106              | (71 )    | —                    | —      | 51,106              | (71 )    |                      |        |
| Total marketable securities           | \$51,106            | \$ (71 ) | \$ —                 | \$ —   | \$51,106            | \$ (71 ) |                      |        |

|                                       | August 4, 2018      |           |                      |         | February 3, 2018    |           |                      |        |
|---------------------------------------|---------------------|-----------|----------------------|---------|---------------------|-----------|----------------------|--------|
|                                       | Less Than 12 Months |           | 12 Months or Greater |         | Less Than 12 Months |           | 12 Months or Greater |        |
|                                       | Unrealized          |           | Unrealized           |         | Unrealized          |           | Unrealized           |        |
|                                       | Fair Value          | Losses    | Fair Value           | Losses  | Fair Value          | Losses    | Fair Value           | Losses |
| Marketable securities:                |                     |           |                      |         |                     |           |                      |        |
| State and local government securities | 53,655              | (129 )    | 610                  | (1 )    | 54,265              | (130 )    |                      |        |
| Total marketable securities           | \$53,655            | \$ (129 ) | \$ 610               | \$ (1 ) | \$54,265            | \$ (130 ) |                      |        |

We did not record a realized loss for other-than-temporary impairments during the three and six months ended August 4, 2018 or July 29, 2017.

## 4. Commitments and Contingencies

Leases—We lease our stores and certain corporate and other operating facilities under operating leases. Total rent expense is as follows (in thousands):

|                         | Three Months Ended |               | Six Months Ended |               |
|-------------------------|--------------------|---------------|------------------|---------------|
|                         | August 4, 2018     | July 29, 2017 | August 4, 2018   | July 29, 2017 |
| Minimum rent expense    | \$19,905           | \$19,316      | \$40,027         | \$38,294      |
| Contingent rent expense | 773                | 619           | 1,527            | 1,216         |
| Total rent expense (1)  | \$20,678           | \$19,935      | \$41,554         | \$39,510      |

(1) Total rent expense does not include real estate taxes, insurance, common area maintenance charges and other executory costs, which were \$10.3 million and \$20.4 million for the three and six months ended August 4, 2018 and \$10.4 million and \$20.9 million for the three and six months ended July 29, 2017.

A majority of our leases provide for ongoing co-tenancy requirements or early cancellation clauses that would further lower rental rates, or permit lease terminations, or both, in the event that co-tenants cease to operate for specific periods or if certain sales levels are not met in specific periods. Most of the store leases require payment of a specified minimum rent and a contingent rent based on a percentage of the store's net sales in excess of a specified threshold, as well as real estate taxes, insurance, common area maintenance charges and other executory costs. Future minimum lease payments at August 4, 2018 are as follows (in thousands):

|             |           |
|-------------|-----------|
| Fiscal 2018 | \$35,853  |
| Fiscal 2019 | 66,369    |
| Fiscal 2020 | 62,090    |
| Fiscal 2021 | 56,198    |
| Fiscal 2022 | 50,665    |
| Thereafter  | 118,683   |
| Total (1)   | \$389,858 |

(1) Amounts in the table do not include contingent rent and real estate taxes, insurance, common area maintenance charges and other executory costs obligations.

Purchase Commitments—At August 4, 2018, we had outstanding purchase orders to acquire merchandise from vendors of \$249.5 million. We have an option to cancel these commitments with no notice prior to shipment, except for certain private label and international purchase orders in which we are obligated to repay contractual amounts upon cancellation.

Litigation—We are involved from time to time in claims, proceedings and litigation arising in the ordinary course of business. We have made accruals with respect to these matters, where appropriate, which are reflected in our condensed consolidated financial statements. For some matters, the amount of liability is not probable or the amount cannot be reasonably estimated and therefore accruals have not been made. We may enter into discussions regarding settlement of these matters, and may enter into settlement agreements, if we believe settlement is in the best interest of our shareholders.

A putative class action, Alexia Herrera, on behalf of herself and all other similarly situated, v. Zumiez Inc., was filed against us in the Eastern District Court of California, Sacramento Division under case number 2:16-cv-01802-SB in August 2016. Alexandra Bernal filed the initial complaint and then in October 2016 added Alexia Herrera as a named plaintiff and Alexandra Bernal left the case. The putative class action lawsuit against us alleges, among other things, various violations of California's wage and hour laws, including alleged violations of failure to pay reporting time. In May 2017 we moved for judgment on the pleadings in that plaintiff's cause of action for reporting-time pay should fail as a matter of law as the plaintiff and the other putative class members did not "report for work" with respect to certain shifts on which the plaintiff's claims are based. In August 2017, the court denied the motion. However, in October 2017 the district court certified the order denying the motion for judgment on the pleadings for immediate interlocutory review by the United States Court of Appeals for the Ninth Circuit. We then filed a petition for permission to appeal the order denying the motion for judgment on the pleadings with the United States Court of Appeals for the Ninth Circuit, which petition was then granted in January 2018. Our opening appellate brief was filed on June 6, 2018 and the plaintiff's answering appellate brief was filed August 6, 2018. Our reply brief to the Plaintiff's answering appellate brief is due on September 26, 2017. Given the current status of this case, we are unable to express a view regarding the ultimate outcome or, if the outcome is adverse, to estimate an amount, or range, of reasonably possible loss. We have defended this case vigorously and will continue to do so.

**Insurance Reserves**—We use a combination of third-party insurance and self-insurance for a number of risk management activities including workers' compensation, general liability and employee-related health care benefits. We maintain reserves for our self-insured losses, which are estimated based on historical claims experience and actuarial and other assumptions. The self-insurance reserve at August 4, 2018 and February 3, 2018 was \$2.5 million and \$2.1 million.

## 5. Revolving Credit Facilities and Debt

On February 5, 2016, the Company entered into an asset-based revolving credit agreement with Wells Fargo Bank, National Association, as administrative agent, collateral agent, letter of credit issuer and lenders, which provides for a senior secured revolving credit facility of up to \$100 million ("ABL Facility"), subject to a borrowing base, with a letter of credit sub-limit of \$10 million. The ABL Facility is available for working capital and other general corporate purposes. The ABL Facility will mature on February 5, 2021.

The ABL Facility is secured by a first-priority security interest in substantially all of the personal property (but not the real property) of the borrowers and guarantors. Amounts borrowed under the ABL Facility bear interest, at the Company's option, at either an adjusted LIBOR rate plus a margin of 1.25% to 1.75% per annum, or an alternate base rate plus a margin of 0.25% to 0.75% per annum. The Company is also required to pay a fee of 0.25% per annum on undrawn commitments under the ABL Facility. Customary agency fees and letter of credit fees are also payable in respect of the ABL Facility.

There were no borrowings outstanding under the ABL Facility at August 4, 2018 and at February 3, 2018. We had no open commercial letters of credit outstanding under these lines of credit at August 4, 2018 and February 3, 2018.

Additionally, we have revolving lines of credit with UniCredit Bank Austria and Commerzbank Germany of up to 9.0 million Euro (\$10.4 million) at August 4, 2018, the proceeds of which are used to fund certain international operations. The revolving lines of credit bear interest at 1.55% to 1.65%. The utilized facility amount, in whole or in part, is subject to termination with three months' notice and with immediate effect to the unused facility amount. There was \$5.6 million of borrowings outstanding at August 4, 2018 and \$0.9 million in borrowings outstanding at February 3, 2018. We had no open commercial letters of credit outstanding under these lines of credit at August 4, 2018 and at February 3, 2018.

## 6. Fair Value Measurements

We apply the following fair value hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

- Level 1— Quoted prices in active markets for identical assets or liabilities;
- Level 2— Quoted prices for similar assets or liabilities in active markets or inputs that are observable; and
- Level 3— Inputs that are unobservable.

The following tables summarize assets measured at fair value on a recurring basis (in thousands):

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|                                       | August 4, 2018 |           |       |
|---------------------------------------|----------------|-----------|-------|
|                                       | Level          |           | Level |
|                                       | 1              | Level 2   | 3     |
| Cash equivalents:                     |                |           |       |
| Money market funds                    | \$ 929         | \$ —      | \$ —  |
| Marketable securities:                |                |           |       |
| State and local government securities | —              | 69,270    | —     |
| Variable-rate demand notes            | —              | 22,230    | —     |
| Other long-term assets:               |                |           |       |
| Money market funds                    | 1,148          | —         | —     |
| Total                                 | \$ 2,077       | \$ 91,500 | \$ —  |

|                                       | February 3, 2018 |          |         |
|---------------------------------------|------------------|----------|---------|
|                                       | Level 1          | Level 2  | Level 3 |
| Cash equivalents:                     |                  |          |         |
| Money market funds                    | \$2,130          | \$—      | \$—     |
| Marketable securities:                |                  |          |         |
| State and local government securities | —                | 68,499   | —       |
| Variable-rate demand notes            | —                | 29,365   | —       |
| Other long-term assets:               |                  |          |         |
| Money market funds                    | 1,437            | —        | —       |
| Equity investments                    | —                | —        | 151     |
| Total                                 | \$3,567          | \$97,864 | \$151   |

The Level 2 marketable securities include state and local municipal securities and variable-rate demand notes. Fair values are based on quoted market prices for similar assets or liabilities or determined using inputs that use readily observable market data that are actively quoted and can be validated through external sources, including third-party pricing services, brokers and market transactions. We review the pricing techniques and methodologies of the independent pricing service for Level 2 investments and believe that its policies adequately consider market activity, either based on specific transactions for the security valued or based on modeling of securities with similar credit quality, duration, yield and structure that were recently traded. We monitor security-specific valuation trends and we make inquiries with the pricing service about material changes or the absence of expected changes to understand the underlying factors and inputs and to validate the reasonableness of the pricing.

