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PRESENTATION

Operator

Welcome to the Q1 2019 Fossil Group Incorporated Earnings Conference Call. My name is Adrienne, and I'll be your operator for today's call. At this time, all participants are in a listen-only mode. Later, we'll conduct a question and answer session. (Operator Instructions) Please note this conference is being recorded.

I'll now turn the call over to Allison Malkin. Allison Malkin, you may begin.

Allison C. Malkin ***ICR, LLC - Senior MD***

Thank you. Good afternoon, everyone. Thank you for joining us, and welcome to Fossil Group's First Quarter 2019 Earnings Conference Call. I would like to remind you that information made available during this conference call contains forward-looking information and actual results could differ materially from those that will be discussed during this call.

Fossil Group's policy on forward-looking statements and additional information concerning a number of factors that could cause actual results to differ materially from such statements is readily available in our Form 8-K and 10-Q reports filed with the SEC.

In addition, the company assumes no obligation to publicly update or revise any forward-looking statements whether as a result of new information, future events or otherwise, except as required by law. Please note that you can find a reconciliation and other information regarding non-GAAP financial measures discussed on this call in our earnings release filed on Form 8-K and in the Investors section of our Website. Please note that you may listen to a live Webcast or replay of this call by visiting www.fossilgroup.com under the Investors section.

Now, I would like to turn the call over to the company's Chairman and CEO, Kosta Kartsotis.

Kosta N. Kartsotis ***Fossil Group, Inc. - Chairman & CEO***

Good afternoon everyone and thanks for joining our call today. I will begin with a few prepared remarks and then turn the call over to Jeff Boyer, our CFO, to cover our Q1 financial performance and financial outlook for the year. Following Jeff's comments, we'll have Greg McKelvey, our Chief Commercial and Strategy Officer join us for the Q&A. Note that our sales comments today will be based on constant currency unless otherwise noted.

In the first quarter, sales performed at the higher end of our expectations, though down to last year. We're continuing to see growth in our Asia business, where core sales grew 7% in the quarter with both China and India delivering double-digit growth. Our direct business also continues to see encouraging trends driven by our digital marketing and our consumer experience focus. Full price retail comps on a global basis, which include full price retail stores in our own e-commerce sites were roughly flat for the quarter with a modest negative impact due to Easter shifting to the second quarter.

As we expected, our connected business declined for the quarter. This was due to higher liquidation levels last year which were not repeated, our Generation 4 smartwatch availability issue and store closures. The underlying performance of our newest generation display product, however, continues to perform well and grew for the quarter. Despite these positives, our overall core sales declined 12% in the quarter with currency, store closures and business exits negatively impacting reported sales by approximately 600 basis points.

As we outlined in our February call, our core business continues to be affected by the disruptive environment. The watch and accessories business is changing at a rapid pace and consumer-shopping patterns continue to shift. Product innovation in watches has expanded the category overall but has caused a move away from traditional watches to connected product. We are working aggressively to transform our sales channels and to increase product innovation to regain market share in this environment.

Though our core sales have been pressured, our New World Fossil program continues to deliver profitability enhancements by delivering better than expected gross margins and a significant reduction in operating expenses. Gross margin for the quarter was 53.3%, above our guidance range and almost 300 basis points better than last year. Our SG&A expense for the quarter, including $10 million of restructuring expense, declined 15% to last year as our New World Fossil initiatives continue to create efficiencies in our operating model.

Adjusted operating income for the quarter was above the high end of our guidance range and roughly flat to last year. We continue to be highly focused on the 4 overarching priorities we shared with you in February. One, improving our overall profitability; two, driving product innovation; three, maximizing top line growth; and four, transforming our business model. As we are focused on improving profitability and transforming our business model, product innovation and differentiation remain at the core of our business. Delivering exciting new products and engaging in creative new ways is critical in this retail environment. Our brands are positioned well to deliver great fashion and function across the marketplace.

We've recently announced the extension of 2 license agreements, Tory Burch and DKNY and we're excited about the future opportunities within our portfolio, including the rollout of the PUMA and BMW brands, which are launching this year.

Near term, we have a tremendous pipeline of new product ideas and concepts coming to market in 2019 across all our categories. In watches, our teams have developed great new fashion ideas across traditional and connected. We're also ramping up our use of exclusives and limited edition products across all of our brands. Consumers and our retail partners are telling us they want more innovation, more exclusives and more personalization, all of which we're focused on accelerating.

