

DECKERS OUTDOOR CORP
Form 10-Q
February 09, 2015
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark one)

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

For the quarterly period ended December 31, 2014

or

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

For the transition period from _____ to _____

Commission File Number: 000-22446

DECKERS OUTDOOR CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

95-3015862

(I.R.S. Employer Identification No.)

250 Coromar Drive, Goleta, California

(Address of principal executive offices)

93117

(zip code)

(805) 967-7611

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at January 30, 2015
Common Stock, \$0.01 par value	34,568,408

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES
Table of Contents

	Page
Part I. Financial Information	
Item 1.	Financial Statements (Unaudited):
	Condensed Consolidated Balance Sheets as of December 31, 2014 and March 31, 2014 <u>1</u>
	Condensed Consolidated Statements of Comprehensive Income for the Three Months and Nine Months Ended December 31, 2014 and 2013 <u>2</u>
	Condensed Consolidated Statements of Cash Flows for the Nine Months Ended December 31, 2014 and 2013 <u>3</u>
	<u>Notes to Condensed Consolidated Financial Statements</u> <u>4</u>
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> <u>16</u>
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u> <u>33</u>
<u>Item 4.</u>	<u>Controls and Procedures</u> <u>34</u>
Part II. <u>Other Information</u>	
<u>Item 1.</u>	<u>Legal Proceedings</u> <u>35</u>
<u>Item 1A.</u>	<u>Risk Factors</u> <u>35</u>
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u> <u>35</u>
<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u> <u>36</u>
<u>Item 4.</u>	<u>Mine Safety Disclosures</u> <u>36</u>
<u>Item 5.</u>	<u>Other Information</u> <u>36</u>
<u>Item 6.</u>	<u>Exhibits</u> <u>37</u>
<u>Signatures</u>	<u>38</u>

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIESCondensed Consolidated Balance Sheets
(Unaudited)

(amounts in thousands, except par value)

	December 31, 2014	March 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 369,442	\$ 245,088
Trade accounts receivable, net of allowances (\$23,443 at December 31, 2014 and \$15,569 at March 31, 2014)	189,548	106,199
Inventories	293,905	211,519
Prepaid expenses	14,934	12,067
Other current assets	54,366	27,118
Deferred tax assets	20,967	21,871
Total current assets	943,162	623,862
Property and equipment, net of accumulated depreciation (\$123,299 at December 31, 2014 and \$103,090 at March 31, 2014)	216,055	184,570
Goodwill	127,934	127,934
Other intangible assets, net of accumulated amortization (\$35,561 at December 31, 2014 and \$26,026 at March 31, 2014)	92,033	91,411
Deferred tax assets	16,556	17,062
Other assets	21,101	19,365
Total assets	\$ 1,416,841	\$ 1,064,204
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Short-term borrowings	\$ 5,367	\$ 6,702
Trade accounts payable	171,167	76,139
Accrued payroll	27,197	22,927
Other accrued expenses	32,438	11,624
Income taxes payable	46,419	2,908
Value added tax (VAT) payable	12,643	1,915
Total current liabilities	295,231	122,215
Mortgage payable	33,282	—
Other long-term liabilities	55,100	53,140
Commitments and contingencies (note 5)		
Stockholders' equity:		
Common stock, \$0.01 par value; 125,000 shares authorized; shares issued and outstanding of 34,567 at December 31, 2014 and 34,624 at March 31, 2014	346	346
Additional paid-in capital	154,429	146,731
Retained earnings	890,884	743,815
Accumulated other comprehensive loss	(12,431	) (2,043)
Total stockholders' equity	1,033,228	888,849
Total liabilities and stockholders' equity	\$ 1,416,841	\$ 1,064,204

See accompanying notes to condensed consolidated financial statements.

1

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIESCondensed Consolidated Statements of Comprehensive Income
(Unaudited)

(amounts in thousands, except per share data)

	Three Months Ended		Nine Months Ended	
	December 31,		December 31,	
	2014	2013	2014	2013
Net sales	\$ 784,678	\$ 736,048	\$ 1,476,420	\$ 1,292,858
Cost of sales	369,539	359,848	750,636	679,934
Gross profit	415,139	376,200	725,784	612,924
Selling, general and administrative expenses	200,558	174,701	502,102	407,679
Income from operations	214,581	201,499	223,682	205,245
Other expense (income), net:				
Interest income	(38	) (18	) (122	) (34
Interest expense	1,308	1,293	3,746	2,740
Other, net	(5	) (173	) (130	) (508
Total other expense (income), net	1,265	1,102	3,494	2,198
Income before income taxes	213,316	200,397	220,188	203,047
Income tax expense	56,610	59,500	59,814	58,365
Net income	156,706	140,897	160,374	144,682
Other comprehensive loss, net of tax:				
Unrealized (loss) gain on foreign currency hedging	(682	) (34	) 759	(2,016
Foreign currency translation adjustment	(6,647	) (1,892	) (11,147	) (83
Total other comprehensive loss	(7,329	) (1,926	) (10,388	) (2,099
Comprehensive income	\$ 149,377	\$ 138,971	\$ 149,986	\$ 142,583
Net income per share:				
Basic	\$ 4.54	\$ 4.08	\$ 4.64	\$ 4.19
Diluted	\$ 4.50	\$ 4.04	\$ 4.59	\$ 4.15
Weighted-average common shares outstanding:				
Basic	34,537	34,541	34,598	34,496
Diluted	34,853	34,893	34,912	34,855

See accompanying notes to condensed consolidated financial statements.

Table of Contents

DECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Unaudited)
(amounts in thousands)

	Nine Months Ended December 31,	
	2014	2013
Cash flows from operating activities:		
Net income	\$ 160,374	\$ 144,682
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation, amortization and accretion	37,808	32,469
Change in fair value of contingent consideration	(1,559	) 836
Provision for doubtful accounts, net	987	439
Provision for deferred income taxes	1,342	(3,925
Stock compensation	9,450	10,732
Other	2,835	1,250
Changes in operating assets and liabilities:		
Trade accounts receivable	(83,207	) (74,133
Inventories	(81,742	) (2,496
Prepaid expenses and other current assets	(29,843	) (51,141
Income tax receivable	2,303	4,799
Other assets	(1,374	) (4,334
Trade accounts payable	94,365	93,546
Contingent consideration	(364) —
Accrued expenses	33,508	42,725
Income taxes payable	44,444	46,121
Long-term liabilities	3,400	4,788
Net cash provided by operating activities	192,727	246,358
Cash flows from investing activities:		
Purchases of property and equipment	(66,663	) (67,725
Purchases of intangibles and other assets, net	(9,489	) (5,368
Net cash used in investing activities	(76,152	) (73,093
Cash flows from financing activities:		
Cash paid for shares withheld for taxes	(3,956	) (4,932
Excess tax benefits from stock compensation	1,614	1,801
Cash paid for repurchases of common stock	(13,306) —
Contingent consideration paid	(115) —
Proceeds from issuance of short-term borrowing	199,784	310,728
Cash paid for repayment of short-term borrowings	(201,706	) (311,000
Cash received from issuances of common stock	—	52
Proceeds from mortgage loan	33,931	—
Mortgage loan origination costs	(338) —
Repayment of mortgage principal	(157) —
Net cash provided by (used in) financing activities	15,751	(3,351
Effect of exchange rates on cash	(7,972) 2,620
Net change in cash and cash equivalents	124,354	172,534

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Cash and cash equivalents at beginning of period	245,088	64,591
Cash and cash equivalents at end of period	\$369,442	\$237,125
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes	\$4,363	\$11,237
Interest	\$2,660	\$2,518
Non-cash investing and financing activities:		
Accruals for purchases of property and equipment	\$2,593	\$2,283
Accruals for asset retirement obligations	\$297	\$1,936
Accruals for shares withheld for taxes	\$1,713	\$3,702
Write-off for shares exercised with a tax deficit	\$—	\$1,752
See accompanying notes to condensed consolidated financial statements.		