There were no material assets measured at fair value on a nonrecurring basis for the three and six months ended August 4, 2018 and July 29, 2017.

## 7. Stockholders' Equity

**Accumulated Other Comprehensive Loss**—The components of accumulated other comprehensive loss and the adjustments to other comprehensive income for amounts reclassified from accumulated other comprehensive loss into net income are as follows (in thousands):

|                                            | Net unrealized   |                    |                   |
|--------------------------------------------|------------------|--------------------|-------------------|
|                                            | Foreign currency | gains (losses) on  | Accumulated other |
|                                            | translation      | available-for-sale | comprehensive     |
|                                            | adjustments      | debt securities    | loss              |
| <b>Three months ended August 4, 2018:</b>  |                  |                    |                   |
| Balance at May 5, 2018                     | \$ (4,766        | ) \$ (142          | ) \$ (4,908       |
| Other comprehensive (loss) income, net (1) | (3,293           | ) 100              | (3,193            |

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|                                     |            |          |              |   |
|-------------------------------------|------------|----------|--------------|---|
| Balance at August 4, 2018           | \$ (8,059  | ) \$ (42 | ) \$ (8,101  | ) |
| Three months ended July 29, 2017:   |            |          |              |   |
| Balance at April 27, 2017           | \$ (14,995 | ) \$ (3  | ) \$ (14,998 | ) |
| Other comprehensive income, net (1) | 8,305      | 17       | 8,322        |   |
| Balance at July 29, 2017            | \$ (6,690  | ) \$ 14  | \$ (6,676    | ) |

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|                                     | Net unrealized   |                    |                   |   |
|-------------------------------------|------------------|--------------------|-------------------|---|
|                                     | Foreign currency | gains (losses) on  | Accumulated other |   |
|                                     | translation      | available-for-sale | comprehensive     |   |
|                                     | adjustments      | investments        | loss              |   |
| Six months ended August 4, 2018:    |                  |                    |                   |   |
| Balance at February 3, 2018         | \$ 109           | \$ (74             | ) \$ 35           |   |
| Other comprehensive income, net (1) | (8,168           | ) 32               | (8,136            | ) |
| Balance at August 4, 2018           | \$ (8,059        | ) \$ (42           | ) \$ (8,101       | ) |
| Six months ended July 29, 2017:     |                  |                    |                   |   |
| Balance at January 28, 2017         | \$ (16,474       | ) \$ (14           | ) \$ (16,488      | ) |
| Other comprehensive income, net (1) | 9,784            | 28                 | 9,812             |   |
| Balance at July 29, 2017            | \$ (6,690        | ) \$ 14            | \$ (6,676         | ) |

(1) Other comprehensive (loss) income is net of immaterial taxes for the three and six months ended August 4, 2018 and July 29, 2017 for both net unrealized gains (losses) on available-for-sale investments. Foreign currency translation adjustments are not adjusted for income taxes as they relate to permanent investments in our international subsidiaries.

## 8. Equity Awards

We maintain several equity incentive plans under which we may grant incentive stock options, nonqualified stock options, stock bonuses, restricted stock awards, restricted stock units and stock appreciation rights to employees (including officers), non-employee directors and consultants.

We account for stock-based compensation by recording the estimated fair value of stock-based awards granted as compensation expense over the vesting period, net of estimated forfeitures. Stock-based compensation expense is attributed to earnings using a straight-line method. We estimate forfeitures of stock-based awards based on historical experience and expected future activity.

The fair value of restricted stock awards and units is measured based on the closing price of our common stock on the date of grant. The fair value of stock option grants is estimated on the date of grant using the Black-Scholes option pricing model.

Total stock-based compensation expense is recognized on our condensed consolidated income statements as follows (in thousands):

| Three Months |      | Six Months |      |
|--------------|------|------------|------|
| Ended        |      | Ended      |      |
| August       | July | August     | July |
| 4,           | 29,  | 4,         | 29,  |

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|                                              | 2018    | 2017    | 2018    | 2017    |
|----------------------------------------------|---------|---------|---------|---------|
| Cost of goods sold                           | \$269   | \$238   | \$577   | \$505   |
| Selling, general and administrative expenses | 1,102   | 983     | 2,435   | 1,995   |
| Total stock-based compensation expense       | \$1,371 | \$1,221 | \$3,012 | \$2,500 |

At August 4, 2018, there was \$10.6 million of total unrecognized compensation cost related to unvested stock options, restricted stock awards and restricted stock units. This cost has a weighted-average remaining recognition period of 1.4 years.

The following table summarizes restricted stock awards and restricted stock units activity (in thousands, except grant date weighted-average fair value):

|                                 |              | Grant Date   |           |
|---------------------------------|--------------|--------------|-----------|
|                                 | Restricted   | Weighted-    |           |
|                                 | Stock        | Average Fair | Intrinsic |
|                                 | Awards/Units | Value        | Value     |
| Outstanding at February 3, 2018 | 524          | \$ 20.11     |           |
| Granted                         | 262          | \$ 23.93     |           |
| Vested                          | (209 )       | \$ 20.84     |           |
| Forfeited                       | (14 )        | \$ 20.27     |           |
| Outstanding at August 4, 2018   | 563          | \$ 21.61     | \$13,249  |

We had 0.3 million stock options outstanding at August 4, 2018 with a weighted average exercise price of \$23.06 and 0.3 million stock options outstanding at February 3, 2018 with a weighted average exercise price of \$22.82.

## 9. Earnings (Loss) per Share, Basic and Diluted

The following table sets forth the computation of basic and diluted earnings (loss) per share (in thousands, except per share amounts):

|                                                                       | Three Months |           | Six Months Ended |            |
|-----------------------------------------------------------------------|--------------|-----------|------------------|------------|
|                                                                       | Ended        |           | August           | July 29,   |
|                                                                       | August       | July 29,  | August           | July 29,   |
|                                                                       | 4, 2018      | 2017      | 4, 2018          | 2017       |
| Net income (loss)                                                     | \$ 4,377     | \$(608 )  | \$ 1,770         | \$(5,056 ) |
| Weighted average common shares for basic earnings (loss) per share:   | 24,955       | 24,689    | 24,894           | 24,635     |
| Dilutive effect of stock options and restricted stock                 | 233          | —         | 317              | —          |
| Weighted average common shares for diluted earnings (loss) per share: | 25,188       | 24,689    | 25,211           | 24,635     |
| Basic earnings (loss) per share                                       | \$ 0.18      | \$(0.02 ) | \$ 0.07          | \$(0.21 )  |
| Diluted earnings (loss) per share                                     | \$ 0.17      | \$(0.02 ) | \$ 0.07          | \$(0.21 )  |

Total anti-dilutive common shares related to stock-based awards not included in the calculation of diluted earnings per share were 0.1 million and 0.2 million for the three and six months ended August 4, 2018 and 0.3 million and 0.5 million for the three and six months ended July 29, 2017.

## Item 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this document. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those discussed in "Item 1A Risk Factors" in our Form 10-K filed with the SEC on March 19, 2018 and in this Form 10-Q.

Forward-looking statements relate to our expectations for future events and future financial performance. Generally, the words "anticipates," "expects," "intends," "may," "should," "plans," "believes," "predicts," "potential," "continue" and similar expressions identify forward-looking statements. Forward-looking statements involve risks and uncertainties, and future events and circumstances could differ significantly from those anticipated in the forward-looking statements. These statements are only predictions. Actual events or results may differ materially. Factors which could affect our financial results are described below under the heading "Risk Factors" and in "Item 1A Risk Factors" of our Form 10-K referred to in the preceding paragraph. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Moreover, neither we nor any other person assume responsibility for the accuracy and completeness of the forward-looking statements. We undertake no duty to update any of the forward-looking statements after the date of this report to conform such statements to actual results or to changes in our expectations.

Fiscal 2018 is the 52-week period ending February 2, 2019. Fiscal 2017 was the 53-week period ended February 3, 2018. The first six months of fiscal 2018 was the 26-week period ended August 4, 2018. The first six months of fiscal 2017 was the 26-week period ended July 29, 2017.

"Zumiez," the "Company," "we," "us," "its," "our" and similar references refer to Zumiez Inc. and its wholly-owned subsidiaries.