Within the connected category, our next-gen products are bringing great new technology and innovation to the market with a particular focus on the sports segment of the market. We have several new connected products planned for introduction at the end of third quarter, and we'll share more with you on the next call. Our new product innovation efforts support our strategy to maximize sales growth across multiple channels. As consumer-shopping patterns continue to rapidly evolve, digital engagement is now the first critical step in attracting and engaging customers. We're continuing to see great results with our digital marketing programs, which are focused on driving awareness and purchase intent across channels.

To further expand our ability to drive consumer awareness and engagement, later this year, we'll complete the integration and rollout of a new state of the art e-commerce and marketing technology platform. This platform will provide better insights and targeted support across both our direct and wholesale channels and will also enable us to expand the number of countries in which we have direct e-commerce sites. We're also testing new price points and promotional programs across segments of our watch offering to ensure that we are communicating the great value of our outstanding products.

Though product innovation and sales growth are critical to our business, given the significant disruption in the market, it is now more important than ever to transform our business model. We have recently launched a transformation project that we're calling New World Fossil 2.0; transformed to grow. In New World Fossil 2.0, we'll be focused on creating organizational and spending efficiencies as well as gross margin expansion opportunities to fund our sales expansion initiatives. We continue to see significant opportunities to capture market share across our categories and channels but we know over time this will require a significant reallocation of resources and strategic investments.

In New World Fossil 2.0, we will rework our business model so we can invest more in digital capabilities and marketing, move closer to the consumer and react more quickly to the ever-evolving consumer shopping patterns. To do this, we're taking a zero-based budgeting approach and working with the support of a major consulting firm to create organizational opportunities and efficiencies and reallocate resources to the most critical parts of our business. While New World Fossil 1.0 has been a clear success, we believe based on additional insights and analysis, there is a much broader opportunity to create efficiencies to enable investment for growth. We have completed the initial phase of this project and work continues on specifically defining the potential profit enhancements New World Fossil 2.0 can deliver.

The early work we've completed in revenue management, supply chain transformation, procurement and zero-based budgeting indicates the savings benefit are expected to be similar to the New World Fossil 1.0. We look forward to updating you more on this topic in our next call.

In closing, while we're pleased the company performed better than expected in the first quarter, we remain unsatisfied with our sales decline. In the near term, we will continue to plan our top line conservatively but we are on a mission to change the trajectory of sales with a relentless approach to bringing innovation and excitement to the market while we expand our digital capabilities. We will also continue to transform the company to put us in position to unlock significant growth in the future. And now I'd like to turn the call over to Jeff.

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

Thanks Kosta, and good afternoon everyone. As Kosta mentioned, we continue to operate in a disruptive environment. During this period of disruption, our focus continues to be in improving our overall profitability while also strengthening our balance sheet. While our top line sales have been challenging, we are pleased with our progress to improve profitability through both gross margin expansion and reduced operating expenses.

We expanded gross margin rate to 53.3%, an increase of nearly 300 basis points and we've reduced expenses by $48 million or 15%. We are also pleased with our progress on the balance sheet as we improved our net debt position by nearly $280 million with our debt down to $230 million and our cash position expanding to $271 million by the end of the first quarter.

We reported net loss of $12 million for the first quarter compared to a net loss of $48 million last year. Our reported loss of $0.25 per diluted share included New World Fossil restructuring charges of $0.16 per diluted share and included a gain on sale of intellectual property of Google, up $0.33 per diluted share.

Last year, our first quarter EPS was a loss of $0.99 and included a restructuring charge of $0.35 per diluted share. Excluding these items, our adjusted EPS was a loss of $0.42 this year as compared to a $0.64 loss last year. Currencies, including both the translation impact on operating earnings and the impact of foreign currency hedging contracts had an unfavorable $0.08 impact on our EPS in the first quarter. Sales, which were within our expectations decreased 18% to $465 million and decreased 15% on a constant currency basis while store closures unfavorably impacted sales comparisons during the quarter, profitability in our direct business improved significantly as we exited unprofitable stores and were less promotional overall in our retail concepts.

