

SKECHERS USA INC  
Form 10-K  
March 01, 2019  
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT  
OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 001-14429

SKECHERS U.S.A., INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of

95-4376145  
(I.R.S. Employer

Incorporation or Organization)

Identification No.)

228 Manhattan Beach Blvd., Manhattan Beach, California  
(Address of Principal Executive Offices)

90266  
(Zip Code)

Registrant's telephone number, including area code: (310) 318-3100

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Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Class A Common Stock, \$0.001 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 every interactive Data File required to be submitted 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 such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See definitions 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

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As of June 30, 2018, the aggregate market value of the voting and non-voting Class A and Class B Common Stock held by non-affiliates of the Registrant was approximately \$4.0 billion based upon the closing price of \$30.01 of the Class A Common Stock on the New York Stock Exchange on such date.

The number of shares of Class A Common Stock outstanding as of February 15, 2019: 133,460,317.

The number of shares of Class B Common Stock outstanding as of February 15, 2019: 23,983,312.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement issued in connection with the 2019 Annual Meeting of the Stockholders of the Registrant are incorporated by reference into Part III.

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Skechers U.S.A., INC. and subsidiaries

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for the year ended DECEMBER 31, 2018

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This annual report includes our trademarks including Skechers®, Skechers Performance™, Skechers GOrun®, Skechers GOwalk®, Skechers GOgolf®, You by Skechers™, ®, ®, Skechers Cali™, Relaxed Fit®, Skecher Street™, D'Lites DLT-A™, Skechers Memory Foam™, BOSS Energy Lights®, and Twinkle Toes®, each of which is our property. This report contains additional trademarks of other companies. We do not intend our use or display of other companies' trade names or trademarks to imply an endorsement or sponsorship of us by such companies, or any relationship with any of these companies.

## SPECIAL NOTE ON Forward-looking Statements

This annual report on Form 10-K contains forward-looking statements that are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, including statements with regards to future revenue, projected 2019 operating results, earnings, spending, margins, cash flow, orders, expected timing of shipment of products, inventory levels, future growth or success in specific countries, categories or market sectors, continued or expected distribution to specific retailers, liquidity, capital resources and market risk, strategies and objectives. Forward-looking statements include, without limitation, any statement that may predict, forecast, indicate or simply state future results, performance or achievements, and can be identified by the use of forward-looking language such as “believe,” “anticipate,” “expect,” “estimate,” “intend,” “plan,” “project,” “will be,” “will continue,” “will result,” “could,” “may,” or any variations of such words with similar meanings. These forward-looking statements involve risks and uncertainties that could cause actual results to differ materially from those projected in forward-looking statements, and reported results shall not be considered an indication of our company’s future performance. Factors that might cause or contribute to such differences include:

- global economic, political and market conditions including the challenging consumer retail market in the United States;
- our ability to maintain our brand image and to anticipate, forecast, identify, and respond to changes in fashion trends, consumer demand for the products and other market factors;
- our ability to remain competitive among sellers of footwear for consumers, including in the highly competitive performance footwear market;
- our ability to sustain, manage and forecast our costs and proper inventory levels;
- the loss of any significant customers, decreased demand by industry retailers and the cancellation of order commitments;
- our ability to continue to manufacture and ship our products that are sourced in China and Vietnam, which could be adversely affected by various economic, political or trade conditions, or a natural disaster in China or Vietnam;
- our ability to predict our revenues, which have varied significantly in the past and can be expected to fluctuate in the future due to a number of reasons, many of which are beyond our control; and
- sales levels during the spring, back-to-school and holiday selling seasons.

The risks included here are not exhaustive. Other sections of this report may include additional factors that could adversely impact our business, financial condition and results of operations. Moreover, we operate in a very competitive and rapidly changing environment, and new risk factors emerge from time to time. We cannot predict all such risk factors, nor can we assess the impact of all such risk factors on our business or the extent to which any factor or combination of factors may cause actual results to differ materially from those contained in any forward-looking statements. Given these inherent and changing risks and uncertainties, investors should not place undue reliance on forward-looking statements, which reflect our opinions only as of the date of this annual report, as a prediction of actual results. We undertake no obligation to publicly release any revisions to the forward-looking statements after the date of this document, except as otherwise required by reporting requirements of applicable federal and states securities laws.

## PART I

### ITEM 1. BUSINESS

We were incorporated in California in 1992 and reincorporated in Delaware in 1999. Throughout this annual report, we refer to Skechers U.S.A., Inc., a Delaware corporation, its consolidated subsidiaries and certain variable interest entities (“VIE’s”) of which it is the primary beneficiary, as “we,” “us,” “our,” “our Company” and “Skechers” unless otherwise indicated. Our internet address is [www.skechers.com](http://www.skechers.com). Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, Form 3’s, 4’s and 5’s filed on behalf of directors, officers and 10% stockholders, and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 are available free of charge on our corporate website, [www.skx.com](http://www.skx.com), as soon as reasonably practicable after we electronically file such material with, or furnish it to, the U.S. Securities and Exchange Commission (“SEC”). You can learn more about us by reviewing such filings at [www.skx.com](http://www.skx.com) or at the SEC’s website at [www.sec.gov](http://www.sec.gov).

### GENERAL

We design and market Skechers-branded lifestyle footwear for men, women and children, and performance footwear for men and women under the Skechers Performance brand name. Our footwear reflects a combination of innovation, style, comfort, quality and value that appeals to a broad range of consumers. Our brands are sold through department and specialty stores, athletic and independent retailers, boutiques and internet retailers. In addition to wholesale distribution, our footwear is available at our e-commerce websites and our own retail stores. As of February 1, 2019, we owned and operated 113 concept stores, 170 factory outlet stores and 187 warehouse outlet stores in the United States, and 134 concept stores, 78 factory outlet stores, and 10 warehouse outlet stores internationally. Our objective is to profitably grow our operations worldwide while leveraging our recognizable Skechers brand through our diversified product lines, innovative advertising and diversified distribution channels.

We seek to offer consumers a vast array of stylish and comfortable footwear that satisfies their active, casual, dress casual and athletic footwear needs. Our core consumers are style-conscious men and women attracted to our relevant brand image, fashion-forward designs and affordable product, as well as athletes and fitness enthusiasts attracted to our performance footwear. Many of our best-selling and core styles are also developed for children with colors and materials that reflect a playful image appropriate for this demographic. Further, we offer children a unique collection of footwear designed just for them, including those with innovative light technology.

We believe that brand recognition is an important element for success in the footwear business. We have aggressively marketed our brands through comprehensive marketing campaigns for men, women and children. During 2018, the Skechers brand was supported by print, television, digital and outdoor campaigns for men and women; animated and live action kids’ television and digital campaigns; marathons and other events for Skechers Performance and BOBS from Skechers divisions. To further drive recognition, we have enlisted numerous celebrities, former and current athletes, and influencers to appear in our campaigns, including globally-known recording artists Camila Cabello; sports legends Sugar Ray Leonard, Howie Long, David Ortiz, and Tony Romo; and television personalities and actresses Brooke Burke-Charvet and Kelly Brook. For the Skechers Performance Division, we also had Olympians Meb Keflezighi, Kara Goucher, and Matt Kuchar; and professional golfers Ashlan Ramsey, Belen Mozo, Brooke Henderson, Russell Knox, Wesley Bryan, Billy Andrade, Colin Montgomerie and Edward Cheserek, who won 17 National Collegiate Athletic Association (“NCAA”) distance running titles.

Since 1992, when we introduced our first line, Skechers USA Sport Utility Footwear, we have expanded our product offering and grown our net sales while substantially increasing the breadth and penetration of our account base. Our men’s, women’s and children’s product lines benefit from the Skechers reputation for styling, quality, comfort, innovation and affordability. Our performance lines benefit from our marketing, product development, manufacturing support, and management expertise. To promote innovation and brand relevance, we manage our product lines

separately by utilizing dedicated sales and design teams. Our product lines share back office services in order to limit our operating expenses and fully utilize our management's vast experience in the footwear industry.

#### SKECHERS LINES

We offer a wide array of Skechers-branded footwear lines for men, women and children, many of which have categories that have developed into well-known names. Most of these categories are marketed and packaged with unique shoe boxes, hangtags and in-store support, and are generally sold through department stores, footwear specialty stores, athletic retailers, Skechers retail stores as well as skechers.com and numerous online accounts. Management evaluates segment performance based primarily on net sales and gross margins; however, sales and costs are not allocated to specific product lines.



In addition, Skechers designs and markets running and golf apparel under the Skechers Performance brand, as well as casual lifestyle apparel under the Skechers and BOBS brands. The apparel is primarily available at Skechers retail stores, but is also available to domestic wholesale accounts and select international partners.

### Lifestyle Brands

Skechers USA. Our Skechers USA category for men and women includes: (i) Dress Casuals and Modern Comfort, (ii) Casuals, (iii) Casual Athletic, and (iv) seasonal sandals and boots. Styles are available in several fits including Classic Fit, Relaxed Fit, Wide Fit and Extra Wide.

• The Dress Casuals category for men is comprised of basic “black and brown” men’s shoes that feature shiny leathers and dress details, but may utilize traditional or lugged outsoles as well as value-oriented materials. The Dress Casuals line, which is also referred to as the Modern Comfort collection for women, is comprised of trend-influenced, stylized boots and shoes, which may include leather uppers, shearling or faux fur lining or trim, and water-resistant materials.

- The Casuals line for men and women is defined by lugged outsoles and utilizes value-oriented and leather materials in the uppers. For men, the Casuals category includes “black and brown” boots, shoes and sandals that generally have a rugged urban design—some with industrial-inspired fashion features. For women, the Casuals category includes basic “black and brown” oxfords and slip-ons, lug outsole and fashion boots, and casual sandals. We design and price both the men’s and women’s categories to appeal primarily to younger consumers with broad acceptance across age groups.

• Our Casual Athletic line is comprised of low-profile, sport-influenced streetwear targeted to trend-conscious young men and women. The outsoles are primarily rubber and are sometimes adopted from our men’s Sport and women’s Active lines. This collection features leather or nubuck uppers, but may also include mesh.

• Our seasonal sandals and boots for men and women are designed with many of our existing and proven outsoles, stylized with basic or core uppers as well as fresh looks. These styles are generally made with quality leather uppers, but may also be in canvas or fabric for sandals, and water-resistant materials, faux fur and sherpa linings for boots.

Skechers Sport. Our Skechers Sport footwear collection for men and women includes: (i) lightweight sport athletic lifestyle products, (ii) classic athletic-inspired styles, (iii) sport sandals and booties, and (iv) retro and fashion. Many Skechers Sport styles are enhanced with comfort features such as Skechers Air-Cooled Memory Foam™ insoles, lightweight designs, flexible outsoles and soft uppers such as bio-engineered mesh, soft knit fabrics and stretchable woven materials. Known for bright, multi-colored and solid basic-colored uppers, Skechers Sport is distinguished by its technical performance-inspired looks; however, we generally do not promote the technical performance features of these shoes. Styles are available in several fits including Classic Fit, Relaxed Fit, Wide Fit and Extra Wide.

• Our lightweight sport athletic product is designed with comfort and flexibility in mind. Careful attention is devoted to the cushioning, weight, design and construction by using innovative materials and technologies including Skech-Knit uppers. Designed as a versatile, trend-right athletic shoe suitable for all-day wear, the product line features styles in both bright and classic athletic colors.

• Classic Skechers styles are core-proven looks that continue to be strong performers. With all-day comfort and durable rubber tread, these shoes are intended to be a mainstay of any footwear collection. Many of the designs are in white, black and natural shades, with some athletic accents. The uppers are designed in leather, suede and nubuck.

• Our sport sandals and booties are primarily designed from existing Skechers Sport outsoles and may include many of the same sport features as our sneakers with the addition of new technologies geared toward making comfortable seasonal footwear.

• Retro and fashion styles feature throwback fashionable profiles with sport-inspired features and trend-right silhouettes. At the forefront is the D’Lite® collection with iconic Skechers sneaker looks updated with contemporary Skechers Air-Cooled Memory Foam™ insoles for total comfort. Collaborations of our fashion collections like Skechers D’Lites X One Piece that features colorways from the popular manga series help generate buzz and expand awareness

the brand.

Skechers Active and Skechers Sport Active. A natural companion to Skechers Sport, Skechers Active and Skechers Sport Active have grown from a casual everyday line into two complete lines of sneakers and casual sneakers for active females of all ages. The Skechers Active line, with lace-ups, Mary Janes, sandals and open back styles, is available in a multitude of colors as well as solid white or black, in knits, fabrics, leathers and meshes, and with various closures — traditional laces, zig-zag and cross straps, among others. The Skechers Sport Active line includes low-profile, lightweight, flexible and sporty styles, many of which have Skechers Air-Cooled Memory Foam.<sup>TM</sup>

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Skecher Street™. A bold urban street-inspired sneaker collection for millennials, Gen Y's and young women, Skecher Street™ Los Angeles delivers sneakers, platforms and fashion trainers with premium metallic finishes, sophisticated takes on glimmer embellishments and playful embroidered pairs with star and graphic treatments. Skecher Street™ styles pair the latest trends with comfort features including Air Cooled Memory Foam insoles, the brand's patented Rise Fit technology and contoured barefoot liners.

BOBS from Skechers. At the core of the BOBS from Skechers line is its vast collection of colorful, playful as well as basic espadrilles. The line now also includes wedges, vulcanized looks and comfortable faux fur styles for home. Many styles also include Skechers Memory Foam™.

•The BOBS classic espadrille collection is designed in basic colors with canvas, tweed, crochet and boiled wool uppers, suede and patterned fabrics. We also have a collection with dog and cat prints for our BOBS for Dogs charitable offering.

•BOBS' vulcanized and sport looks have a very youthful and California lifestyle appeal. Primarily designed with canvas uppers but also jersey fabrics, the line features both classic retro looks and fresh colors and materials for a relevant style.

For each pair of specially packaged BOBS from Skechers sold in the United States from September 1, 2015 through August 31, 2018, twenty-five cents was donated to Best Friends to help save the lives of dogs and cats in America's shelters totaling more than \$3.9 million dollars to Best Friends Animal Society. This helped more than 583,000 shelter pets in the United States, including saving the lives of more than 241,000 animals. Skechers also continues to donate new shoes to children in need through the BOBS program for which more than 15.6 million pairs of new kids' shoes have been donated, including approximately 395,000 pairs in 2018. The charitable shoes are primarily donated to charity partner Delivering Good, which then donates the shoes to various reputable charity organizations in the United States and around the world.

Mark Nason. Inspired by classic rock and roll and its trends, the Mark Nason collection originally started in Italy with an exotic offering of boots and accessories. The high-end collection has evolved into Mark Nason Los Angeles, an expanded offering of dress, casual and active styles for style-conscious men, with many featuring Premium Relaxed Fit construction and Memory Foam Lux insoles for enhanced comfort.

#### Performance Brands

Skechers Performance. Skechers Performance is a collection of technical footwear designed with a focus on a specific activity to maximize performance and promote natural motion. Developed by the Skechers Performance Division, the footwear utilizes the latest advancements in materials and innovative design, including ultra-lightweight Resalyte or the latest 5GEN midsole compounds for comfort and an outsole that delivers responsive feedback. Limited edition features such as Skechers Nite Owl glow-in-the-dark technology or special colorways are featured across multiple product lines.

•Skechers GORun. Skechers GORun is a collection of lightweight, flexible running shoes that feature a midfoot strike design for efficient running. Skechers GORun Ride features similar designs to their GORun counterparts, with enhanced cushioning for elevated comfort and support. Skechers GORun Forza offers extra stability on long runs. The Skechers GOMeb collection includes the high-performance racing and training shoes worn by elite marathon runner Meb Keflezighi. These flagship lines, as well as other Skechers GORun products, are marketed to serious runners and recreational runners alike, and are available in running stores as well as other retailers. Special limited-edition collections of key running styles are released to commemorate major marathon events in cities like New York, Houston and Los Angeles.

•Skechers GOWalk. Skechers GOWalk is designed for walking and casual wear, and offers performance features in a comfortable casual slip-on or lace-up sneaker. The product line features a lightweight and flexible design to promote

natural foot movement when walking as well as more advanced performance technologies including a high-rebound GogaMax insole, comfortable 5GEN cushioning and Memory Form Fit for a custom-fit experience. Skechers GOwalk Joy adds knitted upper sneaker styles to the collection. Skechers GO FLEX Walk features a unique articulated, segmented flexible outsole that is designed to move with you. Skechers on-the-GO footwear fuses iconic designs and premium materials with Skechers Performance technologies for comfort and style.

Skechers GOtrain. Skechers GOtrain is designed for the gym and features a wider forefoot and extended outriggers for maximum stability and control at lateral and medial strike points. This shoe is an all-encompassing trainer that meets the need of intense and rigorous workouts.

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• **Skechers GOtrail.** The Skechers GOtrail collection features the performance materials and innovations found in our running shoes with rugged designs that can protect against impact during all-terrain runs.

• **Skechers GO GOLF.** Skechers GO GOLF is designed for the golf course and offers a zero heel drop design, which keeps feet in a neutral position that is low to the ground to promote a solid foundation while playing golf. A grip outsole helps with traction control and 5GEN cushioning delivers comfort. Styles in the Skechers GO GOLF Pro line, worn by PGA golfer Matt Kuchar and a roster of other golf pros, also offers H2GO Shield waterproof protection and features replaceable softspikes on the outsole.

• **YOU by Skechers™.** The versatile YOU by Skechers™ footwear collection combines lifestyle with wellness in an eclectic assortment of easy-to-wear and comfortable knitted lace-up and slip-on sneakers for women.

#### Skechers Kids

The Skechers Kids line includes: (i) Skechers Kids, which is a range of infants', toddlers', boys' and girls' boots, shoes, high-tops, sneakers and sandals, (ii) Skechers' athletic-inspired sneakers with Memory Foam, (iii) Twinkle Toes, (iv) character supported collections, and (v) Lighted footwear.

• The Skechers Kids line is inspired by our many adult styles and includes embellishments or adornments such as fresh colors and fabrics. Some of these styles are also adapted for toddlers with softer, more pliable outsoles and for infants with soft, leather-sole crib shoes. The line's Fashion Hi-Tops subcategory offers trend-forward high-top looks designed to appeal to fashion-conscious young girls.

• Skechers' athletic-inspired collection includes Memory Foam sneakers designed with many of the same meshes, knits and weaves as the company's adult styles such as Skechers Sport in bright colors and patterns, Skechers GOrun and Skech-Air athletic sneakers which have a unique visible air-cushioned outsole and a gel-infused memory foam insole. The collection is designed to offer the latest comfort innovations and appeal both to younger kids as well as tweens transitioning to adult shoes.

• Twinkle Toes by Skechers is a line of girls' sneakers and boots that feature bejeweled toe caps and brightly designed uppers. Some styles also include lights. The product line is marketed with the character Twinkle Toes.

- Along with Twinkle Toes, we market several of our collections with characters that resonate with younger consumers. Skechers Super Z-Strap is a line of athletic-styled sneakers with an easy "z"-shaped closure system marketed with the character Z-Strap; and Mega Flex is a line of athletic sneakers with heel springs or articulated blades for boys based on a robot character.
- Skechers' lighted footwear collection for boys and girls includes multiple categories, featuring S-Lights and rechargeable technology with brands like Energy Lights by Skechers footwear. S-Lights combine patterns of lights on the outsoles and sides of the shoes, while Energy Lights by Skechers is a classic high-top or low-top sneaker with a rechargeable lighted outsole that features a variety of colors and light. Luminators feature an innovative illuminated mesh fabric upper for a bolder look.

Skechers Kids lines include shoes that are designed as "takedowns" of their adult counterparts, allowing the younger consumers the opportunity to wear the same popular styles as their older siblings and schoolmates. This "takedown" strategy maintains the product's integrity by offering premium leathers, hardware and outsoles without the costs involved in designing and developing new products. In addition, we adapt current fashions from our men's and women's lines by modifying designs and choosing colors and materials that are more suitable for the playful image that we have established in the children's footwear market. Each Skechers Kids line is marketed and packaged separately with a distinct shoe box.

#### Skechers Work

Skechers Work offers a complete line of men's and women's casuals such as field boots, hikers and athletic shoes, many of which may also include Skechers Memory Foam.™ The Skechers Work line includes athletic-inspired, casual safety toe and non-slip safety toe categories that may feature lightweight aluminum safety toe, electrical hazard and slip-resistant technologies, as well as breathable, seam-sealed waterproof membranes. Designed for men and women

working in jobs with certain safety requirements, these durable styles are constructed on high-abrasion, long-wearing soles, and feature breathable lining, oil- and abrasion-resistant outsoles offering all-day comfort and prolonged durability. The Skechers Work line incorporates design elements from other Skechers men's and women's lines. The uppers are comprised of high-quality leather, nubuck, trubuck and durabuck. Our safety toe athletic sneakers, boots, hikers and casuals are ideal for environments requiring safety footwear, and offer comfort and safety in dry or wet conditions. Our slip-resistant boots, hikers, athletics, casuals, clogs and comfortable Shape-ups are ideal for the service industry. The Skechers Healthcare Pro SR Series offers slip and stain resistant footwear with air-cooled memory foam in a wide range of colors for medical professionals. Our safety toe products have been independently tested and certified to meet ASTM standards, and our slip-resistant soles have been tested pursuant to the Mark II testing method for slip-resistance. Skechers Work is typically sold through department stores, athletic footwear retailers and specialty shoe stores, and is marketed directly to consumers through business-to-business channels.

## PRODUCT DESIGN AND DEVELOPMENT

Our principal goal in product design is to generate fresh and innovative footwear in all of our product lines. Targeted to the active, youthful and style-savvy, we design our lifestyle line to be comfortable, fashionable and marketable to the 12- to 24-year-old consumer, with broader appeal to 5- to 50-year olds, and an exclusive selection for infants and toddlers. Designed by the Skechers Performance Division, our performance products are for professional and recreational athletes who want a technical fitness shoe.

We believe that our products' success is related to our ability to recognize trends in the footwear markets and to design products that anticipate and accommodate consumers' ever-evolving preferences. We are able to quickly translate the latest fashion trends into stylish, quality footwear at a reasonable price by analyzing and interpreting current and emerging lifestyle trends. Lifestyle trend information is compiled and analyzed by our designers in various ways, including reviewing and analyzing pop culture, clothing, and trend-setting media; traveling to domestic and international fashion markets to identify and confirm current trends; consulting with our retail and e-commerce customers for information on current retail selling trends; participating in major footwear trade shows to stay abreast of popular brands, fashions and styles; and subscribing to various fashion and color information services. In addition, a key component of our design philosophy is to continually reinterpret and develop our successful styles in our brands' images.

The footwear design process typically begins about nine months before the start of a season. Our products are designed and developed primarily by our in-house design staff. To promote innovation and brand relevance, we utilize dedicated design teams, who report to our senior design executives and focus on each of the men's, women's and children's categories. In addition, we utilize outside design firms on an item-specific basis to supplement our internal design efforts. The design process is extremely collaborative, as members of the design staff frequently meet with the heads of retail, merchandising, sales, production and sourcing to further refine our products to meet the particular needs of the target market.