### General

Net sales constitute gross sales (net of actual and estimated returns and deductions for promotions) and shipping revenue. Net sales include our store sales and our ecommerce sales. We record the sale of gift cards as a current liability and recognize revenue when a customer redeems a gift card. Additionally, the portion of gift cards that will not be redeemed ("gift card breakage") is recognized based on our historical redemption rate in proportion to the pattern of rights exercised by the customer.

We report "comparable sales" based on net sales beginning on the first anniversary of the first day of operation of a new store or ecommerce business. We operate a sales strategy that integrates our stores with our ecommerce platform. There is significant interaction between our store sales and our ecommerce sales channels and we believe that they are utilized in tandem to serve our customers. Therefore, our comparable sales also include our ecommerce sales. Changes in our comparable sales between two periods are based on net sales of store or ecommerce businesses which were in operation during both of the two periods being compared and, if a store or ecommerce business is included in the calculation of comparable sales for only a portion of one of the two periods being compared, then that store or ecommerce business is included in the calculation for only the comparable portion of the other period. Any increase or decrease less than 25% in square footage of an existing comparable store, including remodels and relocations within the same mall, or temporary closures less than seven days does not eliminate that store from inclusion in the calculation of comparable sales. Any store or ecommerce business that we acquire will be included in the calculation of comparable sales after the first anniversary of the acquisition date. Current year foreign exchange rates are applied to both current year and prior year comparable sales to achieve a consistent basis for comparison. There may be variations in the way in which some of our competitors and other apparel retailers calculate comparable sales. As a result, data herein regarding our comparable sales may not be comparable to similar

data made available by our competitors or other retailers.

Cost of goods sold consists of branded merchandise costs and our private label merchandise costs including design, sourcing, importing and inbound freight costs. Our cost of goods sold also includes shrinkage, buying, occupancy, distribution and warehousing costs (including associated depreciation) and freight costs for store merchandise transfers. This may not be comparable to the way in which our competitors or other retailers compute their cost of goods sold. Cash consideration received from vendors is reported as a reduction of cost of goods sold if the inventory has sold, a reduction of the carrying value of the inventory if the inventory is still on hand, or a reduction of selling, general and administrative expense if the amounts are reimbursements of specific, incremental and identifiable costs of selling the vendors' products.

With respect to the freight component of our ecommerce sales, amounts billed to our customers are included in net sales and the related freight cost is charged to cost of goods sold.

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Selling, general and administrative expenses consist primarily of store personnel wages and benefits, administrative staff and infrastructure expenses, freight costs for merchandise shipments from the distribution centers to the stores, store supplies, depreciation on fixed assets at our home office and stores, facility expenses, training expenses and advertising and marketing costs. Credit card fees, insurance, public company expenses, legal expenses, incentive compensation, stock-based compensation and other miscellaneous operating costs are also included in selling, general and administrative expenses. This may not be comparable to the way in which our competitors or other retailers compute their selling, general and administrative expenses.

### Key Performance Indicators

Our management evaluates the following items, which we consider key performance indicators, in assessing our performance:

**Comparable sales.** As previously described in detail under the caption “General,” comparable sales provide a measure of sales growth for stores and ecommerce businesses open at least one year over the comparable prior year period.

We consider comparable sales to be an important indicator of our current performance. Comparable sales results are important to achieve leveraging of our costs, including store payroll and store occupancy. Comparable sales also have a direct impact on our total net sales, operating profit, cash and working capital.

**Gross profit.** Gross profit measures whether we are optimizing the price and inventory levels of our merchandise. Gross profit is the difference between net sales and cost of goods sold. Any inability to obtain acceptable levels of initial markups or any significant increase in our use of markdowns could have an adverse effect on our gross profit and results of operations.

**Operating profit.** We view operating profit as a key indicator of our success. Operating profit is the difference between gross profit and selling, general and administrative expenses. The key drivers of operating profit are comparable sales, gross profit, our ability to control selling, general and administrative expenses and our level of capital expenditures affecting depreciation expense.

### Results of Operations

The following table presents selected items on the condensed consolidated statements of income as a percent of net sales:

|                                              | Three Months<br>Ended<br>August<br>4,<br>2018 |   | July<br>29,<br>2017 |    | Six Months<br>Ended<br>August<br>4,<br>2018 |   | July<br>29,<br>2017 |    |
|----------------------------------------------|-----------------------------------------------|---|---------------------|----|---------------------------------------------|---|---------------------|----|
| Net sales                                    | 100.0                                         | % | 100.0               | %  | 100.0                                       | % | 100.0               | %  |
| Cost of goods sold                           | 66.9                                          |   | 68.9                |    | 68.2                                        |   | 70.0                |    |
| Gross profit                                 | 33.1                                          |   | 31.1                |    | 31.8                                        |   | 30.0                |    |
| Selling, general and administrative expenses | 30.0                                          |   | 31.5                |    | 30.6                                        |   | 31.9                |    |
| Operating profit (loss)                      | 3.1                                           |   | (0.4)               | )  | 1.2                                         |   | (1.9)               | )  |
| Interest and other income (expense), net     | 0.2                                           |   | —                   |    | —                                           |   | (0.1)               | )  |
| Earnings (loss) before income taxes          | 3.3                                           |   | (0.4)               | )  | 1.2                                         |   | (2.0)               | )  |
| Provision (benefit) for income taxes         | 1.3                                           |   | (0.1)               | )  | 0.8                                         |   | (0.6)               | )  |
| Net income (loss)                            | 2.0                                           | % | (0.3)               | )% | 0.4                                         | % | (1.4)               | )% |

Three Months (13 weeks) Ended August 4, 2018 Compared With Three Months (13 weeks) Ended July 29, 2017

#### Net Sales

Net sales were \$219.0 million for the three months ended August 4, 2018 compared to \$192.2 million for the three months ended July 29, 2017, an increase of \$26.7 million or 13.9%. The increase primarily reflected an increase in comparable sales of \$12.8 million, an increase of \$9.9 million due to the calendar shift to include an additional week of back-to-school season, and the net addition of 11 stores (made up of 10 new stores in North America, 5 new stores in Europe and 1 new store in Australia partially offset by 5 store closures in North America) subsequent to July 29, 2017. By region, North America sales increased \$24.6 million or 13.9% and other international sales (which consists of Europe and Australia sales) increased \$2.2 million or 13.8% for the three months ended August 4, 2018 compared to the three months ended July 29, 2017.

Comparable sales increased 6.3% primarily driven by an increase in comparable transactions partially offset by a decrease in dollars per transaction. Dollars per transaction decreased due to a decrease in units per transaction partially offset by an increase in average unit retail. Comparable sales were primarily driven by an increase in men's clothing followed by footwear and women's clothing.

These increases were partially offset by decreases in comparable sales in hardgoods followed by accessories. For information as to how we define comparable sales, see “General” above.

#### Gross Profit

Gross profit was \$72.5 million for the three months ended August 4, 2018 compared to \$59.8 million for the three months ended July 29, 2017, an increase of \$12.7 million, or 21.3%. As a percent of net sales, gross profit increased 200 basis points for the three months ended August 4, 2018 to 33.1%. The increase was primarily driven by 160 basis point leveraging of our store occupancy costs, 30 basis point increase in product margin and 30 basis points in lower shrinkage of inventory partially offset by 30 basis points in higher shipping costs.

#### Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses were \$65.8 million for the three months ended August 4, 2018 compared to \$60.6 million for the three months ended July 29, 2017, an increase of \$5.3 million, or 8.7%. SG&A expenses as a percent of net sales decreased 150 basis points for the three months ended August 4, 2018 to 30.0%. The decrease was primarily driven by 140 basis points from the leveraging of our store costs and 40 basis points decrease due to the timing of annual training events partially offset by a 40 basis point increase related to the accrual of annual incentive compensation.

#### Net Income

Net income for the three months ended August 4, 2018 was \$4.4 million, or \$0.17 earnings per diluted share, compared with net loss of \$0.6 million, or \$0.02 loss per diluted share, for the three months ended July 29, 2017. Our effective income tax rate for the three months ended August 4, 2018 was a 39.1% provision for income taxes compared to a 12.3% benefit from income taxes for the three months ended July 29, 2017. The increase was primarily due to the exclusion of net losses, due to the uncertainty of the realization of our deferred tax assets in Austria, from our estimated annual effective tax rate. The increase in our effective income tax rate was partially offset by a reduction in the U.S. federal tax rate due to the U.S. Tax Cuts and Jobs Act enacted in December 2017.

#### Six Months (26 weeks) Ended August 4, 2018 Compared With Six Months (26 weeks) Ended July 29, 2017

#### Net Sales

Net sales were \$425.3 million for the six months ended August 4, 2018 compared to \$373.4 million for the six months ended July 29, 2017, an increase of \$51.9 million or 13.9%. The increase primarily reflected an increase in comparable sales of \$28.0 million, an increase of \$13.0 million due to the calendar shift to include an additional week of back-to-school season, and the net addition of 11 stores (made up of 10 new stores in North America, 5 new stores in Europe and 1 new stores in Australia offset by 5 store closures in North America) subsequent to July 29, 2017. By region, North America sales increased \$43.3 million or 12.8% and other international sales (which consists of Europe and Australia) increased \$8.6 million or 25.0% for the six months ended August 4, 2018 compared to the six months ended July 29, 2017.