Store closures negatively impacted total year-over-year sales comparisons by approximately 160 basis points. We have closed 59 stores since the first quarter of last year and ended the quarter with $461 stores. Overall, retail comps sales decreased 9% as a 7% positive e-commerce comp was more than offset by declines in our retail stores. Our first quarter underlying core sales results were negatively impacted by lower promotional levels, less off price and liquidation sales and a display watch availability issue.

The supply chain issue on our display watch product has been corrected but it will take through the second quarter for inventory levels to build to appropriate levels. Our traditional wholesale channel remains the most challenging. Our wholesale business declined double digits in the Americas and Europe, net sellout trends remains soft while Asia wholesale business increased double digits in the first quarter.

Our watch sales declined 15% in constant currency for the quarter with decreases in both traditional and connected products. Sales in our traditional watch business generally performed within our overall expectations with continued weakness in the Americas and Europe, modest growth in Asia and the unfavorable impact of license brand exits. While our next generation of smartwatches are resonating well with consumers, connected sales decreased moderately during the quarter, largely due to delays in inventory receipts, the impact of store closures and reduced liquidation levels as compared to last year.

Our connected watch business delivered $62 million in sales representing 17% of total watch sales for the quarter as compared to 18% last year. Total Fossil brand sales decreased 9% in constant dollars compared to last year with declines in watches and leathers and a modest increase in jewelry sales.

Fossil watch sales decreased 6% in constant dollars driven mainly by the closure of underperforming stores and significant declines in the traditional wholesale business in Europe. Our connected business continues to gain traction, positively impacting the category growth rate by about 4 percentage points. Despite display watch availability issues and difficult liquidation comparisons, our Fossil brand connected business did grow 10% in the quarter primarily driven by our Gen 4 product introduced last fall.

Excluding business exits and store closures, direct channel Fossil watch sales increased single digits in the Americas and Asia while sales declined single digits in Europe largely driven by a more challenging macroeconomic environment.

Total sales decreases in our retail stores driven by a reduction in promotional activity to increase profitability combined with store closures drove an overall 11% decrease in our total direct channel while our global direct e-commerce sales increased double digits. Store closures negatively impacted our total direct channel by approximately 430 basis points. Michael Kors brands sales declined 35% with declines in both watches and jewelry. Kors watch sales declined 32% for the quarter as the liquidation sales that occurred last year, mainly in older generation connected product were not repeated.

We continue to partner closely with the Kors team to bring great new watch products to market globally. Regionally, Kors watches decreased double digits in both the Americas and Europe while decreasing modestly in Asia. The Kors jewelry business continued to be negatively impacted by the reposition of the line as we transitioned into a higher priced assortment. In the Americas, first quarter sales decreased 24% on a reported basis to $190 million with declines in our 3 main product categories.

Sales declines were primarily driven by softness in the wholesale channel, retail store closures, reduced promotions, lower levels of liquidation sales as well as license brand terminations. Wholesale sellout trends remain down double digits the last year with retailers continuing to tighten inventory levels. Our overall reach and performance in the Americas declined, as e-commerce growth was more than offset by negative store comps driven by lower promotions especially in our outlets. The negative impact on sales from closing unproductive stores and delays in connected inventory receipts.

While retail sales declined, profitability increased solidly. Fossil watch sales in the Americas were modestly negative with declines in traditional watch sales partially offset by strong growth in connected sales. On a core sales basis, excluding store closures and a minor currency effect, Fossil watch sales in America were slightly positive. In Europe, reported sales decreased 24% to $153 million. On a constant dollar basis, sales declined 19% representing decreases across all product categories. During the first quarter, soft sales trends continued across all channels reflective of the challenging macroeconomic environment and general softness in the European markets in the mid-priced fashion watch segment.

Retail comps were moderately negative with negative comps across all concepts partially offset by modestly positive e-commerce comps. Fossil brand decreased double digits in Europe driven by softening sales trends due in part to fewer promotions in the retail channel and delays in connected inventory receipts. Display watch inventory levels should normalize during the second quarter. Within our watch portfolio, sales declined across most brands. Across the euro zone, sales were down in most major markets with the greatest declines in Germany, France and the U.K.