After a design team arrives at a consensus regarding the fashion themes for the coming season, the designers then translate these themes into our products. These interpretations include variations in product color, material structure and embellishments, which are arrived at after close consultation with our production department. Prototype blueprints and specifications are created and forwarded to our manufacturers for design prototypes. The design prototypes are then sent back to our design teams. Our major retail customers may also review these new design concepts. Customer input not only allows us to measure consumer reaction to the latest designs, but also affords us an opportunity to foster deeper and more collaborative relationships with our customers. We also occasionally order limited production runs that may initially be tested in our concept stores with our test and react program, which gives us further insight into the strength of particular styles and allow our design teams to quickly modify and refine our designs. Generally, the production process can take six to nine months from design concept to commercialization.

For disclosure of product design and development costs during the last three fiscal years, see Note 1 - The Company and Summary of Significant Accounting Policies in the Consolidated Financial Statements included in this annual report.

## SOURCING

Factories. Our products are produced by independent contract manufacturers located primarily in China and Vietnam. We do not own or operate any manufacturing facilities. We believe that the use of independent manufacturers substantially increases our production flexibility and capacity, while reducing capital expenditures and avoiding the costs of managing a large production work force. For disclosure of information regarding the risks associated with having our manufacturing operations abroad and relying on independent contract manufacturers, see the relevant risk

factors under Item 1A of this annual report.

When possible, we seek to use manufacturers that have previously produced our footwear, which we believe enhances continuity and quality while controlling production costs. We source product for styles that account for a significant percentage of our net sales from at least five different manufacturers. During 2018, five of our contract manufacturers accounted for approximately 41.9% of total purchases. One manufacturer accounted for 12.8%, and another accounted for 10.1% of our total purchases. To date, we have not experienced difficulty in obtaining manufacturing services or with the availability of raw materials.

We finance our production activities in part through the use of interest-bearing open purchase arrangements with certain of our contract manufacturers. These facilities currently bear interest at a rate between 0.0% and 0.5% for 30- to 60-day financing, depending on the factory. We believe that the use of these arrangements affords us additional liquidity and flexibility. We do not have any long-term contracts with any of our manufacturers. However, we have long-standing relationships with many of our contract manufacturers and believe our relationships to be good.

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We closely monitor sales activity after initial introduction of a product in our concept stores to determine whether there is substantial demand for a style, thereby aiding us in our sourcing decisions. Styles that have substantial consumer appeal are highlighted in upcoming collections or offered as part of our periodic style offerings, while less popular styles can be discontinued after a limited production run. We believe that sales in our concept stores can also help forecast sales in national retail stores, and we share this sales information with our wholesale customers. Sales, merchandising, production and allocations management analyze historical and current sales, and market data from our wholesale account base and our own retail stores to develop an internal product quantity forecast that allows us to better manage our future production and inventory levels. For those styles with high sell-through percentages, we maintain an in-stock position to minimize the time necessary to fill customer orders by placing orders with our manufacturers prior to the time we receive customers' orders for such footwear.

**Production Oversight.** To safeguard product quality and consistency, we oversee the key aspects of production from initial prototype manufacture, through initial production runs, to final manufacture. Monitoring of all production is performed in the United States by our in-house production department and in Asia through a 343-person staff working from our offices in China and Vietnam. We believe that our Asian presence allows us to negotiate supplier and manufacturer arrangements more effectively, decrease product turnaround time, and ensure timely delivery of finished footwear. In addition, we require our manufacturers to certify that neither convicted, forced nor indentured labor (as defined under U.S. law), nor child labor (as defined by law in the manufacturer's country) is used in the production process, that compensation will be paid according to local law, and that the factory is in compliance with local safety regulations.

**Quality Control.** We believe that quality control is an important and effective means of maintaining the quality and reputation of our products. Our quality control program is designed to ensure that not only finished goods meet our established design specifications, but also that all goods bearing our trademarks meet our standards for quality. Our quality control personnel located in China and Vietnam perform an array of inspection procedures at various stages of the production process, including examination and testing of prototypes of key raw materials prior to manufacture, samples and materials at various stages of production and final products prior to shipment. Our employees are on-site at each of our major manufacturers to oversee production. For some of our lower volume manufacturers, our staff is on-site during significant production runs, or we will perform unannounced visits to their manufacturing sites to further monitor compliance with our manufacturing specifications.

## ADVERTISING AND MARKETING

With a marketing philosophy of "Unseen, Untold, Unsold," we take a targeted approach to marketing to drive traffic, build brand recognition and properly position our diverse lines within the marketplace. Senior management is directly involved in shaping our image and the conception, development and implementation of our advertising and marketing activities. Our marketing plan has a multi-pronged approach: traditional print and television advertising, supported by digital, outdoor, trend-influenced marketing, public relations, social media, promotions, events and in-store. In addition, we utilize celebrity endorsers in some of our advertisements. We also believe our websites and trade shows are effective marketing tools to both consumers and wholesale accounts. We have historically budgeted advertising as a percentage of projected net sales.

The majority of our advertising is conceptualized by our in-house design team. We believe that our advertising strategies, methods and creative campaigns are directly related to our success. We generally seek to build and drive brand awareness, create purchase intent and inform the consumer about new innovations and lines. Our campaigns are designed to provide merchandise flexibility and to facilitate the brand's direction.

To further build brand awareness and influence consumer spending, we have selectively signed endorsement agreements with celebrities whom we believe will reach new markets. In 2018, our Skechers lifestyle endorsees

included Camila Cabello, Brooke Burke-Charvet, Kelly Brook, Sugar Ray Leonard, Howie Long, David Ortiz, and Tony Romo. Our Skechers Performance Division 2018 endorsees included elite runner and Olympic medalist Meb Keflezighi, elite runners Kara Goucher and Edward Cheserek, and professional golfers Matt Kuchar, Belen Mozo, Brooke Henderson, Ashlan Ramsey, Billy Andrade, Russell Knox, Wesley Bryan and Colin Montgomerie. Additionally, several international markets signed local ambassadors for marketing campaigns. Along with these global ambassadors, we also had local or regional ambassadors including pop groups for numerous countries in Asia. From time to time, we may sign other celebrities to endorse our brand name and image in order to strategically market our products among specific consumer groups in the future.

With a targeted approach, our print ads appear in popular fashion, lifestyle and pop culture publications in the United States and around the world.

Our television commercials are produced both in-house and through producers that we have utilized in the past who are familiar with our brands. In 2018, we developed commercials for men, women and children for our Skechers brands, including our animated spots for kids featuring our own action heroes, as well as live action commercials that appeal to older kids and tweens. We also had commercials for our golf collection lines that featured our elite golfers, and for our lifestyle lines that feature musicians, actors and retired athletes. We have found these to be cost-effective ways to advertise on key national and cable programming during high-selling seasons. In 2018, many of our television commercials were translated into multiple languages and aired in numerous markets around the world. Further, select markets have created television commercials specific to their market with local celebrities.

Outdoor. In an effort to reach consumers where they shop and in high-traffic areas as they travel to and from work, at times we execute outdoor campaigns that may include mall and telephone kiosks, billboards, transportation systems and airports, and the covering of large stadiums and buildings around the world. In many markets these now include LED billboards that broadcast our commercials. In addition, we advertised on perimeter boards at soccer matches and professional sporting events in Japan, Europe, Latin America and Canada. We believe these mediums are an effective and efficient way to target specific consumers.

Public Relations/Trend-Influenced Marketing. Our public relations objectives are to accurately position Skechers as a leading footwear brand within the business, general news and trade publications as well as to secure product placement in key magazines and television shows, and place our footwear on the feet of trend-setting influencers, celebrities and their families. We have been featured in leading business publications with interviews of our executives discussing our business strategy and position within the footwear market. We have amassed an array of prominent product placements in leading fashion, lifestyle, sports and pop culture magazines and websites. Additionally, we have partnered with influencers, bloggers and vloggers who have both appeared at events and posted on their social media channels about our footwear.

Social Media. With the goal of engaging with consumers, showcasing our product in relatable settings and relaying the latest news, we have built communities on Facebook, Twitter, Instagram, and YouTube in the United States and in countries around the world where our product is sold. To promote both our lifestyle and performance brands, we have developed several unique channels under Skechers®, Skechers Performance™, BOBS from Skechers and Mark Nason. The social platforms are divided into Skechers and Skechers Performance sites, as well as a BOBS page to feature our charitable footwear line. The online communities also connect consumers around the world, allowing an easy glimpse into trends and events in other countries. Additionally, many countries also utilize platforms specific to their market, such as Line in Japan and Weibo in China.

Promotions and Events. By applying creative sales techniques via a broad spectrum of media, our marketing team seeks to build brand recognition and drive traffic to Skechers retail stores, websites and our retail partners' locations. Skechers' promotional strategies have encompassed in-store specials, charity events, product tie-ins and giveaways and collaborations with national retailers and radio stations. In 2018, we appeared at walks and at numerous marathons in Boston, New York, London, Paris, Santiago and other cities with Skechers Performance branded booths to allow runners the ability to try on and often buy our products. In 2018, the Skechers Performance Division was the footwear and apparel sponsor for the Houston Marathon, the title sponsor of the Skechers Performance Los Angeles Marathon, and the footwear sponsor for Ironman across Europe. Our products were made available to consumers directly or through key accounts at many of these events. In addition, we partnered with key accounts by donating BOBS footwear to children in need at donation events in cities throughout the United States which built our relationships with these accounts as well as the local communities. As part of our BOBS for Dogs charity program we also partnered with Best Friends Animal Society, an organization dedicated to saving the lives of dogs and cats, in Strut your Mutt Dog donation events across the country.

Visual Merchandising. Our in-house visual merchandising department supports wholesale customers, distributors and our retail stores by developing displays that effectively leverage our products at the point of sale. Our point-of-purchase display items include signage, graphics, displays, counter cards, banners and other merchandising items for each of our brands. These materials mirror the look and feel of each brand and reinforce the image, and draw consumers into stores.

Our visual merchandising coordinators ("VMC's") work with our sales force and directly with our customers to ensure better sell-through at the retail level by generating greater consumer awareness through Skechers brand displays. Our VMC's communicate with and visit our wholesale customers on a regular basis to aid in proper display of our merchandise. They also run in-store promotions to enhance the sale of Skechers footwear and create excitement

surrounding the Skechers brand. We believe that these efforts help stimulate impulse sales and repeat purchases.

**Trade Shows.** To showcase our diverse products to footwear buyers in the United States and Europe and to distributors around the world, we regularly exhibit at leading trade shows. Along with specialty trade shows, we exhibit at FFANY, The Licensing Show and Outdoor Retailer in the United States; MICAM, Gallery and ISPO in Europe; and other international shows.

**Digital.** In 2018, we launched marketing campaigns on YouTube, Facebook and Instagram, and launched digital campaigns in many international markets to coincide with key selling time periods. We promote and sell our products through our e-commerce sites in the United States, Canada, United Kingdom, Germany, Spain, Chile and China, among other countries, as well as through non-ecommerce sites in many other countries. Our websites are a venue for dialog and feedback from customers about our products, which enhances the Skechers brand experience while driving sales through all our retail channels.

## PRODUCT DISTRIBUTION CHANNELS

We have three reportable segments: domestic wholesale sales, international wholesale sales, and retail sales, which includes e-commerce sales. In the United States, our products are available through a network of wholesale customers comprised of department, athletic and specialty stores and online retailers. Internationally, our products are available through wholesale customers in more than 170 countries and territories via our global network of distributors, in addition to our subsidiaries in Asia, Europe, Canada, Central America and South America. Skechers owns and operates retail stores both domestically and internationally through three integrated retail formats—concept, factory outlet and warehouse outlet stores. Each of these channels serves an integral function in the global distribution of our products. In addition, 18 distributors and 48 licensees have opened and operate 700 distributor-owned or -licensed Skechers retail stores and 1,813 licensee-owned Skechers retail stores, respectively, in over 170 countries as of December 31, 2018.

**Domestic Wholesale.** We distribute our footwear through the following domestic wholesale distribution channels: department stores, specialty stores, athletic specialty shoe stores, independent retailers, and internet retailers. While department stores and specialty retailers are the largest distribution channels, we believe that we appeal to a variety of wholesale customers, many of whom may operate stores within the same retail location due to our distinct product lines, variety of styles and the price criteria of their specific customers. Management has a clearly defined growth strategy for each of our channels of distribution. An integral component of our strategy is to offer our accounts the highest level of customer service so that our products will be fully represented in existing and new customer retail locations.

In an effort to provide knowledgeable and personalized service to our wholesale customers, the sales force is segregated by product line, each of which is headed by a vice president or national sales manager. Reporting to each sales manager are knowledgeable account executives and territory managers. The vice presidents and national sales managers report to our senior vice president of sales. All of our vice presidents and national sales managers are compensated on a salary basis, while our account executives and territory managers are compensated on a commission basis. None of our domestic sales personnel sells competing products.

We believe that we have developed a loyal account base through exceptional customer service. We believe that our close relationships with these accounts help us to maximize their retail sell-through. Our marketing teams work with our wholesale customers to ensure that our merchandise and marketing materials are properly presented. Sales executives and merchandise personnel work closely with accounts to ensure that appropriate styles are purchased for specific accounts and for specific stores within those accounts, as well as to ensure that appropriate inventory levels are carried at each store. Such information is then utilized to help develop sales projections and determine the product needs of our wholesale customers. The value-added services we provide our wholesale customers help us maintain strong relationships with our existing wholesale customers and attract potential new wholesale customers.

**Retail stores and e-commerce.** We pursue our retail store strategy through our three integrated retail formats: concept stores, factory outlet stores and warehouse outlet stores. Our three store formats enable us to promote the full Skechers product offering in an attractive environment that appeals to a broad group of consumers. In addition, most of our retail stores are profitable and have a positive effect on our operating results. We review all of our stores for impairment annually or more frequently if events or changes in circumstances require it. We prepare a summary of cash flows for each of our retail stores to assess potential impairment of the fixed assets and leasehold improvements. If the assets are considered to be impaired, the impairment we recognize is the amount by which the carrying value of the assets exceeds the fair value of the assets. In addition, we base the useful lives and related amortization or depreciation expense on our estimate of the period that the assets will generate revenues or otherwise be used by us. As of February 1, 2019, we owned and operated 113 concept stores, 170 factory outlet stores and 187 warehouse outlet stores in the United States, and 134 concept stores, 78 factory outlet stores, and 10 warehouse outlet stores

internationally. We plan to open 70 to 80 new stores in 2019.

Our retail stores are supported by our company-owned ecommerce businesses in the United States, Canada, United Kingdom, Germany, Spain, Chile and China, among other countries. These virtual storefronts are designed to provide a positive shopping and brand experience, showcasing our products in an easy-to-navigate format, allowing consumers to browse our selections and purchase our footwear. These virtual stores provide a convenient, alternative shopping environment and brand experience, and are an additional efficient and effective retail distribution channel, which has improved our customer service. They enable consumers to shop, browse, find store locations, socially interact, post a shoe review, photo, video or question, and immerse themselves in our brands.

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### ◆ Concept Stores

Our concept stores are located at marquee street locations, major tourist areas or in key shopping malls in metropolitan cities. Our concept stores have a threefold purpose in our operating strategy. First, concept stores serve as a showcase for a wide range of our product offering for the current season, as we estimate that our average wholesale customer carries no more than 5% of the complete Skechers line in any one location. Our concept stores showcase our products in an attractive, easy-to-shop open-floor setting, providing the customer with the complete Skechers story. Second, retail locations are generally chosen to generate maximum marketing value for the Skechers brand name through signage, store front presentation and interior design. Domestic locations include concept stores at Times Square, 5<sup>th</sup> Avenue, SOHO, and 34<sup>th</sup> Street, in New York; Powell Street in San Francisco; Santa Monica's Third Street Promenade; Ala Moana Center in Hawaii; South Beach Miami's Lincoln Road and Las Vegas' Grand Canal Shoppes at the Venetian. International locations include Oxford Street and Covent Garden in London; Buchanan Street in Glasgow; Princes Street in Edinburgh; Toronto's Eaton Centre; Vancouver's Pacific Centre; the Shinsaibashi shopping district of Osaka and Harajuku and Shibuya in Tokyo. The stores are typically designed to create a distinctive Skechers look and feel, and enhance customer association of the Skechers brand name with current youthful lifestyle trends and styles. Third, the concept stores serve as marketing and product testing venues. We believe that product sell-through information and rapid customer feedback derived from our concept stores enables our design, sales, merchandising and production staff to respond to market changes and new product introductions. Such responses serve to augment sales and limit our inventory markdowns and customer returns and allowances.

The typical Skechers concept store is approximately 3,000 square feet, although in certain markets we have opened concept stores as large as 8,000 square feet or as small as 800 square feet. When deciding where to open concept stores, we identify top geographic markets in the larger metropolitan cities in North America, Europe, Central America, South America and Asia. When selecting a specific site, we evaluate the proposed sites' traffic pattern, co-tenancies, sales volume of neighboring concept stores, lease economics and other factors considered important within the specific location. If we are considering opening a concept store in a shopping mall, our strategy is to obtain space as centrally located as possible in the mall, where we expect foot traffic to be most concentrated. We believe that the strength of the Skechers brand name has enabled us to negotiate more favorable terms with shopping malls that want us to open up concept stores to attract customer traffic to their venues.

### ◆ Factory Outlet Stores

Our factory outlet stores are generally located in manufacturers' direct outlet centers in the United States and in select international markets. Our factory outlet stores provide opportunities for us to sell discontinued and excess merchandise, thereby reducing the need to sell such merchandise to discounters at excessively low prices and potentially compromise the Skechers brand image. Skechers' factory outlet stores range in size from approximately 1,800 to 24,100 square feet. Unlike our warehouse outlet stores, inventory in these stores is supplemented by certain first-line styles sold at full retail price points.

### ◆ Warehouse Outlet Stores

Our free-standing and inline warehouse outlet stores, which are primarily located throughout the United States and Canada, enable us to liquidate excess merchandise, discontinued lines and odd-size inventory in a cost-efficient manner. Skechers' warehouse outlet stores are typically larger than our factory outlet stores and typically range in size from approximately 4,000 to 30,600 square feet. Our warehouse outlet stores enable us to sell discontinued and excess merchandise that would otherwise typically be sold to discounters at excessively low prices, which could otherwise compromise the Skechers brand image. We seek to open our warehouse outlet stores in areas that are in close proximity to our concept stores to facilitate the timely transfer of inventory that we want to liquidate as soon as practicable.

Store count, openings and closings for our domestic, international and consolidated joint venture stores are as follows:

	Number of Store Locations			Number of Store Locations
	December 31, 2017	Opened during 2018	Closed during 2018	December 31, 2018
<b>Domestic stores</b>				
Concept	117	1	(4 )	114
Factory Outlet	170	1	—	171
Warehouse Outlet	162	23	—	185
Domestic stores total	449	25	(4 )	470
<b>International stores</b>				
Concept	120	14	—	134
Factory Outlet	67	11	—	78
Warehouse Outlet	9	1	—	10
International stores total	196	26	—	222
<b>Joint venture stores</b>				
China Concept	55	21	(13 )	63
China Factory Outlet	70	12	(14 )	68
Hong Kong Concept	36	6	(3 )	39
Hong Kong Outlet	4	—	—	4
India Concept	44	13	—	57
India Outlet	2	2	—	4
Israel Concept	7	3	—	10
Israel Outlet	—	2	—	2
South Korea Concept	6	4	(5 )	5
South Korea Outlet	11	11	(5 )	17
South East Asia Concept	22	1	(2 )	21
South East Asia Outlet	5	2	—	7
Joint venture stores total	262	77	(42 )	297
<b>Total domestic, international and joint venture stores</b>				
	907	128	(46 )	989

International Wholesale. Our products are sold in more than 170 countries and territories throughout the world. We generate revenues from outside the United States from three principal sources: (i) direct sales to department stores and specialty retail stores through our joint ventures in Asia and the Middle East, as well as through our subsidiaries in the Americas, Europe, and Japan; (ii) sales to foreign distributors who distribute our footwear to department stores and specialty retail stores in select countries and territories across Asia, South America, Africa, the Middle East and Australia; and (iii) to a lesser extent, royalties from licensees who manufacture and distribute our non-footwear products outside the United States.

We believe that international distribution of our products represents a significant opportunity to increase net sales and profits. We intend to further increase our share of the international footwear market by heightening our marketing in those countries in which we currently have a presence through our international advertising campaigns, which are



designed to establish Skechers as a global brand synonymous with trend-right casual shoes.

International Subsidiaries

Europe

We currently merchandise, market and distribute product in most of Europe through the following subsidiaries: Skechers USA Ltd., with its offices and showrooms in London, England; Skechers S.a.r.l., with its offices in Lausanne, Switzerland; Skechers USA France S.A.S., with its offices and showrooms in Paris, France; Skechers USA Deutschland GmbH, with its offices and showrooms in Dietzenbach, Germany; Skechers USA Iberia, S.L., with its offices and showrooms in Madrid, Spain; Skechers USA Benelux B.V., with its offices and showrooms in Waalwijk, the Netherlands; Skechers USA Italia S.r.l., with its offices and showrooms in Milan, Italy; Skechers CEE, Kft. with its offices and showrooms in Budapest, Hungary as well as regional showrooms in Albania, Bosnia-Herzegovina, Bulgaria, Croatia, the Czech Republic, Kosovo, Macedonia, Moldova, Montenegro, Romania, Serbia, Slovakia and Slovenia. To accommodate our European subsidiaries' operations, we operate a 1.3 million square-foot distribution center in Liege, Belgium.

#### Canada

We currently merchandise, market and distribute product in Canada through Skechers USA Canada, Inc. with its offices and showrooms outside Toronto in Mississauga, Ontario. Product sold in Canada is primarily sourced from our U.S. distribution center in Rancho Belago, California. We have company-owned retail stores in key locations across Canada.

#### South America and Central America

We currently merchandise, market and distribute product in South America and Central America through the following subsidiaries: Skechers Do Brasil Calçados LTDA, with its offices and showrooms located in Sao Paulo, Brazil; Comercializadora Skechers Chile Limitada, with its offices and showrooms located in Santiago, Chile; Skechers Latin America LLC, with its offices and showrooms in Panama City, Panama as well as regional showrooms in Panama, Peru, Colombia and Costa Rica. Our Latin America subsidiary also distributes products in the Caribbean, Ecuador, Guatemala, El Salvador, Honduras and Nicaragua. Product sold in South America and Central America is primarily shipped directly from our contract manufacturers' factories in China and Vietnam. We have retail stores in key locations such as Santiago, Panama City, Bogota, Lima and Sao Paulo.

#### Japan

We currently merchandise, market and distribute product in Japan through our wholly-owned subsidiary, Skechers Japan GK, with its offices and showrooms located in Tokyo, Japan. Product sold in Japan is primarily shipped directly from our contract manufacturers' factories in China. We have retail stores in key locations such as Osaka and Tokyo.

#### China and Hong Kong

We have a 50% interest in a joint venture in China and a minority interest in a joint venture in Hong Kong that operate and generate net sales in those countries. Under the joint venture agreements, the joint venture partners contribute capital in proportion to their respective ownership interests. We have retail stores in key locations such as Shanghai, Beijing, Guangzhou, Hong Kong and Macau. These joint ventures are consolidated in our financial statements.