3

Table of Contents

DECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

(1) General

(a) Basis of Presentation

The unaudited condensed consolidated financial statements have been prepared on the same basis as the annual audited consolidated financial statements and, in the opinion of management, reflect all adjustments necessary for a fair presentation for each of the periods presented. The results of operations for interim periods are not necessarily indicative of results to be achieved for full fiscal years or other interim periods. Deckers Outdoor Corporation (also referred to as Deckers or the Company) is a global leader in designing, marketing and distributing innovative footwear, apparel, and accessories developed for both everyday casual lifestyle use and high performance activities. The Company's business is seasonal, with the highest percentage of UGG® brand net sales occurring in the quarters ending September 30 and December 31 and the highest percentage of Teva® and Sanuk® brand net sales occurring in the quarters ending March 31 and June 30 of each year. The other brands do not have a significant seasonal impact on the Company.

In February 2014, our Board of Directors approved a change in the Company's fiscal year (FY) end from December 31 to March 31. The change is intended to better align our planning, financial and reporting functions with the seasonality of our business.

In July 2014, the Company acquired its UGG brand distributor that sold to retailers in Germany and now operates a wholesale business in Germany through the newly acquired subsidiary. The acquisition included certain intangible and tangible assets and the assumption of liabilities. The purchase price of the acquisition was not material to the Company's condensed consolidated financial statements.

We sell our brands through quality domestic retailers and international distributors and retailers, as well as directly to end-user consumers through our E-Commerce business and our retail stores. Independent third parties manufacture all of our products.

As contemplated by the Securities and Exchange Commission (SEC) under Rule 10-01 of Regulation S-X, the accompanying condensed consolidated financial statements and related footnotes have been condensed and do not contain certain information that will be included in the Company's annual consolidated financial statements and footnotes thereto. For further information, refer to the consolidated financial statements and related footnotes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, filed with the SEC on March 3, 2014 (Annual Report).

(b) Use of Estimates

The preparation of the Company's condensed consolidated financial statements in accordance with United States generally accepted accounting principles (US GAAP) requires management to make estimates and assumptions that affect the amounts reported in these condensed consolidated financial statements and accompanying notes. Management bases these estimates and assumptions upon historical experience, existing and known circumstances,

authoritative accounting pronouncements and other factors that management believes to be reasonable. Significant areas requiring the use of management estimates relate to inventory write-downs, accounts receivable reserves, returns liabilities, stock compensation, performance based compensation, impairment assessments, depreciation and amortization, income tax liabilities and uncertain tax positions, fair value of financial instruments, and fair values of acquired intangibles, assets and liabilities, including estimated contingent consideration payments. Actual results could differ materially from these estimates.

(c) Recent Accounting Pronouncement

On May 28, 2014, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

revenue recognition guidance in US GAAP when it becomes effective. The new standard is effective for the Company on April 1, 2017. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

(2) Goodwill and Other Intangible Assets

The Company's goodwill and other intangible assets are summarized as follows:

	Goodwill, Net	Other Intangible Assets, Net	
Balance at March 31, 2014	\$ 127,934	\$ 91,411	
Purchase of intangible assets	—	12,472	
Amortization expense	—	(9,300)
Changes in foreign currency exchange rates	—	(2,550)
Balance at December 31, 2014	\$ 127,934	\$ 92,033	

The Company's goodwill by segment is as follows:

	December 31, 2014	March 31, 2014
UGG brand	\$ 6,101	\$ 6,101
Sanuk brand	113,944	113,944
Other brands	7,889	7,889
Total	\$ 127,934	\$ 127,934

(3) Fair Value Measurements

The fair values of the Company's cash and cash equivalents, trade accounts receivable, prepaid expenses, other current assets, short-term borrowings, trade accounts payable, accrued payroll, other accrued expenses, income taxes payable and VAT payable approximate the carrying values due to the relatively short maturities of these instruments. The fair values of the Company's long-term liabilities, other than contingent consideration, recalculated using current interest rates, would not significantly differ from the recorded amounts. The fair value of the contingent consideration related to acquisitions and of the Company's derivatives are measured and recorded at fair value on a recurring basis. Changes in fair value resulting from either accretion or changes in discount rates or in the expectations of achieving the performance targets are recorded in selling, general and administrative expenses (SG&A). The Company records the fair value of assets or liabilities associated with derivative instruments and hedging activities in other current assets or other accrued expenses, respectively, in the condensed consolidated balance sheets.

In 2010, the Company established a nonqualified deferred compensation program that permits a select group of management employees to defer earnings to a future date on a nonqualified basis. For each plan year, on behalf of the Company, the Company's Board of Directors (the Board) may, but is not required to, contribute any amount it desires to any participant under this program. The Company's contribution will be determined by the Board annually, most likely in the quarter ending March 31. The value of the deferred compensation is recognized based on the fair value of the participants' accounts. The Company has established a rabbi trust for the purpose of supporting the benefits payable under this program. The assets of the trust are reported in other assets on the Company's condensed consolidated balance sheets. All amounts deferred are presented in long-term liabilities in the condensed consolidated balance sheets.

The inputs used in measuring fair value are prioritized into the following hierarchy:

5

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices included within Level 1 that are either directly or indirectly observable.

Level 3: Unobservable inputs in which little or no market activity exists, therefore requiring an entity to develop its own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The table below summarizes the Company's financial assets and liabilities that are measured on a recurring basis at fair value:

	Fair value at December 31, 2014	Fair Value Measurement Using		
		Level 1	Level 2	Level 3
Assets (liabilities) at fair value				
Nonqualified deferred compensation asset	\$ 5,321	\$ 5,321	\$—	\$—
Nonqualified deferred compensation liability	\$ (5,321)	\$ (5,321)	\$—	\$—
Contingent consideration for acquisition of business	\$ (27,700)	\$—	\$—	\$ (27,700)

	Fair value at March 31, 2014	Fair Value Measurement Using		
		Level 1	Level 2	Level 3
Assets (liabilities) at fair value				
Nonqualified deferred compensation asset	\$ 4,534	\$ 4,534	\$—	\$—
Nonqualified deferred compensation liability	\$ (4,534)	\$ (4,534)	\$—	\$—
Designated derivatives liability	\$ (832)	\$—	\$ (832)	\$—
Contingent consideration for acquisition of business	\$ (30,000)	\$—	\$—	\$ (30,000)

The Level 2 inputs consist of forward spot rates at the end of the reporting period (see note 7).

The fair value of the contingent consideration is based on subjective assumptions. It is reasonably possible the estimated fair value of the contingent consideration could change in the near-term and the effect of the change could be material.

Sanuk®

The estimated fair value of the contingent consideration attributable to our Sanuk® (Sanuk) brand acquisition is based on the Sanuk brand's estimated future gross profit in calendar year 2015, using a probability weighted average sales forecast to determine a best estimate of gross profit. The estimated sales forecast includes a compound annual growth rate (CAGR) of 14.9% from calendar year 2013 through calendar year 2015. The gross profit forecast for calendar year 2015 is approximately \$71,000, which is then used to apply the contingent consideration percentage in accordance with the applicable agreement. The total estimated contingent consideration is then discounted to the present value with a discount rate of 7.0%. The Company's use of different estimates and assumptions could produce different estimates of the value of the contingent consideration. For example, a 5.0% change in the estimated CAGR would change the total liability balance at December 31, 2014 by approximately \$2,000.

Hoka One One®

In connection with the Company's acquisition of the Hoka One One® (Hoka) brand, the purchase price includes contingent consideration with maximum payments of \$2,000, which is based on the Hoka brand's net sales for calendar years 2013 through 2017. The Company estimates future net sales using a probability weighted average sales forecast to determine a best estimate. The Company's use of different estimates and assumptions is not expected to have a material impact to the value of the contingent consideration.

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

Refer to note 5 for further information on the contingent consideration arrangements.