In Asia, we reported a sales decline of 1% on $117 million of sales and on a constant currency basis, sales increased 4% driven by the wholesale channel. Retail sales decreased modestly as strong e-commerce growth was offset by the negative impact of non-productive store closures, reduced levels of liquidation and display watch inventory delays. Excluding store closures and business exits, our underlying core sales growth in Asia was positive 7%. Fossil brand decreased modestly in Asia with decreases in the watches and leathers. Emporio Armani, which became our largest brand in Asia this quarter, posted strong double-digit growth driven by traditional watches. Most other brands in our portfolio are relatively flat to modestly down in sales for the first quarter.

Strong growth momentum continued in China and India primarily driven by third party e-com and wholesale growth. Hong Kong and Korea posted modestly positive results while Australia, Japan and Taiwan were down moderately during the quarter. Gross profit increased to $248 million and gross margin increased 280 basis points to 53.3%.

The gross margin expansion was driven by decreased off-price sales mix with improved margins, favorable region and product mix from higher margin Asia sales and stronger Emporio Armani sales. Lower promotions and markdowns, as well as the benefits from our New World Fossil initiatives also contributed to the improved gross margin. These benefits were partially offset by unfavorable factory cost absorption on lower sales volumes and an unfavorable currency impact of approximately 50 basis points.

On a reported basis, first quarter operating expenses were $268 million including $10 million in restructuring costs. Last year, operating expenses were $316 million and included $21 million in restructuring costs. Excluding restructuring charges, operating expenses decreased to $37 million in the first quarter as compared to the prior year and included a $9 million favorable currency impact. The lower expenses in the first quarter resulted from lower store expenses given the significant number of stores we've closed since last year. Corporate and regional infrastructure reductions driven by our New World Fossil initiatives and the currency effects of a stronger dollar.

Our first quarter operating loss was $20 million, an improvement of $8 million compared to a year ago. Interest expense decreased $3 million to $8 million on lower outstanding debt. First quarter other income of $26 million was favorable to last year, mainly due to a $22 million gain on the sale of intellectual property to Google in the first quarter.

Income tax expenses were approximately $10 million in the first quarter on pre-taxed losses of $2 million. The resulting negative effective tax rate was driven primarily by the recognition of deferred tax asset valuation allowances. Income taxes in the prior year were $7 million on a pretax loss of $41 million. We continue to establish valuation allowances on our deferred tax assets in the U.S. and certain international subsidiaries given our operating losses in those jurisdictions thereby increasing our effective tax rate. We improved our net debt position by $277 million compared to a year ago and into the quarter with more cash than debt by almost $45 million. Cash was $271 million compared to $230 million last year and debt was $227 million compared to $463 million a year ago. During the quarter, we invested $7 million in capex.

Our adjusted EBITDA for the quarter was $35 million, resulting in a trailing 12-month adjusted EBITDA of $234 million. Our first quarter bank leverage was 1.0x. Comparable inventory levels at the end of the quarter were down 28% versus a year ago, driven by reducing slower moving traditional product inventories in clearing our previous generation connected products.

Additionally, our display watch inventory levels were constrained due to supplier delays through the first quarter. Accounts receivable decreased by 15% to roughly $200 million and wholesale DSOs increased 4 days as compared to the prior year as we did not participate in early paid discount programs in the Americas, as terms were not economically attractive this year. Depreciation and amortization expense totaled $14 million for the quarter.

Now let's move to our 2019 outlook. As we outlined in our February call, and Kosta mentioned earlier, we are working aggressively to change sales trends and drive improved profitability. However, given our limited visibility on top line revenue due to watch and accessory market disruptions, it remains prudent for us to continue to plan our finances conservatively. As we look to the remainder of 2019, we're maintaining our guidance for the Q2 to Q4 period while adjusting full year guidance for the actual results in Q1.

As a result, the -- for the full year, we expect total reported sales to range from negative 12% to negative 7%. The upper end of the sales range reflects additional opportunities in connected and e-commerce across our owned and third party platforms, while the lower end reflects a potential change in sales trends given macro factors.

As a reminder, our full year sales guidance includes approximately 250 basis points of headwinds related to store closures and business exits as well as 150 basis points of headwinds from changes in foreign exchange rates. We're continuing to see momentum in gross margin through our New World Fossil program in addition to regional and channel mix benefits. We expect these drivers to continue through the balance of the year to deliver roughly 100 basis points of gross margin improvement, though changes in currency rates will offset most of the underlying improvements. Overall, we expect our full year gross margins to be 52% to 53.5%.

