

ABERCROMBIE & FITCH CO /DE/

Form 10-Q

June 08, 2018

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended May 5, 2018

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 1-12107

ABERCROMBIE & FITCH CO.

(Exact name of Registrant as specified in its charter)

Delaware 31-1469076  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

6301 Fitch Path, New Albany, Ohio 43054  
(Address of principal executive offices) (Zip Code)  
Registrant's telephone number, including area code: (614) 283-6500

Not Applicable

(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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company   
Emerging growth company

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

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

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

Class A Common Stock    Outstanding at June 5, 2018

\$.01 Par Value                      67,790,465 Shares

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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

ABERCROMBIE & FITCH CO.  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 AND COMPREHENSIVE LOSS

(Thousands, except per share amounts)

(Unaudited)

	Thirteen Weeks Ended	
	May 5, 2018	April 29, 2017
Net sales	\$730,899	\$661,099
Cost of sales, exclusive of depreciation and amortization	288,554	262,174
Gross profit	442,345	398,925
Stores and distribution expense	361,155	359,929
Marketing, general and administrative expense	124,897	109,893
Asset impairment	1,056	730
Other operating income, net	(2,560 )	(1,686 )
Operating loss	(42,203 )	(69,941 )
Interest expense, net	3,018	4,120
Loss before taxes	(45,221 )	(74,061 )
Income tax benefit	(3,713 )	(13,052 )
Net loss	(41,508 )	(61,009 )
Less: Net income attributable to noncontrolling interests	953	691
Net loss attributable to A&F	\$(42,461 )	\$(61,700 )
Net loss per share attributable to A&F		
Basic	\$(0.62 )	\$(0.91 )
Diluted	\$(0.62 )	\$(0.91 )
Weighted-average shares outstanding		
Basic	68,500	68,073
Diluted	68,500	68,073
Dividends declared per share	\$0.20	\$0.20
Other comprehensive income		
Foreign currency translation, net of tax	\$(8,339 )	\$5,607
Derivative financial instruments, net of tax	12,260	(4,600 )
Other comprehensive income	3,921	1,007
Comprehensive loss	(37,587 )	(60,002 )
Less: Comprehensive income attributable to noncontrolling interests	953	691

Comprehensive loss attributable to A&F

\$(38,540 ) \$(60,693 )

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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ABERCROMBIE & FITCH CO.  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (Thousands, except par value amounts)  
 (Unaudited)

	May 5, 2018	February 3, 2018
Assets		
Current assets:		
Cash and equivalents	\$591,960	\$675,558
Receivables	72,795	79,724
Inventories	405,107	424,393
Other current assets	104,806	84,863
Total current assets	1,174,668	1,264,538
Property and equipment, net	709,007	738,182
Other assets	327,844	322,972
Total assets	\$2,211,519	\$2,325,692
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$166,577	\$168,868
Accrued expenses	262,964	308,601
Short-term portion of deferred lease credits	19,269	19,751
Income taxes payable	12,784	10,326
Total current liabilities	461,594	507,546
Long-term liabilities:		
Long-term portion of deferred lease credits	73,660	75,648
Long-term portion of borrowings, net	249,962	249,686
Leasehold financing obligations	48,955	50,653
Other liabilities	188,502	189,688
Total long-term liabilities	561,079	565,675
Stockholders' equity		
Class A Common Stock - \$0.01 par value: 150,000 shares authorized and 103,300 shares issued at each of May 5, 2018 and February 3, 2018	1,033	1,033
Paid-in capital	399,860	406,351
Retained earnings	2,356,880	2,420,552
Accumulated other comprehensive loss, net of tax	(91,133 )	(95,054 )
Treasury stock, at average cost: 35,484 and 35,105 shares at May 5, 2018 and February 3, 2018, respectively	(1,488,373 )	(1,490,503 )
Total Abercrombie & Fitch Co. stockholders' equity	1,178,267	1,242,379
Noncontrolling interests	10,579	10,092
Total stockholders' equity	1,188,846	1,252,471
Total liabilities and stockholders' equity	\$2,211,519	\$2,325,692

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.