Comparable sales increased 7.2% primarily driven by an increase in comparable transactions partially offset by a decrease in dollars per transaction. Dollars per transaction decreased due to a decrease in units per transaction partially offset by an increase in average unit retail. Comparable sales were primarily driven by an increase in men’s clothing followed by women’s clothing and footwear. These increases were partially offset by decreases in comparable sales in accessories followed by hardgoods.

#### Gross Profit

Gross profit was \$135.1 million for the six months ended August 4, 2018 compared to \$111.8 million for the six months ended July 29, 2017, an increase of \$23.3 million, or 20.8%. As a percent of net sales, gross profit increased 180 basis points for the six months ended August 4, 2018 to 31.8%. The increase was primarily driven by 160 basis point leveraging of our store occupancy costs, 20 basis point increase in product margin and 20 basis points in lower shrinkage of inventory partially offset by 30 basis points in higher shipping costs.

#### Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses were \$130.1 million for the six months ended August 4, 2018 compared to \$118.8 million for the six months ended July 29, 2017, an increase of \$11.3 million, or 9.5%. SG&A expenses as a percent of net sales decreased by 130 basis points for the six months ended August 4, 2018 to 30.6%. The decrease was primarily driven by 150 basis points from the leveraging of our store costs partially offset by a 20 basis point increase related to the accrual of annual incentive compensation.

## Net Income

Net income for the six months ended August 4, 2018 was \$1.8 million, or \$0.07 earnings per diluted share, compared with net loss of \$5.1 million, or \$0.21 loss per diluted share, for the six months ended July 29, 2017. Our effective income tax rate for the six months ended August 4, 2018 was a 66.5% provision for income taxes compared to a 30.7% benefit from income taxes for the six months ended July 29, 2017. The increase was primarily due to the exclusion of net losses for certain European jurisdictions from our estimated annual effective tax rate. At August 4, 2018 and February 3, 2018, we had valuation allowances on our deferred tax assets of \$5.5 million and \$3.6 million, respectively, primarily due to the uncertainty of the realization of deferred tax assets in Austria. The increase in our effective income tax rate was partially offset by a reduction in the U.S. federal tax rate due to the U.S. Tax Cuts and Jobs Act enacted in December 2017.

## Liquidity and Capital Resources

Our primary uses of cash are for operational expenditures, inventory purchases and capital investments, including new stores, store remodels, store relocations, store fixtures and ongoing infrastructure improvements. Additionally, our Board of Directors may authorize us from time to time to use cash for the repurchase of our common stock. Historically, our main source of liquidity has been cash flows from operations.

The significant components of our working capital are inventories and liquid assets such as cash, cash equivalents, current marketable securities and receivables, reduced by accounts payable, accrued payroll and accrued expenses. Our working capital position benefits from the fact that we generally collect cash from sales to customers the same day or within several days of the related sale, while we typically have longer payment terms with our vendors.

Our capital requirements include construction and fixture costs related to the opening of new stores and remodel and relocation expenditures for existing stores. Future capital requirements will depend on many factors, including the pace of new store openings, the availability of suitable locations for new stores and the nature of arrangements negotiated with landlords. Our net investment to open a new store has varied significantly in the past due to a number of factors, including the geographic location and size of the new store, and is likely to vary significantly in the future.

During fiscal 2018, we expect to spend approximately \$21 million to \$23 million on capital expenditures, a majority of which will relate to leasehold improvements and fixtures for the approximately 13 new stores we remain on track to open in fiscal 2018 and remodels or relocations of existing stores. There can be no assurance that the number of stores that we actually open in fiscal 2018 will not be different from the number of stores we plan to open, or that actual fiscal 2018 capital expenditures will not differ from our expectations.

## Operating Activities

Net cash from operating activities increased by \$11.8 million to \$15.5 million provided by operating activities for the six months ended August 4, 2018 from \$3.8 million provided by operating activities for the six months ended July 29, 2017. Our operating cash flows result primarily from cash received from our customers, offset by cash payments we make for inventory, employee compensation, store occupancy expenses and other operational expenditures. Cash received from our customers generally corresponds to our net sales. Because our customers primarily use credit cards or cash to buy from us, our receivables from customers settle quickly. Historically, changes to our operating cash flows have been driven primarily by changes in operating income, which is impacted by changes to non-cash items such as depreciation, amortization and accretion, deferred taxes, and changes to the components of working capital.

## Investing Activities

Net cash used in investing activities was \$2.9 million for the six months ended August 4, 2018, related to \$9.1 million of capital expenditures primarily for new store openings and existing store remodels or relocations partially offset by \$6.2 million in net sales of marketable securities. Net cash used in investing activities was \$7.4 million for the six months ended July 29, 2017, related to \$12.5 million of capital expenditures primarily for new store openings and existing store remodels or relocations partially offset by \$5.0 million in net sales of marketable securities.

## Financing Activities

Net cash provided by financing activities for the six months ended August 4, 2018 was \$5.4 million, primarily related to \$5.0 million in net proceeds from revolving credit facilities and \$0.6 million proceeds from the issuance and exercise of stock-based awards partially offset by \$0.2 million in payments for tax withholding obligations upon vesting of restricted stock. Net cash provided by financing activities for the six months ended July 29, 2017 was \$0.2 million, primarily related to \$0.4 million proceeds from the issuance and exercise of stock-based awards partially offset by \$0.2 million in payments for tax withholding obligations upon vesting of restricted stock.

## Sources of Liquidity

Our most significant sources of liquidity continue to be funds generated by operating activities and available cash, cash equivalents and current marketable securities. We expect these sources of liquidity and available borrowings under our revolving credit facility will be sufficient to meet our foreseeable cash requirements for operations and planned capital expenditures for at least the next twelve months. Beyond this time frame, if cash flows from operations are not sufficient to meet our capital requirements, then we will be required to obtain additional equity or debt financing in the future. However, there can be no assurance that equity or debt financing will be available to us when we need it or, if available, that the terms will be satisfactory to us and not dilutive to our then-current shareholders.

We maintain an asset-based revolving credit agreement with Wells Fargo Bank, National Association, as administrative agent, collateral agent, letter of credit issuer and lenders, which provides for a senior secured revolving credit facility of up to \$100 million (“ABL Facility”), subject to a borrowing base, with a letter of credit sub-limit of \$10 million. The ABL Facility is available for working capital and other general corporate purposes. The ABL Facility will mature on February 5, 2021.

The ABL Facility is secured by a first-priority security interest in substantially all of the personal property (but not the real property) of the borrowers and guarantors. Amounts borrowed under the ABL Facility bear interest, at the Company’s option, at either an adjusted LIBOR rate plus a margin of 1.25% to 1.75% per annum, or an alternate base rate plus a margin of 0.25% to 0.75% per annum. The Company is also required to pay a fee of 0.25% per annum on undrawn commitments under the ABL Facility. Customary agency fees and letter of credit fees are also payable in respect of the ABL Facility.

There were no borrowings outstanding under the ABL Facility at August 4, 2018 and at February 3, 2018. We had no open commercial letters of credit outstanding under these lines of credit at August 4, 2018 and February 3, 2018.

Additionally, we have revolving lines of credit with UniCredit Bank Austria and Commerzbank Germany of up to 9.0 million Euro (\$10.4 million) at August 4, 2018, the proceeds of which are used to fund certain international operations. The revolving lines of credit bear interest at 1.55% to 1.65%. The utilized facility amount, in whole or in part, is subject to termination with three months’ notice and with immediate effect to the unused facility amount. There was \$5.6 million of borrowings outstanding at August 4, 2018 and \$0.9 million in borrowings outstanding at February 3, 2018. We had no open commercial letters of credit outstanding under these lines of credit at August 4, 2018 and at February 3, 2018.

## Critical Accounting Estimates

Our condensed consolidated financial statements are prepared in accordance with U.S. GAAP. In connection with the preparation of our condensed consolidated financial statements, we are required to make assumptions and estimates about future events and apply judgments that affect the reported amounts of assets, liabilities, revenue, expenses and the related disclosures. We base our assumptions, estimates and judgments on historical experience, current trends and other factors that we believe to be relevant at the time our condensed consolidated financial statements are

prepared. On a regular basis, we review the accounting policies, assumptions, estimates and judgments to ensure that our condensed consolidated financial statements are presented fairly and in accordance with U.S. GAAP. However, because future events and their effects cannot be determined with certainty, actual results could differ from our assumptions and estimates, and such differences could be material.

There have been no significant changes to our critical accounting estimates as discussed in our Annual Report on Form 10-K for the fiscal year ended February 3, 2018, other than those related to the adoption of ASC 606 as disclosed in Note 1 “Nature of Business and Basis of Presentation” in the Notes to Condensed Consolidated Financial Statements found in Item I of this Form 10-Q.