#### Malaysia and Singapore

We have a 50% interest in a joint venture in Malaysia and Singapore that operates and generates net sales in those countries. Under the joint venture agreement, the joint venture partners contribute capital in proportion to their respective ownership interests. We have retail stores in key locations such as Singapore and Kuala Lumpur. These joint ventures are consolidated in our financial statements.

#### India

We have a 51% interest in Skechers South Asia Private Limited and Skechers Retail India Private Limited, which are both joint ventures, that operate and generate net sales in India. Under the joint venture agreements, the joint venture partners contribute capital in proportion to their respective ownership interests. We have retail stores in key locations such as Bangalore, Mumbai and New Delhi. These joint ventures are consolidated in our financial statements. In 2019, we entered into an agreement to purchase the minority interest in our India joint venture that we did not own for \$82.5 million which will make our India joint venture a wholly owned subsidiary.

#### Israel

We have a 51% interest in Skechers Ltd. (Israel), which is a joint venture that operates and generates net sales in Israel. Under the joint venture agreement, the joint venture partners contribute capital in proportion to their respective ownership interests. We have retail stores in key locations such as Jerusalem and Tel Aviv. This joint venture is consolidated in our financial statements.

#### South Korea

We have a 65% interest in Skechers Korea Co., Ltd., which is a joint venture that operates and generates net sales in South Korea. Under the joint venture agreement, the joint venture partners contribute capital in proportion to their respective ownership interests. We have retail stores in key locations such as Seoul and Busan. This joint venture is consolidated in our financial statements.

•Distributors and Licensees

Where we do not sell directly through our international subsidiaries and joint ventures, our footwear is distributed through an extensive network of more than 22 distributors who sell our products to department, athletic and specialty stores. As of December 31, 2018, we also had agreements with 18 of these distributors and 48 licensees regarding 700 distributor-owned or licensed Skechers retail stores and 1,813 licensee-owned Skechers retail stores, respectively. Our distributors, licensees and franchisees own and operate the following retail stores in more than 170 countries around the world:

	Number of Store Locations			Number of Store Locations
	December 31, 2017	Opened during 2018	Closed during 2018	December 31, 2018
Distributor, licensee and franchise stores				
Africa Concept	46	8	(9 )	45
Africa Outlet	—	1	—	1
Asia Concept	754	261	(67 )	948
Asia Factory Outlet	334	105	(39 )	400
Australasia Concept	60	7	—	67
Australasia Outlet	15	5	—	20
Central America Concept	7	2	—	9
Europe Concept	174	75	(43 )	206
Europe Factory Outlet	15	10	—	25
Middle East Concept	148	10	(2 )	156
Middle East Factory Outlet	4	—	—	4
North America Concept	64	5	—	69
North America Factory Outlet	17	—	—	17
South America Concept	25	4	—	29
Total distributor, licensee and franchise stores	1,663	493	(160 )	1,996

Distributors and licensees are responsible for their respective stores' operations, have ownership of their respective stores' assets, and select the broad collection of our products to sell to consumers in their regions. In order to maintain a globally consistent image, we provide architectural, graphic and visual guidance and materials for the design of the stores, and we train the local staff on our products and corporate culture. We intend to expand our international presence and global recognition of the Skechers brand name by continuing to sell our footwear to foreign distributors and by opening retail stores with distributors that have local market expertise.

For disclosure of financial information about geographic areas and segment information for our three reportable segments—domestic wholesale sales, international wholesale sales, and retail sales, see Note 19 – Segment and Geographic Reporting in the consolidated financial statements included in this annual report.

## LICENSING

We believe that selective licensing of the Skechers brand name and our product line names to manufacturers may broaden and enhance the individual brands without requiring significant capital investments or additional incremental

operating expenses. Our multiple product lines plus additional subcategories present many potential licensing opportunities on terms with licensees that we believe will provide more effective manufacturing, distribution or marketing of non-footwear products. We also believe that the reputation of Skechers and its history in launching brands has also enabled us to partner with reputable non-footwear brands to design and market their footwear.

As of February 1, 2019, we had 22 active domestic and international licensing agreements in which we are the licensor. These include Skechers-branded kids' apparel; bags, backpacks and lunch boxes; belts, wallets and watches; headwear, socks and shoe care; prescription and sunglass eyewear; outerwear, swimwear, underwear, sleepwear and medical scrubs; fitness, yoga and running accessories; consumer electronics; bicycles and safety gear and cold weather products. Additional category-specific collections include Skechers Sport apparel, bags, backpacks and headwear; Twinkle Toes backpacks, lunchboxes, do-it-yourself fashion kits, sunglasses and hair accessories; and Skechers Work socks. We also have BOBS for DOGS pet accessories in Petco. We have international licensing agreements for the design and distribution of men's, women's and kids' apparel in the United Kingdom; socks throughout Europe; bags and backpacks in the Philippines, Taiwan, Australia, New Zealand, Europe and the Middle East; apparel, socks, headwear, bags, backpacks in Indonesia; apparel, socks, bags in Mexico; bags, backpacks, luggage, wallets, apparel, watches, medical scrubs and accessories in Latin America; and watches in the Philippines.

## DISTRIBUTION FACILITIES AND OPERATIONS

We believe that strong distribution support is a critical factor in our operations. Once manufactured, our products are packaged in shoe boxes bearing bar codes that are shipped either: (i) to our approximate 1.8 million square-foot distribution center located in Rancho Belago, California, (ii) to our approximate 1.3 million square-foot European Distribution Center (“EDC”) located in Liege, Belgium, (iii) to our company-operated distribution centers or third-party distribution centers in Central America, South America and Asia or (vi) directly from third-party manufacturers to our other international customers and other international third-party distribution centers. Upon receipt at either of the distribution centers, merchandise is inspected and recorded in our management information system and packaged according to customers’ orders for delivery. Merchandise is shipped to customers by whatever means each customer requests, which is usually by common carrier. The distribution centers have multi-access docks, enabling us to receive and ship simultaneously, and to pack separate trailers for shipments to different customers at the same time. We have an electronic data interchange system (“EDI system”) which is linked to some of our larger customers. This system allows these customers to automatically place orders with us, thereby eliminating the time involved in transmitting and inputting orders, and it includes direct billing and shipping information.

## INTELLECTUAL PROPERTY RIGHTS

We own and utilize a variety of trademarks, including the Skechers trademark. We have a significant number of both registrations and pending applications for our trademarks in the United States. In addition, we have trademark registrations and trademark applications in approximately 139 foreign countries. We also have design patents and pending design and utility patent applications in both the United States and approximately 21 foreign countries. We continuously look to increase the number of our patents and trademarks both domestically and internationally, where necessary to protect valuable intellectual property. We regard our trademarks and other intellectual property as valuable assets, and believe that they have significant value in marketing our products. We vigorously protect our trademarks against infringement, including through the use of cease and desist letters, administrative proceedings and lawsuits.

We rely on trademark, patent, copyright and trade secret protection, non-disclosure agreements and licensing arrangements to establish, protect and enforce intellectual property rights in our logos, trade names and in the design of our products. In particular, we believe that our future success will largely depend on our ability to maintain and protect the Skechers trademark and other key trademarks. Despite our efforts to safeguard and maintain our intellectual property rights, we cannot be certain that we will be successful in this regard. Furthermore, we cannot be certain that our trademarks, products and promotional materials or other intellectual property rights do not, or will not, violate the intellectual property rights of others, that our intellectual property would be upheld if challenged, or that we would, in such an event, not be prevented from using our trademarks or other intellectual property rights. Such claims, if proven, could materially and adversely affect our business, financial condition, results of operations and cash flows. In addition, although any such claims may ultimately prove to be without merit, the necessary management attention and associated legal costs with litigation or other resolution of future claims concerning trademarks and other intellectual property rights could materially and adversely affect our business, financial condition and results of operations. We have sued and have been sued by third parties for infringement of intellectual property. It is our opinion that none of these claims filed against us has materially impaired our ability to utilize our intellectual property rights.

The laws of certain foreign countries do not protect intellectual property rights to the same extent, or in the same manner, as do the laws of the United States. Although we continue to implement protective measures and intend to defend our intellectual property rights vigorously, these efforts may not be successful, or the costs associated with protecting our rights in certain jurisdictions may be prohibitive. From time to time, we discover products in the marketplace that are counterfeit reproductions of our products or that otherwise infringe upon intellectual property

rights held by us. Actions taken by us to establish and protect our trademarks and other intellectual property rights may not be adequate to prevent imitation of our products by others, or to prevent others from seeking to block sales of our products as violating trademarks and intellectual property rights. If we are unsuccessful in challenging a third party's products on the basis of infringement of our intellectual property rights, continued sales of such products by that or any other third party could adversely impact the Skechers brand, result in the shift of consumer preferences away from our products, and generally have a material adverse effect on our business, financial condition, results of operations and cash flows.

## COMPETITION

The global footwear industry is a competitive business. Although we believe that we do not compete directly with any single company with respect to its entire range of products, our products compete with other branded products within their product category as well as with private label products sold by retailers, including some of our customers. Our casual shoes and utility footwear compete with footwear offered by companies such as Columbia Sportswear Company, Converse by Nike, Inc., Deckers Outdoor Corporation, Kenneth Cole Productions Inc., Steven Madden, Ltd., The Timberland Company, V.F. Corporation and Wolverine World Wide, Inc. Our athletic lifestyle and performance shoes compete with footwear offered by companies such as Nike, Inc., adidas AG, Reebok International Ltd., Puma SE, ASICS America Corporation, New Balance Athletic Shoe, Inc. and Under Armour, Inc. The

intense competition among these companies and the rapid changes in technology and consumer preferences in the markets for performance footwear, including the walking fitness category, constitute significant risk factors in our operations. Our children's shoes compete with footwear offered by these companies and with other brands such as Stride Rite by Wolverine World Wide, Inc. In varying degrees, depending on the product category involved, we compete on the basis of style, price, quality, comfort and brand name prestige and recognition, among other factors. These and other competitors pose challenges to our market share in domestic and international markets. We also compete with numerous manufacturers, importers and distributors of footwear for the limited shelf space available for displaying such products to the consumer. Moreover, the general availability of contract manufacturing capacity allows ease of access by new market entrants. Some of our competitors are larger, have been in existence for a longer period of time, have strong brand recognition, have captured greater market share and/or have substantially greater financial, distribution, marketing and other resources than we do. We cannot be certain that we will be able to compete successfully against present or future competitors, or that competitive pressures will not have a material adverse effect on our business, financial condition, results of operations and cash flows.

## EMPLOYEES

As of January 31, 2019, we employed approximately 12,600 persons, of whom approximately 5,400 were employed on a full-time basis and approximately 7,200 were employed on a part-time basis, primarily in our retail stores. None of our employees are subject to a collective bargaining agreement. We believe that our relations with our employees are satisfactory.

## Item 1A. RISK FACTORS

In addition to the other information in this annual report, the following factors should be considered in evaluating us and our business.

### Our Future Success Depends On Our Ability To Maintain Our Brand Name And Image With Consumers.

Our success to date has in large part been due to the strength of the Skechers brand. Maintaining, promoting and growing our brand name and image depends on sustained effort and commitment to, and significant investment in, both the successful development of high-quality, innovative, fashion forward products, and fresh and relevant marketing and advertising campaigns. Even if we are able to timely and appropriately respond to changing consumer preferences and trends with new high-quality products, our marketing and advertising campaigns may not resonate with consumers, or consumers may consider our brand to be outdated or associated with footwear styles that are no longer popular or relevant. Our brand name and image with consumers could also be negatively impacted if we or any of our products were to receive negative publicity, whether related to our products or otherwise. If we are unable to maintain, promote and grow our brand image, then our business, financial condition, results of operations and cash flows could be materially and adversely affected.

### Our Future Success Also Depends On Our Ability To Respond To Changing Consumer Preferences, Identify And Interpret Consumer Trends, And Successfully Market New Products.

The footwear industry is subject to rapidly changing consumer preferences. The continued popularity of our footwear and the development of new lines and styles of footwear with widespread consumer appeal, including consumer acceptance of our performance footwear, requires us to accurately identify and interpret changing consumer trends and preferences, and to effectively respond in a timely manner. Continuing demand and market acceptance for both



existing and new products are uncertain and depend on the following factors:

- substantial investment in product innovation, design and development;
- commitment to product quality; and
- significant and sustained marketing efforts and expenditures, including with respect to the monitoring of consumer trends in footwear specifically, and in fashion and lifestyle categories generally.

In assessing our response to anticipated changing consumer preferences and trends, we frequently must make decisions about product designs and marketing expenditures several months in advance of the time when actual consumer acceptance can be determined. As a result, we may not be successful in responding to shifting consumer preferences and trends with new products that achieve market acceptance. Because of the ever-changing nature of consumer preferences and market trends, a number of companies in the footwear industry, including ours, experience periods of both rapid growth, followed by declines, in revenue and earnings. If we fail to identify and interpret changing consumer preferences and trends, or are not successful in responding to these changes with the timely development of products that achieve market acceptance, we could experience excess inventories, higher than normal

markdowns, returns, order cancellations or an inability to profitably sell our products, and our business, financial condition, results of operations and cash flows could be materially and adversely affected.

#### Our Business Could Be Harmed If We Fail To Maintain Proper Inventory Levels.

We place orders with our manufacturers for some of our products prior to the time we receive all of our customers' orders. We do this to minimize purchasing costs, the time necessary to fill customer orders and the risk of non-delivery. We also maintain an inventory of certain products that we anticipate will be in greater demand. Any unanticipated decline in the popularity of Skechers footwear or other unforeseen circumstances may make it difficult for us and our customers to accurately forecast product demand trends, and we may be unable to sell the products we have ordered in advance from manufacturers or that we have in our inventory. Inventory levels in excess of customer demand may result in inventory write-downs and the sale of excess inventory at discounted prices, which could significantly impair our brand image and have a material adverse effect on our operating results, financial condition and cash flows. Conversely, if we underestimate consumer demand for our products or if our manufacturers fail to supply the quality products that we require at the time we need them, we may experience inventory shortages. Inventory shortages might delay shipments to customers, negatively impact retailer and distributor relationships, and diminish brand loyalty.

#### We Face Intense Competition, Including Competition From Companies In The Performance Footwear Market and Those With Significantly Greater Resources Than Ours, And If We Are Unable To Compete Effectively With These Companies, Our Market Share May Decline And Our Business Could Be Harmed.

We face intense competition from other established companies in the footwear industry. Our competitors' product offerings, pricing, costs of production, and advertising and marketing expenditures are highly competitive areas in our business. If we do not adequately and timely anticipate and respond to our competitors, consumer demand for our products may decline significantly. A number of our competitors have significantly greater financial, technological, engineering, manufacturing, marketing and distribution resources than we do. Their greater capabilities in these areas may enable them to better withstand periodic downturns in the footwear industry, compete more effectively on the basis of price and production, keep up with rapid changes in footwear technology, and more quickly develop new products. New companies may also enter the markets in which we compete, further increasing competition in the footwear industry. In addition, negative consumer perceptions of our performance features due to our historical reputation as a fashion and lifestyle footwear company may place us at a competitive disadvantage in the performance footwear market. We may not be able to compete successfully in the future, and increased competition may result in price reductions, cost increases, reduced profit margins, loss of market share and an inability to generate cash flows that are sufficient to maintain or expand our development and marketing of new products, which would materially adversely impact our business, results of operations and financial condition.

#### Our Operating Results Could Be Negatively Impacted If Our Sales Are Concentrated In Any One Style Or Group Of Styles.

If any single style or group of similar styles of our footwear were to represent a substantial portion of our net sales, we could be exposed to risk should consumer demand for such style or group of styles decrease in subsequent periods. We attempt to mitigate this risk by offering a broad range of products, and no style comprised over 5% of our gross wholesale sales during 2018 or 2017. However, this may change in the future, and fluctuations in sales of any style representing a significant portion of our future net sales could have a negative impact on our operating results.

#### The Uncertainty Of Global Market Conditions May Continue To Have A Negative Impact On Our Business, Results Of Operations Or Financial Condition.

While global economic conditions have recently improved slightly, their uncertain state, including the challenging consumer retail market in the United States, continues to negatively impact our business, which depends on the general economic environment and levels of consumers' discretionary spending that affect not only the ultimate consumer, but also retailers, who are our primary direct customers. If the current economic situation does not improve or if it weakens, we may not be able to maintain or increase our sales to existing customers, make sales to new customers, open and operate new retail stores, maintain sales levels at our existing stores, maintain or increase our international operations on a profitable basis, or maintain or improve our earnings from operations as a percentage of net sales. Additionally, if there is an unexpected decline in sales, our results of operations will depend on our ability to implement a corresponding and timely reduction in our costs and manage other aspects of our operations. These challenges include (i) managing our infrastructure, (ii) hiring and maintaining, as required, the appropriate number of qualified employees, (iii) managing inventory levels and (iv) controlling other expenses. If the uncertain global market conditions continue for a significant period of time or worsen, our results of operations, financial condition, and cash flows could be materially adversely affected.

#### Our Business Could Be Adversely Affected By Changes In The Business Or Financial Condition Of Significant Customers Due To Global Economic Conditions.

The global financial crisis affected the banking system and financial markets and resulted in a tightening in the credit markets, more stringent lending standards and terms, and higher volatility in fixed income, credit, currency and equity markets. In addition, our business could be adversely affected by other economic conditions, such as the insolvency of certain of our key distributors, which could impair our distribution channels, or the diminished liquidity or an inability to obtain credit to finance purchases of our product

by our significant customers. Our customers may also experience weak demand for our products or other difficulties in their businesses. If economic, financial or political conditions in global markets deteriorate in the future, demand may be lower than forecasted and insufficient to achieve our anticipated financial results. Any of these events would likely harm our business, results of operations, financial condition and cash flows.

#### We Depend Upon A Relatively Small Group Of Customers For A Portion Of Our Sales.

During 2018, 2017 and 2016, our net sales to our five largest customers accounted for approximately 10.4%, 10.5% and 11.3% of total net sales, respectively. No customer accounted for more than 10.0% of our net sales during 2018, 2017 and 2016. No customer accounted for more than 10.0% of trade receivables at December 31, 2018 and 2017. These customers are primarily retailers who also distribute products for our competitors. Although we have long-term relationships with many of our customers, our customers do not have a contractual obligation to purchase our products and we cannot be certain that we will be able to retain our existing major customers. Furthermore, the retail industry regularly experiences consolidation, contractions and closings which may result in our loss of customers or our inability to collect accounts receivable of major customers. If we lose a major customer, experience a significant decrease in sales to a major customer or are unable to collect the accounts receivable of a major customer, our business could be harmed.

#### We May Experience Losses Because Of The Inability To Collect Accounts Receivable If Our Customers Are Unable To Pay Their Debts To Us When Due.

We rely on our network of domestic and international wholesale customers, comprised of department, athletic and specialty stores and online retailers, to distribute our products. Certain of our wholesale customers may from time to time experience bankruptcy, insolvency, and/or an inability to pay their debts to us as they come due. If our wholesale customers suffer significant financial difficulty, they may be unable to pay their debts to us timely or at all, which could have a material adverse effect on our results of operations. It is possible that wholesale customers may contest their contractual obligations to us under bankruptcy laws or otherwise. Significant customer bankruptcies could further adversely affect our net sales and increase our operating expenses by requiring larger accruals for bad debt expense. In addition, even when our contracts with these customers are not contested, if customers are unable to meet their obligations on a timely basis, it could adversely affect our ability to collect receivables. Further, we may have to negotiate significant discounts and/or extended financing terms with these customers in such a situation. If we are unable to collect upon our accounts receivable as they come due in an efficient and timely manner, our business, financial condition, or results of operations may be materially adversely affected. We also face risk from international customers that file for bankruptcy protection in foreign jurisdictions, as the application of foreign bankruptcy laws may be more difficult to predict. Although we believe that we have sufficient reserves to cover anticipated customer bankruptcies, there can be no assurance that such reserves will be adequate, and if they are not adequate, our business, cash flows, operating results and financial condition would be adversely affected.

#### Our Global Retail Business Has Required, And Will Continue To Require, A Substantial Investment And Commitment Of Resources And Is Subject To Numerous Risks And Uncertainties.

Our global retail business has required substantial investments in leasehold improvements, inventory and personnel. We have also made substantial operating lease commitments for retail space worldwide. Due to the high fixed-cost structure associated with our global retail business, a decline in sales or the closure or poor performance of individual or multiple stores could result in significant lease termination costs, write-offs or impairments of leasehold improvements, and employee-related termination costs. The success of our global retail operations also depends on our ability to identify and adapt to changes in consumer spending patterns and retail shopping preferences globally, including the shift from brick and mortar to e-commerce and mobile channels, and our ability to effectively develop our e-commerce and mobile channels. Our failure to successfully respond to these factors could adversely affect our

retail business, as well as damage our brand and reputation, and could materially affect our results of operations, financial position and cash flows.

**Our Quarterly Revenues And Operating Results Fluctuate As A Result Of A Variety Of Factors, Including Seasonal Fluctuations In Demand For Footwear, Delivery Date Delays And Potential Fluctuations In Our Estimated Annualized Tax Rate, Which May Result In Volatility Of Our Stock Price.**

Our quarterly revenues and operating results have varied significantly in the past and can be expected to fluctuate in the future due to a number of factors, many of which are beyond our control. Our major customers have no obligation to purchase forecasted amounts, may and have canceled orders in the past, and may change delivery schedules or change the mix of products ordered with minimal notice and without penalty. As a result, we may not be able to accurately predict our quarterly sales. In addition, sales of footwear products have historically been somewhat seasonal in nature, with the strongest domestic sales generally occurring in our second and third quarters for the back-to-school selling season. Domestically, back-to-school sales typically ship in June, July and August, and delays in the timing, cancellation, or rescheduling of these customer orders and shipments by our wholesale customers

could negatively impact our net sales and results of operations for our second or third quarters. More specifically, the timing of when products are shipped is determined by the delivery schedules set by our wholesale customers, which could cause sales to shift between our second and third quarters. Because our expense levels are partially based on our expectations of future net sales, our expenses may be disproportionately large relative to our revenues, and we may be unable to adjust spending in a timely manner to compensate for any unexpected revenue shifts, which could have a material adverse effect on our operating results.

Our annualized tax rate is based on projections of our domestic and international operating results for the year, which we review and revise as necessary at the end of each quarter, and it is highly sensitive to fluctuations in projected international earnings. Any quarterly fluctuations in our annualized tax rate that may occur could have a material impact on our quarterly operating results. As a result of these specific and other general factors, our operating results will likely vary from quarter to quarter, and the results for any particular quarter may not be necessarily indicative of results for the full year. Any shortfall in revenues or net earnings from levels expected by securities analysts and investors could cause a decrease in the trading price of our Class A Common Stock.

#### Foreign Currency Exchange Rate Fluctuations Could Have A Material Adverse Effect On Our Business And Results Of Operations.

Foreign currency fluctuations affect our revenue and profitability. Changes in currency exchange rates may impact our financial results positively or negatively in one period and not another, which may make it difficult to compare our operating results from different periods. Currency exchange rate fluctuations may also adversely impact third parties that manufacture our products by making their costs of raw materials or other production costs more expensive and more difficult to finance, thereby raising prices for our company, our distributors and/or our licensees. We do not currently engage in hedging activities with respect to these currency exchange rate risks. For a more detailed discussion of the risks related to foreign currency fluctuation, see Item 7A: “Quantitative and Qualitative Disclosures About Market Risk.”