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ABERCROMBIE & FITCH CO.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Thousands)  
 (Unaudited)

	Thirteen Weeks Ended	
	May 5, 2018	April 29, 2017
Operating activities		
Net loss	\$(41,508 )	\$(61,009 )
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and amortization	47,647	48,789
Asset impairment	1,056	730
Loss on disposal	1,239	2,378
Amortization of deferred lease credits	(5,040 )	(5,325 )
Benefit from deferred income taxes	(12,290 )	(15,100 )
Share-based compensation	4,783	4,880
Changes in assets and liabilities		
Inventories	11,444	1,316
Accounts payable and accrued expenses	(32,186 )	(62,120 )
Lessor construction allowances	1,778	2,940
Income taxes	2,526	(634 )
Long-term lease deposits	1,469	(41 )
Other assets	2,655	8,497
Other liabilities	256	(9,433 )
Net cash used for operating activities	(16,171 )	(84,132 )
Investing activities		
Purchases of property and equipment	(23,700 )	(32,081 )
Proceeds from sale of property and equipment	—	203
Net cash used for investing activities	(23,700 )	(31,878 )
Financing activities		
Purchase of treasury stock	(18,670 )	—
Dividends paid	(13,642 )	(13,554 )
Other financing activities	(5,176 )	(551 )
Net cash used for financing activities	(37,488 )	(14,105 )
Effect of exchange rates on cash	(5,914 )	4,497
Net decrease in cash and equivalents, and restricted cash	(83,273 )	(125,618 )
Cash and equivalents, and restricted cash, beginning of period	697,955	567,632
Cash and equivalents, and restricted cash, end of period	\$614,682	\$442,014
Significant non-cash investing activities		
Change in accrual for construction in progress	\$1,658	\$(4,297 )
Supplemental information		
Cash paid for interest	\$3,492	\$3,391
Cash paid for income taxes	\$6,683	\$3,550
Cash received from income taxes	\$6,762	\$186



The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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ABERCROMBIE & FITCH CO.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. BASIS OF PRESENTATION

Nature of Business

Abercrombie & Fitch Co. (“A&F”), a company incorporated in Delaware in 1996, through its subsidiaries (collectively, A&F and its subsidiaries are referred to as “Abercrombie & Fitch” or the “Company”), is a global, multi-brand, specialty retailer, which primarily sells its products through its wholly-owned store and direct-to-consumer channels, as well as through various third-party wholesale, franchise and licensing arrangements. The Company offers a broad assortment of apparel, personal care products and accessories for men, women and kids under the Hollister, Abercrombie & Fitch and abercrombie kids brands. The Company has operations in North America, Europe, Asia and the Middle East.

Principles of Consolidation

The accompanying Condensed Consolidated Financial Statements include historical financial statements of, and transactions applicable to, the Company and reflect its assets, liabilities, results of operations and cash flows.

The Company has interests in a United Arab Emirates business venture and in a Kuwait business venture with Majid al Futtaim Fashion L.L.C. (“MAF”), each of which meets the definition of a variable interest entity (“VIE”). The Company is deemed to be the primary beneficiary of these VIEs; therefore, the Company has consolidated the operating results, assets and liabilities of these VIEs, with MAF’s portion of net income presented as net income attributable to noncontrolling interests (“NCI”) on the Condensed Consolidated Statements of Operations and Comprehensive Loss and MAF’s portion of equity presented as NCI in the Consolidated Balance Sheets.

Fiscal Year

The Company’s fiscal year ends on the Saturday closest to January 31. All references herein to “Fiscal 2018” and “Fiscal 2017” represent the fifty-two week fiscal year ending on February 2, 2019 and the fifty-three week fiscal year ended on February 3, 2018, respectively.

Interim Financial Statements

The Condensed Consolidated Financial Statements as of May 5, 2018, and for the thirteen-week periods ended May 5, 2018 and April 29, 2017, are unaudited and are presented pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). Accordingly, these Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and notes thereto contained in A&F’s Annual Report on Form 10-K for Fiscal 2017 filed with the SEC on April 2, 2018. The February 3, 2018 consolidated balance sheet data, included herein, were derived from audited consolidated financial statements, but do not include all disclosures required by accounting principles generally accepted in the United States of America (“U.S. GAAP”).