The following table presents a reconciliation of the Level 3 measurement:

Balance at March 31, 2014	\$ 30,000	
Payments	(500)
Change in fair value	(1,800)
Balance at December 31, 2014	\$ 27,700	

(4) Notes Payable and Long Term Debt

In August 2011, the Company entered into a Credit Agreement (Credit Agreement) with JPMorgan Chase Bank, National Association (JPMorgan) as the administrative agent, Comerica Bank (Comerica) and HSBC Bank USA, National Association (HSBC) as syndication agents, and the lenders party thereto. In August 2012, the Company amended and restated in its entirety the Credit Agreement (Amended and Restated Credit Agreement). In November 2014, the Company amended and restated in its entirety the Amended and Restated Credit Agreement (Second Amended and Restated Credit Agreement). The Second Amended and Restated Credit Agreement is a five-year, \$400,000 secured revolving credit facility that contains a \$75,000 sublimit for the issuance of letters of credit and a \$5,000 sublimit for swingline loans and matures on November 13, 2019. Subject to customary conditions and the approval of any lender whose commitment would be increased, the Company has the option to increase the maximum principal amount available under the Second Amended and Restated Credit Agreement by up to an additional \$200,000, resulting in a maximum available principal amount of \$600,000. None of the lenders under the Second Amended and Restated Credit Agreement has committed at this time or is obligated to provide any such increase in the commitments. In addition to allowing borrowings in US dollars, the Second Amended and Restated Credit Agreement provides a \$150,000 sublimit for borrowings in Euros, British pounds and any other currency that is subsequently approved by JPMorgan, each lender and the issuing bank. At the Company's option, revolving loans issued under the Second Amended and Restated Credit Agreement will initially bear interest at either the adjusted London Interbank Offered Rate (LIBOR) for 30 days (0.17% at December 31, 2014) plus 1.25% per annum, in the case of LIBOR borrowings, or at the alternate base rate plus 0.25% per annum, and thereafter the interest rate will fluctuate between adjusted LIBOR plus 1.25% per annum and adjusted LIBOR plus 2.00% per annum (or between the alternate base rate plus 0.25% per annum and the alternate base rate plus 1.00% per annum), based upon the Company's total adjusted leverage ratio at such time. In addition, the Company will initially be required to pay fees of 0.175% per annum on the daily amount of the revolving credit facility, and thereafter the fee rate will fluctuate between 0.175% and 0.30% per annum, based upon the Company's total adjusted leverage ratio.

The Company's obligations under the Second Amended and Restated Credit Agreement are guaranteed by the Company's existing and future wholly-owned domestic subsidiaries (other than certain immaterial subsidiaries, foreign subsidiaries, foreign subsidiary holding companies and specified excluded subsidiaries) (the Guarantors), and is secured by a first-priority security interest in substantially all of the assets of the Company and the Guarantors, including all or a portion of the equity interests of certain of the Company's domestic and first-tier foreign subsidiaries.

The Second Amended and Restated Credit Agreement contains financial covenants which include: the total adjusted leverage ratio must not be greater than 3.25 to 1.00; the sum of the consolidated annual earnings before interest, taxes, depreciation, and amortization (EBITDA) and annual rental expense, divided by the sum of the annual interest expense and the annual rental expense must be greater than 2.25 to 1.00; and other customary limitations. The Second Amended and Restated Credit Agreement contains certain other covenants which include: the maximum amount paid for capital expenditures may not exceed \$110,000 per year if the total adjusted leverage ratio is equal to or exceeds 2.75 to 1.00; the maximum additional unsecured debt may not exceed \$200,000; the Company may not have aggregate ERISA events that are considered materially adverse; the Company may not have a change of control (as defined in the Second Amended and Restated Credit Agreement); and no restrictions on dividends, share repurchases or acquisitions if the total adjusted leverage ratio does not exceed 2.75 to 1.00.

Table of Contents

DECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

At December 31, 2014, the Company had no outstanding borrowings under the Second Amended and Restated Credit Agreement and outstanding letters of credit of approximately \$100. As a result, the unused balance and the amount available to borrow after applying the total adjusted leverage ratio under the Second Amended and Restated Credit Agreement was approximately \$399,900 at December 31, 2014. In August 2012, the Company incurred approximately \$1,700 of deferred financing costs which were included in prepaid expenses and amortized over the term of the Amended and Restated Credit Agreement using the straight-line method. In November 2014, the Company incurred approximately \$800 of additional deferred financing costs which were combined with the remaining unamortized balance from the Amended and Restated Credit Agreement included in prepaid expenses. The combined amount is being amortized over the term of the Second Amended and Restated Credit Agreement using the straight-line method.

In October 2014, the China Credit Facility was amended (Amended China Credit Facility) to include, among other things, an extension of the aggregate period of borrowing from 12 months to 18 months. At December 31, 2014, the Company had approximately \$4,900 of outstanding borrowings under the Amended China Credit Facility. Interest is based on the People's Bank of China rate, which was 5.6% at December 31, 2014.

In July 2014, the Company obtained a mortgage secured by its corporate headquarters property for approximately \$33,900. At December 31, 2014 the outstanding balance under the mortgage was approximately \$33,800, which includes approximately \$500 in short-term borrowings and approximately \$33,300 in mortgage payable in the condensed consolidated balance sheet. The mortgage has a fixed interest rate of 4.928%. Payments include interest and principal in an amount that will amortize the principal balance over a 30 year period. Minimum principal payments over the next 5 years are approximately \$2,700. The loan will mature and have a balloon payment due in 15 years of approximately \$23,400. In December 2014, the mortgage financial covenants were amended to be consistent with the financial covenants of the Second Amended and Restated Credit Agreement as discussed above.

(5) Commitments and Contingencies

The Company is currently involved in various legal claims arising in the ordinary course of business. Management does not believe that the disposition of these matters, whether individually or in the aggregate, will have a material effect on the Company's financial position or results of operations.

Contingent Consideration. In July 2011, the Company acquired the Sanuk brand, and the total purchase price included contingent consideration payments. As of December 31, 2014, the remaining contingent consideration payment, which has no maximum, is 40.0% of the Sanuk brand gross profit in calendar year 2015 and is to be paid within 60 days following the end of the performance period.

As of December 31, 2014 and March 31, 2014, contingent consideration for the acquisition of the Sanuk brand of approximately \$26,200 and \$28,000, respectively, is included within long-term liabilities in the condensed consolidated balance sheets. Refer to note 3 for further information on the contingent consideration amounts.

In September 2012, the Company acquired Hoka, and the total purchase price included contingent consideration payments with a maximum of \$2,000. As of December 31, 2014 and March 31, 2014, contingent consideration for

the acquisition of the Hoka brand of approximately \$1,500 and \$1,800, respectively, is included within other accrued expenses and long-term liabilities in the condensed consolidated balance sheets. Refer to note 3 for further information on the contingent consideration amounts.

Future Capital Commitments. As of December 31, 2014, the Company had approximately \$7,000 of material commitments for future capital expenditures primarily related to equipment costs of its new distribution center and tenant improvements for retail store space in Japan and China.

Income Taxes. The Company files income tax returns in the US federal jurisdiction and various state, local, and foreign jurisdictions. When tax returns are filed, some positions taken are subject to uncertainty about the merits of the position taken or the amount that would be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period during which the Company believes it is more likely than not that the position will be sustained upon examination.

Table of Contents

DECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

Tax positions that meet the more likely than not recognition threshold are measured as the largest amount of tax benefit that is more than 50% likely of being realized upon settlement. The portion of the benefits that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying condensed consolidated balance sheets along with any associated interest and penalties that would be payable to the taxing authorities upon examination. With few exceptions, the Company is no longer subject to US federal, state, local, or non-US income tax examinations by tax authorities for years before 2008.

Although the Company believes its tax estimates are reasonable and prepares its tax filings in accordance with all applicable tax laws, the final determination with respect to any tax audits, and any related litigation, could be materially different from the Company's estimates or from its historical income tax provisions and accruals. The results of an audit or litigation could have a material effect on operating results or cash flows in the periods for which that determination is made. In addition, future period earnings may be adversely impacted by litigation costs, settlements, penalties, or interest assessments.