In addition, our foreign subsidiaries purchase products in U.S. dollars in which the cost of those products will vary depending on the foreign currency rates and will impact the price charged to customers. Our foreign distributors also purchase products in U.S. dollars and sell in local currencies, which impacts the price to foreign consumers. As the U.S. dollar strengthens relative to foreign currencies, our revenues and profits are reduced when translated into U.S. dollars and our margins may be negatively impacted by the increase in product costs due to foreign currency rates. Although we typically work to mitigate this negative foreign currency transaction impact through price increases and further actions to reduce costs, we may not be able to fully offset the impact, if at all. Our success depends, in part, on our ability to manage or mitigate these foreign currency impacts as changes in the value of the U.S. dollar relative to other currencies could have a material adverse effect on our business, results of operations, financial position and cash flows.

#### Recent U.S. Tax Legislation May Materially Adversely Affect Our Financial Condition, Results of Operations and Cash Flows.

U.S. tax legislation enacted at the end of 2017 has significantly changed the U.S. federal income taxation of U.S. corporations, by reducing the U.S. corporate income tax rate, permitting immediate expensing of certain capital expenditures, adopting elements of a territorial tax system, imposing a one-time transition tax (“Transition Tax”) on all undistributed earnings and profits of certain U.S.-owned foreign corporations, revising the rules governing foreign tax credits, and introducing new anti-base-erosion provisions. Many of these changes were effective immediately, without any transition periods or grandfathering for existing transactions. The legislation is unclear in many respects and could be subject to potential amendments and technical corrections, as well as interpretations and implementing regulations by the U.S. Treasury Department (“Treasury”) and U.S. Internal Revenue Service (“IRS”), any of which could lessen or

increase certain adverse impacts of the legislation. In addition, it is unclear how these U.S. federal income tax changes will affect state and local taxation, which often uses federal taxable income as a starting point for computing state and local tax liabilities.

While some of the changes made by the tax legislation may adversely affect the Company in one or more reporting periods and prospectively, other changes may be beneficial on a going forward basis.

**An Increase In Our Effective Tax Rate Could Have A Material Adverse Effect On Our Results Of Operations And Financial Position.**

A significant amount of our foreign earnings are generated in low or zero tax jurisdictions. As a result, our income tax expense has historically been lower than the tax computed at the U.S. statutory income tax rate. Our future effective tax rates could be unfavorably affected by a number of factors, including but not limited to, changes in the tax rates or the tax rules and regulations (including rules and regulations related to recently enacted U.S. tax legislation), or in the interpretation thereof, in the jurisdictions in which we do business; decreases in the amount of earnings in countries with low statutory tax rates; increases in the amount of earnings in countries with high statutory tax rates; or if we need to make significant taxable distributions of foreign earnings for which

foreign taxes have not been provided. An increase in our effective tax rate could have a material adverse effect on our business, results of operations, financial position and cash flows.

#### Changes In Tax Laws Or The Potential Imposition Of Additional Duties, Quotas, Tariffs And Other Trade Restrictions Could Have An Adverse Impact On Our Sales And Profitability.

All of our products manufactured overseas and imported into the United States, the European Union (“EU”) and other countries are subject to customs duties collected by customs authorities. Customs information submitted by us is routinely subject to review by customs authorities. We are unable to predict whether there may be unfavorable changes in tax laws in the United States or overseas, additional customs duties, quotas, tariffs, anti-dumping duties, safeguard measures, cargo restrictions to prevent terrorism or other trade restrictions imposed on the importation of our products in the future. Such actions could adversely affect our ability to produce and market footwear at competitive prices and might have an adverse impact on the sales and profitability of Skechers.

#### Our International Sales And Manufacturing Operations Are Subject To The Risks Of Doing Business Abroad, Particularly In China and Vietnam, Which Could Affect Our Ability To Sell Or Manufacture Our Products In International Markets, Obtain Products From Foreign Suppliers Or Control The Costs Of Our Products.

Substantially all of our net sales during the year ended December 31, 2018, were derived from sales of footwear manufactured in foreign countries, with most manufactured in China and Vietnam. We also sell our footwear in several foreign countries and plan to increase our international sales efforts as part of our growth strategy. Foreign manufacturing and sales are subject to a number of risks, including the following: political and social unrest, including terrorism; changing economic conditions, including higher labor costs; increased costs of raw materials; currency exchange rate fluctuations; labor shortages and work stoppages; electrical shortages; transportation delays; loss or damage to products in transit; expropriation; nationalization; the adjustment, elimination or imposition of domestic and international duties, tariffs, quotas, import and export controls and other non-tariff barriers; exposure to different legal standards (particularly with respect to intellectual property); compliance with foreign laws; and changes in domestic and foreign governmental policies. We have not, to date, been materially affected by any such risks, but we cannot predict the likelihood of such developments occurring or the resulting long-term adverse impact on our business, results of operations, financial condition and cash flows.

In particular, because most of our products are manufactured in China and Vietnam, the possibility of adverse changes in trade or political relations with China or Vietnam, political instability in China or Vietnam, increases in labor costs, the occurrence of prolonged adverse weather conditions or a natural disaster such as an earthquake or typhoon in China or Vietnam, or the outbreak of a pandemic disease in China or Vietnam could severely interfere with the manufacturing and/or shipment of our products and would have a material adverse effect on our operations. Our business operations may be adversely affected by the current and future political environment in the Communist Party of China (“PRC”). The government of the PRC has exercised and continues to exercise substantial control over virtually every sector of the Chinese economy through regulation and state ownership. Our ability to operate in the PRC may be adversely affected by changes in Chinese laws and regulations, including those relating to taxation, import and export tariffs, raw materials, environmental regulations, land use rights, property and other matters. Under its current leadership, the government of the PRC has been pursuing economic reform policies that encourage private economic activity and greater economic decentralization. There is no assurance, however, that the government of the PRC will continue to pursue these policies, or that it will not significantly alter these policies from time to time without notice. A change in policies by the PRC government could adversely affect our interests by, among other factors: changes in laws, regulations or the interpretation thereof, confiscatory taxation, restrictions on currency conversion, imports or sources of supplies, or the expropriation or nationalization of private enterprises. In addition, electrical shortages, labor shortages or work stoppages may extend the production time necessary to produce our orders, and there may be circumstances in the future where we may have to incur premium freight charges to expedite the delivery of product to



our customers. If we incur a significant amount of premium charges to airfreight product for our customers, our gross profit will be negatively affected if we are unable to collect those charges.

Many Of Our Retail Stores Depend Heavily On The Customer Traffic Generated By Shopping And Factory Outlet Malls Or By Tourism.

Many of our concept stores are located in shopping malls, and some of our factory outlet stores are located in manufacturers' outlet malls where we depend on obtaining prominent locations and the overall success of the malls to generate customer traffic. We cannot control the success of individual malls, and an increase in store closures by other retailers may lead to mall vacancies and reduced foot traffic. Some of our concept stores occupy street locations that are heavily dependent on customer traffic generated by tourism. Any substantial decrease in tourism resulting from an economic slowdown, political, social or military events or otherwise, is likely to adversely affect sales in our existing stores, particularly those with street locations. The effects of these factors could reduce sales of particular existing stores or hinder our ability to open retail stores in new markets, which could negatively affect our operating results.

### We Rely On Independent Contract Manufacturers And, As A Result, Are Exposed To Potential Disruptions In Product Supply.

Our footwear products are currently manufactured by independent contract manufacturers. During 2018 and 2017, the top five manufacturers of our products produced approximately 41.9% and 47.5% of our total purchases, respectively. One manufacturer accounted for 12.8% and 17.9% of total purchases during 2018 and 2017, respectively. Another manufacturer accounted for 10.1% and 11.1% of our total purchases during 2018 and 2017, respectively. We do not have long-term contracts with manufacturers, and we compete with other footwear companies for production facilities. We could experience difficulties with these manufacturers, including reductions in the availability of production capacity, failure to meet our quality control standards, failure to meet production deadlines, or increased manufacturing costs. This could result in our customers canceling orders, refusing to accept deliveries, or demanding reductions in purchase prices, any of which could have a negative impact on our cash flow and harm our business.

If our current manufacturers cease doing business with us, we could experience an interruption in the manufacture of our products. Although we believe that we could find alternative manufacturers, we may be unable to establish relationships with alternative manufacturers that will be as favorable as the relationships we have now. For example, new manufacturers may have higher prices, less favorable payment terms, lower manufacturing capacity, lower quality standards, or higher lead times for delivery. If we are unable to provide products consistent with our standards, or the manufacture of our footwear is delayed or becomes more expensive, our business would be harmed.

### Our Ability To Deliver Our Products To The Market Could Be Disrupted If We Encounter Problems Affecting Our Logistics And Distribution Systems.

We rely on owned or independently operated distribution facilities to transport, warehouse and ship products to our customers. Our logistic and distribution systems include computer-controlled and automated equipment, which may be subject to a number of risks related to security or computer viruses, the proper operation of software and hardware, power interruptions or other system failures. Substantially all of our products are distributed from a few key locations. Therefore, our operations could be interrupted by earthquakes, floods, fires or other natural disasters near our distribution centers. Our business interruption insurance may not adequately protect us from the adverse effects that could be caused by significant disruptions affecting our distribution facilities, such as the long-term loss of customers or an erosion of brand image. In addition, our distribution capacity is dependent on the timely performance of services by third parties, including the transportation of products to and from our distribution facilities. If we encounter problems affecting our distribution system, our ability to meet customer expectations, manage inventory, complete sales and achieve operating efficiencies could be materially adversely affected.

### Our Business Could Be Harmed If Our Contract Manufacturers, Suppliers Or Licensees Violate Labor, Trade Or Other Laws.

We require our independent contract manufacturers, suppliers and licensees to operate in compliance with applicable laws and regulations. Manufacturers are required to certify that neither convicted, forced or indentured labor (as defined under United States law) nor child labor (as defined by law in the manufacturer's country) is used in the production process, that compensation is paid in accordance with local law and that their factories are in compliance with local safety regulations. Although we promote ethical business practices and our sourcing personnel periodically visit and monitor the operations of our independent contract manufacturers, suppliers and licensees, we do not control them or their labor practices. If one of our independent contract manufacturers, suppliers or licensees violates labor or other laws or diverges from those labor practices generally accepted as ethical in the United States, it could result in adverse publicity for us, damage our reputation in the United States, or render our conduct of business in a particular foreign country undesirable or impractical, any of which could harm our business.

In addition, if we, or our foreign manufacturers, violate United States or foreign trade laws or regulations, we may be subject to extra duties, significant monetary penalties, the seizure and the forfeiture of the products we are attempting to import, or the loss of our import privileges. Possible violations of United States or foreign laws or regulations could include inadequate record-keeping of our imported products, misstatements or errors as to the origin, quota category, classification, marketing or valuation of our imported products, fraudulent visas, or labor violations. The effects of these factors could render our conduct of business in a particular country undesirable or impractical, and have a negative impact on our operating results.

Our Strategies Involve A Number Of Risks That Could Prevent Or Delay The Successful Opening Of New Stores As Well As Negatively Impact The Performance Of Our Existing Stores.

Our ability to successfully open and operate new stores depends on many factors, including, among others, our ability to identify suitable store locations, the availability of which is outside of our control; negotiate acceptable lease terms, including desired tenant improvement allowances; source sufficient levels of inventory to meet the needs of new stores; hire, train and retain store personnel; successfully integrate new stores into our existing operations; and satisfy the fashion preferences in new geographic areas.

In addition, some or a substantial number of new stores could be opened in regions of the United States in which we currently have few or no stores. Any expansion into new markets may present competitive, merchandising and distribution challenges that are different from those currently encountered in our existing markets. Any of these challenges could adversely affect our business and results of operations. In addition, to the extent that any new store openings are in existing markets, we may experience reduced net sales volumes in existing stores in those markets.

**We Depend On Key Personnel To Manage Our Business Effectively In A Rapidly Changing Market, And If We Are Unable To Retain Existing Personnel, Our Business Could Be Harmed.**

Our future success depends upon the continued services of Robert Greenberg, Chairman of the Board and Chief Executive Officer; Michael Greenberg, President and a member of our Board of Directors; and David Weinberg, Executive Vice President, Chief Operating Officer and a member of our Board of Directors. The loss of the services of any of these individuals or any other key employee could harm us. Our future success also depends on our ability to identify, attract and retain additional qualified personnel. Competition for employees in our industry is intense, and we may not be successful in attracting and retaining such personnel.

**The Disruption, Expense And Potential Liability Associated With Existing And Unanticipated Future Litigation Against Us Could Have A Material Adverse Effect On Our Business, Results Of Operations, Financial Condition And Cash Flows.**

In addition to the legal matters included in our reserve for loss contingencies, we occasionally become involved in litigation arising from the normal course of business, and we are unable to determine the extent of any liability that may arise from any such unanticipated future litigation. We have no reason to believe that there is a reasonable possibility or a probability our company may incur a material loss, or a material loss in excess of a recorded accrual, with respect to any other such loss contingencies. However, the outcome of litigation is inherently uncertain and assessments and decisions on defense and settlement can change significantly in a short period of time. Therefore, although we consider the likelihood of such an outcome to be remote with respect to those matters for which we have not reserved an amount for loss contingencies, if one or more of these legal matters were resolved against us in the same reporting period for amounts in excess of our expectations, our consolidated financial statements of a particular reporting period could be materially adversely affected. Further, any unanticipated litigation in the future, regardless of its merits, could also significantly divert management's attention from our operations and result in substantial legal fees being incurred. Such disruptions, legal fees and any losses resulting from these unanticipated future claims could have a material adverse effect on our business or financial condition.

**Our Ability To Compete Could Be Jeopardized If We Are Unable To Protect Our Intellectual Property Rights Or If We Are Sued For Intellectual Property Infringement.**

We believe that our trademarks, design patents and other proprietary rights are important to our success and our competitive position. We use trademarks on nearly all of our products and believe that having distinctive marks that are readily identifiable is an important factor in creating a market for our goods, in identifying us and in distinguishing our goods from the goods of others. We consider our Skechers®, Skechers Sport®, Skechers USA®, D'Lite®, Skechers Performance™, Skechers GOrun®, Skechers GOwalk®, Hyper Burst™, You by Skechers®, ®, ®, Skechers Cali®, Relaxed Fit®, Skecher Street®, Air-Cooled Memory Foam®, Skechers Memory Foam™, Skech-Air®, BOBS®, Energy Lights®, S-Lights® and Twinkle Toes® trademarks to be among our most valuable assets, and we have registered these trademarks in many countries. In addition, we own many other trademarks that we utilize in marketing our products. We also have a number of design patents and a limited number of utility patents covering components and features used in various shoes. We believe that our patents and trademarks are generally sufficient to permit us to carry on our business as presently conducted. While we vigorously protect our trademarks against infringement, we cannot guarantee that we will be able to secure patents or trademark protection for our intellectual property in the future or

that protection will be adequate for future products. Further, we have been sued in the past for patent and trademark infringement and cannot be sure that our activities do not and will not infringe on the intellectual property rights of others. If we are compelled to prosecute infringing parties, defend our intellectual property or defend ourselves from intellectual property claims made by others, we may face significant expenses and liability as well as the diversion of management's attention from our business, each of which could negatively impact our business or financial condition.

In addition, the laws of foreign countries where we source and distribute our products may not protect intellectual property rights to the same extent as do the laws of the United States. We cannot assure you that the actions we have taken to establish and protect our trademarks and other intellectual property rights outside the United States will be adequate to prevent imitation of our products by others or, if necessary, successfully challenge another party's counterfeit products or products that otherwise infringe on our intellectual property rights on the basis of trademark or patent infringement. Continued sales of these products could adversely affect our sales and our brand and result in the shift of consumer preference away from our products. We may face significant expenses and liability in connection with the protection of our intellectual property rights outside the United States, and if we are

unable to successfully protect our rights or resolve intellectual property conflicts with others, our business or financial condition could be adversely affected.

**Breaches Or Compromises Of Our Information Security Systems, Information Technology Systems And Our Infrastructure To Support Our Business Could Result In Exposure Of Private Information, Disruption Of Our Business And Damage To Our Reputation, Which Could Harm Our Business, Results Of Operation And Financial Condition.**

As a routine part of our business, we utilize information security and information technology systems and websites that allow for the secure storage and transmission of proprietary or private information regarding our customers, employees, vendors and others. A security breach of our network, hosted service providers, or vendor systems, may expose us to a risk of loss or misuse of this information, litigation and potential liability. Hackers and data thieves are increasingly sophisticated and operate large-scale and complex automated attacks, and the retail industry, in particular, has been the target of many recent cyber-attacks. Although we take measures to safeguard this sensitive information, we may not have the resources or technical sophistication to anticipate or prevent rapidly-evolving types of cyber-attacks targeted at us, our customers, or others who have entrusted us with information. Actual or anticipated attacks may cause us to incur costs, including costs to deploy additional personnel and protection technologies, train employees, and engage third-party experts and consultants.

We invest in industry standard security technology to protect personal information. Advances in computer capabilities, new technological discoveries, or other developments may result in the technology used by us to protect against transaction or other data being breached or compromised. In addition, data and security breaches can also occur as a result of non-technical issues, including breach by us or by persons with whom we have commercial relationships that result in the unauthorized release of personal or confidential information. Although we maintain insurance designed to provide coverage for cyber risks related to what we believe to be adequate and collectible insurance in the event of theft, loss, fraudulent or unlawful use of customer, employee or company data, any compromise or breach of our cyber security systems could result in private information exposure and a violation of applicable privacy and other laws, significant potential liability including legal and financial costs, and loss of confidence in our security measures by customers, which could result in damage to our brand and have an adverse effect on our business, financial condition and reputation. In addition, we must comply with increasingly complex and rigorous regulatory standards enacted to protect business and personal data. Compliance with existing and proposed laws and regulations can be costly, and any failure to comply with these regulatory standards could subject us to legal and reputational risks. Misuse of or failure to secure personal information could also result in violation of data privacy laws and regulations, proceedings against us by governmental entities or others, damage to our reputation and credibility and could have a negative impact on revenues and profits.

**Natural Disasters Or A Decline In Economic Conditions In California Could Increase Our Operating Expenses Or Adversely Affect Our Sales Revenue.**

As of December 31, 2018, a substantial portion of our operations are located in California, including 99 of our retail stores, our headquarters in Manhattan Beach, and our domestic distribution center in Rancho Belago. Because a significant portion of our net sales is derived from sales in California, a decline in the economic conditions in California, whether or not such decline spreads beyond California, could materially adversely affect our business. Furthermore, a natural disaster or other catastrophic event, such as an earthquake or wild fire affecting California, could significantly disrupt our business including the operation of our only domestic distribution center. We may be more susceptible to these issues than our competitors whose operations are not as concentrated in California.

**Two Principal Stockholders Are Able To Exert Significant Influence Over All Matters Requiring A Vote Of Our Stockholders, And Their Interests May Differ From The Interests Of Our Other Stockholders.**

As of December 31, 2018, our Chairman of the Board and Chief Executive Officer, Robert Greenberg, beneficially owned 77.0% of our outstanding Class B common shares, members of Mr. Greenberg's immediate family beneficially owned an additional 13.4% of our outstanding Class B common shares, and Gil Schwartzberg, trustee of several trusts formed by Mr. Greenberg and his wife for estate planning purposes, beneficially owned 30.6% of our outstanding Class B common shares. The holders of Class A common shares and Class B common shares have identical rights except that holders of Class A common shares are entitled to one vote per share while holders of Class B common shares are entitled to ten votes per share on all matters submitted to a vote of our stockholders. As a result, as of December 31, 2018, Mr. Greenberg beneficially owned 35.9% of the aggregate number of votes eligible to be cast by our stockholders, and together with shares beneficially owned by other members of his immediate family, Mr. Greenberg and his immediate family beneficially owned 45.1% of the aggregate number of votes eligible to be cast by our stockholders, and Mr. Schwartzberg beneficially owned 19.7% of the aggregate number of votes eligible to be cast by our stockholders. Therefore, Messrs. Greenberg and Schwartzberg are each able to exert significant influence over all matters requiring approval by our stockholders. Matters that require the approval of our stockholders include the election of directors and the approval of mergers or other business combination transactions. Mr. Greenberg also has significant influence over our management and

operations. As a result of such influence, certain transactions are not likely without the approval of Messrs. Greenberg and Schwartzberg, including proxy contests, tender offers, open market purchase programs or other transactions that can give our stockholders the opportunity to realize a premium over the then-prevailing market prices for their shares of our Class A common shares. Because Messrs. Greenberg's and Schwartzberg's interests may differ from the interests of the other stockholders, their ability to substantially control or significantly influence, respectively, actions requiring stockholder approval, may result in our company taking action that is not in the interests of all stockholders. The differential in the voting rights may also adversely affect the value of our Class A common shares to the extent that investors or any potential future purchaser view the superior voting rights of our Class B common shares to have value.

**Our Charter Documents And Delaware Law May Inhibit A Takeover, Which May Adversely Affect The Value Of Our Stock.**

Provisions of Delaware law, our certificate of incorporation or our bylaws could make it more difficult for a third party to acquire us, even if closing such a transaction would be beneficial to our stockholders. Mr. Greenberg's substantial beneficial ownership position, together with the authorization of Preferred Stock, the disparate voting rights between our Class A Common Stock and Class B Common Stock, the classification of our Board of Directors and the lack of cumulative voting in our certificate of incorporation and bylaws, may have the effect of delaying, deferring or preventing a change in control, may discourage bids for our Class A Common Stock at a premium over the market price of the Class A Common Stock and may adversely affect the market price of our Class A Common Stock.



#### ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

#### ITEM 2. PROPERTIES

Our corporate headquarters are located at several properties in or near Manhattan Beach, California, which consist of an aggregate of approximately 188,000 square feet. We own and lease portions of our corporate headquarters.

Our U.S. distribution center is a 1.8 million square-foot facility located on approximately 110 acres in Rancho Belago, California. We are leasing the distribution center from a joint venture, HF Logistics-SKX (the "JV"), that we formed with HF Logistics I, LLC ("HF") in January 2010 for the purpose of building and operating the facility. The lease for this facility expires in November 2031, with a base rent of \$940,695 per month, or approximately \$11.3 million per year. The JV is consolidated in our financial statements.

Our European Distribution Center occupies approximately 1.3 million square feet in Liege, Belgium under five operating leases, with base rents of approximately \$5.5 million per year. These leases provide for original terms of 10-15 years, commencing between January 2016 and June 2016, subject to automatic extensions for recurring periods of five years unless we or the landlord terminates the lease in writing 12 months prior to the expiration of the original lease term or 12 months prior to the end of the then applicable five-year extension.

All of our domestic retail stores and showrooms are leased with terms expiring between August 2019 and October 2033. The leases provide for rent escalations tied to either increases in the lessor's operating expenses, fluctuations in the consumer price index in the relevant geographical area, or a percentage of the store's gross sales in excess of the base annual rent. Total base rent expense related to our domestic retail stores and showrooms was \$103.6 million for the year ended December 31, 2018.

We also lease all of our international administrative offices, retail stores, showrooms and distribution facilities located in Asia, Central America, Europe, North America and South America. The property leases expire at various dates between March 2019 and March 2029. Total base rent for the leased properties aggregated approximately \$113.9 million for the year ended December 31, 2018.