In the opinion of management, the accompanying Condensed Consolidated Financial Statements reflect all adjustments (which are of a normal recurring nature) necessary to state fairly, in all material respects, the financial position and results of operations and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for Fiscal 2018.



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## Recent Accounting Pronouncements

The Company reviews recent accounting pronouncements on a quarterly basis and has excluded discussion of those not applicable to the Company and those not expected to have a material impact on the Company's financial statements. The following table provides a brief description of recent accounting pronouncements the Company has adopted or that could affect the Company's financial statements.

Accounting Standards Update (ASU)	Description	Date of Adoption	Effect on the Financial Statements or Other Significant Matters
Standards adopted ASU 2014-09, Revenue from Contracts with Customers	This update superseded the revenue recognition guidance in ASC 605, Revenue Recognition. The new guidance requires entities to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration which the entity expects to be entitled to in exchange for those goods or services.	February 4, 2018	The Company adopted this guidance and all related amendments using the modified retrospective method, and applied the standard to contracts that were not complete as of the adoption date. Comparative period information has not been restated and continues to be reported under the account standards in effect for those periods. This guidance primarily impacts the classification and timing of the recognition of the Company's gift card breakage and timing of direct-to-consumer revenue. Adoption of this guidance had an immaterial impact on net loss attributable to A&F in the Company's Condensed Consolidated Statements of Operations and Comprehensive Loss.

The cumulative effect of applying the new standard on the Condensed Consolidated Balance Sheets as of May 5, 2018 was recognized as an adjustment to the opening balance of retained earnings, increasing beginning retained earnings by \$6.9 million, with corresponding reductions in accrued expenses, inventories, and other assets of \$4.7 million, \$6.4 million, and \$2.2 million, respectively, and increases to receivables and other current assets of \$6.4 million and \$4.4 million, respectively.

In accordance with the new guidance, expected gift card breakage is now recognized as net sales as gift cards are redeemed. Previously, gift card breakage was recognized as other operating income when the Company determined that the likelihood of redemption was remote. Under the new guidance, direct-to-consumer revenue is recognized

when control is passed to the customer, typically upon shipment or pick-up of goods. Previously, direct-to-consumer revenue was recognized upon customer acceptance, which typically occurred upon the customer's possession of the merchandise. The Company does not expect this guidance to have a material impact on store, direct-to-consumer, wholesale, franchise or license revenues on an ongoing basis.

The Company's revenue recognition accounting policies are discussed further in this Note 1 under "Revenue Recognition." The Company adopted this guidance under the retrospective method. For the thirteen weeks ended April 29, 2017, adoption of this guidance resulted in a \$0.1 million increase to net cash used for operating activities and increases of \$20.4 million and \$20.6 million to beginning and ending cash and equivalents, and restricted cash, respectively. In addition, captions have been updated in the Condensed Consolidated Statements of Cash Flows to reflect the inclusion of restricted cash. Restricted cash is classified as other assets on the Condensed Consolidated Balance Sheets, as was the case at year-end.

ASU 2016-18, Statement of Cash Flows

This update amends the guidance in ASC 230, Statement of Cash Flows. The new guidance requires an entity to show the changes in total cash, cash equivalents and restricted cash in the statement of cash flows. Consequently, an entity is no longer required to present transfers between cash and equivalents and restricted cash.

February 4, 2018

Standards not yet adopted

ASU 2016-02, Leases

This update supersedes the leasing guidance in ASC 840, Leases. The new guidance requires an entity to recognize lease assets and lease liabilities on the balance sheet and disclose key leasing information that depicts the lease rights and obligations of an entity.

February 3, 2019\*

The Company expects that this guidance will result in a material increase in the Company's long-term assets and long-term liabilities on the Company's Condensed Consolidated Balance Sheets, and is currently evaluating additional impacts that this guidance may have on its consolidated financial statements. The Company will not be early adopting this guidance.