Operating expenses for the full year are expected to be $1.13 billion to $1.19 billion, inclusive of restructuring charges expected in the range of $40 million to $50 million. Our full year expenses are declining compared to 2018 due to the ongoing success of our New World Fossil program. In addition, we continue to refine our store base with an expected reduction in store count of 30 stores in 2019. Therefore, for the full year, we expect an operating margin of 1.5% to 3%.

Excluding restructuring charges, adjusted operating margin is forecast to range from 3.5% to 5.5%. Overall, unfavorable currency fluctuations are expected to have a $20 million negative impact on our operating income metrics. In constant currency, the midpoint of our guidance reflects modest growth in adjusted operating income over last year.

Looking at 2019 on a sequential basis, reported sales are expected to improve as we move throughout the year due to tougher comparisons in the first 2 quarters, which moderate in the back half. As a reminder, first half results in 2018 were stronger primarily driven by currency fluctuations as well as higher liquidation levels early last year.

For the year, we are maintaining a prevailing rate assumptions for the Europe and the British pound of $1.14 and $1.27, respectively. For the second quarter, we expect sales in the range of a negative 16% to negative 10%, which includes approximately 300 basis points of negative headwind from store closures and business exits and approximately 200 basis points of negative impact due to foreign currency fluctuations.

The second quarter will also be negatively impacted by lower inventory liquidation sales compared to Q2 last year. New World Fossil will continue to deliver gross margin expansion as we move through the year, but this will be offset by moderate in-channel mix benefit and a larger negative impact from currency in the second and third quarters. For the second quarter, we expect gross margin of 52.5% to 54.5%. Operating expenses for the second quarter are expected to be $265 million to $279 million, including restructuring charges expected to range from $9 million to $11 million.

Therefore, we expect second quarter operating margin of negative 2.5% to positive 1%. Given lower debt levels, we expect interest expense to decline in 2019, with relatively flat sequential interest expense throughout the year. We expect full year net interest expense to be $31 million. Based on the foreign exchange rates embedded in our planned assumptions, other income and expense is expected to be flat to a modest positive for each of the remaining quarters.

For the full year, we expect other income and expense to be approximately $29 million, primarily driven by the first quarter gain on the sale of assets to Google. Therefore, we expect full year earnings before tax of approximately $30 million to $75 million, and we expect second quarter earnings before tax of approximately negative $17 million to negative $3 million. Based on the profile of our geographical earnings, including the tax loss in our U.S. companies, we expect tax expense to range from $20 million to $30 million and we expect second quarter tax expense to be approximately $3 million. We're planning to invest approximately $30 million in capital expenditures in 2019.

Now I'd like to turn the call over to the operator to open up the lines for Q&A. Thanks.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from Edward Yruma from KeyBanc.

Edward James Yruma ***KeyBanc Capital Markets Inc., Research Division - MD & Senior Research Analyst***

I guess first on traditional watch business, is there any way you could contextualize the performance of Kors X, the liquidation drop off, and I'm just trying to understand has the trajectory changed, is the -- and in particular, as you think about kind of the lineup of fashion watches going forward, are there reasons to get more constructive or do you believe at this stage we're in kind of a continued secular pressure phase?

And then second, as a follow-up, I know that you gave some cadence information on New World Fossil 1.0, are we expecting any benefit from 2.0 this fiscal year?

Kosta N. Kartsotis ***Fossil Group, Inc. - Chairman & CEO***

First on Kors, the decline we had, as we mentioned, was largely due to what we were liquidating last year with large numbers of wearables in the category. But I would say, overall, if you look at the health of the business in all 3 categories, traditional, wearables and in jewelry, we're seeing sequential improvement on sell-throughs. And overall health, it's still declining, and -- but it's not declining as much as the overall number is. And then going forward, I think we have a lot of opportunity to change the direction. We've been working very closely with Kors in all categories, but in traditional watches, we've identified some trends that really are getting back to more of the iconic oversize look. I think in the past year or so, we tried more minimal which was a trend and we think that's going to change the direction.

In wearables, we've got more platforms coming this year than last year and one of them is a sport version, health and wellness oriented. It could be a game changer in the wearables business, so new function and features. So we'll be talking more about that later in the year, it could be good.

