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FOSL - Fossil, Inc. at Integrated Corporate Relations (ICR) XCHANGE

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CORPORATE PARTICIPANTS

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Dennis Secor *Fossil, Inc. - EVP & CFO*

CONFERENCE CALL PARTICIPANTS

Allison Malkin *ICR - Analyst*

PRESENTATION

Allison Malkin *- ICR - Analyst*

I'm Allison Malkin, I'm a Senior Managing Director with ICR. Welcome to our 16th Annual ICR Xchange. We are excited to be here in Orlando. (conference instructions)

I'd like to just get the presentations started with our first company management and that is Fossil Group. In terms of Fossil, Fossil's actually celebrating its 30th year and that's its anniversary. The Company started with one single brand of Fossil in one geography, which is in the US and it has grown to become a global leader in the watch industry, designs distributing some of the world's most sought-after brands.

The Company has seen consistent growth in sales and earnings driven by the successful execution of its global growth strategy, supported by a strong operating platform and several unique competitive strengths. Here to delve into the business in more detail are Kosta Kartsotis, the Company's Chairman and CEO; Dennis Secor, EVP and CFO; also here with us today are Greg McKelvey of Strategy and Sunil Doshi, who is the CFO of the Americas. With that I'd like to turn the podium over to Kosta.

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

Thanks, Allison. Good morning, everyone.

It's great to be here at ICR again and it's great to be in Orlando. It's a great retail market.

If you haven't already I'd encourage you to get out and see some of the stores in the market. We have a number of stores here that are very successful and a good representation of what we do.

We're very pleased to be able to tell our story to you today and tell you why we think we're a great long-term investment. So we'll get started in just a minute.

I do want to tell you, remind you, that our statements today are covered by our Safe Harbor provisions that's in our SEC documents. So with that we'll get started.

At our core the Company is a growth company. This is what we've always done from the very beginning and we think that we are now positioned for even future long-term sustainable growth and we have a number of initiatives we're putting in place to do just that. We have a very diversified business model that enables us to go to market in a more predictable, diversified way and adapt to different markets and get critical mass, which makes the Company inherently more profitable.

We also have, we think, a significant amount of opportunity for additional leverage in the Company. We think the Company has the capability of becoming more profitable as we get larger and increasing dramatically the shareholder value.

The way we look at the Company is there are actually three distinct businesses -- the two lifestyle brands which are Fossil and Skagen. Skagen was the acquisition we made last year in the portfolio, which is our multi-brand watch business. So these three businesses are distinct and we go to market globally using shared services so the combination of the three going to market is very powerful.

Fossil, as you know, is an American-based lifestyle brand, based on accessories and rooted in vintage. It works everywhere in the world.

It's about a $2 billion business at retail. About two-thirds of that we capture ourselves in our own Company. There's a number of stores that communicate the brands, and we have successful stores all over the world and we know the brand works in Europe, Asia and the US and is a very significant long-term opportunity.

The Skagen opportunity for us and is to basically do what we've done with Fossil. Skagen, our mission is to curate and communicate Danish design.

It's a more contemporary brand. It's going to be an accessories lifestyle brand. It started in watches, we added jewelry last year, we'll be adding leather goods this year and communicating broadly a lifestyle brand image through stores, websites, etc.

And, of course, our portfolio. We think we have the biggest and the best brands in the world to be able to go to market with such powerful legacy brands such as Armani and Burberry and also to bring to market emerging brands such as Marc by Marc and Michael Kors. And, of course, this year, late this year, we'll be launching Tory Burch, which is a very unique and powerful brand emerging across the globe.

So we are really the benefactor of a number of strategic growth drivers. We happen to operate in a very large and growing category. Watches and accessories, as you know, has been very strong and we think it will continue to do so.

Now, the apparel business is much larger than accessories, but there's a little less interest in accessories and some of that's disposable income goes into watches and accessories, it has a huge impact on our industry. There are relatively few players that are focused on accessories like we are that benefit from this over a long period of time.

We also have a number of competitive advantages that come from the major investments and the initiatives we put in place over the last 30 years. We are in a unique position to capture additional sales and margin as we spread out our business across the globe.

And we also are in a position where we have the benefit of having the wind at our back of lifestyle brands. It started with Fossil a long time ago.

We're a lifestyle brand based on vintage with Fossil, displace watch brands and local brands across the world and that process continues. As the world gets increasingly globally branded to tell our story and have an emotional attachment to brands and accessory products around the world is a huge weapon for us.

The consumers of today they grew up with lifestyle brands and we are largely selling a dream and an emotional attachment where our competitors are selling things that tell time. This is a major wind at our back.