ASU 2017-12, Derivatives and Hedging — Targeted Improvements to Accounting for Hedging Activities

This update amends ASC 815, Derivatives and Hedging. The new guidance simplifies certain aspects of hedge accounting for both financial and commodity risks to more accurately present the economic effects of an entity's risk management activities in its financial statements. Under the new standard, more hedging strategies will be eligible for hedge accounting, including hedges of the benchmark rate component of the contractual coupon cash flows of fixed-rate assets or

February 3, 2019\*

The Company is currently evaluating the impact that this guidance will have on its consolidated financial statements. The Company will not be early adopting this guidance.

liabilities and partial-term hedges of fixed-rate assets or liabilities. For cash flow and net investment hedges, the guidance requires a modified retrospective approach while the amended presentation and disclosure guidance requires a prospective approach.

\* Early adoption is permitted.

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The Company's significant accounting policies as of May 5, 2018 have not changed materially from those disclosed in Note 2, "SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES," of the Notes to Consolidated Financial Statements contained in "ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA" of A&F's Annual Report on Form 10-K for Fiscal 2017, with the exception of those discussed below:

Revenue recognition

The Company recognizes revenue from product sales when control of the good is transferred to the customer, generally upon pick up at, or shipment from, a Company location.

The Company provides shipping and handling services to customers in certain direct-to-consumer transactions. Revenue associated with the related shipping and handling obligations is deferred until the obligation is fulfilled, typically upon the customer's receipt of the merchandise. The related shipping and handling costs are classified in stores and distribution expense on the Condensed Consolidated Statements of Operations and Comprehensive Loss.

Revenue is recorded net of estimated returns, associate discounts, promotions and other similar customer incentives. The Company estimates reserves for sales returns based on historical experience among other factors. The sales return reserve is classified in accrued expenses on the Condensed Consolidated Balance Sheets.

The Company accounts for gift cards sold to customers by recognizing an unearned revenue liability at the time of sale, which remains until income from gift cards not expected to be redeemed, referred to as gift card breakage, is recognized as revenue proportionally with gift card redemptions. Gift cards sold to customers do not expire or lose value over periods of inactivity and the Company is not required by law to escheat the value of unredeemed gift cards to the jurisdictions in which it operates.

The Company also maintains loyalty programs, which primarily provides customers with the opportunity to earn points toward future merchandise discount rewards with qualifying purchases. The Company accounts for expected future reward redemptions by recognizing an unearned revenue liability when customers reach certain point thresholds, which remains until revenue is recognized at the earlier of redemption or expiration.

Unearned revenue liabilities are primarily recorded when prepayments for future merchandise are received through gift card purchases or when loyalty rewards are earned by a customer in a sales transaction, and are classified in accrued expenses on the Condensed Consolidated Balance Sheets and are typically recognized as revenue within a 12-month period. Unearned revenue liabilities as of the beginning of the period and May 5, 2018 were approximately \$38.7 million and \$36.0 million, respectively, which included an adjustment related to the adoption of new revenue recognition standards that decreased the beginning of period balance \$6.2 million. During the thirteen weeks ended May 5, 2018, the Company recognized revenue of approximately \$21.0 million related to previous deferrals of revenue resulting from the Company's gift cards and loyalty programs.

The Company also recognizes revenue under wholesale arrangements, which is generally recognized upon shipment, when control passes to the wholesale partner. Revenue from the Company's franchise and license arrangements, primarily royalties earned upon sale of merchandise, is generally recognized at the time merchandise is sold to the franchisees' retail customers.

All revenues are recognized in net sales in the Condensed Consolidated Statements of Operations and Comprehensive Loss. For discussion on the disaggregation of revenue, refer to Note 9, "SEGMENT REPORTING." The Company does not include tax amounts collected from customers on behalf of third parties, including sales and indirect taxes, in net sales.





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## 2. NET LOSS PER SHARE

Net loss per basic and diluted share attributable to A&F is computed based on the weighted-average number of outstanding shares of Class A Common Stock (“Common Stock”).

Additional information pertaining to net income per share attributable to A&F is as follows:

(in thousands)	Thirteen Weeks Ended	
	May 5, 2018	April 29, 2017
Shares of Common Stock issued	103,300	103,300
Weighted-average treasury shares	(34,800 )	(35,227 )
Weighted-average — basic shares	68,500	68,073
Dilutive effect of share-based compensation awards	—	—
Weighted-average — diluted shares	68,500	68,073
Anti-dilutive shares <sup>(1)</sup>	4,599	5,263

(1) Reflects the total number of shares related to outstanding share-based compensation awards that have been excluded from the computation of net loss per diluted share because the impact would have been anti-dilutive.