And in jewelry, we also -- we've identified some tweaks to the model. I think we've seen some things that we can change to improve the business, but I think we're going to see ongoing improvement in all 3 of those categories. The other question about the watches in general is, I would say over the last couple of years we had a lot of initiatives and emphasis on building our wearables business and traditional business has been soft. This year, I think for the last 6 to 8 months we've kind of taken the gloves off on innovation, design, new materials and traditional watches. We've got a lot of new ideas hitting the market this year. Our idea is to distort differentiation as much as possible in the market as soon as possible. You'll see a lot of that product flow in the second, third and fourth quarter. We're also spending a lot of time and energy on making the cases look different with new marketing. We're emphasizing more digital capabilities to broadcast this, but we definitely think that in our experience sometimes the watch business, the traditional watch business is cyclical and what changes the direction is innovation and differentiation, and we're taking the gloves off and we're bringing as much as we can and market as we can.

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

There are a couple of more financial questions that you asked about, one was the liquidation impact on Kors and how much of that decline was due to that. I'll tell you about 1/3 of the decline, year-over-year was due to the liquidation. We had the additional liquidation last year, particularly in their Bradshaw connected product so that made a tougher comparison and for some of that decline.

You asked the question about New World Fossil 2.0 and whether we'd see benefits in the P&L this year, yes, we will. We've recorded -- we've incorporated those into our forecast already. They were part of our underlying forecast on it. It's going to be a smaller amount as we're just getting started on the program overall. $10 million, $20 million of benefit is embedded in the forecast right now for some of the operates, they were getting an early start on New World Fossil 2.0.

Operator

And our next question comes from Omar Saad from Evercore.

Omar Regis Saad ***Evercore ISI Institutional Equities, Research Division - Senior MD and Head of Softlines, Luxury & Department Stores Team***

Actually, I just wanted to clarify first, did you give the growth rate of the wearables business excluding the impact of the smaller liquidation versus -- this year versus last year?

Kosta N. Kartsotis ***Fossil Group, Inc. - Chairman & CEO***

I don't believe...

Omar Regis Saad ***Evercore ISI Institutional Equities, Research Division - Senior MD and Head of Softlines, Luxury & Department Stores Team***

Grow excluding that?

Kosta N. Kartsotis ***Fossil Group, Inc. - Chairman & CEO***

Yes, it did. We gave it on the Fossil one, was when we called out connected growth on Fossil business been up about 10% and that's a good portion of our business overall and Gen 4 product, this product did grow year-over-year about 10% in the first quarter. So we feel great about that. And that's even with the situation where we really had a limited supply. We were constrained because of the supply issue we had, so we feel really good going into Q2 and the rest of the year in terms of what that product did in a constrained supply situation and what it means for the back half of the year.

So there's a lot of noise with numbers, last year's liquidation of wearables and also hybrids and also store closures. But we're on track this year to have a double-digit increase in wearables.

Omar Regis Saad ***Evercore ISI Institutional Equities, Research Division - Senior MD and Head of Softlines, Luxury & Department Stores Team***

Yes, that was my follow-up. Just kind of jog to the -- the shift towards the sport, it sounds like that business is doing well but it's still small. Can you maybe give us more context around the shift towards sport. Why that makes sense as an increased focus? Is that what's been missing in the wearables offering and this is a key kind of moment when you're adding those types of functionalities? Can you give us some more context around that please?

Gregory A. McKelvey ***Fossil Group, Inc. - Executive VP & Chief Commercial Officer***