## Contractual Obligations and Commercial Commitments

There were no material changes outside the ordinary course of business in our contractual obligations during the six months ended August 4, 2018. The following table summarizes the total amount of future payments due under our contractual obligations at August 4, 2018 (in thousands):

|                                 |           | Fiscal    | Fiscal 2019 and | Fiscal 2021 and |            |
|---------------------------------|-----------|-----------|-----------------|-----------------|------------|
|                                 | Total     | 2018      | Fiscal 2020     | Fiscal 2022     | Thereafter |
| Operating lease obligations (1) | \$389,858 | \$35,853  | \$ 128,459      | \$ 106,863      | \$ 118,683 |
| Purchase obligations (2)        | 249,534   | 246,190   | 3,344           | —               | —          |
| Total                           | \$639,392 | \$282,043 | \$ 131,803      | \$ 106,863      | \$ 118,683 |

(1) Amounts do not include contingent rent and real estate taxes, insurance, common area maintenance charges and other executory costs obligations. See Note 4, “Commitments and Contingencies,” in the Notes to Condensed Consolidated Financial Statements found in Item 1 of this Form 10-Q, for additional information related to our operating leases.

(2) We have an option to cancel these commitments with no notice prior to shipment, except for certain private label, packaging supplies and international purchase orders in which we are obligated to repay contractual amounts upon cancellation.

## Off-Balance Sheet Arrangements

At August 4, 2018, we did not have any off-balance sheet arrangements.

## Impact of Inflation/Deflation

We do not believe that inflation has had a material impact on our net sales or operating results for the past three fiscal years. However, substantial increases in costs, including the price of raw materials, labor, energy and other inputs used in the production of our merchandise, could have a significant impact on our business and the industry in the future. Additionally, while deflation could positively impact our merchandise costs, it could have an adverse effect on our average unit retail price, resulting in lower sales and operating results.

## Risk Factors

Investing in our securities involves a high degree of risk. The following risk factors, issues and uncertainties should be considered in evaluating our future prospects. In particular, keep these risk factors in mind when you read “forward-looking” statements elsewhere in this report. Forward-looking statements relate to our expectations for future events and time periods. Generally, the words “anticipates,” “expects,” “intends,” “may,” “should,” “plans,” “believes,” “predicts,” “potential,” “continue” and similar expressions identify forward-looking statements. Forward-looking statements involve risks and uncertainties, and future events and circumstances could differ significantly from those anticipated in the forward-looking statements. Any of the following risks could harm our business, operating results or financial condition and could result in a complete loss of your investment. Additional risks and uncertainties that are not yet identified or that we currently think are immaterial may also harm our business and financial condition in the future.

Failure to anticipate, identify and respond to changing fashion trends, customer preferences and other fashion-related factors could have a material adverse effect on us.

Customer tastes and fashion trends in our market are volatile and tend to change rapidly. Our success depends on our ability to effectively anticipate, identify and respond to changing fashion tastes and consumer preferences, and to translate market trends into appropriate, saleable product offerings in a timely manner. If we are unable to

successfully anticipate, identify or respond to changing styles or trends and misjudge the market for our products or any new product lines, including adequately anticipating the correct mix and trends of our private label merchandise, our sales may be lower than predicted and we may be faced with a substantial amount of unsold inventory or missed opportunities. In response to such a situation, we may be forced to rely on markdowns or promotional sales to dispose of excess or slow-moving inventory, which could have a material adverse effect on our results of operations.

We may be unable to compete favorably in the highly competitive retail industry, and if we lose customers to our competitors, our sales could decrease.

The teenage and young adult retail apparel, footwear, accessories and hardgoods industry is highly competitive. We compete with other retailers for vendors, teenage and young adult customers, suitable store locations, qualified store associates, management personnel, on-line marketing content, social media engagement and ecommerce traffic. Some of our competitors are larger than we are and have substantially greater financial and marketing resources, including advanced ecommerce market capabilities. Additionally, some of our competitors may offer more options for free and/or expedited shipping for ecommerce sales. Direct competition with these and other retailers may increase significantly in the future, which could require us, among other things, to

lower our prices and could result in the loss of our customers. Current and increased competition could have a material adverse effect on our business, results of operations and financial condition.

U.S. and global economic and political uncertainty, coupled with cyclical economic trends in retailing, could have a material adverse effect on our results of operations.

Our retail market historically has been subject to substantial cyclicity. As the U.S. and global economic and political conditions change, the trends in discretionary consumer spending become unpredictable and discretionary consumer spending could be reduced due to uncertainties about the future. When disposable income decreases or discretionary consumer spending is reduced due to a decline in consumer confidence, purchases of apparel and related products may decline. The current uncertainty in the U.S. and global economies and political environment could have a material adverse impact on our results of operations and financial position.

In response to a decline in disposable income and consumer confidence, we believe the “value” message has become more important to consumers. As a retailer that sells approximately 80% branded merchandise, this trend may negatively affect our business, as we generally will have to charge more than vertically integrated private label retailers or we may be forced to rely on promotional sales to compete in our market which could have a material adverse effect on our financial position.

A decrease in consumer traffic could cause our sales to be less than expected.

We depend heavily on generating customer traffic to our stores and websites. This includes locating many of our stores in prominent locations within successful shopping malls. Sales at these stores are derived, in part, from the volume of traffic in those malls. Our stores benefit from the ability of a mall’s “anchor” tenants, generally large department stores and other area attractions, to generate consumer traffic in the vicinity of our stores and the continuing popularity of malls as shopping destinations. In addition, some malls that were in prominent locations when we opened our stores may cease to be viewed as prominent. If this trend continues or if the popularity of mall shopping continues to decline generally among our customers, our sales may decline, which would impact our results of operations. Furthermore, we depend on generating increased traffic to our websites and converting that traffic into sales. This requires us to achieve expected results from our marketing and social media campaigns, accuracy of data analytics, reliability of our website, network, and transaction processing and a high-quality on-line customer experience. Our sales volume and customer traffic in our stores and on our websites generally could be adversely affected by, among other things, economic downturns, competition from other ecommerce retailers, non-mall retailers and other malls, increases in gasoline prices, fluctuations in exchange rates in border or tourism-oriented locations and the closing or decline in popularity of other stores in the malls in which we are located. An uncertain economic outlook could curtail new shopping mall development, decrease shopping mall and ecommerce traffic, reduce the number of hours that shopping mall operators keep their shopping malls open or force them to cease operations entirely. A reduction in consumer traffic to our stores or websites could have a material adverse effect on our business, results of operations and financial condition.

Our growth strategy depends on our ability to grow customer engagement in our current markets and expand into new markets, which could strain our resources and cause the performance of our existing business to suffer.

Our growth largely depends on our ability to optimize our customer engagement in our current trade areas and operate successfully in new geographic markets. However, our ability to open stores in new geographic markets in the U.S. and international locations is subject to a variety of risks and uncertainties, and we may be unable to open new stores as planned or have access to desirable lease space, and any failure to successfully open and operate in new markets could have a material adverse effect on our results of operations. We intend to continue to open new stores in future years, while remodeling a portion of our existing store base such that we have the optimum number of stores in any given trade area. The expansion into new markets may present competitive, merchandising, hiring and distribution challenges that are different from those currently encountered in our existing markets. In addition, our proposed

expansion will place increased demands on our operational, managerial and administrative resources. These increased demands could cause us to operate our business less effectively, which in turn could cause deterioration in the financial performance of our individual stores and our overall business. In addition, successful execution of our growth strategy may require that we obtain additional financing, and we may not be able to obtain that financing on acceptable terms or at all.

Failure to successfully integrate any businesses that we acquire could have an adverse impact on our results of operations and financial performance.

We may, from time to time, acquire businesses, such as our acquisition of Blue Tomato, which operates in the European market, and Fast Times, which operates in the Australian market. We may experience difficulties in integrating any businesses we may acquire, including their stores, websites, facilities, personnel, financial systems, distribution, operations and general operating procedures, and any such acquisitions may also result in the diversion of our capital and our management's attention from other business issues and opportunities. If we experience difficulties in integrating acquisitions or if such acquisitions do not provide the benefits that we expect to receive, we could experience increased costs and other operating inefficiencies, which could have an adverse effect on our results of operations and overall financial performance.

Our plans for international expansion include risks that could have a negative impact on our results of operations.

We plan to continue to open new stores in the Canadian, European, and Australian markets. We may continue to expand internationally in other markets, either organically, or through additional acquisitions. International markets may have different competitive conditions, consumer tastes and discretionary spending patterns than our existing U.S. market. As a result, operations in international markets may be less successful than our operations in the U.S. Additionally, consumers in international markets may not be familiar with us or the brands we sell, and we may need to build brand awareness in the markets. Furthermore, we have limited experience with the legal and regulatory environments and market practices in new international markets and cannot guarantee that we will be able to penetrate or successfully operate in these new international markets. We also expect to incur additional costs in complying with applicable foreign laws and regulations as they pertain to both our products and our operations. Accordingly, for the reasons noted above, our plans for international expansion include risks that could have a negative impact on our results of operations.