The Company has ongoing income tax examinations in various state and foreign tax jurisdictions. During the three and nine months ended December 31, 2014, the Company recorded an accrual for uncertain tax positions of approximately \$200 and \$2,200. In addition, accruals for interest and potential penalties of approximately \$1,100 were recorded during the nine months ended December 31, 2014. The accrual relates to tax positions taken in prior years that are subject to examination. The Company records accruals relating to interest and potential penalties related to income tax matters within interest expense. It is reasonably possible that approximately \$300 of uncertain tax positions will be settled within the next 12 months.

Indemnification. The Company has agreed to indemnify certain of its licensees, distributors, and promotional partners in connection with claims related to the use of the Company's intellectual property. The terms of such agreements range up to five years initially and generally do not provide for a limitation on the maximum potential future payments. From time to time, the Company also agrees to indemnify its licensees, distributors and promotional partners in connection with claims that the Company's products infringe the intellectual property rights of third parties. These agreements may or may not be made pursuant to a written contract. In addition, from time to time, the Company also agrees to standard indemnification provisions in commercial agreements in the ordinary course of business.

Management believes the likelihood of any payments under any of these arrangements is remote and would be immaterial. This determination was made based on a prior history of insignificant claims and related payments. There are no currently pending claims relating to indemnification matters involving the Company's intellectual property.

(6) Stockholders' Equity

In May 2006, the Company adopted the 2006 Equity Incentive Plan (2006 Plan), which was amended by Amendment No. 1 dated May 9, 2007. The primary purpose of the 2006 Plan is to encourage ownership in the Company by key personnel, whose long-term service is considered essential to the Company's continued success. The 2006 Plan reserves 6,000,000 shares of the Company's common stock for issuance to employees, directors, or consultants. The

maximum aggregate number of shares that may be issued under the 2006 Plan through the exercise of incentive stock options (Options) is 4,500,000. Pursuant to the Deferred Stock Unit Compensation Plan, a sub plan under the 2006 Plan, a participant may elect to defer settlement of their outstanding unvested awards until such time as elected by the participant.

The Company has elected to grant nonvested stock units (NSUs) annually to key personnel. The NSUs granted entitle the employee recipients to receive shares of common stock in the Company upon vesting of the NSUs. The vesting of most NSUs is subject to achievement of certain performance targets. During the three months ended December 31, 2014, the Company granted approximately 10,000 time-based equity award units at a weighted-average grant date fair value of \$89.43 per share under the 2006 Plan. During the nine months ended December 31, 2014, the Company granted approximately 143,000 NSUs at a weighted-average grant date fair value of \$83.99 per share, as well as approximately 33,000 time-based equity award units at a weighted-average grant date fair value of \$82.64 per share under the 2006 Plan. The NSUs will vest in equal one-third installments at the end of each of the three years after the performance goal has been achieved, and the time-based equity award units have no Company performance targets and will vest in equal annual installments over a three year period. The vesting schedule for these awards was established to encourage officers and key employees to remain

Table of Contents

DECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

with the Company for the long-term. As of December 31, 2014, future unrecognized compensation cost for these NSUs and time-based equity award units, excluding estimated forfeitures, was approximately \$9,200. As of December 31, 2014, the Company believed that the achievement of at least the threshold performance objective of the NSU awards was probable, and therefore recognized compensation expense accordingly for these awards.

On a quarterly basis, the Company grants fully-vested shares of its common stock to each of its outside directors. The fair value of such shares is expensed on the date of issuance.

In September 2014, the Board of Directors of the Company approved a long-term incentive award (2015 LTIP Awards) under its 2006 Equity Incentive Plan. The shares under these awards will be available for issuance to current and future members of the Company's leadership team, including the Company's named executive officers. Each recipient will receive a specified maximum number of restricted stock units (RSUs), each of which will represent the right to receive one share of the Company's common stock. These awards vest subject to certain long-term performance objectives and certain long-term service conditions. The awards will vest on March 31, 2017 only if the Company meets certain revenue targets ranging between approximately \$2,155,000 and approximately \$2,447,000 and certain EBITDA targets ranging between approximately \$336,000 and approximately \$394,000 for the fiscal year ending March 31, 2017. No vesting of any 2015 LTIP Awards will occur if either of the threshold performance criteria is not met for the year ending March 31, 2017. To the extent financial performance is achieved above the threshold levels, the number of RSUs that will vest will increase up to the maximum number of units granted under the award. Under this new program, the Company granted awards that contain a maximum amount of approximately 160,000 RSUs during the nine months ended December 31, 2014. The average grant date fair value of these RSUs was \$98.29 per share. As of December 31, 2014, future unrecognized compensation cost for the 2015 LTIP Awards, excluding estimated forfeitures, was approximately \$6,800. As of December 31, 2014, based on the Company's current long-range forecast, the Company believed that the achievement of at least the threshold performance objectives of these awards was probable, and therefore the Company recognized compensation expense accordingly.

In June 2012, the Company approved a stock repurchase program to repurchase up to \$200,000 of the Company's common stock in the open market or in privately negotiated transactions, subject to market conditions, applicable legal requirements, and other factors. The program does not obligate the Company to acquire any particular amount of common stock and the program may be suspended at any time at the Company's discretion. Under this program, during the three and nine months ended December 31, 2014 the Company repurchased approximately 157,000 shares, for approximately \$13,300, or an average price of \$84.69. Through December 31, 2014, the Company had repurchased approximately 2,922,000 shares under this program, for approximately \$134,000, or an average price of \$45.87 per share, leaving the remaining approved amount at approximately 66,000. Between January 1, 2015 and February 6, 2015, the Company repurchased approximately 468,000 shares under the stock repurchase program approved in June 2012 for approximately \$34,000, or an average price of \$72.55 per share, leaving the remaining approved amount at approximately \$32,000.

Subsequent to December 31, 2014, the Company approved a new stock repurchase program to repurchase up to \$200,000 of the Company's common stock in the open market or in privately negotiated transactions, subject to market conditions, applicable legal requirements, and other factors. The program does not obligate the Company to acquire any particular amount of common stock and the program may be suspended at any time at the Company's discretion.

Subsequent to December 31, 2014, the Company granted approximately 13,000 time-based equity award units at a weighted-average grant date fair value of \$68.96 per share. Future unrecognized compensation cost for these awards, excluding estimated forfeitures, is approximately \$900.

The following is a reconciliation of the Company's retained earnings:

10

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

	Retained Earnings
Balance at March 31, 2014	\$ 743,815
Net income	160,374
Repurchase of common stock	(13,305)
Balance at December 31, 2014	\$ 890,884

(7) Foreign Currency Exchange Contracts and Hedging

As of December 31, 2014, the Company had no foreign currency forward contracts designated as cash-flow hedges and had no non-designated derivative contracts. At March 31, 2014, the Company had foreign currency forward contracts designated as cash-flow hedges with notional amounts totaling approximately \$64,000, held by four counterparties.

The following table summarizes the effect of foreign exchange contracts designated as cash flow hedging relationships on the condensed consolidated financial statements:

For the Nine Months Ended December 31,	Amount of Gain (Loss) Recognized in OCI/L on Derivative (Effective Portion)	Location of Gain (Loss) Reclassified from AOCI/L into Income (Effective Portion)	Reclassified from AOCI/L into Income (Effective Portion)	Location of Amount Excluded from Effectiveness Testing	Gain (Loss) from Amount Excluded from Effectiveness Testing
2014	\$ 2,053	Net sales	\$ 1,226	SG&A	\$ (79)
2013	\$ (3,253)	Net sales	\$ 17	SG&A	\$ 22

The following table summarizes the effect of foreign exchange contracts not designated as hedging instruments on the condensed consolidated financial statements:

For the Nine Months Ended December 31,	Location of Gain (Loss) Recognized in Income (Loss) on Derivatives	Amount of Gain (Loss) Recognized in Income (Loss) on Derivatives
2014	SG&A	\$ 5,909
2013	SG&A	\$ 727

Subsequent to December 31, 2014, the Company entered into non-designated derivative contracts with notional amounts totaling approximately \$54,000, held by five counterparties.