Yes, absolutely. So there -- Omar, this is Greg. There's actually 5 things, I'll start with sport. That is the reason why the back half we see actually a step -- a significant step-up to the business. First, sports, as you know, sport drives the category broadly. We've largely been focused on fashion SKUs, metal -- I think, metal, leather, just -- and we've done really big business off that. But Fossil Sport right out of the gates has done incredibly well. We couldn't keep it in stock and we're going to be driving that sport platform with silicon, lighter weight materials, latest tech across several brands as we go through the year. So that's just a significant addressable market we really weren't going after before. As we mentioned, back half, we won't be -- we won't have a liquidation in our base so that will be clean in terms of what we're lapping. We had significant inventory issues, as you know, so we couldn't actually fulfill demand Q4 or Q1. We're actually back up and running and caught up with significant capacity expansion in the back half to take advantage of the growth that we perceive. Michael Kors, in particular, the fourth point, the runway platform that we launched, we really bet everything on one platform which is a bit minimalist, and we believe moved a little bit away from the jet set and true runway appeal that the customer -- Michael Kors customer knows. We've got multiple proven platforms coming back in that are much more consistent with what their customer expects. We just launched, April 25, the Sofie product, which was a huge success when it launched 1.5 years ago, and we've got more coming in the fall. So we expect proven platforms to play out. And then we are seeing a lot of opportunity in sharper price points during key periods that we think are going to get us good margins and drive a lot of volumes, taking advantage of key moments.

Last thing is there's going to be, as Kosta mentioned, a lot of partnership with our customers and completely overhauling point of sale to make sure that we are being disruptive and communicating at point of sale the right messaging that gets customers to stop and quickly understand what these products do for them.

Operator

And your next question comes from Dana Telsey from The Telsey Advisory Group.

Dana Lauren Telsey ***Telsey Advisory Group LLC - CEO & Chief Research Officer***

As you think about the gross margin and SG&A, the variables going forward with obviously Fossil 2.0 and lesser promotions, can you unpack what that means, either as you're thinking about it by region or by channel both on the SG&A side and the gross margin side? And just one quick thing, on Tory Burch and DKNY, were those renewals under the same terms as they had been before and for the same time frame?

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

On the Foss -- on the New World Fossil 2.0, U.S. channels and regions on it and broadly, this is a broader initiative then really -- that really effect the broader base. And if you think about New World Fossil 1.0, we saved about $100 million in gross margin but $100 million in SG&A. So, from that detailed piece, we can share that. So it will be a couple hundred million dollars over a 3-year period with some start this year but really the bulk of it in 2020, in 2021.

Again, split in those categories. On the gross margin side, it will be things such as strategic sourcing, manufacturing and logistics efficiencies as well as revenue management, category management efforts. On the cost side of it, I would tell you, it's spending efficiencies; continuing to take a look at it. We mentioned in our comments we're doing zero-based budgeting. So take a really hard look at where our spending is at and looked at where we could do much better from a spending standpoint and from an organizational efficiency standpoint as well and that will go -- that won't be limited or focused particularly in regions necessarily, or channels, it will be a broader corporate program along those dimensions Dana.

You want to answer that...

Kosta N. Kartsotis ***Fossil Group, Inc. - Chairman & CEO***

Yes. On the licensing, it's pretty much the same terms as the last one so we look forward to working with both brands into the future.

Dana Lauren Telsey ***Telsey Advisory Group LLC - CEO & Chief Research Officer***

And lastly, just any update on tariffs if it does go to 25%, how you're thinking about it?

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

Yes, we've done the analysis on that and the good news is we have very limited exposure. Most of our product categories have been exempted already. Traditional watches are exempted definitionally and connected watches had an exemption that was granted. So it's really on the existing product that's 10%. The in-year impact right now that we're anticipating, without any additional efforts, which obviously with additional efforts, is under $5 million. So it's not a very material impact to us overall and that's kind of a worse case in-year impact without any additional work but we're working hard to continue to shift our production, our sourcing around, to minimize negative impacts from the tariff program.

Kosta N. Kartsotis ***Fossil Group, Inc. - Chairman & CEO***

The good thing is in watches, the country of origin is actually Japan because we use Japanese movements so there's no risk there.

Operator

And our next question comes from Ike Boruchow from Wells Fargo.

Irwin Bernard Boruchow ***Wells Fargo Securities, LLC, Research Division - MD and Senior Specialty Retail Analyst***

So congrats on the profitability improvements. It's good to see on the margins but I guess I wanted to talk about the top line for a second. On the wearables side, I think, Jeff, I think you said modest decline in the first quarter. But if I'm just going through the numbers, the decline looks like it's closer to 23%, so is that accurate or am I looking at the wrong numbers? I'm trying to understand how much year-over-year the total wearables business looked like?

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

Yes. The total wearables business was down more in the mid-teens. It's -- your backwards math, trying to triangulate on that is probably a little bit high but it was down about mid-teens with a fair amount of -- it's all being driven by Bradshaw and hybrid liquidation on it. And, constrained a little bit because of the supply chain issues still, with the supply chain issues we had, the display watch, excluding that group, grew 10%.