#### ITEM 3. LEGAL PROCEEDINGS

Converse, Inc. v. Skechers U.S.A., Inc. – On October 14, 2014, Converse filed an action against our company in the United States District Court for the Eastern District of New York, Brooklyn Division, Case 1:14-cv-05977-DLI-MDG, alleging trademark infringement, false designation of origin, unfair competition, trademark dilution and deceptive practices arising out of our alleged use of certain design elements on footwear. The complaint seeks, among other things, injunctive relief, profits, actual damages, enhanced damages, punitive damages, costs and attorneys' fees. On October 14, 2014, Converse also filed a complaint naming 27 respondents including our company with the U.S. International Trade Commission (the "ITC" or "Commission"), Federal Register Doc. 2014 24890, alleging violations of federal law in the importation into and the sale within the United States of certain footwear. Converse has requested that the Commission issue a general exclusion order, or in the alternative a limited exclusion order, and cease and desist orders. On December 8, 2014, the District Court stayed the proceedings before it. On December 19, 2014, Skechers responded to the ITC complaint, denying the material allegations and asserting affirmative defenses. A trial before an administrative law judge of the ITC was held in August 2015. On November 15, 2015, the ITC judge issued his interim decision finding that certain discontinued products (Daddy's Money and HyDee HyTops) infringed on Converse's intellectual property, but that other, still active product lines (Twinkle Toes and Bobs Utopia) did not. On

February 3, 2016, the ITC decided that it would review in part certain matters that were decided by the ITC judge. On June 28, 2016, the full ITC issued a ruling affirming that Skechers Twinkle Toes and Bobs canvas shoes do not infringe Converse's Chuck Taylor Midsole Trademark and affirming that Converse's common law trademark was invalid. The full ITC also invalidated Converse's registered trademark. Converse appealed this decision to the United States Court of Appeals for the Federal Circuit. On January 27, 2017, Converse filed its appellate brief but did not contest the portion of the decision that held that Skechers Twinkle Toes and Bobs canvas shoes do not infringe. On June 26, 2017, we filed our responsive brief, on February 8, 2018 the court heard oral argument, and on June 7, 2018 the Court requested supplemental briefing on certain issues. On October 30, 2018, the United States Court of Appeals for the Federal Circuit vacated the ITC's ruling and remanded the matter back to the ITC for further proceedings. While it is too early to predict the outcome of these legal proceedings or whether an adverse result in either or both of them would have a material adverse impact on our operations or financial position, we believe we have meritorious defenses and intend to defend these legal matters vigorously.

Nike, Inc. v. Skechers USA, Inc. – On January 4, 2016, Nike filed an action against our company in the United States District Court for the District of Oregon, Case No. 3:16-cv-0007, alleging that certain Skechers shoe designs (Men’s Burst, Women’s Burst, Women’s Flex Appeal, Men’s Flex Advantage, Girls’ Skech Appeal, and Boys’ Flex Advantage) infringe the claims of eight design patents. Nike seeks injunctive relief, disgorgement of Skechers’ profits, damages (including treble damages), pre-judgment and post-judgment interest, attorneys’ fees, and costs. In April and May, 2016, we filed petitions with the United States Patent and Trademark Office’s Patent Trial and Appeal Board (the “PTAB”) for inter partes review of all eight design patents, seeking to invalidate those patents. In September and November 2016, the Patent Trial and Appeal Board denied each of our petitions. On January 6, 2017, we filed several additional petitions for inter partes review with the PTAB, seeking to invalidate seven of the eight designs patents that Nike is asserting. In July 2017, we were notified that the PTAB granted our petitions and instituted inter partes review proceedings with respect to two of the seven design patents but denied our petitions as to the others. In June 2017, we filed a motion to transfer venue from the District of Oregon to the Central District of California based on a recent United States Supreme Court decision and the motion was granted in late 2017. On June 28, 2018, the PTAB issued final decisions in the two inter partes review proceedings, rejecting the invalidity challenges made by our company in those proceedings. On June 4, 2018, the Court, over Nike’s opposition, granted our request for a claim construction hearing. A claim construction hearing was held on August 28, 2018 and we are currently waiting for a ruling. While it is too early to predict the outcome of the case or whether an adverse result would have a material adverse impact on our operations or financial position, we believe we have meritorious defenses and intend to defend this legal matter vigorously.

Steamfitters Local 449 Pension Plan v. Skechers USA, Inc., Robert Greenberg and David Weinberg. – On October 20, 2017, the Steamfitters Local 449 Pension Plan filed a securities class action, on behalf of itself and purportedly on behalf of other shareholders who purchased Skechers stock in a five-month period in 2015, against our company and certain of its officers in the United States District Court for the Southern District of New York, case number 1:17-cv-08107. On April 4, 2018, the plaintiffs filed an amended and consolidated complaint and on July 24, 2018 plaintiffs filed a second amended and consolidated complaint. The lawsuit alleges that, between April 23 and October 22, 2015, we made materially false statements or omissions of material fact about the anticipated performance of our Domestic Wholesale segment and asserts claims for unspecified damages, attorneys' fees and equitable relief based on two counts for alleged violations of federal securities laws. On November 21, 2018 we filed a motion to dismiss. On January 10, 2019 plaintiffs filed an opposition and on February 11, 2019 we filed a reply. There is no date set for the hearing. Given the early stage of this proceeding and the limited information available, we cannot predict the outcome of this legal proceeding or whether an adverse result in this case would have a material adverse impact on our operations or financial position. We believe we have meritorious defenses and intend to defend this matter vigorously.

In Re Skechers Securities Litigation (formerly Laborers Local 235 Benefit Fund v. Skechers USA, Inc. Robert Greenberg, David Weinberg and John Vandemore) – On September 4, 2018, Laborers Local 235 Benefit Fund filed a securities class action on behalf of itself and purportedly on behalf of other shareholders who purchased the company’s stock between October 20, 2017 and July 19, 2018 (the “Class Period”), against our company and certain of its officers in the United States District Court for the Southern District of New York, case number 1:18-cv-8039. The complaint alleges that throughout the Class Period we made materially false statements or omissions of material fact regarding our sales growth and controlling expenses in an effort to artificially inflate the price of our stock for the personal gain of the Company’s founding family. Beginning October 17, 2018, copycat cases were filed and on January 22, 2019 a consolidated amended class action complaint was filed as In Re Skechers Securities Litigation. Given the early stages of these proceedings and the limited information available, we cannot predict the outcome of these legal proceedings or whether an adverse result in these cases would have a material adverse impact on our operations or financial position. We believe we have meritorious defenses and intend to defend these matters vigorously.

Kathleen Houseman v. Robert Greenberg, et al. – On November 27, 2018, the Company, the Board of Directors and CFO John Vandemore were sued by a shareholder and the Company in a derivative action in the United States District Court for the District of Delaware, Case No 1:18tc222. The complaint is based largely on the same underlying factual allegations as In Re Skechers Securities Litigation. By mutual agreement of the parties this case has been stayed pending the outcome of In Re Skechers Securities Litigation. We believe we have meritorious defenses and intend to defend this matter vigorously. Notwithstanding, given the early stages of these proceedings and the limited information available, we cannot predict the outcome of this legal proceeding or whether an adverse result in this case would have a material adverse impact on our operations or financial position.

Jesse Chen v. Robert Greenberg, et al. – On January 16, 2019, the Company, the Board of Directors and CFO John Vandemore were sued by a shareholder and the Company in a derivative action in the Superior Court for the State of California for the County of Los Angeles, Case No.19-STC-CV00393. The complaint mirrors the Houseman case, supra, and based largely on the same underlying factual allegations as In Re Skechers Securities Litigation. By mutual agreement of the parties this case has been stayed pending the outcome of In Re Skechers Securities Litigation. We believe we have meritorious defenses and intend to defend this matter vigorously. Notwithstanding, given the early stages of these proceedings and the limited information available, we cannot predict the outcome of this legal proceeding or whether an adverse result in this case would have a material adverse impact on our operations or financial position.

Yolanda Zuniga v. Team One Employment Specialists, LLC, Skechers USA, Inc., Dolores Carte et al. – On December 20, 2017, our company was named as a defendant in an action filed by a former employee named Yolanda Zuniga in the Superior Court of California, County of Riverside, Case No. RIC 1723878, alleging discrimination, harassment, retaliation, violation of the Family Medical Leave Act/California Family Rights Act, breach of contract and wrongful termination, among other causes of action, and seeking compensatory damages, punitive and exemplary damages, and attorneys' fees. This case was stayed pending the outcome of an arbitration between the parties involving identical claims. This case has been settled and the settlement funded by a co-defendant. The settlement did not have a material adverse impact on our operations or financial position.

Ealeen Wilk v. Skechers U.S.A., Inc. – On September 10, 2018, Ealeen Wilk filed a putative class action lawsuit against our company in the United States District Court for the Central District of California, Case No. 5:18-cv-01921, alleging violations of the California Labor Code, including unpaid overtime, unpaid wages due upon termination and unfair business practices. The complaint seeks actual, compensatory, special and general damages; penalties and liquidated damages; restitutionary and injunctive relief; attorneys' fees and costs; and interest as permitted by law. While it is too early to predict the outcome of the litigation or a reasonable range of potential losses and whether an adverse result would have a material adverse impact on our results of operations or financial position, we believe that we have meritorious defenses, vehemently deny the allegations, and intend to defend the case vigorously.

In addition to the matters included in its reserve for loss contingencies, we occasionally become involved in litigation arising from the normal course of business, and we are unable to determine the extent of any liability that may arise from any such unanticipated future litigation. We have no reason to believe that there is a reasonable possibility or a probability that we may incur a material loss, or a material loss in excess of a recorded accrual, with respect to any other such loss contingencies. However, the outcome of litigation is inherently uncertain and assessments and decisions on defense and settlement can change significantly in a short period of time. Therefore, although we consider the likelihood of such an outcome to be remote with respect to those matters for which we have not reserved an amount for loss contingencies, if one or more of these legal matters were resolved against our company in the same reporting period for amounts in excess of our expectations, our consolidated financial statements of a particular reporting period could be materially adversely affected.

#### ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## PART II

ITEM MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND  
5. ISSUER PURCHASES OF EQUITY SECURITIES

Our Class A Common Stock trades on the New York Stock Exchange under the symbol "SKX."

## HOLDERS

As of February 1, 2019, there were 88 holders of record of our Class A Common Stock (including holders who are nominees for an undetermined number of beneficial owners) and 36 holders of record of our Class B Common Stock. These figures do not include beneficial owners who hold shares in nominee name. The Class B Common Stock is not publicly traded, but each share is convertible upon request of the holder into one share of Class A Common Stock.

## DIVIDEND POLICY

## Share Repurchase Program

On February 6, 2018, the Company's Board of Directors authorized a share repurchase program (the "Share Repurchase Program"), pursuant to which the Company may, from time to time, purchase shares of its Class A common stock, par value \$0.001 per share ("Class A common stock"), for an aggregate repurchase price not to exceed \$150 million. The Share Repurchase Program expires on February 6, 2021. Share repurchases may be executed through various means, including, without limitation, open market transactions, privately negotiated transactions or pursuant to any trading plan that may be adopted in accordance with Rule 10b5-1 of the Securities and Exchange Act of 1934, as amended, subject to market conditions, applicable legal requirements and other relevant factors. The Share Repurchase Program does not obligate the Company to acquire any particular amount of shares of Class A common stock and the program may be suspended or discontinued at any time.

## ISSUER PURCHASES OF EQUITY SECURITIES

The table below summarizes the number of shares of our Class A Common Stock that were repurchased during the three months ended December 31, 2018.

Month Ended	Total Number of Shares Purchased (1) (2)	Average Price Paid Per Share	Total Number of Shares Purchased from Certain Employees (1)	Total Number of Shares Purchased under the Share Repurchase Program (2)	Maximum Dollar Value of Shares that May Yet Be Purchased under the Program
October 31, 2018	133,945	\$ 27.25	—	133,945	\$88,322,000
November 30, 2018	648,935	\$ 27.95	96,200	552,735	72,964,000
December 31, 2018	976,947	\$ 23.49	513	976,434	50,023,000
Total	1,759,827	\$ 25.42	96,713	1,663,114	\$50,023,000

- (1) The Company repurchased 96,713 shares from certain employees to facilitate income tax withholding payments pertaining to restricted stock awards that vested during the three months ended December 31, 2018. Such shares were not repurchased pursuant to a publicly announced plan or program.
- (2) As announced on February 6, 2018, the Board of Directors of the Company has approved a share repurchase program, authorizing the repurchase of up to an aggregate of \$150.0 million of the Company's Class A common stock. The program allows the Company to repurchase shares of Class A common stock from time to time for cash in the open market or privately negotiated transactions or other transactions, as market and business conditions warrant and subject to applicable legal requirements. The share repurchase program does not obligate the Company to repurchase any particular amount of common stock, and it could be modified, suspended or discontinued at any time.

#### EQUITY COMPENSATION PLAN INFORMATION

Our equity compensation plan information is provided as set forth in Part III, Item 12 of this annual report on Form 10-K.

## PERFORMANCE GRAPH

The following graph demonstrates the total return to stockholders of our company's Class A Common Stock from December 31, 2013 to December 31, 2018, relative to the performance of the Russell 2000 Index, which includes our Class A Common Stock, and the peer group index, which is believed to include companies engaged in businesses similar to ours. The peer group index consists of six companies: Nike, Inc., adidas AG, Steven Madden, Ltd., Wolverine World Wide, Inc., Crocs, Inc., and Deckers Outdoor Corporation.

The graph assumes an investment of \$100 on December 31, 2013 in each of our company's Class A Common Stock and the stocks comprising each of the Russell 2000 Index and the customized peer group index. Each of the indices assumes that all dividends were reinvested. The stock performance of our company's Class A Common Stock shown on the graph is not necessarily indicative of future performance. We will neither make nor endorse any predictions as to our future stock performance.

## COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURNS

(in dollars)	12/13	12/14	12/15	12/16	12/17	12/18
Skechers U.S.A., Inc.	100.00	166.77	273.56	222.58	342.65	207.27
Russell 2000	100.00	104.89	100.26	121.63	139.44	124.09
Peer Group	100.00	100.49	127.51	126.31	160.09	186.43



## ITEM 6. SELECTED FINANCIAL DATA

The following tables set forth our company's selected consolidated financial data as of and for each of the years in the five-year period ended December 31, 2018 and should be read in conjunction with our audited consolidated financial statements and notes thereto included under Part II, Item 8 of this annual report.

(In thousands, except net earnings per share)

Statement of Earnings Data:	Years Ended December 31,				
	2018	2017	2016	2015	2014
Net sales	\$4,642,068	\$4,164,160	\$3,563,311	\$3,147,323	\$2,377,561
Gross profit	2,223,605	1,938,889	1,634,596	1,424,008	1,071,905
Earnings from operations	437,765	382,880	370,518	350,824	209,071
Earnings before income taxes	431,884	384,260	359,484	333,497	191,380
Net earnings attributable to Skechers U.S.A., Inc.	301,041	179,190	243,493	231,912	138,811
Net earnings per share: <sup>(1)</sup>					
Basic	1.93	1.15	1.58	1.52	0.91
Diluted	1.92	1.14	1.57	1.50	0.91
Weighted average shares: <sup>(1)</sup>					
Basic	155,815	155,651	154,169	152,847	151,839
Diluted	156,450	156,523	155,084	154,200	153,079

Balance Sheet Data:	As of December 31,				
	2018	2017	2016	2015	2014
Working capital	\$1,621,918	\$1,507,676	\$1,206,036	\$971,179	\$779,277
Total assets	3,228,255	2,735,082	2,393,670	2,039,878	1,674,918
Long-term borrowings, excluding current installments	88,119	71,103	67,159	68,942	15,081
Skechers U.S.A., Inc. equity	2,034,958	1,829,064	1,603,633	1,327,556	1,075,249

<sup>(1)</sup>Basic earnings per share represents net earnings divided by the weighted-average number of common shares outstanding for the period. Diluted earnings per share, in addition to the weighted average determined for basic earnings per share, reflects the potential dilution that could occur if options to issue common stock were exercised or converted into common stock. All share and per share information has been retroactively adjusted for the three-for-one stock split that was effective on October 16, 2015.

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### GENERAL

We design, market and sell contemporary footwear for men, women and children under the Skechers brand. Our footwear is sold through a wide range of department stores and leading specialty retail stores, mid-tier retailers, boutiques, our own retail stores, distributor and licensee-owned international retail stores and our e-commerce websites. Our objective is to continue to profitably grow our domestic operations while leveraging our brand name to expand internationally.

Our operations are organized along our distribution channels, and we have the following three reportable sales segments: domestic wholesale sales, international wholesale sales, which include international direct subsidiary sales and international distributor sales, and retail sales, which includes our e-commerce sales. We evaluate segment performance based primarily on net sales and gross margins. See detailed segment information in Note 19 – Segment and Geographic Reporting in our Consolidated Financial Statements included under Part II, Item 8 of this annual report.

### FINANCIAL OVERVIEW

Our net sales for 2018 increased \$477.9 million, or 11.5%, to \$4.642 billion, compared to net sales of \$4.164 billion in 2017. The increase in net sales primarily came from our international subsidiaries and retail businesses. Our international wholesale and international retail businesses represented 54.2% of our net sales during 2018. The largest increases in our domestic wholesale segment came in our Work, BOBS, Men's U.S.A., Cali, and You divisions. During 2018, earnings from operations increased \$54.9 million, or 14.3%, to \$437.8 million compared to \$382.9 million in 2017. Net earnings attributable to Skechers U.S.A., Inc. were \$301.0 million for 2018, an increase of \$121.8 million, or 68.0%, compared to net earnings of \$179.2 million in 2017. Diluted earnings per share for 2018 were \$1.92, which reflected a 68.4% increase from the \$1.14 diluted earnings per share reported in the prior year. Our working capital was \$1.622 billion at December 31, 2018, which was an increase of \$114.2 million from working capital of \$1.508 billion at December 31, 2017. Our cash and cash equivalents increased \$135.8 million to \$872.2 million at December 31, 2018 from \$736.4 million at December 31, 2017. The increase in cash and cash equivalents was primarily the result of our increased net earnings and accounts payable which were partially offset by decreased accounts receivable, increased capital investments, increased investment and share repurchases.

### 2018 OVERVIEW

In 2018, we focused on product development, growing our position in our domestic wholesale accounts, growing our international market share, opening retail stores in key locations worldwide, continuing to develop our global infrastructure, and balance sheet and expense management.

**New product design and delivery.** In 2018, we focused on fresh updates to our core and existing styles—including Skechers GO Walk Joy, adding collaborations with accessible characters such as Garfield and Grumpy Cat as well as the more niche but still successful anime series One Piece, and broadening our reach to more trend-focused men and women through our heritage Skechers D'Lites collection.

**Grow our domestic business.** In 2018, our focus was on returning to growth domestically in our domestic wholesale accounts by delivering the right product to accounts at the right time, while finding new opportunities to add shelf space and expand into new locations with new Skechers categories. In 2018, we remained the number one walking, work, casual lifestyle, and casual dress footwear brand, and the number two casual athletic footwear brand.

Further develop our international businesses. During 2018, we continued to focus on improving our international sales by increasing our product offering to accounts around the world, delivering the right product to accounts at the right time, and increasing our shelf space with new and updated products as well as increasing our customer base.

Expand Skechers global retail base. Believing that Skechers retail stores are effective brand building tools, we continued to focus on opening Skechers stores around the world—both company-owned and third-party owned through our distributors, franchisees or joint venture partners. In 2018, we opened 25 additional company-owned domestic stores and 26 additional company-owned international stores. Additionally, we continued to expand our franchise retail base with more Skechers branded stores in countries where we directly handle the distribution of our product.

Develop our global infrastructure. In 2018, through our joint-venture in China we purchased land to construct our new China distribution center to support our sales in the region. We completed designing the building, tenant improvements and equipment for this facility and began construction in the fourth quarter of 2018.

Balance sheet and expense management. During 2018, we continued to focus on managing our balance sheet and bringing our marketing expenses and general and administrative expenses in line with expected sales. During 2018, we returned \$100.0 million to shareholders by repurchasing 3.7 million Class A shares.

## OUTLOOK FOR 2019

During 2019, we will continue to innovate our lifestyle and performance product lines by developing new styles and expanding into new categories. This includes building on our heritage collection and chunky footwear offering with Skechers D'Lites, Skechers D'Lites 3.0, Skechers Stamina, and Skechers Energy, among others. The global footwear market is competitive; however, we believe demand for the brand globally will remain strong because our products are marketed at affordable prices and our styles resonate with consumers worldwide. We believe appeal for our product is broad and demand will continue to grow due to a team of brand ambassadors—including sports icons Tony Romo, David Ortiz, Sugar Ray Leonard and Howie Long for men; pop superstar Camila Cabello for women; elite athlete Meb Keflezighi; and professional golfers Matt Kuchar and Brooke Henderson. We expect to continue to broaden the targeted demographic profile of our consumer base, increase our shelf space and to open another 70 to 80 company-owned retail locations worldwide. In addition, we will continue the construction of our new 1.62 million square foot distribution center in China to support our business in the region—with an expected completion date of 2020, and on the expansion of our corporate headquarters. In 2019, we entered into an agreement to purchase the minority interest in our India joint venture that we did not own for \$82.5 million which will make our India joint venture a wholly owned subsidiary. In 2019, we also agreed in principle to form a joint venture with our distributor in Mexico.

## DEFINITIONS

### Comparable sales

As part of our discussion of our results of operations, we disclose comparable store sales, for which we typically include the impact of e-commerce sales on our company-owned websites. With respect to any reporting period, we define comparable store sales as sales for stores that are owned and operated for at least thirteen full calendar months as of the last day of any calendar month within the current reporting period, and include only those sales for each of the comparable full calendar months that the store is open within each period. When a store closes at the end of a lease during a reporting period, we include in comparable store sales the sales for the number of comparable full calendar months that the store was open within the reporting period. We include new stores in comparable store sales commencing with the fourteenth month of operations because we believe it provides a more meaningful comparison of operating results of months with stabilized operations, and excludes a new store's first full calendar month of operations when operating results may not be representative for a variety of reasons.

Definitions and calculations of comparable store sales differ among companies in the retail industry, and therefore comparable store sales disclosed by us may not be comparable to the metrics disclosed by other companies.

### Cost of sales or Gross margins

Our cost of sales includes the cost of footwear purchased from our manufacturers, duties, quota costs, inbound freight (including ocean, air and freight from the dock to our distribution centers), broker fees and storage costs. Because we include expenses related to our distribution network in general and administrative expenses, while some of our competitors may include expenses of this type in cost of sales, our gross margins may not be comparable and we may report higher gross margins than some of our competitors in part for this reason.

### Selling expenses

Selling expenses consist primarily of the following: sales representative sample costs, sales commissions, trade shows, advertising and promotional costs, which may include television and ad production costs, and point-of-purchase costs.