Our sales and inventory levels fluctuate on a seasonal basis. Accordingly, our quarterly results of operations are volatile and may fluctuate significantly.

Our quarterly results of operations have fluctuated significantly in the past and can be expected to continue to fluctuate significantly in the future. Our sales and profitability are typically disproportionately higher in the third and fourth fiscal quarters of each fiscal year due to increased sales during the back-to-school and winter holiday shopping seasons. Sales during these periods cannot be used as an accurate indicator of annual results. As a result of this seasonality, any factors negatively affecting us during the last half of the year, including unfavorable economic conditions, adverse weather or our ability to acquire seasonal merchandise inventory, could have a material adverse effect on our financial condition and results of operations for the entire year. In addition, in order to prepare for the back-to-school and winter holiday shopping seasons, we must order and keep in stock significantly more merchandise than we carry during other times of the year. Any unanticipated decrease in demand for our products during these peak shopping seasons could require us to sell excess inventory at a substantial markdown, which could have a material adverse effect on our business, results of operations and financial condition.

Our quarterly results of operations are affected by a variety of other factors, including:

- the timing of new store openings and the relative proportion of our new stores to mature stores;
- whether we are able to successfully integrate any new stores that we acquire and the presence of any unanticipated liabilities in connection therewith;
- fashion trends and changes in consumer preferences;
- calendar shifts of holiday or seasonal periods;
- changes in our merchandise mix;
- timing of promotional events;

• general economic conditions and, in particular, the retail sales environment;

• actions by competitors or mall anchor tenants;

• weather conditions;

• the level of pre-opening expenses associated with our new stores; and

• inventory shrinkage beyond our historical average rates.

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Significant fluctuations and volatility in the cost of raw materials, global labor, shipping and other costs related to the production of our merchandise may have a material adverse effect on our business, results of operations and financial conditions.

Increases in the cost of raw materials, global labor costs, freight costs and other shipping costs in the production and transportation of our merchandise can result in higher costs for this merchandise. The costs for these products are affected by weather, consumer demand, government regulation, speculation on the commodities market and other factors that are generally unpredictable and beyond our control. Our gross profit and results of operations could be adversely affected to the extent that the selling prices of our products do not increase proportionately with the increases in the costs of raw materials. Increasing labor costs and oil-related product costs, such as manufacturing and transportation costs, could also adversely impact gross profit. Additionally, significant changes in the relationship between carrier capacity and shipper demand could increase transportation costs, which could also adversely impact gross profit.

Most of our merchandise is produced by foreign manufacturers; therefore, the availability, quality and costs of our merchandise may be negatively affected by risks associated with international trade and other international conditions.

Most of our merchandise is produced by manufacturers around the world. Some of these facilities are located in regions that may be affected by natural disasters, political instability or other conditions that could cause a disruption in trade. Trade restrictions such as increased tariffs or quotas, or both, could also increase the cost and reduce the supply of merchandise available to us. Any reduction in merchandise available to us or any increase in its cost due to tariffs, quotas or local issues that disrupt trade could have a material adverse effect on our results of operations. This includes costs to comply with regulatory developments regarding the use of “conflict minerals,” certain minerals originating from the Democratic Republic of Congo and adjoining countries, which may affect the sourcing and availability of raw materials used by manufacturers and subject us to increased costs associated with our products, processes or sources of our inputs. Our business could be adversely affected by disruptions in the supply chain, such as strikes, work stoppages, or port closures.

Fluctuations in foreign currency exchange rates could impact our financial condition and results of operations.

We are exposed to foreign currency exchange rate risk with respect to our sales, profits, assets and liabilities denominated in currencies other than the U.S. dollar. As a result, the fluctuation in the value of the U.S. dollar against other currencies could have a material adverse effect on our results of operations, financial condition and cash flows. Upon translation, operating results may differ materially from expectations. As we continue to expand our international operations, our exposure to exchange rate fluctuations will increase. Tourism spending may be affected by changes in currency exchange rates, and as a result, sales at stores with higher tourism traffic may be adversely impacted by fluctuations in currency exchange rates. Further, although the prices charged by vendors for the merchandise we purchase are primarily denominated in U.S. dollars, a decline in the relative value of the U.S. dollar to foreign currencies could lead to increased merchandise costs, which could negatively affect our competitive position and our results of operations.

Our business could be adversely affected by increased labor costs, including costs related to an increase in minimum wage and health care.

Labor is one of the primary components in the cost of operating our business. Increased labor costs, whether due to competition, unionization, increased minimum wage, state unemployment rates, health care, or other employee benefits costs may adversely impact our operating expenses. A considerable amount of our store team members are paid at rates related to the federal or state minimum wage and any changes to the minimum wage rate may increase our operating expenses. Furthermore, inconsistent increases in state and or city minimum wage requirements limit our ability to increase prices across all markets and channels. Additionally, we are self-insured with respect to our health care coverage in the U.S. and do not purchase third party insurance for the health insurance benefits provided to

employees with the exception of pre-defined stop loss coverage, which helps limit the cost of large claims. There is no assurance that future health care legislation will not adversely impact our results or operations.

Our business could suffer if a manufacturer fails to use acceptable labor and environmental practices.

We do not control our vendors or the manufacturers that produce the products we buy from them, nor do we control the labor and environmental practices of our vendors and these manufacturers. The violation of labor, safety, environmental and/or other laws and standards by any of our vendors or these manufacturers, or the divergence of the labor and environmental practices followed by any of our vendors or these manufacturers from those generally accepted as ethical in the U.S., could interrupt, or otherwise disrupt, the shipment of finished products to us or damage our reputation. Any of these, in turn, could have a material adverse effect on our reputation, financial condition and results of operations. In that regard, most of the products we sell are manufactured overseas, primarily in Asia, Mexico and Central America, which may increase the risk that the labor and environmental practices followed by the manufacturers of these products may differ from those considered acceptable in the U.S.

Additionally, our products are subject to regulation of and regulatory standards set by various governmental authorities with respect to quality and safety. These regulations and standards may change from time to time. Our inability to comply on a timely basis with regulatory requirements could result in significant fines or penalties, which could adversely affect our reputation and sales. Issues with the quality and safety of merchandise we sell, regardless of our culpability, or customer concerns about such issues, could result in damage to our reputation, lost sales, uninsured product liability claims or losses, merchandise recalls and increased costs.

If we fail to develop and maintain good relationships with vendors or if a vendor is otherwise unable or unwilling to supply us with adequate quantities of their products at acceptable prices, our business and financial performance could suffer.

Our business is dependent on developing and maintaining good relationships with a large number of vendors to provide our customers with an extensive selection of current and relevant brands. In addition to maintaining our large number of current vendor relationships, this includes identifying, attracting and launching new vendors every year to provide a diverse and unique product assortment. We believe that we generally are able to obtain attractive pricing and terms from vendors because we are perceived as a desirable customer, and deterioration in our relationship with our vendors could have a material adverse effect on our business.

However, there can be no assurance that our current vendors or new vendors will provide us with an adequate supply or quality of products or acceptable pricing. Our vendors could discontinue selling to us, raise the prices they charge, sell through direct channels or allow their merchandise to be discounted by other retailers. There can be no assurance that we will be able to acquire desired merchandise in sufficient quantities on terms acceptable to us in the future. In addition, certain of our vendors sell their products directly to the retail market and therefore compete with us directly and other vendors may decide to do so in the future. There can be no assurance that such vendors will not decide to discontinue supplying their products to us, supply us only less popular or lower quality items, raise the prices they charge us or focus on selling their products directly.

In addition, a number of our vendors are smaller, less capitalized companies and are more likely to be impacted by unfavorable general economic and market conditions than larger and better capitalized companies. These smaller vendors may not have sufficient liquidity during economic downturns to properly fund their businesses and their ability to supply their products to us could be negatively impacted. Any inability to acquire suitable merchandise at acceptable prices, or the loss of one or more key vendors, could have a material adverse effect on our business, results of operations and financial condition.

Our omni-channel strategy may not have the return we anticipate, which could have an adverse effect on our results of operations.

We are executing an omni-channel strategy to enable our customers to shop wherever, whenever and however they choose to engage with us. Our omni-channel strategy may not deliver the results we anticipate or may not adequately anticipate changing consumer trends, preferences and expectations. We will continue to develop additional ways to execute our superior omni-channel experience and interact with our customers, which requires significant investments in IT systems and changes in operational strategy, including localization, on-line and in-store point of sale systems, order management system, and transportation management system. If we fail to effectively integrate our store and ecommerce shopping experiences, effectively scale our IT structure or we do not realize the return on our investments that we anticipate our operating results could be adversely affected. Our competitors are also investing in omni-channel initiatives. If our competitors are able to be more effective in their strategy, it could have an adverse effect on our results of operations. If our omni-channel strategy fails to meet customer expectations related to functionality, timely delivery, or customer experience, our business and results of operations may be adversely affected. Additionally, to manage the anticipated growth of our operations and personnel, we will need to continue to improve our operational and financial systems, transaction processing, procedures and controls, and in doing so could incur substantial additional expenses that could impact our financial results.