Irwin Bernard Boruchow ***Wells Fargo Securities, LLC, Research Division - MD and Senior Specialty Retail Analyst***

Right. And I guess my follow-up to that is, I mean, on the last call you had said you expected it to be down low single so it means, there's clearly something that came in in the quarter worse, down mid-teens. Was it the supply chain constraints or was there something in point of sales? So just trying to understand the down -- I guess, mid-teens relative down low single.

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

It's -- the supply chain. We got back in the business a little later, it took a little bit longer to bring inventory back up again. We're actually just getting there now. We thought we'd be back in business a little bit faster on that. So the vast majority of it was supply chain.

Irwin Bernard Boruchow ***Wells Fargo Securities, LLC, Research Division - MD and Senior Specialty Retail Analyst***

Got it, and so when we look at the guide of the year on total top line now, there's clearly improvement baked in, I guess, just 2 questions I have to that and then I'm done would be, are you getting there? Are you assuming the improvement is driven by the wearables inflecting or is it maybe a stabilization of traditional or both; just trying to understand how you get there and then how Q4 weighted would that back-half improvement relative to the first half be?

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

If you think about the timing issues we had, we have a lot of kind of structural comparison issues this year versus last year. So, it is weighted to the back-half improvement. Liquidation was heavily weighted, connected in traditional business in the first half of the year. And then in the back half of the year, we also had connected supply issues. So those are the big structural things. The good news is you can kind of identify those things and look at them. I will tell you that from a traditional watch standpoint, the underlying forecast and expectation for traditional watches is really a continuation of that. So we get some benefit, decent amount of benefit, just from the structural comparison changes of not going up against liquidation numbers in the back half of the year. Being back in business in a connected product that we feel really good about what's happening right now plus what's coming. So we're very excited about that. So overall, we get into a much better year-over-year comparison by the time we get to Q4.

Operator

(Operator Instructions) And our next question comes from Simeon Siegel from Nomura.

Stephen James McManus ***Nomura Securities Co. Ltd., Research Division - Research Analyst***

This is Steve McManus on for Simeon. So just thinking through the store closures, can you give us some color around what you guys have been seeing in terms of any sales or recapture, whether online or nearby doors and then maybe remind us the cadence of store closures moving through the balance of the year?

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

From a recapture standpoint, we don't have a great deal of density in stores so you tend to get recapture when you're favorite grocery chain or something -- or have stores within a 5 mile radius. Our radius tends to be quite a bit further than that, so we don't get a lot of store recapture in that. And with -- what's always a tough thing to truly capture is how much we pick up online on it. We know we're picking up some element of it from some of our Omni channel work but really hard to quantify that. It's an excellent question Simeon but it's one of the great mysteries right now in terms of the Omni channel modeling on it.

In terms of the cadence of store closures, we always close most of our stores in the first quarter. That's where most of them happen. We have 30 that we anticipate closing for the full year and so that will -- those will phase out mostly in Q2, Q3 because Q4 you don't really close many stores in Q4, it's generally the most profitable quarter. So, it tends to be the first 3 quarters of the year with the heaviest weighting in Q1.

Kosta N. Kartsotis ***Fossil Group, Inc. - Chairman & CEO***

The other thing I'd comment on is, as we mentioned on the prepared remarks, we are now in the process of implementing a new e-com and marketing cloud. So it's the latest state-of-the-art technology that's going to enable us to do exactly what you mentioned, which is recapture our customers as they migrate to different places and it's really going to up our game quite a lot, both on the e-com side, building e-com sites around the world where we don't have them, but also on CRM, omnichannel capabilities, use of data, etc. So, it's going to be, we think, quite a game changer for us in that regard as well.

Operator

And that concludes our question and answer session. I'll now turn the call back over to Jeff Boyer for closing remarks.

Jeffrey N. Boyer ***Fossil Group, Inc. - Executive VP, CFO & Treasurer***

I just want to thank everybody for your support and listening in on the call today. We look forward to updating you in about 90 days when we close the second quarter. Thanks again.

Operator

Thank you ladies and gentlemen, this concludes today's conference call. Thank you for participating and you may now disconnect.