#### General and administrative expenses

General and administrative expenses consist primarily of the following: salaries, wages and related taxes, various overhead costs associated with our corporate staff, stock-based compensation, domestic and international retail operations, non-selling related costs of our international operations, costs and expenses related to our distribution network for our Rancho Belago, European and other foreign distribution centers, professional fees related to both legal and accounting services, insurance, depreciation and amortization, asset impairment and legal settlements, among other expenses. Our distribution network-related costs are included in general and administrative expenses and are not allocated to specific segments.

YEAR ENDED DECEMBER 31, 2018 COMPARED TO THE YEAR ENDED DECEMBER 31, 2017

Net sales

Net sales for 2018 were \$4.642 billion, which was an increase of \$477.9 million, or 11.5%, compared to net sales of \$4.164 billion for 2017. The increase in net sales primarily came from our international wholesale and retail businesses.

Our domestic wholesale net sales increased \$10.3 million, or 0.8%, to \$1.260 billion for 2018 compared to \$1.250 billion for 2017. The increase in our domestic wholesale segment's net sales was primarily the result of a 3.0% unit sales volume increase, to 58.1 million pairs in 2018 from 56.5 million pairs in 2017, which was partially offset by a decrease in average selling price per pair of 3.8%, to \$21.26 per pair for 2018 from \$22.11 in 2017. This net sales increase was attributable to higher sales in our Work, BOBS, Men's U.S.A., Cali, and You divisions during 2018. The average selling price per pair decrease within the domestic wholesale segment was primarily the result of product sales mix.

Our international wholesale segment net sales increased \$324.9 million, or 18.8%, to \$2.055 billion for 2018 compared to sales of \$1.730 billion for 2017. Our international wholesale sales consist of direct sales by our foreign subsidiaries – those sales we make to department stores and specialty retailers – and sales to our distributors, who in turn sell to retailers in various international regions where we do not sell directly. Direct sales by our foreign subsidiaries, including our joint ventures, increased \$322.2 million, or 23.0%, to \$1.722 billion for 2018 compared to sales of \$1.399 billion for 2017. The largest sales increases during the year came from our subsidiaries in the United Kingdom, Germany and Spain, and our joint ventures in China, India and Singapore. The increases are primarily attributable to sales of our Men's and Women's Sport, YOU, BOBS, and Men's U.S.A., lines. Our distributor sales increased \$2.7 million, or 0.8%, to \$333.3 million for 2018, compared to sales of \$330.6 million for 2017. This was primarily attributable to increased sales to our distributors in Russia, Indonesia and Turkey.

Our retail segment sales increased \$142.7 million to \$1.328 billion for the year ended December 31, 2018, a 12.0% increase over sales of \$1.185 billion for 2017. The increase in retail sales was primarily attributable to increased comparable sales of 9.2%, which included increased sales within our Men's and Women's Sport, Men's U.S.A., Kid's, and Work divisions and a net increase of 25 domestic and 26 international stores compared to 2017. For the year ended December 31, 2018, our domestic retail sales, which includes e-commerce, increased 7.7% compared to 2017, which was primarily attributable to increased domestic store count and to positive comparable domestic store sales of 6.4%, and our international retail store sales increased 21.2% compared to 2017, which was attributable to increased international store count and positive comparable international store sales of 15.5%.

We believe that we have established our presence in most major domestic retail markets. We had 470 domestic stores and 222 international retail stores as of February 15, 2019, and we currently plan to open approximately 70 to 80 stores in 2019. During 2018, we opened one new domestic concept store, one domestic factory outlet store, 23 domestic warehouse outlet stores, 14 international concept stores, 11 international factory outlet stores, and one international warehouse outlet store. During 2018, we closed four domestic concept stores. We periodically review all of our stores for impairment. During 2018 and 2017, we did not record an impairment charge related to our retail stores.

Gross profit

Gross profit for 2018 increased \$284.6 million, or 14.7% to \$2.224 billion from \$1.939 billion for 2017. Gross profit, as a percentage of net sales, or gross margin, increased slightly to 47.9% in 2018 from 46.6% for 2017. Our domestic wholesale segment gross profit increased \$3.7 million, or 0.8%, to \$468.3 million for 2018 from \$464.6 million for

2017, which was attributable to an increase in pairs sold of 3.0%. Domestic wholesale gross margins were 37.2% for 2018 and 2017.

Gross profit for our international wholesale segment increased \$190.0 million, or 24.2%, to \$976.7 million for 2018 compared to \$786.7 million for 2017. Gross margins for the international wholesale segment were 47.5% for 2018 compared to 45.5% for 2017. Gross margins for our international direct subsidiary sales, including our joint ventures, were 51.7% for 2018 as compared to 50.0% for 2017. The increase in gross margins for our international wholesale segment and international direct subsidiary sales were primarily attributable to an increased mix of sales of products with higher gross margins. Gross margins for our international distributor sales were 25.9% for 2018 as compared to 26.3% for 2017.

Gross profit for our retail segment increased \$90.9 million, or 13.2%, to \$778.5 million for 2018 as compared to \$687.6 million for 2017. Gross margins for all stores were 58.6% for 2018 compared to 58.0% for 2017. Gross margins for our domestic stores were 61.3% for 2018 as compared to 59.7% for 2017. Gross margins for our international stores were 53.6% for 2018 as compared to 54.5% for 2017. The increase in our domestic retail margins were attributable to higher average selling prices and lower average product costs.

### Selling expenses

Selling expenses increased by \$23.2 million, or 7.1%, to \$350.4 million for 2018 from \$327.2 million for 2017. As a percentage of net sales, selling expenses were 7.5% and 7.9% for 2018 and 2017, respectively. The increase in selling expenses was primarily the result of higher advertising expense of \$17.6 million and increased sales commissions of \$3.9 million due to increased sales worldwide.

### General and administrative expenses

General and administrative expenses increased by \$211.0 million, or 16.9%, to \$1.456 billion for 2018 from \$1.245 billion for 2017. As a percentage of sales, general and administrative expenses were 31.4% and 29.9% for 2018 and 2017, respectively. The increase in general and administrative expenses was primarily attributable to \$99.9 million related to supporting our growing international operations in China, Japan, South Korea and Latin America, increased store operating costs of \$52.7 million primarily attributable to an additional net 47 stores and increased domestic wholesale general and administrative expenses of \$57.8 million primarily due to increased distribution costs of \$30.0 million. In addition, expenses related to our distribution network, including the functions of purchasing, receiving, inspecting, allocating, warehousing and packaging of our products were \$249.6 million for 2018 compared to \$219.6 million for 2017.

### Other income (expense)

Interest income was \$10.1 million for 2018 compared to \$2.4 million for 2017. The increase in interest income was primarily due to increased interest rates and higher average cash and investment balances as compared to the prior year. Interest expense for 2018 decreased \$0.9 million to \$5.8 million compared to \$6.7 million in 2017. Interest expense decreased primarily due to reduced interest paid to our foreign manufacturers. Loss on foreign currency transactions for 2018 was \$9.2 million compared to a \$6.3 million gain in 2017. This increased foreign currency exchange loss was primarily attributable to the impact of a stronger U.S. dollar on our intercompany balances in our foreign subsidiaries. Loss on disposal of assets for 2018 decreased \$0.1 million to a loss of \$0.5 million as compared to a loss of \$0.6 million in 2017.

### Income taxes

Our provision for income tax expense and our effective income tax rate are significantly impacted by the mix of our domestic and foreign earnings (loss) before income taxes. In the non-U.S. jurisdictions in which we have operations, the applicable statutory rates are generally significantly lower than in the U.S., ranging from 0% to 34.6%. Our provision for income tax expense was calculated using the applicable statutory income tax rate for each jurisdiction applied to our pre-tax earnings (loss) in each jurisdiction, while our effective tax rate is calculated by dividing income tax expense by earnings (loss) before income taxes.

Our earnings (loss) before income taxes and income tax expense for 2018, 2017 and 2016 are as follows (in thousands):

	Years Ended December 31,		
	2018	2017	2016
Income tax jurisdiction	Earnings (loss) before income tax expense	Earnings (loss) before income tax expense	Earnings (loss) before income tax expense



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	taxes	expense (benefit)	taxes		taxes		
United States <sup>(1)</sup>	\$ 16,597	\$ 11,500	\$ 25,628	\$ 113,607	\$ 105,589	\$ 44,654	
Peoples Republic of China (“China”)	89,429	19,595	95,668	12,971	72,584	11,720	
Hong Kong	48,352	8,106	17,778	5,030	15,156	5,206	
Jersey <sup>(2)</sup>	213,327	—	198,048	—	146,880	—	
Non-benefited loss operations <sup>(3)</sup>	(11,422 )	(3,387 )	(17,350 )	3,306	(16,189 )	12	
Other jurisdictions <sup>(4)</sup>	75,601	24,797	64,488	14,242	35,464	12,533	
Earnings before income taxes	\$ 431,884	\$ 60,611	\$ 384,260	\$ 149,156	\$ 359,484	\$ 74,125	
Effective tax rate <sup>(5)</sup>		14.0	%	38.8	%	20.6	%

<sup>(1)</sup>United States income tax expense for 2017 includes a provisional one-time \$99.9 million tax expense related to the enactment of the Tax Act on December 22, 2017.

<sup>(2)</sup>Jersey does not assess income tax on corporate net earnings.

<sup>(3)</sup>Consists of entities in the following tax jurisdictions where no tax benefit is recognized in the period being reported because of the provision of offsetting valuation allowances: Barbados, Brazil, China, India, Israel, Japan, Panama, Romania, Thailand, and South Korea.

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<sup>(4)</sup>Consists of entities in the following tax jurisdictions, each of which comprises not more than 5% of consolidated earnings (loss) before taxes in the period being reported: Albania, Austria, Belgium, Bosnia & Herzegovina, Canada, Chile, Colombia, Costa Rica, France, Germany, Hungary, India, Italy, Kosovo, Macau, Macedonia, Malaysia, Montenegro, Netherlands, Panama, Peru, Poland, Portugal, Serbia, Singapore, Spain, Switzerland, Vietnam, and the United Kingdom,

<sup>(5)</sup>The effective tax rate is calculated by dividing income tax expense by earnings before income taxes. For 2018, the effective tax rate was lower than the U.S. federal and state combined statutory rate of approximately 26%, primarily because of earnings from foreign operations in jurisdictions imposing either lower tax rates on corporate earnings or no corporate income tax. During 2018, as reflected in the table above, earnings (loss) before income taxes in the U.S. were \$16.6 million, with income tax expense of \$11.5 million, which is an average rate of 69.3%. This rate is higher than the 26% U.S. statutory rate primarily due to the impact of U.S. non-deductible expenses. Earnings (loss) before income taxes in non-U.S. jurisdictions were \$415.3 million, with an aggregate income tax expense of \$49.1 million, which is an average rate of 11.8%. Combined, this results in consolidated earnings before income taxes for the period of \$431.9 million, and consolidated income tax expense for the period of \$60.6 million, resulting in an effective tax rate of 14.0%. For 2018, of our \$415.3 million in earnings before income tax earned outside the U.S., \$213.3 million was earned in Jersey, which does not impose a tax on corporate earnings. In Jersey, earnings before income taxes increased by \$15.3 million to \$213.3 million in 2018 from \$198.0 million in 2017. This increase was primarily attributable to an increase in international sales which resulted in an increase in earnings before income taxes in Jersey from royalties and commissions under the terms of our inter-subsi-dary agreements. In addition, there were foreign losses of \$11.2 million for which no tax benefit was recognized during the year ended December 31, 2018, because of the provision of offsetting valuation allowances, but for which \$3.4 million in prior year tax refund were received. Individually, none of the other foreign jurisdictions included in "Other jurisdictions" in the table above had earnings greater than 5% of our consolidated earnings (loss) before taxes in any of the years shown.

As of December 31, 2018, we had approximately \$872.2 million in cash and cash equivalents, of which \$522.2 million, or 59.9%, was outside the U.S. Of the \$522.2 million held by our non-U.S. subsidiaries, approximately \$276.9 million is available for repatriation to the U.S. without incurring U.S. income taxes and applicable non-U.S. income and withholding taxes in excess of the amounts accrued in our consolidated financial statements as of December 31, 2018.

We believe our cash and cash equivalents and investments held in the U.S. and cash provided from operations are sufficient to meet our liquidity needs in the U.S. for the next twelve months, and we do not expect to repatriate any of the funds presently designated as indefinitely reinvested outside the U.S. However, in anticipation of the needs of our share repurchase program and the need to provide payment of our provisional Transition Tax liability, we plan to begin the repatriation of certain funds held outside the U.S. for which tax has been fully provided as of December 31, 2018. We have provided for the tax impact of expected distributions from our joint venture in China as well as from our subsidiary in Chile to our intermediate parent company in Switzerland. Otherwise, because of the need for cash for operating capital and continued overseas expansion, we do not foresee the need for any of our other foreign subsidiaries to distribute funds up to an intermediate foreign parent company in any form of taxable dividend. Under current applicable tax laws, if we chose to repatriate some or all of the funds we have designated as indefinitely reinvested outside the U.S., the amount repatriated would not be subject to U.S. income taxes but may be subject to applicable non-U.S. income and withholding taxes, and to certain state income taxes.

#### Non-controlling interest in net income and loss of consolidated subsidiaries

Net earnings attributable to non-controlling interest for 2018 increased \$14.3 million to \$70.2 million as compared to \$55.9 million for 2017 due to increased profitability of our joint ventures. Non-controlling interest represents the share of net earnings or loss that is attributable to our joint venture partners.

YEAR ENDED DECEMBER 31, 2017 COMPARED TO THE YEAR ENDED DECEMBER 31, 2016

Net sales

Net sales for 2017 were \$4.164 billion, which was an increase of \$600.9 million, or 16.9%, compared to net sales of \$3.563 billion for 2016. The increase in net sales was broad based across all our segments with the largest increases coming from our international businesses.

Our domestic wholesale net sales increased \$49.5 million, or 4.1%, to \$1.249 billion for 2017 compared to \$1.200 billion for 2016. The increase in our domestic wholesale segment's net sales was primarily the result of a 7.8% unit sales volume increase to 56.5 million pairs in 2017 from 52.4 million pairs in 2016, which was partially offset by a decrease in average selling price per pair of 3.4%, to \$22.11 per pair for 2017 from \$22.89 in 2016. This net sales increase was attributable to higher sales in our Men's Sport, Men's U.S.A., Cali, You, and Kid's divisions during 2017. The average selling price per pair decrease within the domestic wholesale segment was primarily the result of product sales mix with lower average selling prices.

Our international wholesale segment net sales increased \$338.7 million, or 24.3%, to \$1.730 billion for 2017 compared to sales of \$1.391 billion for 2016. Direct sales by our foreign subsidiaries, including our joint ventures, increased \$311.3 million, or 28.6%, to \$1.399 billion for 2017 compared to sales of \$1.088 billion for 2016. The largest sales increases during the year came from our subsidiaries in the United Kingdom, Germany and Spain, and our joint ventures in China and Korea. The increases are primarily attributable to sales of our Women's and Men's Go, Women's Active and Men's and Women's Sport lines. Our distributor sales increased \$27.4 million, or 9.0%, to \$330.6 million for 2017, compared to sales of \$303.2 million for 2016. This was primarily attributable to increased sales to our distributors in Australia and New Zealand, Indonesia, and Turkey.

Our retail segment sales increased \$212.8 million to \$1.185 billion for the year ended December 31, 2017, a 21.9% increase over sales of \$972.2 million for 2016. The increase in retail sales was primarily attributable to increased comparable sales of 7.2%, which included increased sales within our Men's and Women's Sport, Men's U.S.A., Kid's, and Work divisions and a net increase of 36 domestic and 39 international stores compared to 2016. For the year ended December 31, 2017, our domestic retail sales, which includes e-commerce, increased 11.9% compared to 2016, which was primarily attributable to increased domestic store count and to positive comparable domestic store sales of 6.4%, and our international retail store sales increased 50.3% compared to 2016, which was attributable to increased international store count and positive comparable international store sales of 10.1%.

During 2017, we opened five new domestic concept stores, seven domestic factory outlet stores, 29 domestic warehouse outlet stores, 19 international concept stores, 16 international factory outlet stores, and four international warehouse outlet stores. During 2017, we closed five domestic concept stores. We periodically review all of our stores for impairment. During 2017 and 2016, we did not record an impairment charge related to our retail stores.

#### Gross profit

Gross profit for 2017 increased \$304.3 million, or 18.6% to \$1.939 billion from \$1.635 billion for 2016. Gross profit, as a percentage of net sales, or gross margin, increased slightly to 46.6% in 2017 from 45.9% for 2016. Our domestic wholesale segment gross profit increased \$10.5 million, or 2.3%, to \$464.6 million for 2017 from \$454.1 million for 2016, which was attributable to an increase in pairs sold of 7.8%. Domestic wholesale margins decreased to 37.2% for 2017 from 37.8% for 2016. The decrease in domestic wholesale margins was primarily attributable to a product sales mix with lower average selling prices.

Gross profit for our international wholesale segment increased \$170.6 million, or 27.7%, to \$786.7 million for 2017 compared to \$616.1 million for 2016. Gross margins for the international wholesale segment were 45.5% for 2017 compared to 44.3% for 2016. Gross margins for our international direct subsidiary sales, including our joint ventures, were 50.0% for 2017 as compared to 49.3% for 2016. The increase in gross margins for our international wholesale segment and international direct subsidiary sales were primarily attributable to sales of products with higher average selling prices. Gross margins for our international distributor sales were 26.3% for 2017 as compared to 26.2% for 2016.

Gross profit for our retail segment increased \$123.2 million, or 21.8%, to \$687.6 million for 2017 as compared to \$564.4 million for 2016. Gross margins for all stores were 58.0% for 2017 compared to 58.1% for 2016. Gross margins for our domestic stores were 59.7% for 2017 as compared to 60.1% for 2016. Gross margins for our international stores were 54.5% for 2017 as compared to 52.3% for 2016. The decrease in our domestic retail margins were attributable to a product sales mix with lower average selling prices.

#### Selling expenses

Selling expenses increased by \$70.1 million, or 27.3%, to \$327.2 million for 2017 from \$257.1 million for 2016. As a percentage of net sales, selling expenses were 7.9% and 7.2% for 2017 and 2016, respectively. The increase in selling expenses was primarily the result of increased sales commissions of \$22.7 million due to increased sales worldwide and \$13.2 million from our South Korean joint venture and \$47.3 million in higher advertising expenses, which slightly increased as a percentage of net sales to 5.8% in 2017 from 5.5% in 2016.

#### General and administrative expenses

General and administrative expenses increased by \$224.7 million, or 22.0%, to \$1.245 billion for 2017 from \$1.021 billion for 2016. As a percentage of sales, general and administrative expenses were 29.9% and 28.6% for 2017 and 2016, respectively. The increase in general and administrative expenses was primarily attributable to \$109.5 million related to supporting our growing international operations in China, Japan, South Korea and Latin America, increased store operating costs of \$73.8 million primarily attributable to an additional 75 stores and increased domestic wholesale general and administrative expenses of \$41.4 million primarily due to increased headcount in the United States to support our brand worldwide. In addition, expenses related to our distribution network, including the functions of purchasing, receiving, inspecting, allocating, warehousing and packaging of our products increased \$32.3 million, due to increased shipments, to \$219.6 million from \$187.3 million for 2017 and 2016, respectively.

Other income (expense)

Interest income was \$2.4 million for 2017 compared to \$1.2 million for 2016. Interest expense for 2017 increased \$0.4 million to \$6.7 million compared to \$6.3 million in 2016. Gain or loss on foreign currency transactions for 2017 increased \$11.3 million to a gain of \$6.3 million compared to a \$5.0 million loss in 2016. This increased foreign currency exchange gain was primarily attributable to the impact of a weaker U.S. dollar on our intercompany balances in our foreign subsidiaries. Loss on disposal of assets for 2017 decreased \$0.5 million to a loss of \$0.6 million as compared to a loss of \$1.1 million in 2016.

Income taxes

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act makes broad and complex changes to the U.S. tax code that affected our financial results for the year ended December 31, 2017, including, but not limited to: (1) requiring a one-time Transition Tax, payable over eight years, on certain unrepatriated earnings of foreign subsidiaries; (2) a future reduction of the U.S. federal corporate tax rate from 35% to 21% that affects the current value of our deferred tax assets ("DTAs") and deferred tax liabilities ("DTLs"); and (3) bonus depreciation that allows for full expensing of qualified property placed in service after September 27, 2017. In addition, the Tax Act establishes new tax laws that will affect our financial results for the year ending December 31, 2018, including, but not limited to: (1) a reduction of the U.S. federal corporate tax rate from 35% to 21%; (2) a general elimination of U.S. federal income taxes on dividends from foreign subsidiaries; (3) a new provision designed to tax global intangible low-taxed income ("GILTI"); (4) limitations on the deductibility of certain executive compensation; and (5) limitations on the use of Foreign Tax Credit ("FTC's") to reduce the U.S. income tax liability.

The SEC staff issued SAB 118, which provides guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for us to complete the accounting under Accounting Standards Codification 740 ("ASC 740"). In accordance with SAB 118, we must reflect the income tax effects of those aspects of the Act for which the accounting under ASC 740 is complete. To the extent that our accounting for certain income tax effects of the Tax Act is incomplete but we are able to determine a reasonable estimate, we must record a provisional estimate in the financial statements. If we cannot determine a provisional estimate to be included in the financial statements, we should continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the enactment of the Tax Act.

In connection with our initial analysis of the impact of the Tax Act, we have recorded a provisional one-time net tax expense of \$99.9 million for the year-ended December 31, 2017. This net tax expense primarily consists of the \$1.9 million net tax impact to our DTA's from the corporate rate reduction and a net expense for the Transition Tax of \$98.0 million. For various reasons that are discussed more fully below, we did not completed our accounting for the income tax effects of certain elements of the Tax Act. If we were able to make reasonable estimates of the effects of elements for which our analysis was not yet complete, we recorded provisional adjustments.

Our accounting for the following elements of the Tax Act was provisional. However, we were able to make reasonable estimates of certain effects and, therefore, recorded the following provisional adjustments:

**Transition Tax:** The Transition Tax is a one-time tax on previously untaxed current and accumulated earnings and profits (“E&P”) of certain of our foreign subsidiaries. To determine the amount of the Transition Tax, we must determine, in addition to other factors, the amount of post-1986 E&P of the relevant subsidiaries, as well as the amount of non-U.S. income taxes paid on such earnings. We were able to make a reasonable estimate of the Transition Tax and recorded a provisional Transition Tax liability of \$98.0 million at December 31, 2017. However, during the measurement period, we continued to gather additional information to more precisely compute the amount of the Transition Tax. As a result of the additional information gathered, we reduced the provisional estimate from \$98.0 million to \$87.1 million and recorded a \$10.9 million adjustment to reduce the tax provision for the year ended December 31, 2018.

**Reduction of U.S. federal corporate tax rate:** The Tax Act reduces the corporate tax rate from 35% to 21%, effective January 1, 2018. As a result, we have recorded a provisional decrease in value of our net DTAs of \$1.9 million, with a corresponding net adjustment to deferred income tax expense of \$1.9 million for the year ended December 31, 2017. No additional adjustment to this provisional estimate of the impact of the Tax Act on our net DTA’s was necessary, and no related adjustment was recorded in the tax provision for the year ended December 31, 2018.