(8) Accumulated Other Comprehensive Loss

Accumulated balances of the components within accumulated other comprehensive loss were as follows:

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	December 31, 2014	March 31, 2014	
Unrealized loss on foreign currency hedging, net of tax	\$—	\$ (759)
Cumulative foreign currency translation adjustment, net of tax	(12,431	) (1,284)
Accumulated other comprehensive loss	\$(12,431	) \$(2,043)

(9) Net Income per Share

11

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

Basic net income per share represents net income divided by the weighted-average number of common shares outstanding for the period. Diluted net income per share represents net income divided by the weighted-average number of common shares outstanding, including the dilutive impact of potential issuances of common stock. The reconciliations of basic to diluted weighted-average common shares outstanding were as follows:

	Three Months Ended		Nine Months Ended	
	December 31,		December 31,	
	2014	2013	2014	2013
Weighted-average shares used in basic computation	34,537,000	34,541,000	34,598,000	34,496,000
Dilutive effect of stock-based awards*	316,000	352,000	314,000	359,000
Weighted-average shares used for diluted computation	34,853,000	34,893,000	34,912,000	34,855,000
*Excluded NSUs	140,000	—	140,000	—
*Excluded RSUs	642,000	795,000	642,000	795,000
*Excluded stock appreciation rights (SARs)	525,000	525,000	525,000	525,000

* The share-based awards that were excluded from the dilutive effect were excluded because necessary conditions had not been satisfied for the shares to be issuable based on the Company's performance through the three and nine months ended December 31, 2014 and 2013, respectively. The excluded awards include the maximum amounts achievable for these awards.

(10) Business Segments, Concentration of Business, and Credit Risk and Significant Customers

The Company's accounting policies of the segments below are the same as those described in the summary of significant accounting policies in the Annual Report, except that the Company does not allocate corporate overhead costs or non-operating income and expenses to segments. The Company evaluates segment performance primarily based on net sales and income (loss) from operations. The Company's reportable segments include the strategic business units for the worldwide wholesale operations of the UGG brand, Teva brand, Sanuk brand, and other brands, its E-Commerce business and its retail store business. The wholesale operations of each brand are managed separately because each requires different marketing, research and development, design, sourcing, and sales strategies. The E-Commerce and retail store segments are managed separately because they are Direct-to-Consumer sales, while the brand segments are wholesale sales. The income (loss) from operations for each of the segments includes only those costs that are specifically related to each segment, which consist primarily of cost of sales, costs for research and development, design, selling and marketing, depreciation, amortization, and the costs of employees and their respective expenses that are directly related to each segment. The unallocated corporate overhead costs include: costs of the distribution centers, certain executive and stock compensation, accounting and finance, legal, information technology, human resources, and facilities costs, among others. During the nine months ended December 31, 2014, the Company converted seven of its retail stores in China to partner retail stores, whereby, upon conversion, the stores became wholly-owned and operated by local, third party companies within China. These conversions included the assignment of the lease and the sale of both the Company's on-hand inventory and store leasehold improvements to the operator. As of the date of conversion, partner retail stores sales are included in the UGG brand wholesale segment and not included in the retail stores segment. During the three months ended September 30, 2014, certain

operating expenses were classified as unallocated expenses and are now classified as segment expenses, as well as certain segment expenses that were classified in one segment are now classified in a different segment. This change in segment reporting only changed the presentation within the below table and did not impact the Company's condensed consolidated financial statements for any period. The segment information for the nine months ended December 31, 2014 has been adjusted retrospectively to conform to the current period presentation.

The Company's other brands include Ahnu®, Hoka One One® (Hoka), MOZO® and TSUBO®. The wholesale operations of the Company's other brands are included as one reportable segment, other wholesale, presented in the figures below. Business segment information is summarized as follows:

12

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

	Three Months Ended		Nine Months Ended	
	December 31,		December 31,	
	2014	2013	2014	2013
Net sales to external customers:				
UGG wholesale	\$ 401,702	\$ 399,628	\$ 815,694	\$ 735,671
Teva wholesale	12,373	14,189	65,641	58,830
Sanuk wholesale	17,763	19,974	66,047	64,409
Other wholesale	13,211	6,936	47,153	27,907
E-Commerce	146,871	117,300	183,902	142,920
Retail stores	192,758	178,021	297,983	263,121
	\$ 784,678	\$ 736,048	\$ 1,476,420	\$ 1,292,858
Income (loss) from operations:				
UGG wholesale	\$ 135,893	\$ 128,909	\$ 261,614	\$ 210,655
Teva wholesale	(660)	(1,258)	3,812	(475)
Sanuk wholesale	(282)	1,085	9,307	11,231
Other wholesale	(4,522)	(4,549)	(9,104)	(7,227)
E-Commerce	67,006	53,536	75,256	57,883
Retail stores	74,302	67,328	51,979	55,250
Unallocated overhead costs	(57,156)	(43,552)	(169,182)	(122,072)
	\$ 214,581	\$ 201,499	\$ 223,682	\$ 205,245

Inter-segment sales from the Company's wholesale segments to the Company's E-Commerce and retail stores segments are at the Company's cost, and there is no inter-segment profit on these inter-segment sales. Income (loss) from operations of the wholesale segments does not include any inter-segment gross profit from sales to the E-Commerce and retail stores segments.

Business segment asset information is summarized as follows:

	December 31,	March 31,
	2014	2014
Total assets for reportable segments:		
UGG wholesale	\$ 334,860	\$ 153,341
Teva wholesale	45,661	81,766
Sanuk wholesale	208,277	214,627
Other wholesale	53,625	41,281
E-Commerce	10,697	3,129
Retail stores	173,253	160,535
	\$ 826,373	\$ 654,679

The assets allocable to each segment include accounts receivable, inventory, fixed assets, goodwill, other intangible assets, and certain other assets that are specifically identifiable with one of the Company's segments. Unallocated assets are the assets not specifically related to the segments and include cash and cash equivalents, deferred tax assets,

and various other assets shared by the Company's segments. Reconciliations of total assets from reportable segments to the condensed consolidated balance sheets are as follows:

13

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

	December 31, 2014	March 31, 2014
Total assets for reportable segments	\$ 826,373	\$ 654,679
Unallocated cash and cash equivalents	369,442	245,088
Unallocated deferred tax assets	37,523	38,933
Other unallocated corporate assets	183,503	125,504
Consolidated total assets	\$ 1,416,841	\$ 1,064,204

The Company does not consider international operations a separate segment, as management reviews such operations in the aggregate with the aforementioned segments. Long-lived assets, which consist of property and equipment, in the US and all other countries combined were as follows:

	December 31, 2014	March 31, 2014
US	\$ 180,484	\$ 148,178
All other countries*	35,571	36,392
Total	\$ 216,055	\$ 184,570

* No other country's long-lived assets comprised more than 10% of total long-lived assets as of December 31, 2014 and March 31, 2014.

The Company sells its products to customers throughout the US and to foreign customers located in Europe, Asia, Canada, Australia, and Latin America, among other regions. International sales were 32.9% and 30.6% of the Company's total net sales for the three months ended December 31, 2014 and 2013, respectively. International sales were 35.8% and 33.5% of the Company's total net sales for the nine months ended December 31, 2014 and 2013, respectively. For the nine months ended December 31, 2014 and 2013, no single foreign country comprised more than 10% of total net sales.

Management performs regular evaluations concerning the ability of its customers to satisfy their obligations and records a provision for doubtful accounts based upon these evaluations. No single customer accounted for more than 10% of net sales for either the nine months ended December 31, 2014 or 2013. As of December 31, 2014, the Company had one customer representing 20.3% of net trade accounts receivable. As of March 31, 2014, the Company had one customer representing 11.8% of net trade accounts receivable, and a second customer representing 11.4% of net trade accounts receivable.