One of the things that this chart actually shows, in 2013 estimates are that the watch business is about $62 billion. This information comes from Euromonitor International.

It actually shows that in 2008 to 2013, the watch business grew at 5.1% and they're projecting for it to grow at 5.9% for the next five years. There's been a lot of discussion about the watch cycle and where are we on it. And our growth during this time has actually been, our CAGR has been, 15.7%, three times what the watch growth industry has been and it's actually estimated to be larger.

So the point of this is that there is well enough runway and headroom for us to continue to grow in a double-digit pace. We're not saying we're going to grow at 30% like we did in 2010 and 2011. There's plenty of room for us to have a double-digit growth and continue to grow across the world especially when you consider the huge amount of consumers that are joining the middle class in Asia, which is a huge opportunity for the Company.

We also have a number of competitive advantages that we've developed over the last many years in manufacturing and sourcing. Watches and accessories is a complex business, and it's very unique to be able to make and distribute very quickly the type of product that we make. But we have a, through our owned and our controlled sourcing, we have been able to develop a very fast, best-in-class watch production facility that enables us to test and react and make sure that we have the right products for the consumer at the right time.

We also have scale in a large way, our design and creativity capabilities, with hundreds of people working on product development using 3-D design tools and attracting new talent all the time. We are a major weapon in the design and creativity of accessories and watches.

We also have a global support structure including all the infrastructure and logistics to ship in real time products to consumers globally including automated warehouses and computer systems and a repair structure. All of our watches have a warranty behind them and we have a very large global, sophisticated repair facility so we can repair watches for customers very quickly.

And we actually spend about $75 million a year in SG&A just to support our repair facility globally. Huge barrier to entry for new companies.

We also have global management around the world. Over the last many years we have a number of people in our regions in all the countries that we operate in that have been with the Company for a long time and know how we operate, know our secret sauce, and can execute very quickly our objectives. This is increasingly become a very powerful thing for the Company.

And probably our biggest advantage is our global distribution. We sell about 30,000 doors globally. That is very diverse whether you're in the United States or Europe or in Asia.

In the US we sell largely department stores and specialty stores. In Europe it's largely a lot of mom-and-pop jewelry stores and some jewelry chains. In Asia it's largely department stores and concessions.

We have a diverse set of infrastructures around the world to distribute to these 30,000 doors. Our objective is to put additional markets in those doors. Not all of those doors carry all our brands or have as large a presence as we would like so the process we're in is continuing to develop each of those doors and adding additional products to it and as we add additional brands we'll have additional opportunity.

So we have, also as we mentioned, the wind at our back of lifestyle brands. This chart is from Euromonitor also. It shows market share gains for Fossil over the last five years.

We have actually, if you look at the watch business being $62 billion, our Company has something like a single-digit percentage of market share, relatively small considering where we're going in our position in the marketplace. But we're actually gaining share dramatically over the last five years.

And if you look at the chart there, these are traditional watch companies that mostly have lost share to lifestyle brands such as the Fossil brands. There are a few watch companies that have grown, but generally we have gained share against traditional watch companies.

And we think that process is ongoing. As lifestyle brands in our operating model of quickness, design and innovation spreads across the world we believe that we're going to continue to gain share. And we think there's a follow-on opportunity for us in lifestyle brand at Swiss watches, so we're already putting initiatives in place in the future to be able to go after watch brands that are Swiss made with our lifestyle brands.

So before I turn it over to Dennis for more comments, I just want to talk about where the Company is and where we're going. We changed the name of the Company last year to the Fossil Group and we have been looking at and emulating and benchmarking much larger multi-brand companies than ourselves and looking at how we can continue to have sustainable growth over a long period of time.

We think the Company can be much larger than it is today. So we're putting a lot of systems and processes and a lot of investments in place to really do just that.

We feel like we have a great management team, as I mentioned earlier. A lot of our employees have been with the Company for a number of years, have grown up and are becoming major weapons in the Company. Throughout the organization we have promoted people through our organization more than we ever have before.

We also have changed the Company structure where we now have a regional structure. Instead of our Dallas office controlling and approving everything around the world, with our additional management and the teams that have grown up around the world, we have a regional office in Basel for Europe and also in Hong Kong for Asia, and the US is actually in its own, it's an entity in itself.

So we have three regions, but a global office facilitates and gives guidance but the regions are operating on their own autonomously. We think this will unlock even faster growth for the Company and it is the way most global companies are structured as they get larger.

And we also put in place a number of efficiencies to drive -- a number of investments -- to drive efficiency. This includes technology and systems to enable us to scale the Company to a much larger level and to become even more profitable and faster.