**Cost recovery:** We completed provisional computations for expenditures that qualified for immediate expensing and recorded a decrease in our current income tax payable of approximately \$5.9 million based on our estimates related to the additional federal expense allowed as a result of the Tax Act. In addition, we have recorded a corresponding increase in our DTLs of approximately \$3.5 million, which is less than the \$5.9 million liability amount due to the reduction in the corporate tax rate from 35% to 21%, effective January 1, 2018. The \$2.4 million net benefit from the reduction in the future tax rate is included in the \$1.9 million decrease in value of the net DTAs discussed above. No additional adjustment to this provisional estimate of the impact of the Tax Act on our cost recovery was necessary, and no related adjustment was recorded in the tax provision for the year ended December 31, 2018.

Our provision for income tax expense and our effective income tax rate are significantly impacted by the mix of our domestic and foreign earnings (loss) before income taxes. In the non-U.S. jurisdictions in which we have operations, the applicable statutory rates are generally significantly lower than in the U.S., ranging from 0% to 34%. Our provision for income tax expense was calculated using the applicable statutory income tax rate for each jurisdiction applied to our pre-tax earnings (loss) in each jurisdiction, while our effective tax rate is calculated by dividing income tax expense by earnings (loss) before income taxes.

Our earnings (loss) before income taxes and income tax expense for 2017, 2016 and 2015 are as follows (in thousands):

	Years Ended December 31,					
	2017		2016		2015	
	Earnings (loss)		Earnings (loss)		Earnings (loss)	
	before income tax		before income tax		before income tax	
Income tax jurisdiction	taxes	expense	taxes	expense	taxes	expense
United States <sup>(1)</sup>	\$25,628	\$ 113,607	\$105,589	\$ 44,654	\$136,726	\$ 52,173
Peoples Republic of China (“China”)	95,668	12,971	72,584	11,720	49,027	11,084
Jersey <sup>(2)</sup>	198,048	—	146,880	—	123,721	—
Non-benefited loss operations <sup>(3)</sup>	(17,350 )	3,306	(16,189 )	12	(16,719 )	164
Other jurisdictions <sup>(4)</sup>	82,266	19,272	50,620	17,739	40,742	9,029
Earnings before income taxes	\$384,260	\$ 149,156	\$359,484	\$ 74,125	\$333,497	\$ 72,450
Effective tax rate <sup>(5)</sup>		38.8 %		20.6 %		21.7 %

<sup>(1)</sup>United States income tax expense for 2017 includes a provisional one-time \$99.9 million tax expense related to the enactment of the Tax Act on December 22, 2017.

<sup>(2)</sup>Jersey does not assess income tax on corporate net earnings.

<sup>(3)</sup>Consists of entities in the following tax jurisdictions where no tax benefit is recognized in the period being reported because of the provision of offsetting valuation allowances: Brazil, India, Israel, Japan, Macau, Panama, and South Korea.

<sup>(4)</sup>Consists of entities in the following tax jurisdictions, each of which comprises not more than 5% of consolidated earnings (loss) before taxes in the period being reported: Albania, Austria, Belgium, Bosnia & Herzegovina, Canada, Chile, Colombia, Costa Rica, France, Germany, Hong Kong, Hungary, India, Italy, Kosovo, Macedonia, Malaysia, Montenegro, Netherlands, Panama, Peru, Poland, Portugal, Romania, Serbia, Singapore, Spain, Switzerland, Thailand, Vietnam, and the United Kingdom.

<sup>(5)</sup>The effective tax rate is calculated by dividing income tax expense by earnings before income taxes.

For 2017, the effective tax rate was lower than the U.S. federal and state combined statutory rate of approximately 39%, primarily because of earnings from foreign operations in jurisdictions imposing either lower tax rates on corporate earnings or no corporate income tax. During 2017, as reflected in the table above, earnings (loss) before income taxes in the U.S. were \$25.6 million, with income tax expense of \$113.6 million, which is an average rate of 443%. The U.S. tax expense includes a provisional one-time tax expense of \$99.9 million related to the enactment of the Tax Act on December 22, 2017. Earnings (loss) before income taxes in non-U.S. jurisdictions were \$358.6 million, with an aggregate income tax expense of \$35.5 million, which is an average rate of 9.9%. Combined, this results in consolidated earnings before income taxes for the period of \$384.3 million, and consolidated income tax expense for the period of \$149.2 million, resulting in an effective tax rate of 38.8%. For 2017, of our \$358.6 million in



earnings before income tax earned outside the U.S., \$198.0 million was earned in Jersey, which does not impose a tax on corporate earnings. In Jersey, earnings before income taxes increased by \$51.1 million, or 35%, to \$198.0 million in 2017 from \$146.9 million in 2016. This increase was primarily attributable to an increase of \$435.6 million in net sales in the “Other international” geographic area for 2017 (see Note 18 – Segment and Geographic Reporting in our consolidated financial statements included under Part II, Item 8 of this annual report), which resulted in a significant increase in earnings before income taxes in Jersey from royalties and commissions under the terms of inter-subsidiary agreements. Due to the scalability of our operations, increases in net sales in the “Other international” geographic area from 2016 to 2017 resulted in a disproportionately greater increase in earnings before income taxes in Jersey. In addition, there were foreign losses of \$17.4 million for which no tax benefit was recognized during the year ended December 31, 2017 because of the provision of offsetting valuation allowances, but in which \$3.3 million in nonrefundable and other withholding taxes were paid. Individually, none of the other foreign jurisdictions included in “Other jurisdictions” in the table above had earnings greater than 5% of our consolidated earnings (loss) before taxes in any of the years shown.

As of December 31, 2017, we had approximately \$736.4 million in cash and cash equivalents, of which \$391.6 million, or 53.2%, was held outside the U.S. Of the \$391.6 million held by our non-U.S. subsidiaries, approximately \$227.5 million is available for repatriation to the U.S. without incurring U.S. income taxes and applicable non-U.S. income and withholding taxes in excess of the amounts accrued in our consolidated financial statements as of December 31, 2017. As of December 31, 2017, U.S. income taxes have been provided but non-U.S. income taxes have not been provided on cumulative total earnings of \$178.8 million. As of December 31, 2016, U.S. and non-U.S. income taxes have not been provided on cumulative total earnings of \$699.6 million.

#### Non-controlling interest in net income and loss of consolidated subsidiaries

Net earnings attributable to non-controlling interest for 2017 increased \$14.0 million to \$55.9 million as compared to \$41.9 million for 2016 due to increased profitability of our joint ventures. Non-controlling interest represents the share of net earnings or loss that is attributable to our joint venture partners.

### LIQUIDITY AND CAPITAL RESOURCES

#### Cash Flows

Our working capital at December 31, 2018 was \$1.622 billion, an increase of \$114.2 million from working capital of \$1.508 billion at December 31, 2017. Our cash and cash equivalents at December 31, 2018 was \$872.2 million, compared to \$736.4 million at December 31, 2017. This increase in cash and cash equivalents of \$135.8 million, after consideration of the effect of exchange rates, was the result of our net earnings of \$371.3 million, and increased accrued expenses and other long-term liabilities of \$19.7 million, which was partially offset by increased receivables of \$136.2 million, capital expenditures of \$143.0 million and share repurchases of \$100.0 million. Our primary sources of operating cash are collections from customers on wholesale and retail sales. Our primary uses of cash are inventory purchases, selling, general and administrative expenses and capital expenditures.

#### Operating Activities

Net cash provided by operating activities was \$568.6 million for 2018 and \$159.3 million for 2017. On a comparative year to year basis, the \$409.3 million increase in cash flows from operating activities in 2018 primarily resulted from \$187.1 million increase in accounts payable, a smaller increase in inventories of \$151.4 million, which were partially offset by a larger increase in accounts receivable of \$34.0 million and a smaller increase in accrued expenses and other long-term liabilities of \$66.4 million.

#### Investing Activities

Net cash used in investing activities was \$319.4 million for 2018, as compared to \$138.3 million in 2017. The increase in cash used in investing activities in 2018 as compared to 2017 was due to a net increase in investment purchases of \$176.4 million and increased capital expenditures of \$7.1 million. Capital expenditures for 2018 were approximately \$143.0 million, which primarily consisted of \$50.0 million for new store openings and remodels, \$28.8 million for the construction for our China distribution center, \$20.6 million to support our international wholesale operations, \$17.6 million for the upgrades to our domestic distribution center, and \$10.5 million for new retail locations in our China joint venture. This compares to capital expenditures of \$136.0 million in the prior year, which primarily consisted of \$68.5 million for new store openings and remodels, \$19.9 million for land for our China distribution center, \$15.4 million to support our international wholesale operations and \$12.0 million for new retail locations in our China joint venture. We expect capital expenditures for 2019 to be between \$275.0 million and \$300.0 million, which includes the construction of our China distribution center, upgrades for our domestic and European distribution centers, opening 70 to 80 retail stores, store remodels, corporate office and information technology upgrades. We believe our current cash, investments, operating cash flows, available lines of credit and current financing arrangements should be adequate to fund these capital expenditures, although we may seek additional funding for all or a portion of these expenditures.

#### Financing Activities

Net cash used in financing activities was \$119.7 million during 2018, compared \$14.5 million during 2017. The increase in cash used by financing activities was primarily attributable to repurchases of our Class A common stock of \$100.0 million and increased payments for taxes related to net share settlement of equity awards of \$14.2 million.

## Capital Resources and Prospective Capital Requirements

### Share Repurchase Program

On February 6, 2018, the Company's Board of Directors authorized a share repurchase program (the "Share Repurchase Program"), pursuant to which the Company may, from time to time, purchase shares of its Class A common stock, par value \$0.001 per share ("Class A common stock"), for an aggregate repurchase price not to exceed \$150.0 million. The Share Repurchase Program expires on February 6, 2021. Share repurchases may be executed through various means, including, without limitation, open market transactions, privately negotiated transactions or pursuant to any trading plan that may be adopted in accordance with Rule 10b5-1 of the Securities and Exchange Act of 1934, as amended, subject to market conditions, applicable legal requirements and other relevant factors. The Share Repurchase Program does not obligate the Company to acquire any particular amount of shares of Class A common stock and the program may be suspended or discontinued at any time. As of December 31, 2018, there was \$50.0 million available under the Share Repurchase Program.

## Acquisitions

In 2019, we entered into an agreement to purchase the minority interest in our India joint venture that we did not own for \$82.5 million which will make our India joint venture a wholly owned subsidiary. Also, in 2019, we agreed in principle to form a joint venture with our distributor in Mexico.

## Financing Arrangements

On October 24, 2018, through our Chinese joint venture, we entered into a \$17.5 million loan agreement with The Hongkong and Shanghai Banking Corporation Limited (the “China Loan Agreement”). The China Loan Agreement allows for partial drawdown. Interest will be paid at one, two or three months, depending on the period of the drawdown. The interest rate will be based upon the London Interbank Offered Rate (“LIBOR”) plus 1.2% per annum. As specified in the China Loan Agreement, the principal of the loan will be repayable by fifteen equal quarterly installments of \$437,550, commencing fifteen months after drawdown plus a final installment of \$10,937,500. The loan has a term of 5 years. The China Loan Agreement contains customary affirmative and negative covenants for secured credit facilities of this type. The obligations of our Chinese joint venture under the China Loan Agreement are jointly and severally guaranteed by the Company and Luen Thai Enterprises Ltd. There was no amount outstanding as of December 31, 2018.

On October 19, 2018, through a subsidiary of our Chinese joint venture (“the TC Subsidiary”), we entered into a 50 million yuan revolving loan agreement with China Construction Bank Corporation (“the China DC Revolving Loan Agreement”). The proceeds from the China DC Revolving Loan Agreement will be used to finance the construction and operation of our distribution center in China. Interest will be paid quarterly. The interest rate will be based upon the prime rate from the People’s Bank of China less a discount. As specified in the China DC Revolving Loan Agreement, the entire principal balance of the loan will be repaid when the China DC Revolving Loan Agreement matures on October 18, 2019. The TC Subsidiary has the option to extend the China DC Revolving Agreement, conditioned upon the satisfaction of certain terms. The China DC Revolving Loan Agreement contains customary affirmative and negative covenants for secured credit facilities of this type, including covenants that will limit the ability of the TC Subsidiary, to among other things, allow external investment to be added, pledge assets, issue debt with priority over the China DC Revolving Loan Agreement, and adjust the capital stock structure of the TC Subsidiary. The obligations of the TC Subsidiary under the China DC Revolving Loan Agreement are jointly and severally guaranteed by our Chinese joint venture. There is no amount outstanding as of December 31, 2018.

On September 29, 2018, through the TC subsidiary, we entered into a 700 million yuan loan agreement with China Construction Bank Corporation (“the China DC Loan Agreement”). The proceeds from the China DC Loan Agreement will be used to finance the construction of our distribution center in China. Interest will be paid quarterly. The interest rate will float and be calculated at a reference rate provided by the People’s Bank of China. The interest rate at December 31, 2018 was 4.28% and may increase or decrease over the life of the loan, and will be evaluated every 12 months. The principal of the loan will be repaid in semi-annual installments, beginning in 2021, of variable amounts as specified in the China DC Loan Agreement. The China DC Loan Agreement contains customary affirmative and negative covenants for secured credit facilities of this type, including covenants that limit the ability of the joint venture to, among other things, allow external investment to be added, pledge assets, issue debt with priority over the China DC Loan Agreement, and adjust the capital stock structure of the TC Subsidiary. The China DC Loan Agreement matures on September 28, 2023. The obligations of the TC Subsidiary under the China DC Loan Agreement are jointly and severally guaranteed by our Chinese joint venture. As of December 31, 2018 there was \$18.6 million outstanding under this credit facility, which is classified as long-term borrowings in our consolidated balance sheets.

On September 20, 2018, through two subsidiaries of our Chinese joint venture (the “SGZ and SSH Subsidiaries”), we entered into a 125 million yuan revolving loan agreement with HSBC Bank (China) Company Limited, Guangzhou Branch (the “Revolving Loan Agreement”). The Revolving Loan Agreement is comprised of two tranches: a 125 million yuan revolving loan facility and a 15 million yuan non-financial bank guarantee facility. The proceeds from the Revolving Loan Agreement will be used to finance the SGZ and SSH Subsidiaries’ working capital requirements. Interest will be paid at one, two or three months, depending on the term of each loan. The interest rate will be equal to 100% of the applicable People’s Bank of China (PBOC) Benchmark Lending Rate, provided that if the PBOC Benchmark Lending Rate changes during the term of a loan, the applicable interest rate for that loan will not change until the next rollover date of that loan (if any). The Revolving Loan Agreement contains customary affirmative and negative covenants for secured credit facilities of this type, including covenants that limit the ability of the joint venture to, among other things, allow external investment to be added, pledge assets and issue debt with priority over the Revolving Loan Agreement. The term of each loan will be one, three or six months or such other period as agreed by the lender. The term of a loan, including any extension or rollover, shall not exceed twelve months. The obligations of the Subsidiary under the Revolving Loan Agreement are guaranteed by the Company, Luen Thai Enterprises Ltd., Skechers Guangzhou Co., Ltd and Skechers Trading (Shanghai) Co Ltd. There was no amount outstanding as of December 31, 2018.

On June 30, 2015, we entered into a \$250.0 million loan and security agreement, subject to increase by up to \$100.0 million, (the "Credit Agreement"), with the following lenders: Bank of America, N.A., MUFG Union Bank, N.A. and HSBC Bank USA, National Association. The Credit Agreement matures on June 30, 2020. The Credit Agreement replaces the credit agreement dated June 30, 2009, which expired on June 30, 2015. The Credit Agreement permits us and certain of our subsidiaries to borrow based on a percentage of eligible accounts receivable plus the sum of (a) the lesser of (i) a percentage of eligible inventory to be sold at wholesale and (ii) a percentage of net orderly liquidation value of eligible inventory to be sold at wholesale, plus (b) the lesser of (i) a percentage of the value of eligible inventory to be sold at retail and (ii) a percentage of net orderly liquidation value of eligible inventory to be sold at retail, plus (c) the lesser of (i) a percentage of the value of eligible in-transit inventory and (ii) a percentage of the net orderly liquidation value of eligible in-transit inventory. Borrowings bear interest at our election based on (a) LIBOR or (b) the greater of (i) the Prime Rate, (ii) the Federal Funds Rate plus 0.5% and (iii) LIBOR for a 30-day period plus 1.0%, in each case, plus an applicable margin based on the average daily principal balance of revolving loans available under the Credit Agreement. We pay a monthly unused line of credit fee of 0.25%, payable on the first day of each month in arrears, which is based on the average daily principal balance of outstanding revolving loans and undrawn amounts of letters of credit outstanding during such month. The Credit Agreement further provides for a limit on the issuance of letters of credit to a maximum of \$100.0 million. The Credit Agreement contains customary affirmative and negative covenants for secured credit facilities of this type, including covenants that will limit the ability of the Company and its subsidiaries to, among other things, incur debt, grant liens, make certain acquisitions, dispose assets, effect a change of control of the Company, make certain restricted payments including certain dividends and stock redemptions, make certain investments or loans, enter into certain transactions with affiliates and certain prohibited uses of proceeds. The Credit Agreement also requires compliance with a minimum fixed-charge coverage ratio if Availability drops below 10% of the Revolver Commitments (as such terms are defined in the Credit Agreement) until the date when no event of default has existed and Availability has been over 10% for 30 consecutive days. We paid closing and arrangement fees of \$1.1 million on this facility, which are being amortized to interest expense over the five-year life of the facility. As of December 31, 2018, there was \$0.1 million outstanding under this credit facility, which is classified as short-term borrowings in our consolidated balance sheets.

On April 30, 2010, the JV, through HF Logistics-SKX T1, LLC, a Delaware limited liability company and a wholly-owned subsidiary of the JV ("HF-T1"), entered into a construction loan agreement with Bank of America, N.A. as administrative agent and as a lender, and Raymond James Bank, FSB, as a lender (collectively, the "Construction Loan Agreement"), pursuant to which the JV obtained a loan of up to \$55.0 million used for construction of the Project on the Property (the "Original Loan"). On November 16, 2012, HF-T1 executed a modification to the Construction Loan Agreement (the "Modification"), which added OneWest Bank, FSB as a lender, increased the borrowings under the Original Loan to \$80.0 million and extended the maturity date of the Original Loan to October 30, 2015. On August 11, 2015, the JV through HF-T1 entered into an amended and restated loan agreement with Bank of America, N.A., as administrative agent and as a lender, and CIT Bank, N.A. (formerly known as OneWest Bank, FSB) and Raymond James Bank, N.A., as lenders (collectively, the "Amended Loan Agreement"), which amends and restates in its entirety the Construction Loan Agreement and the Modification.

As of the date of the Amended Loan Agreement, the outstanding principal balance of the Original Loan was \$77.3 million. In connection with this refinancing of the Original Loan, the JV, the Company and HF agreed that we would make an additional capital contribution of \$38.7 million to the JV for the JV through HF-T1 to use to make a payment on the Original Loan. The payment equaled our 50% share of the outstanding principal balance of the Original Loan. Under the Amended Loan Agreement, the parties agreed that the lenders would loan \$70.0 million to HF-T1 (the "New Loan"). The New Loan is being used by the JV through HF-T1 to (i) refinance all amounts owed on the Original Loan after taking into account the payment described above, (ii) pay \$0.9 million in accrued interest, loan fees and other closing costs associated with the New Loan and (iii) make a distribution of \$31.3 million less the amounts described in clause (ii) to HF. Pursuant to the Amended Loan Agreement, the interest rate on the New Loan is the LIBOR Daily Floating Rate (as defined in the Amended Loan Agreement) plus a margin of 2%. The maturity

date of the New Loan is August 12, 2020, which HF-T1 has one option to extend by an additional 24 months, or until August 12, 2022, upon payment of a fee and satisfaction of certain customary conditions. On August 11, 2015, HF-T1 and Bank of America, N.A. entered into an ISDA master agreement (together with the schedule related thereto, the "Swap Agreement") to govern derivative and/or hedging transactions that HF-T1 concurrently entered into with Bank of America, N.A. Pursuant to the Swap Agreement, on August 14, 2015, HF-T1 entered into a confirmation of swap transactions (the "Interest Rate Swap") with Bank of America, N.A. The Interest Rate Swap has an effective date of August 12, 2015 and a maturity date of August 12, 2022, subject to early termination at the option of HF-T1, commencing on August 1, 2020. The Interest Rate Swap fixes the effective interest rate on the New Loan at 4.08% per annum. Pursuant to the terms of the JV, HF Logistics is responsible for the related interest expense on the New Loan, and any amounts related to the Swap Agreement. The full amount of interest expense related to the New Loan has been included in our consolidated statements of equity within non-controlling interests. The Amended Loan Agreement and the Swap Agreement are subject to customary covenants and events of default. Bank of America, N.A. also acts as a lender and syndication agent under our credit agreement dated June 30, 2015. We had \$65.1 million outstanding under the Amended Loan Agreement, which is included in long-term borrowings as of December 31, 2018.

As of December 31, 2018, outstanding short-term and long-term borrowings were \$97.0 million, of which \$65.4 million relates to loans for our domestic distribution center and the remaining relates to our international operations. Our long-term debt obligations contain both financial and non-financial covenants, including cross-default provisions. We were in compliance with all debt covenants related to our short-term and long-term borrowings as of the date of this annual report.

We believe that anticipated cash flows from operations, available borrowings under our credit agreement, existing cash and investments balances and current financing arrangements will be sufficient to provide us with the liquidity necessary to fund our anticipated working capital and capital requirements at least through March 31, 2020. Our future capital requirements will depend on many factors, including, but not limited to, the global economy and the outlook for and pace of sustainable growth in our markets, the levels at which we maintain inventory, sale of excess inventory at discounted prices, the market acceptance of our footwear, the number and timing of new store openings, the success of our international operations, costs associated with constructing our China distribution center and distribution center equipment, the costs of upgrading our domestic and European distribution centers, the amount and timing of share repurchases, the levels of advertising and marketing required to promote our footwear, the extent to which we invest in new product design and improvements to our existing product design, costs associated with constructing new corporate offices, and any potential acquisitions of other brands or companies. To the extent that available funds are insufficient to fund our future activities, we may need to raise additional funds through public or private financing of debt or equity. We have been successful in the past in raising additional funds through financing activities; however, we cannot be assured that additional financing will be available to us or that, if available, it can be obtained on past terms which have been favorable to our stockholders and us. Failure to obtain such financing could delay or prevent our current business plans, which could adversely affect our business, financial condition and results of operations. In addition, if additional capital is raised through the sale of additional equity or convertible securities, dilution to our stockholders could occur.

#### Disclosure about Contractual Obligations and Commercial Commitments

The following table summarizes our material contractual obligations and commercial commitments as of December 31, 2018 (In thousands):

	Total	Less than One Year	One to Three Years	Three to Five Years	More Than Five Years
Short-term borrowings	\$7,222	\$7,222	\$—	\$—	\$—
Long-term borrowings <sup>(1)</sup>	96,364	5,097	87,707	3,560	—
Operating lease obligations <sup>(2)</sup>	1,641,384	251,711	432,695	360,077	596,901
Purchase obligations <sup>(3)</sup>	1,071,537	1,071,537	—	—	—
Warehouse and equipment <sup>(4)</sup>	220,200	159,800	60,400	—	—
Corporate construction contracts <sup>(5)</sup>	134,500	61,700	72,800	—	—
Minimum payments related to other arrangements	51,777	18,921	32,856	—	—
Total <sup>(6)</sup>	\$3,222,984	\$1,575,988	\$686,458	\$363,637	\$596,901

<sup>(1)</sup> Amounts include anticipated interest payments based on interest rates currently in effect.