The Company's production is concentrated at a limited number of independent contractor factories in Asia. Sheepskin is the principal raw material for certain UGG products and the majority of sheepskin is purchased from two tanneries in China, which is sourced primarily from Australia and the United Kingdom (UK). The other materials used by the Company in production are sourced primarily in Asia. The Company's operations are subject to the customary risks of doing business abroad, including, but not limited to, currency fluctuations, customs duties and related fees, various import controls and other nontariff barriers, restrictions on the transfer of funds, labor unrest and strikes and, in certain parts of the world, political instability. The supply of sheepskin can be adversely impacted by weather conditions, disease, and harvesting decisions that are completely outside the Company's control. Further, the price of sheepskin is

impacted by demand, industry, and competitors.

A portion of the Company's cash and cash equivalents are held as cash in operating accounts that are with third party financial institutions. These balances, at times, exceed the Federal Deposit Insurance Corporation insurance limits. While the Company regularly monitors the cash balances in its operating accounts and adjusts the balances as appropriate, these cash balances could be impacted if the underlying financial institutions fail or are subject to other adverse conditions in the financial markets.

Table of ContentsDECKERS OUTDOOR CORPORATION
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Three and Nine months ended December 31, 2014 and 2013

(Unaudited)

(amounts in thousands, except share quantity and per share data)

The remainder of the Company's cash equivalents is invested in interest bearing funds managed by third party investment management institutions. These investments can include US treasury bonds and securities, money market funds, and municipal bonds, among other investments. Certain of these investments are subject to general credit, liquidity, market, and interest rate risks. Investment risk has been and may further be exacerbated by US mortgage defaults, credit and liquidity issues, and sovereign debt concerns in Europe, which have affected various sectors of the financial markets. As of December 31, 2014, the Company had experienced no loss or lack of access to cash in its operating accounts, invested cash, and cash equivalents. The Company's cash and cash equivalents are as follows:

	December 31, 2014	March 31, 2014
Money market fund accounts	\$ 203,339	\$ 143,816
Cash	166,103	101,272
Total Cash and Cash Equivalents	\$ 369,442	\$ 245,088

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

SPECIAL NOTE ON FORWARD-LOOKING STATEMENTS

This report and the information incorporated by reference in this report contain "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that concern matters that involve risks and uncertainties that could cause actual results to differ materially from those anticipated or projected in the forward-looking statements. These forward-looking statements are intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact contained in this interim report, including statements regarding future events, our future financial performance, our future business strategy and the plans and objectives of management for future operations, are forward-looking statements. We have attempted to identify forward-looking statements by using words such as "anticipate," "believe," "estimate," "expect," "intend," "may," "project," "plan", "predict", "will," and similar expressions, or the negative of these expressions, as they relate to us, our management and our industry. Specifically, this report and the information incorporated by reference in this report contain forward-looking statements relating to, among other things:

- our global business, growth, operating, investing, and financing strategies;
- our product, distribution channel, and geographic mix;
- the success of new products, new brands, and other growth initiatives;
- the impact of seasonality on our operations;
- expectations regarding our net sales and earnings growth and other financial metrics;
- our development of worldwide distribution channels;
- trends affecting our financial condition, results of operations, or cash flows;
- our expectations for expansion of our retail and E-Commerce capabilities;
- information security and privacy of customer, employee or company information;
- overall global economic trends;
- reliability of overseas factory production and storage; and
- the availability and cost of raw materials.

We have based our forward-looking statements on our current expectations and projections about trends affecting our business and industry and other future events. Although we do not make forward-looking statements unless we believe we have a reasonable basis for doing so, we cannot guarantee their accuracy.

Some of the risks, uncertainties and assumptions that may cause actual results to differ from these forward-looking statements are described in Part II, Item 1A of this interim report in the section entitled "Risk Factors," as well as in our other filings with the Securities and Exchange Commission (SEC). In addition, actual results may differ as a result of additional risks and uncertainties of which we are currently unaware or which we do not currently view as material to our business. We operate in a very competitive and rapidly changing environment. New risk factors emerge from time to time and 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. As a result, actual results may differ materially from the results stated in or implied by our forward-looking statements. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements, which reflect our opinions only as of the date of this quarterly report, as a prediction of actual results.

You should read this report in its entirety, together with our Annual Report on Form 10-K for the fiscal year (FY) ended December 31, 2013 filed with the SEC on March 3, 2014 (Annual Report), and the documents that we file as exhibits to these reports and the documents that we incorporate by reference in these reports, with the understanding that our future results may be materially different from what we currently expect. We qualify all of our

forward-looking statements by these cautionary statements and we

16

Table of Contents

expressly disclaim any intent or obligation to update any forward-looking statements after the date hereof to conform such statements to actual results or to changes in our opinions or expectations, except as required by applicable law or the rules of the New York Stock Exchange.

References to “Deckers,” “we,” “us,” “our,” or similar terms refer to Deckers Outdoor Corporation together with its consolidated subsidiaries. Unless otherwise specifically indicated, all amounts herein are expressed in thousands, except for share quantity, per share data, and selling prices per pair. The following discussion of our financial condition and results of operations should be read together with our condensed consolidated financial statements and the accompanying notes to those statements included elsewhere in this document.

Overview

We are a global leader in designing, marketing and distributing innovative footwear, apparel and accessories developed for both everyday casual lifestyle use and high performance activities. We market our products primarily under three proprietary brands:

• **UGG®:** Premier brand in luxurious comfort footwear, handbags, apparel, home and cold weather accessories;

• **Teva®:** Born from the outdoors, active lifestyle footwear for the adventurous spirit; and

• **Sanuk®:** Innovative action sport footwear brand rooted in the surf community.

In addition to our primary brands, our other brands include Ahnu®, an authentic performance footwear brand that makes footwear for fashion-minded people who prefer trails, yoga mats, and hybrid fitness workouts; Hoka One One® (Hoka), a line of footwear for all capacities of runner designed with a unique performance midsole geometry, oversized midsole volume and active foot frame; MOZO®, a line of footwear crafted for culinary professionals that redefines the industry dress code; and TSUBO®, a line of mid and high-end dress and dress casual comfort footwear that incorporates style and function with maximum comfort.

We sell our brands through quality domestic retailers and international distributors and retailers, as well as directly to our end-user consumers through our E-Commerce business and our retail stores. Independent third parties manufacture all of our products.

Our business has been impacted by, what we believe are, several important trends and we expect that it will continue to be impacted:

Sales of our products are highly seasonal and are sensitive to weather conditions, which are beyond our control. Even though we are creating more year-round styles for our brands, the effect of favorable or unfavorable weather on sales can be significant.

Continuing uncertainty surrounding US and global economic conditions has adversely impacted businesses worldwide. Some of our customers have been, and more may be, adversely affected, which in turn has, and may continue to, adversely impact our financial results.

The sheepskin used in certain UGG products is in high demand and limited supply, and there have been significant fluctuations in the price of sheepskin over the years as the demand from competitors for this material has changed. However, our sheepskin costs are expected to decrease for the fiscal year ending March 31, 2015 compared to the trailing twelve months ended March 31, 2014 due to lower pricing negotiated through our sheepskin contracts.

- Our use of UGGpure™, real wool woven into a durable backing used as an alternative to table grade sheepskin, in select products, primarily in linings and footbeds, continues to grow.

The markets for casual, outdoor, and athletic footwear have grown significantly during the last decade. We believe this growth is a result of the trend toward casual dress in the workplace, increasingly active outdoor lifestyles, and a growing emphasis on comfort.

• Consumers are more often seeking footwear designed to address a broader array of activities with the same quality, comfort, and high performance attributes they have come to expect from traditional athletic footwear.

• Consumers have narrowed their footwear product breadth, focusing on brands with a rich heritage and authenticity as market category creators and leaders.

Table of Contents

Consumers have become increasingly focused on luxury and comfort, seeking out products and brands that are fashionable while still comfortable.