We also have put a number of new people in place. So we have started a strategy function in our Company, an enhanced marketing department to enable us to be better at Omni-channel CRM, consumer insight and measurable advertising. A lot of initiatives in place.

But our overall objective is to continue to be an ongoing entity of excellence. We want to be one of the best companies in the world and world class in every way. So with that, I'm going to turn it over to Dennis.

Dennis Secor - *Fossil, Inc. - EVP & CFO*

Thanks, Kosta. So to build on Kosta's point, we are a global growth company and that's really borne out in our numbers.

Since 2008 through our last third quarter we've increased sales at an annual rate of nearly 16%. In that time, we've used our strategic advantages and industry tailwinds to more than double the size of our business to well over $3 billion today.

The next compelling aspect of our Company is that we operate with a highly diversified business model which helps to limit risk and capture multiple emerging sources of growth. We operate with a portfolio of brands.

Brands go through cycles. Some brands may be hotter in one market than they are in another.

We can leverage the key of one brand in a market to drive growth with others. We believe that with our creative design and global reach we can help build brands to levels that they otherwise would not have achieved.

We're diversified across price points. While we're concentrated in the $100 to $500 space, our pricing starts under $100 and extends into the thousands. We strategically position our brands across a broad spectrum of pricing to maximize the potential for those brands and to gain share.

We operate with multiple categories. While watches is our largest category, for our largest owned brands we also offer leathers, jewelry and a limited apparel assortment.

For several licensed brands we also offer jewelry, which is highly leveragable. Jewelry is often distributed through the same retailers as watches, so it allows us to bring an additional offering to the market and leverage our existing structure.

And finally, we're highly diversified globally. Global diversification allows us to leverage our infrastructure, drive bigger volumes and provide a natural hedge to navigate periodic economic headwinds, and we operate primarily in three major regions around the world.

Our Americas region is a $1.7 billion business. About 30% of that comes from our 273 owned stores.

The largest portion of our American distribution is through department stores where we distribute through thousands of doors. We also distribute through specialty chains, independent retailers and licensed partner boutiques. Our products are also distributed online both through our sites and our partner sites.

Our largest American market is the US where wholesale portfolio strength has offset some weakness in our own retail stores. Mall traffic has been soft but we have been able to improve store conversion. One of our clear goals is to improve our retail productivity and profitability and we're excited to welcome a new US head of stores who is joining us from one of the most successful retailers in our space.

We've also been growing Canada and Mexico. And we recently acquired one of our Latin American distributers, which gives us a solid platform there.

We're focused on wholesale productivity. We're investing in shop in shops which is a great vehicle to upgrade brand presentation while deploying relatively modest levels of capital. And of course we're well positioned to leverage our existing portfolio to drive growth with multiple brands.

Our store expansion is focused on outlets where we feel we're underpenetrated and have greater opportunities as we develop a made for line. And finally, e-commerce. We believe we have opportunities online and we're focused on improving that customer experience.

Next is Europe, which includes the Middle East and Africa for us, and it's a $1 billion business. About 20% of those revenues are generated from our 167 owned retail stores.

Wholesale distribution in Europe is very different from the United States and it varies country to country. In addition to department stores we distribute to a large network of literally thousands of independent watch dealers, many of whom also sell jewelry. Our brands are also sold through shop in shops, concessions and online.

In Europe we're really just scratching the surface in many markets with a more significant presence in Germany, which represents roughly one quarter of our business and most recently in the UK. We have opportunities to grow in new markets as we continue to leverage our strongest brands to drive newer brands. We also see opportunities to grow in countries like France, Italy and Spain as well as in new and emerging distributor markets like Russia and the Middle East.

And next is Asia. Asia is already a significant business for us at about $0.5 billion in revenues.

Our business there is spread throughout many markets, the largest being Japan, South Korea, Australia and China. In Asia we operate 103 of our own retail stores and also distribute through department stores, concessions and specialty chains.

Our regional growth opportunity is supported by the development of the middle class in emerging markets such as China. The Chinese middle-class consumer prefers watches and jewelry to other categories and our lifestyle brand watch price points fit their income level perfectly.

We've also launched a Swiss watch initiative to capitalize on our opportunities in China. Currently we distribute Fossil Swiss watches in Asia as well as in our Fossil stores worldwide and we're set to introduce Armani Swiss in the spring.

Developing distribution has been one of our most significant challenges in China. Unlike the United States where distribution ownership is concentrated, it's highly fragmented in China and takes time and significant relationship building.

We're making great progress as we grew China by more than 50% in the three quarters ended our last third quarter. China is one of our biggest opportunities for the long-term so it's important for us to build the best relationship even if that takes longer.