<sup>(2)</sup>



Operating lease obligations consists primarily of real property leases for our retail stores, corporate offices, European and other international distribution centers. These leases frequently include options that permit us to extend beyond the terms of the initial fixed term. We currently expect to fund these commitments with cash flows from operations and existing cash and investment balances.

- (3) Purchase obligations include the following: (i) accounts payable balances for the purchase of footwear of \$180.5 million, (ii) outstanding letters of credit of \$3.2 million and (iii) open purchase commitments with our foreign manufacturers for \$887.9 million. We currently expect to fund these commitments with cash flows from operations and existing cash and investment balances.
- (4) Amounts include warehouse and equipment upgrades for our China, Rancho Belago, and European distribution centers.
- (5) During 2018, we entered into construction agreements with McCarthy Construction Company for the construction of additional corporate facilities in Manhattan Beach, California.
- (6) Our consolidated balance sheet, as of December 31, 2018, included \$8.0 million in unrecognized tax benefits. Future payments related to these unrecognized tax benefits have not been presented in the table above, due to the uncertainty of the amounts, the potential timing of cash settlements with the tax authorities, and uncertainty whether any settlement would occur. In addition, the table above does not include payments of \$79.8 million over the next seven years related to the provisional one-time tax liability recorded due to the Tax Act.

## OFF-BALANCE SHEET ARRANGEMENTS

We do not have any relationships with unconsolidated entities or financial partnerships such as entities often referred to as structured finance or special purpose entities that would have been established for the purpose of facilitating off-balance-sheet arrangements or for other contractually narrow or limited purposes. As such, we are not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

## CRITICAL ACCOUNTING POLICIES AND USE OF ESTIMATES

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, sales and expenses, and related disclosure of contingent assets and liabilities. We base our estimates and judgments on historical experience, other available information, and on other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for judgments about the carrying values of assets and liabilities. In determining whether an estimate is critical, we consider whether the nature of the estimates or assumptions is material due to the levels of subjectivity and judgment or the susceptibility of such matters to change, and whether the impact of the estimates and assumptions have a material impact on our financial condition or operating performance. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting estimates are affected by significant judgments used in the preparation of our consolidated financial statements: revenue recognition, allowance for bad debts, returns, sales allowances and customer chargebacks, inventory write-downs, valuation of intangibles and long-lived assets, litigation reserves, and tax estimates and valuation of deferred income taxes.

**Revenue Recognition.** We derive income from the sale of footwear and royalties earned from licensing the Skechers brand. We recognize revenue when control of the promised goods or services is transferred to its customers in an amount that reflects the consideration we expect to be entitled to in exchange for those goods or services. For North America, goods are shipped Free on Board ("FOB") shipping point directly from our domestic distribution center in Rancho Belago, California. For international wholesale customers product is shipped FOB shipping point, (i) direct from our distribution center in Liege, Belgium, (ii) to third-party distribution centers in Central America, South America and Asia, (iii) directly from third-party manufacturers to our other international customers. For our distributor sales, the goods are generally delivered directly from the independent factories to third-party distribution centers or to our distributors' freight forwarders on a Free Named Carrier ("FCA") basis. We recognize revenue on wholesale sales upon shipment as that is when the customer obtains control of the promised goods. Related costs paid to third-party shipping companies are recorded as cost of sales and are accounted for as a fulfillment cost and not as a separate performance obligation. We generate retail revenues primarily from the sale of footwear to customers at retail locations or through our websites. For our in-store sales, we recognize revenue at the point of sale. For sales made through our websites, we recognize revenue upon shipment to the customer which is when the customer obtains control of the promised good. Sales and value added taxes collected from e-commerce or retail customers are excluded from reported revenues.

We record accounts receivable at the time of shipment when the Company's right to the consideration becomes unconditional. We typically extends credit terms to our wholesale customers based on their creditworthiness and generally we do not receive advance payments. Generally, wholesale customers do not have the right to return goods, however, we periodically decide to accept returns or provide customers with credits. Allowances for estimated returns, discounts, doubtful accounts and chargebacks are provided for when related revenue is recorded. Retail and e-commerce sales generally represent amounts due from credit card companies and are generally collected within a few days of the purchase. As such, we have determined that no allowance for doubtful accounts for retail and

e-commerce sales is necessary.

We earn royalty income from its licensing arrangements which qualify as symbolic licenses rather than functional licenses. Upon signing a new licensing agreement, we receive up-front fees, which are generally characterized as prepaid royalties. These fees are initially deferred and recognized as revenue is earned (i.e., as licensed sales are reported to us or on a straight-line basis over the term of the agreement). The first calculated royalty payment is based on actual sales of the licensed product or, in some cases, minimum royalty payments. We calculate and accrue estimated royalties based on the agreement terms and correspondence with the licensees regarding actual sales.

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## Judgments

We considered several factors in determining that control transfers to the customer upon shipment of products. These factors include that legal title transfers to the customer, we have a present right to payment, and the customer has assumed the risks and rewards of ownership at the time of shipment. We accrue a liability for product returns at the time of sale based on our historical experience. We also accrue amounts for goods expected to be returned in salable condition. As of December 31, 2018 and December 31, 2017, the Company's sales returns liability totaled \$67.3 million and \$43.4 million, respectively, and was included in accrued expenses and accounts receivable in the consolidated balance sheets, respectively.

Allowance for bad debts, returns, sales allowances and customer chargebacks. We provide a reserve against our receivables for estimated losses that may result from our customers' inability to pay. To minimize the likelihood of uncollectibility, customers' credit-worthiness is reviewed and adjusted periodically in accordance with external credit reporting services, financial statements issued by the customer and our experience with the account. When a customer's account becomes significantly past due, we generally place a hold on the account and discontinue further shipments to that customer, minimizing further risk of loss. We determine the amount of the reserve by analyzing known uncollectible accounts, aged receivables, economic conditions in the customers' countries or industries, historical losses and our customers' credit-worthiness. Amounts later determined and specifically identified to be uncollectible are charged or written off against this reserve. Allowance for returns, sales allowances and customer chargebacks are recorded against revenue. Allowances for bad debts are recorded to general and administrative expenses. Retail and e-commerce receivables represent amounts due from credit card companies and are generally collected within a few days of the purchase. As such we have determined that no allowance for doubtful accounts is necessary.

We also reserve for potential disputed amounts or chargebacks from our customers. Our chargeback reserve is based on a collectability percentage based on factors such as historical trends, current economic conditions, and nature of the chargeback receivables. We also reserve for potential sales returns and allowances based on historical trends.

The likelihood of a material loss on an uncollectible account would be mainly dependent on deterioration in the overall economic conditions in a particular country or region. Reserves are fully provided for all probable losses of this nature. For receivables that are not specifically identified as high risk, we provide a reserve based upon our historical loss rate as a percentage of sales. Gross trade accounts receivable were \$527.5 million and \$457.1 million, and the allowance for bad debts, returns, sales allowances and customer chargebacks were \$74.1 million and \$51.2 million, at December 31, 2018 and 2017, respectively. Our credit losses charged to expense for the years ended December 31, 2018, 2017, and 2016 were \$15.5 million, \$12.8 million, and \$12.7 million, respectively. In addition, we recorded sales return and allowance expense for the years ended December 31, 2018, 2017 and 2016 of \$20.2 million, \$5.6 million, and \$18.1 million, respectively.

Inventory write-downs. Inventories are stated at the lower of cost or market. We continually review our inventory for excess and slow-moving inventory. Our review is based on inventory on hand, prior sales and expected net realizable value. Our analysis includes a review of inventory quantities on hand at period-end in relation to year-to-date sales, existing orders from customers and projections for sales in the foreseeable future. The net realizable value, or market value, is determined based on our estimate of sales prices of such inventory based on historical sales experience on a style-by-style basis. A write-down of inventory is considered permanent, and creates a new cost basis for those units. The likelihood of any material inventory write-down depends primarily on our expectation of future consumer demand for our product. A misinterpretation or misunderstanding of future consumer demand for our product or of the economy, or other failure to estimate correctly, could result in inventory valuation changes, either favorably or unfavorably, compared to the requirement determined to be appropriate as of the balance sheet date. Our gross inventory value was \$876.0 million and \$881.8 million, and our inventory reserve was \$12.8 million and \$8.8 million,

at December 31, 2018 and 2017, respectively.

Valuation of intangibles and long-lived assets. When circumstances warrant, we test for recoverability of the asset groups' carrying value using estimates of undiscounted future cash flows based on the existing service potential of the applicable asset group in determining the fair value of each asset group. We evaluate whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount based on our assessment of the following events or changes in circumstances:

- macroeconomic conditions such as a deterioration in general economic conditions, limitations on accessing capital, fluctuations in foreign exchange rates, or other developments in equity and credit markets;
- industry and market considerations such as a deterioration in the environment in which an entity operates, an increased competitive environment, a decline in market-dependent multiples or metrics, or a change in the market for an entity's products or services, or a regulatory or political development;
- cost factors such as increases in raw materials, labor, or other costs that have a negative effect on earnings and cash flows;
- overall financial performance such as negative or declining cash flows, or a decline in actual or planned revenue or earnings compared with actual and projected results of relevant prior periods;

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• other relevant entity-specific events such as changes in management, key personnel, strategy, customers, contemplation of bankruptcy, or litigation;

• events affecting a reporting unit such as a change in the composition or carrying amount of its net assets, a more-likely-than-not expectation of selling or disposing all, or a portion, of a reporting unit, the testing for recoverability of a significant asset group within a reporting unit, or recognition of a goodwill impairment loss in the financial statements of a subsidiary that is a component of a reporting unit; and

• a sustained decrease in share price.

If the assets are considered to be impaired, the impairment we recognize is the amount by which the carrying value of the assets exceeds the fair value of the assets. We base the useful lives and related amortization or depreciation expense on our estimate of the period that the assets will generate revenues or otherwise be used by us. We review all of our stores for impairment annually or more frequently if events or changes in circumstances require it. We prepare a summary of cash flows for each of our retail stores, to assess potential impairment of the fixed assets and leasehold improvements. Stores with negative cash flows which have been open in excess of twenty-four months are then reviewed in detail to determine whether impairment exists. Management reviews both quantitative and qualitative factors to assess whether a triggering event occurred. For the years ended December 31, 2018, 2017 and 2016, respectively we did not record an impairment charge.

**Litigation reserves.** Estimated amounts for claims that are probable and can be reasonably estimated are recorded as liabilities in our consolidated financial statements. The likelihood of a material change in these estimated reserves would depend on additional information or new claims as they may arise as well as the favorable or unfavorable outcome of the particular litigation. Both the likelihood and amount (or range of loss) on a large portion of our remaining pending litigation is uncertain. As such, we are unable to make a reasonable estimate of the liability that could result from unfavorable outcomes in our remaining pending litigation. As additional information becomes available, we will assess the potential liability related to our pending litigation and revise our estimates. Such revisions in our estimates of potential liability could materially impact our results of operations and financial position.

**Tax estimates and valuation of deferred income taxes.** We record a valuation allowance when necessary to reduce our deferred tax assets to the amount that is more likely than not to be realized. The likelihood of a material change in our expected realization of our deferred tax assets depends on future taxable income and the effectiveness of our tax planning strategies amongst the various domestic and international tax jurisdictions in which we operate. We evaluate our projections of taxable income to determine the recoverability of our deferred tax assets and the need for a valuation allowance. As of December 31, 2018, we had a total deferred tax assets of \$69.2 million which was reduced by a valuation allowance of \$30.2 million and resulted in a net deferred tax assets of \$39.0 million primarily related to loss carry-forwards not expected to be utilized by certain foreign subsidiaries.

On December 22, 2017, the SEC staff issued SAB 118 to address the accounting implications of the 2017 Tax Act. SAB 118 permits a company to recognize provisional amounts for the one-time tax effects of the Tax Act upon enactment when it does not have the necessary information available, prepared or analyzed in reasonable detail to complete its accounting for the change in tax law. The measurement period to finalize our calculations cannot extend beyond one year of the enactment date. Key provisions that have a significant impact on our consolidated financial statements and where we have recognized estimated amounts include the recognition of a tax liability for a one-time Transition Tax on the accumulated earnings of our foreign subsidiaries, and the remeasurement of certain net deferred tax assets and liabilities as a result of the decrease in the U.S. corporate tax rate from 35% to 21%.

Due to the Transition Tax on the accumulated earnings of our foreign subsidiaries, previously unremitted earnings for which no U.S. deferred tax liability had been provided have now been subject to U.S. tax. While we have provided U.S. tax on all our unremitted foreign earnings, we have not provided for additional taxes which may arise upon repatriation of those amounts of unremitted foreign earnings which we believe are indefinitely reinvested outside the U.S.

## INFLATION

We do not believe that the rates of inflation experienced in the United States over the last three years have had a significant effect on our sales or profitability. However, we cannot accurately predict the effect of inflation on future operating results. Although higher rates of inflation have been experienced in a number of foreign countries in which our products are manufactured, we do not believe that inflation has had a material effect on our sales or profitability. While we have been able to offset our foreign product cost increases by increasing prices or changing suppliers in the past, we cannot assure you that we will be able to continue to make such increases or changes in the future.

## EXCHANGE RATES

We receive U.S. dollars for substantially all of our domestic and a portion of our international product sales, as well as our royalty income. Inventory purchases from offshore contract manufacturers are primarily denominated in U.S. dollars. However, purchase prices for our products may be impacted by fluctuations in the exchange rate between the U.S. dollar and the local currencies of the contract manufacturers, which may have the effect of increasing our cost of goods in the future. During 2018 and 2017, exchange rate fluctuations did not have a material impact on our inventory costs. We do not engage in hedging activities with respect to such exchange rate risk.

## RECENT ACCOUNTING PRONOUNCEMENTS

Refer to Note 1 — The Company and Summary of Significant Accounting Policies in the accompanying Notes to the Consolidated Financial Statements for recently adopted and recently issued accounting standards.

## ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the potential loss arising from the adverse changes in market rates and prices, such as interest rates, marketable debt security prices and foreign currency exchange rates. Changes in interest rates, marketable debt security prices and changes in foreign currency exchange rates have and will have an impact on our results of operations.

**Interest rate fluctuations.** As of December 31, 2018, we have \$7.2 million and \$83.8 million of outstanding short-term and long-term borrowings, respectively, subject to changes in interest rates. A 200 basis point increase in interest rates would have increased interest expense by less than \$0.2 million for the year ended December 31, 2018. We do not expect any changes in interest rates to have a material impact on our financial condition or results of operations during the remainder of 2019. The interest rate charged on our domestic secured line of credit facility is based on the prime rate of interest, our domestic distribution center loan is based on the one month LIBOR and our China DC Loan is based on a reference rate provided by the People's Bank of China. Changes in these interest rates will have an effect on the interest charged on outstanding balances. As of December 31, 2018, there was \$0.1 million outstanding under this credit facility, \$65.1 million outstanding on our domestic distribution center loan and \$18.6 million on our China DC Loan.

We have entered into derivative financial instruments such as interest rate swaps in order to mitigate our interest rate risk on our long-term debt. We will not enter into derivative transactions for speculative purposes. We had one derivative instrument in place as of December 31, 2018 to hedge the cash flows on our \$65.1 million variable rate debt on our domestic distribution center. This instrument was a variable to fixed derivative with a notional amount of \$65.1 million at December 31, 2018. Our average receive rate was one month LIBOR and the average pay rate was 2.08%. The rate swap agreement utilized by us effectively modifies our exposure to interest rate risk by converting our floating-rate debt to a fixed rate basis over the life of the loan, thus reducing the impact of interest-rate changes on future interest expense.

**Foreign exchange rate fluctuations.** We face market risk to the extent that changes in foreign currency exchange rates affect our non-U.S. dollar functional currency foreign subsidiaries' revenues, expenses, assets and liabilities. In addition, changes in foreign exchange rates may affect the value of our inventory commitments. Also, inventory purchases of our products may be impacted by fluctuations in the exchange rates between the U.S. dollar and the local currencies of the contract manufacturers, which could have the effect of increasing the cost of goods sold in the future. We manage these risks by primarily denominating these purchases and commitments in U.S. dollars. We do not engage in hedging activities with respect to such exchange rate risks.



Assets and liabilities outside the United States are located in regions where we have subsidiaries or joint ventures: Asia, Central America, Europe, the Middle East, North America, and South America. Our investments in foreign subsidiaries and joint ventures with a functional currency other than the U.S. dollar are generally considered long-term. Accordingly, we do not hedge these net investments. The fluctuation of foreign currencies resulted in a cumulative foreign currency translation loss of \$16.7 million and a cumulative foreign currency translation gain of \$11.9 million for the years ended December 31, 2018 and 2017, respectively, that are deferred and recorded as a component of accumulated other comprehensive income in stockholders' equity. A 200 basis point reduction in each of these exchange rates at December 31, 2018 would have reduced the values of our net investments by approximately \$31.3 million.

ITEM 8. FINANCIAL STATEMENTS AND  
SUPPLEMENTARY DATA

index to CONSOLIDATED FINANCIAL STATEMENTS and Financial statement schedule

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Report of Independent Registered Public Accounting Firm

Shareholders and Board of Directors

Skechers U.S.A., Inc.

Manhattan Beach, California

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Skechers U.S.A., Inc. (the “Company”) and subsidiaries as of December 31, 2018 and 2017, the related consolidated statements of earnings, comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2018, and the related notes and schedule (collectively referred to as the “consolidated financial statements”). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company and subsidiaries at December 31, 2018 and 2017, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (“PCAOB”), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) and our report dated March 1, 2019 expressed an unqualified opinion thereon.

Change in Accounting Method Related to Revenue

As discussed in Note 1 to the consolidated financial statements, the Company has changed its method of accounting for revenue during the year ended December 31, 2018 due to the adoption of the Accounting Standards Codification 606, “Revenue from Contracts with Customers.”

Basis for Opinion

These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s consolidated financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ BDO USA, LLP

We have served as the Company's auditor since 2013.

Los Angeles, California

March 1, 2019

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## SKECHERS U.S.A., INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(In thousands, except par values)

	December 31, 2018	December 31, 2017
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$872,237	\$736,431
Short-term investments	100,029	—
Trade accounts receivable, less allowances of \$25,616 in 2018 and \$51,180 in 2017	501,913	405,921
Other receivables	55,683	27,083
Total receivables	557,596	433,004
Inventories	863,260	873,016
Prepaid expenses and other current assets	79,018	62,573
Total current assets	2,472,140	2,105,024
Property, plant and equipment, net	585,457	541,601
Deferred tax assets	39,431	29,922
Long-term investments	93,745	17,396
Other assets, net	37,482	41,139
Total non-current assets	756,115	630,058
<b>TOTAL ASSETS</b>	<b>\$3,228,255</b>	<b>\$2,735,082</b>
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Current installments of long-term borrowings	\$1,666	\$1,801
Short-term borrowings	7,222	8,011
Accounts payable	679,553	505,334
Accrued expenses	161,781	82,202
Total current liabilities	850,222	597,348
Long-term borrowings, excluding current installments	88,119	71,103
Deferred tax liabilities	451	161
Other long-term liabilities	100,188	118,259
Total non-current liabilities	188,758	189,523
Total liabilities	1,038,980	786,871
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 10,000 shares authorized; none issued		
and outstanding	—	—
Class A common stock, \$0.001 par value; 500,000 shares authorized;		

129,525 and 131,784 shares issued and outstanding at December 31, 2018

and December 31, 2017, respectively

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Class B common stock, \$0.001 par value; 75,000 shares authorized;

23,983 and 24,545 shares issued and outstanding at December 31, 2018

and December 31, 2017, respectively	24	24
Additional paid-in capital	375,017	453,417
Accumulated other comprehensive loss	(31,488 )	(14,744 )
Retained earnings	1,691,276	1,390,235
Skechers U.S.A., Inc. equity	2,034,958	1,829,064
Non-controlling interests	154,317	119,147
Total stockholders' equity	2,189,275	1,948,211
TOTAL LIABILITIES AND EQUITY	\$3,228,255	\$2,735,082

See accompanying notes to consolidated financial statements.

## SKECHERS U.S.A., INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except per share data)

	Years Ended December 31,		
	2018	2017	2016
Net sales	\$4,642,068	\$4,164,160	\$3,563,311
Cost of sales	2,418,463	2,225,271	1,928,715
Gross profit	2,223,605	1,938,889	1,634,596
Royalty income	20,582	16,666	13,885
	2,244,187	1,955,555	1,648,481
Operating expenses:			
Selling	350,435	327,201	257,129
General and administrative	1,455,987	1,245,474	1,020,834
	1,806,422	1,572,675	1,277,963
Earnings from operations	437,765	382,880	370,518
Other income (expense):			
Interest income	10,128	2,420	1,186
Interest expense	(5,847 )	(6,677 )	(6,270 )
Other, net	(10,162 )	5,637	(5,950 )
Total other income (expense)	(5,881 )	1,380	(11,034 )
Earnings before income tax expense	431,884	384,260	359,484
Income tax expense	60,611	149,156	74,125
Net earnings	371,273	235,104	285,359
Less: Net earnings attributable to non-controlling interests	70,232	55,914	41,866
Net earnings attributable to Skechers U.S.A., Inc.	\$301,041	\$179,190	\$243,493
Net earnings per share attributable to Skechers U.S.A., Inc.:			
Basic	\$1.93	\$1.15	\$1.58
Diluted	\$1.92	\$1.14	\$1.57
Weighted average shares used in calculating net earnings per share			
attributable to Skechers U.S.A, Inc.:			
Basic	155,815	155,651	154,169
Diluted	156,450	156,523	155,084

See accompanying notes to consolidated financial statements.

## SKECHERS U.S.A., INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

	Years Ended December 31,		
	2018	2017	2016
Net earnings	\$371,273	\$235,104	\$285,359
Other comprehensive income:			
Gain (loss) on foreign currency translation adjustment	(24,806 )	19,119	(4,698 )
Comprehensive income	346,467	254,223	280,661
Less: Comprehensive income attributable to noncontrolling interests	62,170	63,173	37,467
Comprehensive income attributable to Skechers U.S.A., Inc.	\$284,297	\$191,050	\$243,194

See accompanying notes to consolidated financial statements.



SKECHERS U.S.A., INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EQUITY

(In thousands)

	SHARES CLASS A COMMON STOCK	AMOUNT CLASS B COMMON STOCK	CLASS A COMMON STOCK	CLASS B COMMON STOCK	ADDITIONAL COMMON- IN CAPITAL	OTHER COMPREHENSIVE INCOME (LOSS)	RETAINED EARNINGS	SKECHERS U.S.A., INC. EQUITY	NON- CONTROLLING INTERESTS	TOTAL STOCKHOLDERS' EQUITY
Balance at January 1, 2016	127,324	26,278	\$ 127	\$ 26	\$ 386,156	\$(26,305 )	\$ 967,552	\$ 1,327,556	\$ 48,178	\$ 1,375,734
Net earnings	—	—	—	—	—	—	243,493	243,493	—	—