If our information systems fail to function effectively our operations could be disrupted and our financial results could be harmed.

If our information systems do not work effectively, this could adversely impact the promptness and accuracy of our transaction processing, financial accounting and reporting and our ability to manage our business and properly forecast operating results and cash requirements. Further, we may suffer loss of critical data and interruptions or delays in our operations. Additionally, we rely on third-party service providers for certain information systems functions. If a service provider fails to provide the data quality, communications capacity, security or services we require, the failure could interrupt our services and could have a material adverse effect on our business, financial condition and results of operations.

Our business could suffer if a manufacturer fails to use acceptable labor practices.

We do not control our vendors or the manufacturers that produce the products we buy from them, nor do we control the labor practices of our vendors and these manufacturers. The violation of labor or other laws by any of our vendors or these manufacturers, or the divergence of the labor practices followed by any of our vendors or these manufacturers from those generally accepted as ethical in the U.S., could interrupt, or otherwise disrupt, the shipment of finished products to us or damage our reputation. Any of these, in turn, could have a material adverse effect on our financial condition and results of operations. In that regard, most of the products we sell are manufactured overseas, primarily in Asia and Central America, which may increase the risk that the labor practices followed by the manufacturers of these products may differ from those considered acceptable in the U.S.

Additionally, our products are subject to regulation of and regulatory standards set by various governmental authorities with respect to quality and safety. Regulations and standards in this area are currently in place. These regulations and standards may change from time to time. Our inability to comply on a timely basis with regulatory requirements could result in significant fines or penalties, which could adversely affect our reputation and sales. Issues with the quality and safety of merchandise we sell, regardless of our culpability, or customer concerns about such issues, could result in damage to our reputation, lost sales, uninsured product liability claims or losses, merchandise recalls and increased costs.

Our failure to adequately anticipate a correct mix of private label merchandise may have a material adverse effect on our business.

Sales from private label merchandise account for approximately 20% of our net sales and generally carry higher gross margins than our other merchandise. We may take steps to increase the percentage of net sales of private label merchandise in the future, although there can be no assurance that we will be able to achieve increases in private label merchandise sales as a percentage of net sales. Our failure to anticipate, identify and react in a timely manner to fashion trends with our private label merchandise, could have a material adverse effect on our comparable sales, financial condition and results of operations.

If our information systems hardware or software fails to function effectively or does not scale to keep pace with our planned growth, our operations could be disrupted and our financial results could be harmed.

We are continuing to make investments to improve our information systems infrastructure. If our information systems, including software, do not work effectively, this could adversely impact the promptness and accuracy of our transaction processing, financial accounting and reporting and our ability to manage our business and properly forecast operating results and cash requirements. Additionally, we rely on third-party service providers for certain information systems functions. If a service provider fails to provide the data quality, communications capacity or services we require, the failure could interrupt our services and could have a material adverse effect on our business, financial condition and results of operations. To manage the anticipated growth of our operations and personnel, we may need to continue to improve our operational and financial systems, transaction processing, procedures and controls, and in doing so could incur substantial additional expenses that could impact our financial results.

If the security of our data is breached we may be subjected to adverse publicity, litigation and significant expenses.

Information systems are susceptible to an increasing threat of continually evolving cybersecurity risks. We maintain security systems, devices and activity monitoring to prevent unauthorized access to our network, systems and databases containing confidential, proprietary, and personally identifiable information. Nevertheless, if unauthorized parties gain access to our networks, systems or databases, they may be able to steal, publish, delete or modify confidential information. In such circumstances, we could be held liable to our customers or other parties or be subject to regulatory or other actions for breaching privacy rules and we may be exposed to reputation damage and loss of customers' trust and business. This could result in costly investigations and litigation, civil or criminal penalties and adverse publicity that could adversely affect our financial condition, results of operations and reputation. Actual or anticipated attacks may cause us to incur increasing costs, including costs to deploy additional resources, train employees, and engage third-parties. Further, the regulatory environment surrounding information security, cybersecurity and privacy is increasingly demanding. If we are unable to comply with the new and changing security standards, we may be subject to fines, restrictions and financial exposure, which could adversely affect our retail operations.

If we lose key executives or are unable to attract and retain the talent required for our business, our financial performance could suffer.

Our performance depends largely on the efforts and abilities of our key executives. If we lose the services of one or more of our key executives, we may not be able to successfully manage our business or achieve our growth objectives. Furthermore, as our business grows, we will need to attract and retain additional qualified personnel in a timely manner and we may not be able to do so.

Our failure to meet our staffing needs could adversely affect our ability to implement our growth strategy and could have a material impact on our results of operations.

Our success depends in part upon our ability to attract, motivate and retain a sufficient number of qualified employees who understand and appreciate our culture and brand and are able to adequately represent this culture. Qualified individuals of the requisite caliber, skills and number needed to fill these positions may be in short supply in some areas and the employee turnover rate in the retail industry is high. Our business depends on the ability to hire and retain qualified technical and support roles for procurement, distribution, e-commerce and back office functions. Competition for qualified employees in these areas could require us to pay higher wages to attract a sufficient number of suitable employees.

If we are unable to hire and retain store managers and store associates capable of consistently providing a high level of customer service, as demonstrated by their enthusiasm for our culture and knowledge of our merchandise, our ability to open new stores may be impaired and the performance of our existing and new stores could be materially adversely affected. We are also dependent upon temporary personnel to adequately staff our operations particularly during busy periods such as the back-to-school and winter holiday seasons. There can be no assurance that we will receive adequate assistance from our temporary personnel, or that there will be sufficient sources of temporary personnel. If we are unable to hire qualified temporary personnel, our results of operations could be adversely impacted.

Although none of our employees are currently covered by collective bargaining agreements, we cannot guarantee that our employees will not elect to be represented by labor unions in the future, which could increase our labor costs and could subject us to the risk of work stoppages and strikes. Any such failure to meet our staffing needs, any material increases in employee turnover rates, any increases in labor costs or any work stoppages, interruptions or strikes could have a material adverse effect on our business or results of operations.

A decline in cash flows from operations could have a material adverse effect on our business and growth plans.

We depend on cash flow from operations to fund our current operations and our growth strategy, including the payment of our operating leases, wages, store operation costs and other cash needs. If our business does not generate sufficient cash flow from operating activities, and sufficient funds are not otherwise available to us from borrowings under our credit facility or from other sources, we may not be able to pay our operating lease expenses, grow our business, respond to competitive challenges or fund our other liquidity and capital needs, which could have a material adverse effect on our business.

The terms of our asset-based revolving credit agreement impose certain restrictions on us that may impair our ability to respond to changing business and economic conditions, which could have a significant adverse impact on our business. Additionally, our business could suffer if our ability to acquire financing is reduced or eliminated.

We maintain an asset-based revolving credit agreement with Wells Fargo Bank, N.A., as administrative agent, collateral agent, letter of credit issuer and lenders, which provides for a senior secured revolving credit facility ("ABL Facility") of up to \$100 million. The ABL Facility contains various representations, warranties and restrictive covenants that, among other things and subject to specified circumstances and exceptions, restrict our ability to incur indebtedness (including guarantees), grant liens, make investments, pay dividends or distributions with respect to capital stock, make prepayments on other indebtedness, engage in mergers, dispose of certain assets or change the nature of their business. In addition, excess availability equal to at least 10% of the loan cap must be maintained under the ABL Facility. The ABL Facility does not otherwise contain financial maintenance covenants. These restrictions could (1) limit our ability to plan for or react to market conditions or meet capital needs or otherwise restrict our activities or business plans; and (2) adversely affect our ability to finance our operations, strategic acquisitions, investments or other capital needs or to engage in other business activities that would be in our interest.

The ABL Facility includes customary events of default including non-payment of principal, interest or fees, violation of covenants, inaccuracy of representations or warranties, cross-default to other material indebtedness, bankruptcy and insolvency events, invalidity or impairment of guarantees or security interests, material judgments and change of control. Additionally, we cannot be assured that our borrowing relationship with our lenders will continue or that our lenders will remain able to support their commitments to us in the future. If our lenders fail to do so, then we may not be able to secure alternative financing on commercially reasonable terms, or at all.

Our business could suffer with the closure or disruption of our home office or our distribution centers.

Domestically, we rely on a single distribution center located in Corona, California to receive, store and distribute the vast majority of our merchandise to our domestic stores. Internationally, we operate a combined distribution and ecommerce fulfillment center located in Graz, Austria that supports our Blue Tomato ecommerce and store operations

in Europe. We operate a distribution center located in Delta, British Columbia, Canada to distribute our merchandise to our Canadian stores. We operate a distribution and fulfillment center located in Melbourne, Australia to distribute our merchandise to our Australian stores. Additionally, we are headquartered in Lynnwood, Washington. As a result, a natural disaster or other catastrophic event that affects one of the regions where we operate these centers or our home office could significantly disrupt our operations and have a material adverse effect on our business, results of operations and financial condition.