There is an emerging sustainable lifestyle movement happening all around the world, and consumers are demanding that brands and companies become more environmentally and socially responsible.

Consumers are following a recent trend of buy now, wear now. This trend entails the consumer waiting to purchase shoes until they will actually wear them, contrasted with a tendency in the past to purchase shoes they did not plan to wear until later.

By emphasizing our brands' images and our focus on comfort, performance and authenticity, we believe we can continue to maintain a loyal consumer following that is less susceptible to fluctuations caused by changing fashions and changes in consumer preferences. We have also responded to consumer focus on sustainability by establishing objectives, policies, and procedures to help us drive key sustainability initiatives around human rights, environmental sustainability, and community affairs.

We have experienced significant cost fluctuations, most over the past several years, notably with respect to sheepskin. We attempt to cover the full amount of our sheepskin purchases under fixed price contracts. We continually strive to contain our material costs through increasing the mix of non-sheepskin products, exploring new footwear materials and new production technologies, and utilizing lower cost production. Also, refer to Part I, Item 3. Quantitative and Qualitative Disclosures about Market Risk for further discussion of our commodity price risk.

Below is an overview of the various components of our business, including some key factors that affect each business and some of our strategies for growing each business.

UGG Brand Overview

The UGG brand is one of the most iconic and recognized brands in the global footwear industry and highlights our successful track record of building niche brands into lifestyle market leaders. With loyal consumers around the world the UGG brand has proven to be a highly resilient line of premium footwear, with an expanding product offering and a growing global audience that attracts women, men and children. UGG brand footwear continually earns media exposure from numerous outlets both organically and from strategic public relations efforts, including an increasing amount of exposure internationally. The UGG brand has invested in creating holistic, impactful integrated campaigns across paid, earned and owned media channels, including mobile, digital, social, out-of-home (OOH) and print, which are globally scalable, contributing to broader public awareness of the brand.

We believe the increased global media focus and demand for UGG products has been driven by the following:

• High consumer brand loyalty, due to over 35 years of delivering quality and luxuriously comfortable UGG footwear;

• Continued innovation of new product categories and styles, including those beyond footwear such as loungewear, handbags, cold-weather accessories and a new home offering;

• A more robust footwear offering, including transitional product that bridges the seasons between spring and fall;

• Expanded slipper category showing incremental growth with added styles for both women and men;

• Growing Direct-to-Consumer platform and enhanced OmniChannel capabilities that enable us to increasingly engage existing and prospective consumers in a more connected environment to introduce our evolving product lines;

• Product customization with our UGG by You program allows for a deeper connection with the brand and products;

• Focus on mobile consumers with responsive site design, providing shoppers access to the brand from their mobile device;

• Year-round holistic paid advertising approach for women, men and kids in targeted digital, high-end print, OOH, digital and across multiple social platforms;

• Holiday and winter focused advertising campaign to drive important seasonal sales;

• Continued creation of targeted UGG for Men campaigns featuring brand ambassador Tom Brady;

Table of Contents

- Targeted E-Commerce based marketing to existing and prospective consumers through integrated outreach including email blasts, interactive site design and search engine optimization based content;

- Continued partnership with high-end retailers such as Nordstrom;

- Expanded product assortments from existing accounts;

- Adoption by high-profile celebrities as a favored footwear brand;

- Continued media attention that has enabled us to introduce the brand to consumers much faster than we would have otherwise been able to;

- Increased exposure to the brand driven by our concept stores that showcase all of our product offerings; and

- Continued expansion of worldwide retail through new UGG stores.

We believe the luxurious comfort of UGG products will continue to drive long-term consumer demand. Recognizing that there is a significant fashion element to UGG footwear and that footwear fashions fluctuate, our key strategies include presenting UGG as a year-round global, premium lifestyle brand with a broad product line suitable for wear in a variety of climates and occasions and limiting distribution to select higher-end retailers. As part of this strategic approach, we have increased our product offering, including growing transitional collections and our spring line, an expanded men's line, a fall line that consists of a range of luxurious collections for both genders, an expanded kids' line, as well as home, handbags, cold weather accessories, and apparel. An additional key strategy is to grow casual boots by expanding retail offerings in women's casual boots and cold weather products. We have also recently expanded our marketing and promotional efforts, which we believe has contributed, and will continue to contribute, to our growth. We believe that the evolution of the UGG brand and our strategy of product diversification will also help decrease our reliance on sheepskin, which is in high demand and subject to price volatility. Nonetheless, we cannot assure investors that our efforts will continue to provide UGG brand growth.

Teva Brand Overview

For 30 years Teva has fueled the expression of freedom through the adventure lifestyle around the globe. Teva pioneered the sport sandal category in 1984 and today our mission remains steadfast: to enable spontaneous adventure with versatile, utility-centered footwear for active consumers. By designing simple, functional footwear, Teva is driving growth by extending our established global platforms in sandals and water-related products and by leveraging our authenticity with active lifestyle consumers.

We believe that Teva's Originals collection is a key platform in driving market penetration for the brand. The Originals Collection honors the heritage of Teva by revamping the styles the brand was founded on, blending their original simplicity with modern sophistication. In the US, our focus will be to bolster our leadership position in sandals and grow our market share through casual category extensions. Globally, we seek to establish the Originals collection as a beachhead for the Teva brand across warm-weather climates.

Within the US, we expect that Teva will grow its position as a market leader within the sport sandal category. Growth opportunities within our current core channels of distribution - outdoor specialty, sporting goods, and family footwear retail chains - will be pursued through deepening penetration with evolved and expanded product offerings. Teva plans to support its channel expansion beyond present distribution with focused investments in targeted, solution-driven marketing programs in order to attract new lifestyle consumers to the brand. However, we cannot assure investors that these efforts will be successful.

Sanuk Brand Overview

The Sanuk brand was founded 16 years ago, and from its origins in the Southern California surf culture, has grown into a global brand with an expanding fanbase and growing presence in the casual sneaker and sandal categories. The Sanuk brand's use of unexpected materials and unconventional constructions combined with its fun and funky branding has contributed to the brand's identity and growth since its inception, and led to successful products such as the Yoga Mat™ sandal collection and the patented SIDEWALK SURFERS®. We believe that the Sanuk brand provides substantial growth opportunities, especially within the casual sneaker markets, supporting our strategic initiatives spanning new product launches, OmniChannel development and global expansion. However, we cannot assure investors that our efforts to grow the brand will be successful.

Other Brands Overview

Our other brands consist of Ahnu, Hoka, MOZO and TSUBO. Our other brands are all sold through most of our distribution channels, with the majority sold through wholesale channels.

Table of Contents

Ahnu is an authentic performance footwear brand that makes footwear for fashion-minded people who prefer trails, yoga mats, and hybrid fitness workouts. Ahnu's products feature après-yoga styling, innovative trail and city hikers, and everyday casual shoes and sandals. Ahnu's go-anywhere approach blurs the lines between performance and fashion through modern color and material stories infused with Numentum® performance technology. The Hoka brand focuses on designing shoes with a unique performance midsole geometry, oversized midsole volume and an active foot frame. We believe runners from around the world are experiencing the benefits of Hoka brand products. These shoes are used by marathon runners, and even ultra-marathon runners as well as every day runners to enjoy running.

With respect to Ahnu and Hoka, we expect to leverage our design, marketing, and distribution capabilities to continue to grow them over the next several years, consistent with our mission to build niche brands into global market leaders. Nevertheless, we cannot assure investors that our efforts to grow these brands will be successful.

With respect to MOZO and TSUBO, we recently made the decision to seek strategic alternatives for these businesses.

E-Commerce Overview

Our E-Commerce business, which sells all of our brands, allows us to build our relationship with the consumer and is a key component of our integrated OmniChannel strategy. E-Commerce enables us to meet the growing demand for our products, sell the products at retail prices, and provide significant incremental operating income. The E-Commerce business provides us an opportunity to communicate to the consumer with a consistent brand message that is in line with our brands' promises, drives awareness of key brand initiatives, and offers targeted information to specific consumer segments. Our websites also drive wholesale and distributor sales through brand awareness and directing consumers to retailers that carry our brands, including our own retail stores. In recent years, our E-Commerce business has had significant revenue growth, much of which occurred as the UGG brand gained popularity and as consumers continued to increase internet usage for footwear and other purchases.