So our diversification presents us with many growth drivers and investors often ask us how long will the watch cycle last? Well, we don't view it that way. We don't see our growth as a function of a cycle.

We're competing already in a substantial market and we've been gaining share in the last several years. And this chart really underscores for us the opportunity to capture an even greater share of the market.

Here you see our current share of the under $1,000 global watch market by region, which is the segment where our lifestyle brands primarily compete. We've already captured substantial share in a strong market like the United States. About 44% for this part of the market, but outside the US our share is significantly lower.

Europe and Asia are big watch markets, but lifestyle watches are a small portion of today's market. And we believe that we're better positioned to take advantage of the future growth.

China's watch industry is already larger than the United States primarily focused in the luxury segment. We believe that many of the same factors that drove our US growth can transfer to our international markets. And that gives us confidence that in many of these newer and younger markets we have opportunities to gain significant share.

Now with respect to the United States, while the rate of growth might be lower in absolute dollar terms it can still be significant. So fueled by our industry tailwinds and our own strategic advantages, our goal is to continue to grow our business at a double-digit rate over time.

Our challenge is to manage this growth as consistently as possible considering the natural ebbs and flows of brands and business cycles. We're also studying ways to grow through categories beyond our core that leverage our production and our distribution.

So beyond revenue growth our business model creates value for shareholders through both operational and financial leverage. Our operating model presents us with a strong opportunity to drive margin expansion as we grow.

Using our trailing 12-month results at the end of the last third quarter, we have gained operating margin -- we have improved operating margins -- by more than 4 full points going back to 2008. Gross margins have expanded by more than 3 full points as we've invested in our direct business and grown internationally, which drives higher-margins.

We've reduced SKUs and improved cycle times. We've also invested in supply-chain automation to help offset some of the impact of rising labor costs.

We continue to work on initiatives to drive gross margins and while currencies can certainly impact our margins, we see further opportunities as international becomes a larger part of our mix. Outlet expansion of the development of made for lines is one more margin opportunity for us and a better consumer experience to drive the top line.

Now looking at our expense structure over this time period, we have achieved roughly 1 point of leverage. We've accomplished that despite investments in retail and global infrastructure to support our growth and our larger, more complex operating platform.

We've been investing in technology and efficiencies and one of the biggest issues for us and challenges is complexity. Communication and coordination in a global business is challenging.

We're investing enterprise-wide solutions like product lifecycle management to automate design and development and to help improve speed. We're investing in sales force automation to improve order flow and help our channel partners optimize inventory levels and assortments.

We've been investing in our regional structure, particularly in Asia, to support our growth. And we're investing in brand awareness, marketing enhancements and in customer relationship management to improve consumer insight.

We've already invested much of the capital to support and develop these solutions. We're now reengineering our functions and processes to optimize.

Our goal is to leverage our total expense structure over time to support our overall margin expansion goals. With reengineering work in front of us, however, we're not anticipating that for 2014.

We also operate from a position of financial strength with a strong capital structure in cash flows. Over the past five years our operating cash flows have grown at a CAGR of roughly 34% and in the 12 months ended last third quarter, our operational cash flows were $463 million. Our goal is to leverage the growth and diversification of our model to deliver consistent and predictable cash flows.

And finally, we are very focused on delivering outstanding shareholder returns. We believe that we can generate sufficient cash flow to fund both our operations and our organic growth.

We also know that our shareholders place a high value on our purchase program. For the first three quarters of 2013, we invested $454 million to repurchase 4.3 million shares and we entered the fourth quarter with an outstanding authorization of $615 million. We're committed to this program and we now operate with a share base that is more than 17% lower than it was three years ago.

During this past year we expanded our credit facility and took on a modest amount of debt and we're evaluating the optimal level for us. With this facility we believe we are well situated with ample capital to support our growth and repurchases along with sufficient dry powder for an acquisition if the right opportunity presented itself.

So to close, clearly we are excited about the future for Fossil Group. We are a leader in a growing industry with a strong global footprint and significant competitive advantages.

We're a growth company with an extensive history of delivering strong growth and great prospects for continuing that. We operate with a diversified business model that helps limit risk, capture multiple emerging sources of growth and supports our goal to deliver predictable earnings and cash flows.

We believe we have opportunities to gain share and grow across all of our geographic regions. Beyond the top line we have opportunities to drive margin expansion through operational efficiencies to leverage our strong balance sheet and cash flows. And these three aspects of our business combined can help support our goal of sustainable earnings growth and outstanding returns for our shareholders.

So, we thank you for your attention this morning. We look forward to seeing many of you at our breakouts at 3.00 PM and 11.00 AM this morning. Thank you.