The effects of war, acts of terrorism, threat of terrorism, or other types of mall violence, could adversely affect our business.

Most of our stores are located in shopping malls. Any threat of terrorist attacks or actual terrorist events, or other types of mall violence, such as shootings in malls, particularly in public areas, could lead to lower consumer traffic in shopping malls. In addition, local authorities or mall management could close shopping malls in response to security concerns. Mall closures, as well as lower consumer traffic due to security concerns, could result in decreased sales. Additionally, the threat, escalation or commencement of war or other armed conflict elsewhere, could significantly diminish consumer spending, and result in decreased sales. Decreased sales could have a material adverse effect on our business, financial condition and results of operations.

Our inability or failure to protect our intellectual property or our infringement of other's intellectual property could have a negative impact on our operating results.

We believe that our trademarks and domain names are valuable assets that are critical to our success. The unauthorized use or other misappropriation of our trademarks or domain names could diminish the value of the Zumiez, Blue Tomato, or Fast Times brands, our store concepts, our private label brands or our goodwill and cause a decline in our net sales. Although we have secured or are in the process of securing protection for our trademarks and domain names in a number of countries outside of the U.S., there are certain countries where we do not currently have or where we do not currently intend to apply for protection for certain trademarks. Also, the efforts we have taken to protect our trademarks may not be sufficient or effective. Therefore, we may not be able to prevent other persons from using our trademarks or domain names outside of the U.S., which also could adversely affect our business. We are also subject to the risk that we may infringe on the intellectual property rights of third parties. Any infringement or other intellectual property claim made against us, whether or not it has merit, could be time-consuming, result in costly litigation, cause product delays or require us to pay royalties or license fees. As a result, any such claim could have a material adverse effect on our operating results.

Our operations expose us to the risk of litigation, which could lead to significant potential liability and costs that could harm our business, financial condition or results of operations.

We employ a substantial number of full-time and part-time employees, a majority of whom are employed at our store locations. As a result, we are subject to a large number of federal, state and foreign laws and regulations relating to employment. This creates a risk of potential claims that we have violated laws related to discrimination and harassment, health and safety, wage and hour laws, criminal activity, personal injury and other claims. We are also subject to other types of claims in the ordinary course of our business. Some or all of these claims may give rise to litigation, which could be time-consuming for our management team, costly and harmful to our business.

In addition, we are exposed to the risk of class action litigation. The costs of defense and the risk of loss in connection with class action suits are greater than in single-party litigation claims. Due to the costs of defending against such litigation, the size of judgments that may be awarded against us, and the loss of significant management time devoted to such litigation, we cannot assure you that such litigation will not disrupt our business or impact our financial results.

We are involved, from time to time, in litigation incidental to our business including complaints filed by investors. This litigation could result in substantial costs, and could divert management's attention and resources, which could harm our business. Risks associated with legal liability are often difficult to assess or quantify, and their existence and magnitude can remain unknown for significant periods of time.

Our failure to comply with federal, state, local or foreign laws and regulations, or changes in these laws and regulations, could have an adverse impact on our results of operations and financial performance.

Our business is subject to a wide array of laws and regulations including those related to employment, trade, consumer protection, transportation, occupancy laws, health care, wage laws, employee health and safety, taxes, privacy, health information privacy, identify theft, customs, truth-in-advertising, securities laws, unsolicited commercial communication and environmental issues. Our policies, procedures and internal controls are designed to comply with foreign and domestic laws and regulations, such as those required by the Sarbanes-Oxley Act of 2002 and the U.S. Foreign Corrupt Practices Act. Although we have policies and procedures aimed at ensuring legal and regulatory compliance, our employees or vendors could take actions that violate these laws and regulations. Any violations of such laws or regulations could have an adverse effect on our reputation, results of operations, financial condition and cash flows. Furthermore, changes in the regulations, the imposition of additional regulations, or the enactment of any new legislation, particularly in the U.S. and Europe, could adversely affect our results of operations or financial condition.

Fluctuations in our tax obligations and effective tax rate may result in volatility in our operating results.

We are subject to income taxes in many domestic and foreign jurisdictions. In addition, our products are subject to import and excise duties and/or sales, consumption or value-added taxes in many jurisdictions. We record tax expense based on our estimates of future payments, which include reserves for estimates of probable settlements of domestic and foreign tax audits. At any one time, many tax years are subject to audit by various taxing jurisdictions. There can be no assurance as to the outcome of these audits which may have an adverse effect to our business. In addition, our effective tax rate may be materially impacted by changes in tax rates and duties, the mix and level of earnings or losses by taxing jurisdictions, or by changes to existing accounting rules or regulations. Changes to foreign or domestic tax laws could have a material impact on our financial condition, results of operations or cash flows.

We may fail to meet analyst expectations, which could cause the price of our stock to decline.

Our common stock is traded publicly and various securities analysts follow our financial results and issue reports on us. These reports include information about our historical financial results as well as the analysts' estimates of our future performance. The analysts' estimates are based upon their own independent opinions and can be different from our estimates or expectations. If our operating results are below the estimates or expectations of public market analysts and investors, our stock price could decline.

The reduction of total outstanding shares through the execution of a share repurchase program of common stock may increase the risk that a group of shareholders could form a group to become a controlling shareholder.

A share repurchase program may be conducted from time to time under authorization made by our Board of Directors. We do not have a controlling shareholder, nor are we aware of any shareholders that have formed a “group” (defined as when two or more persons agree to act together for the purposes of acquiring, holding, voting or otherwise disposing of the equity securities of an issuer). The reduction of total outstanding shares through the execution of a share repurchase program of common stock may increase the risk that a group of shareholders could form a group to become a controlling shareholder.

A controlling shareholder would have significant influence over, and may have the ability to control, matters requiring approval by our shareholders, including the election of directors and approval of mergers, consolidations, sales of assets, recapitalizations and amendments to our articles of incorporation. Furthermore, a controlling shareholder may take actions with which other shareholders do not agree, including actions that delay, defer or prevent a change of control of the company and that could cause the price that investors are willing to pay for the company’s stock to decline.

### Item 3: Quantitative and Qualitative Disclosures About Market Risk

Our market risk profile at August 4, 2018 has not significantly changed since February 3, 2018. Our market risk profile at February 3, 2018 is disclosed in our Annual Report on Form 10-K.

### Item 4: Controls and Procedures

Evaluation of Disclosure Controls and Procedures. We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Securities Exchange Act Rule 13a-15(e)). Based on this evaluation, our CEO and CFO concluded that, as of August 4,

2018, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting. There has been no change in our internal control over financial reporting (as defined in Securities Exchange Act Rule 13a-15(f)) during the three months ended August 4, 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

We are involved from time to time in litigation incidental to our business. We are unable to predict the outcome of litigated cases. A court determination in any of litigation actions against us could result in significant liability and could have a material adverse effect on our business, results of operations or financial condition.

See Note 4 to the Notes to Condensed Consolidated Financial Statements found in Part I Item 1 of this Form 10-Q (listed under “Litigation” under Commitments and Contingencies).

Item 1A. Risk Factors

Please refer to the Risk Factors set forth in Item 2 of Part I of this Form 10-Q as well as the risk factors previously disclosed in Item 1A of Part I of our Annual Report on Form 10-K for the year ended February 3, 2018. There have been no material changes in the risk factors set forth in our Annual Report on Form 10-K for the year ended February 3, 2018.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

There were no issuer purchases of common stock during the thirteen weeks ended August 4, 2018.

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None



Item 6. Exhibits

Exhibit No. Description of Exhibits

- |      |                                                                                                                                                                                                                           |
|------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1 | <del>Certification of the Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</del> |
| 31.2 | <del>Certification of the Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</del> |
| 32.1 | <del>Certifications of the Principal Executive Officer and Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350</del>                                            |
| 101  | The following materials from Zumiez Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended August 4, 2018, formatted in XBRL (eXtensible Business Reporting Language):                                       |

(i) Condensed Consolidated Balance Sheets at August 4, 2018 (unaudited) and February 3, 2018; (ii) Unaudited Condensed Consolidated Statements of Income (Loss) for the three and six months ended August 4, 2018 and July 29, 2017; (iii) Unaudited Condensed Consolidated Statements of Comprehensive (Loss) Income for the three and six months ended August 4, 2018 and July 29, 2017; (iv) Unaudited Condensed Consolidated Statements of Changes in Shareholders' Equity for the six months ended August 4, 2018 and July 29, 2017; (v) Unaudited Condensed Consolidated Statements of Cash Flows for the six months ended August 4, 2018 and July 29, 2017; and (vi) Notes to Condensed Consolidated Financial Statements.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

ZUMIEZ INC.

Dated: September 10, 2018 By: /s/ Christopher C. Work  
Christopher C. Work  
Chief Financial Officer

(Principal Financial Officer and  
Principal Accounting Officer)