Managing our E-Commerce business requires us to focus on the latest trends and techniques for web design and marketing, to generate internet traffic to our websites, to effectively convert website visits into orders, and to maximize average order sizes. We plan to continue to grow our E-Commerce business through improved website features and performance, increased marketing, expansion into more international markets, and utilization of mobile and tablet technology. Nevertheless, we cannot assure investors that revenue from our E-Commerce business will continue to grow.

Retail Stores Overview

Our retail stores are predominantly UGG concept stores and UGG outlet stores. In 2013 we expanded our fleet and opened our first Sanuk (two concept, one outlet) stores. Our retail stores enable us to directly impact our customers' experience, meet the growing demand for these products, sell the products at retail prices and generate strong annual operating income. In addition, our UGG concept stores allow us to showcase our entire product line including footwear, accessories, handbags, home, outerwear, lounge and retail exclusive items; whereas, a wholesale account may not represent all of these categories. Through our outlet stores, we sell some of our discontinued styles from prior seasons, as well as full price in-line product, and products made specifically for the outlet stores. Within our OmniChannel strategy, we believe that consumers try on product in our retail stores, perform further online research and order product online and, conversely, E-Commerce fuels our retail locations. As a result, we believe that our stores and websites are interconnected in a way that will allow us to view them on a combined basis. Further, our stores will allow the consumer to buy through our E-Commerce channel using internet capable devices in our stores. As of December 31, 2014, we had a total of 138 retail stores worldwide. These stores are company-owned and operated. During the remainder of fiscal year 2015, we plan to open additional retail stores worldwide. During the nine months ended December 31, 2014, we converted seven of our retail stores in China to partner retail stores, whereby, upon conversion, the stores became wholly-owned and operated by local, third party companies within China. These conversions included the assignment of the lease and the sale of both our on-hand inventory and store leasehold improvements to the operator. As of the date of conversion, partner retail stores sales are included in our UGG brand wholesale segment and not included in our retail stores segment.

Seasonality

Our business is seasonal, with the highest percentage of UGG brand net sales occurring in the quarters ending September 30 and December 31 and the highest percentage of Teva and Sanuk brand net sales occurring in the quarters ending March 31 and June 30 of each year. Our other brands do not have a significant seasonal impact.

In February 2014, our Board of Directors approved a change in our fiscal year end from December 31 to March 31. The change is intended to better align our planning, financial and reporting functions with the seasonality of our business.

Table of Contents

The following table summarizes our quarterly net sales and (loss) income from operations:

	FY 2015			
	Quarter Ended June 30, 2014	Quarter Ended September 30, 2014	Quarter Ended December 31, 2014	Quarter Ending March 31, 2015
Net sales	\$211,469	\$480,273	\$784,678	
(Loss) Income from operations	\$ (50,482	) \$59,583	\$214,581	
	CY 2013			FY 2014
	Quarter Ended June 30, 2013	Quarter Ended September 30, 2013	Quarter Ended December 31, 2013	Quarter Ended March 31, 2014
Net sales	\$170,085	\$386,725	\$736,048	\$294,716
(Loss) Income from operations	\$ (42,751	) \$46,497	\$201,499	\$ (408

With the large growth in the UGG brand over the past several years, net sales in the quarters ending September 30 and December 31 have exceeded net sales in the quarters ending March 31 and June 30. We currently expect this trend to continue. Nonetheless, actual results could differ materially depending upon consumer preferences, availability of product, competition, and our wholesale and distributor customers continuing to carry and promote our various product lines, among other risks and uncertainties.

Results of Operations

Three Months Ended December 31, 2014 Compared to Three Months Ended December 31, 2013

The following table summarizes our results of operations:

	Three Months Ended December 31,							
	2014		2013		Change			
	Amount	%	Amount	%	Amount	%		%
Net sales	\$784,678	100.0	% \$736,048	100.0	% \$48,630	6.6		%
Cost of sales	369,539	47.1	359,848	48.9	9,691	2.7		
Gross profit	415,139	52.9	376,200	51.1	38,939	10.4		
Selling, general and administrative expenses	200,558	25.5	174,701	23.7	25,857	14.8		
Income from operations	214,581	27.4	201,499	27.4	13,082	6.5		
Other expense, net	1,265	0.2	1,102	0.2	163	14.8		
Income before income taxes	213,316	27.2	200,397	27.2	12,919	6.4		
Income tax expense	56,610	7.2	59,500	8.1	(2,890	) (4.9)	
Net income	\$156,706	20.0	% \$140,897	19.1	% \$15,809	11.2		%

Overview. Overall net sales increased for all distribution channels of all segments, except for the Sanuk and Teva brands wholesale sales. The increase in income from operations resulted from increased sales and gross margin, partially offset by higher selling, general and administrative expenses (SG&A).

Table of Contents

Net Sales. The following tables summarize net sales by location, brand, and distribution channel:

	Three Months Ended December 31,				
	2014	2013	Change Amount	%	
Net sales by location:					
US	\$ 526,315	\$ 510,693	\$ 15,622	3.1	%
International	258,363	225,355	33,008	14.6	
Total	\$ 784,678	\$ 736,048	\$ 48,630	6.6	%
Net sales by brand and distribution channel:					
UGG:					
Wholesale	\$ 401,702	\$ 399,628	\$ 2,074	0.5	%
E-Commerce	142,586	114,240	28,346	24.8	
Retail stores	191,711	177,015	14,696	8.3	
Total	735,999	690,883	45,116	6.5	
Teva:					
Wholesale	12,373	14,189	(1,816	) (12.8)
E-Commerce	1,097	1,071	26	2.4	
Retail stores	169	249	(80	) (32.1)
Total	13,639	15,509	(1,870	) (12.1)
Sanuk:					
Wholesale	17,763	19,974	(2,211	) (11.1)
E-Commerce	1,917	1,613	304	18.8	
Retail stores	797	656	141	21.5	
Total	20,477	22,243	(1,766	) (7.9)
Other:					
Wholesale	13,211	6,936	6,275	90.5	
E-Commerce	1,271	376	895	238.0	
Retail stores	81	101	(20	) (19.8)
Total	14,563	7,413	7,150	96.5	
Total	\$ 784,678	\$ 736,048	\$ 48,630	6.6	%
Total E-Commerce	\$ 146,871	\$ 117,300	\$ 29,571	25.2	%
Total Retail stores	\$ 192,758	\$ 178,021	\$ 14,737	8.3	%

In order to provide a framework for assessing how our underlying businesses performed, excluding the effect of foreign currency rate fluctuations, we provide certain financial information on a “constant currency basis,” which is in addition to the actual financial information presented. In order to calculate our constant currency information, we translate the current period financial information using the foreign currency exchange rates that were in effect during the previous comparable period. However, constant currency measures should not be considered in isolation or as an alternative to US dollar measures that reflect current period exchange rates, or to other financial measures calculated and presented in accordance with US generally accepted accounting principles.

The increase in overall net sales was primarily due to an increase in our UGG brand sales through our E-Commerce sites and retail stores as well as an increase in our other brands and UGG brand wholesale sales. These increases in net sales were slightly offset by decreases in Sanuk and Teva brand sales through the wholesale channel. On a constant currency basis, net sales increased 8.2% to approximately \$796,000. We experienced an increase in the number of

pairs sold in the E-Commerce, retail and other brands wholesale segments, partially offset by a decrease in the number of pairs sold in the Teva brand, Sanuk brand and UGG brand wholesale segments. This resulted in an increase in the overall volume of footwear sold for all brands of 3.2% to approximately 9.6 million pairs sold for the three months ended December 31, 2014 from approximately 9.3 million pairs for the three months ended December 31, 2013.