## 3. FAIR VALUE

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The inputs used to measure fair value are prioritized based on a three-level hierarchy. The three levels of inputs to measure fair value are as follows:

Level 1—inputs are unadjusted quoted prices for identical assets or liabilities that are available in active markets that the Company can access at the measurement date.

Level 2—inputs are other than quoted market prices included within Level 1 that are observable for assets or liabilities, directly or indirectly.

Level 3—inputs to the valuation methodology are unobservable.

The lowest level of significant input determines the placement of the entire fair value measurement in the hierarchy. The three levels of the hierarchy and the distribution within it of the Company’s assets and liabilities, which are measured at fair value on a recurring basis, were as follows:

(in thousands)	Assets and Liabilities at Fair Value as of May 5, 2018			
	Level 1	Level 2	Level 3	Total
Assets:				
Trust-owned life insurance policies (at cash surrender value)	\$—	\$ 103,544	\$	—\$ 103,544
Money market funds	60,367	—	—	60,367
Derivative financial instruments	—	6,078	—	6,078
Total assets	\$60,367	\$ 109,622	\$	—\$ 169,989
Liabilities:				
Derivative financial instruments	\$—	\$ 1,166	\$	—\$ 1,166

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Total liabilities	\$—	\$1,166	\$	—\$1,166
	Assets and Liabilities at Fair Value as of February 3, 2018			
(in thousands)	Level 1	Level 2	Level 3	Total
Assets:				
Trust-owned life insurance policies (at cash surrender value)	\$—	\$102,784	\$	—\$102,784
Money market funds	330,649	—	—	330,649
Derivative financial instruments	—	37	—	37
Total assets	\$330,649	\$102,821	\$	—\$433,470
Liabilities:				
Derivative financial instruments	\$—	\$9,147	\$	—\$9,147
Total liabilities	\$—	\$9,147	\$	—\$9,147

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The Level 2 assets and liabilities consist of trust-owned life insurance policies and derivative financial instruments, primarily foreign currency exchange forward contracts. The fair value of foreign currency exchange forward contracts is determined by using quoted market prices of the same or similar instruments, adjusted for counterparty risk.

Fair value of borrowings:

The Company's borrowings under the Company's credit facilities are carried at historical cost in the accompanying Condensed Consolidated Balance Sheets.

The carrying amount and fair value of the Company's borrowings under the term loan facility were as follows:

(in thousands)	May 5, 2018	February 3, 2018
Gross borrowings outstanding, carrying amount	\$253,250	\$253,250
Gross borrowings outstanding, fair value	\$254,516	\$253,250

No borrowings were outstanding under the Company's senior secured revolving credit facility as of May 5, 2018 or February 3, 2018.

#### 4. PROPERTY AND EQUIPMENT, NET

Property and equipment, net consisted of:

(in thousands)	May 5, 2018	February 3, 2018
Property and equipment, at cost	\$2,799,842	\$2,821,709
Less: Accumulated depreciation and amortization	(2,090,835 )	(2,083,527 )
Property and equipment, net	\$709,007	\$738,182

The Company incurred store asset impairment charges of \$1.1 million and \$0.7 million for the thirteen weeks ended May 5, 2018 and April 29, 2017, respectively, primarily related to certain of the Company's international Abercrombie & Fitch flagship stores.

The Company had \$37.0 million and \$38.7 million of construction project assets in property and equipment, net at May 5, 2018 and February 3, 2018, respectively, related to the construction of buildings in certain lease arrangements where the Company is deemed to be the owner of the construction project.

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## 5. INCOME TAXES

The Company's quarterly tax provision and the estimate of the annual effective tax rate are subject to significant variation due to several factors. These include variability in the pre-tax jurisdictional mix of earnings, changes in how the Company does business including entering into new businesses or geographies, changes in foreign currency exchange rates, changes in law, regulations, and administrative practices, relative changes of expenses or losses for which tax benefits are not recognized and the impact of discrete items. The impact of these items on the effective tax rate will be greater at lower levels of pre-tax income (loss).

## Tax Cuts and Jobs Act of 2017

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (the "Act") was signed into law. The Act makes broad and significantly complex changes to the U.S. corporate income tax system by, among other things: reducing the U.S. federal corporate income tax rate from 35% to 21%; transitioning U.S. international taxation to a modified territorial tax system; and imposing a mandatory one-time deemed repatriation tax, payable over eight years, on accumulated undistributed foreign subsidiary earnings and profits as of December 31, 2017. The Company recognized provisional discrete net tax charges of \$19.9 million related to the enactment of the Act in the fourth quarter of Fiscal 2017. Given the significant changes resulting from and complexities associated with the Act, the estimated financial impacts in Fiscal 2017 and Fiscal 2018 are provisional and assessed as of May 22, 2018, and as of this date the Company had not recognized any adjustments to the provisional amounts recognized in the fourth quarter of Fiscal 2017. The ultimate outcome may differ from these provisional amounts, possibly materially, due to, among other things, additional analysis, changes in interpretations and assumptions the Company has made, additional regulatory guidance that may be issued and actions the Company may take as a result of the Act. Provisional amounts are expected to be finalized after the Company's Fiscal 2017 U.S. corporate income tax return is filed in the fourth quarter of Fiscal 2018, but no later than one year from the enactment of the Act.

## Other

The Company incurred \$8.2 million and \$9.3 million of discrete non-cash income tax charges for the thirteen weeks ended May 5, 2018 and April 29, 2017, respectively, related to the expiration of certain share-based compensation awards, recognized in income tax benefit due to changes in share-based compensation accounting standards adopted by the Company in the first quarter of Fiscal 2017.

## 6. SHARE-BASED COMPENSATION

The Company recognized share-based compensation expense of \$4.8 million and \$4.9 million for the thirteen weeks ended May 5, 2018 and April 29, 2017, respectively. The Company recognized tax benefits associated with share-based compensation expense of \$0.9 million and \$1.9 million for the thirteen weeks ended May 5, 2018 and April 29, 2017, respectively.

## Restricted Stock Units

The following table summarizes activity for restricted stock units for the thirteen weeks ended May 5, 2018:

	Service-based	Performance-based	Market-based
	Restricted	Restricted	Restricted
	Stock Units	Stock Units	Stock Units
	Number of Weighted-	Number of Weighted-	Number of Weighted-
	Underlying	Underlying	Underlying

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	Shares	Average Grant Date Fair Value	Shares	Average Grant Date Fair Value	Shares	Average Grant Date Fair Value
Unvested at February 3, 2018	2,520,160	\$ 15.35	690,174	\$ 11.82	383,980	\$ 16.50
Granted	674,690	21.68	142,008	21.31	142,014	33.69
Adjustments for performance achievement	—	—	(43,999 )	20.10	(36,817 )	19.04
Vested	(599,888 )	17.96	—	—	(7,185 )	19.04
Forfeited	(105,827 )	13.21	(6,687 )	9.11	(6,688 )	11.79
Unvested at May 5, 2018 <sup>(1)</sup>	2,489,135	\$ 16.51	781,496	\$ 13.10	475,304	\$ 21.47

Includes 562,435 unvested service-based restricted stock units subject to vesting requirement related to the achievement of certain performance metrics, such as operating income and net income, for the fiscal year immediately preceding the vesting date. Holders of these restricted stock units have the opportunity to earn back one or more installments of the award if the cumulative performance requirements are met in a subsequent year. Unvested shares related to restricted stock units with performance-based and market-based vesting conditions can achieve up to 200% of their target vesting amount and are reflected at 100% of their target vesting amount in the table above.

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Fair value of both service-based and performance-based restricted stock units is calculated using the market price of the underlying Common Stock on the date of grant reduced for anticipated dividend payments on unvested shares. In determining fair value, the Company does not take into account performance-based vesting requirements. Performance-based vesting requirements are taken into account in determining the number of awards expected to vest. For market-based restricted stock units, fair value is calculated using a Monte Carlo simulation with the number of shares that ultimately vest dependent on the Company's total stockholder return measured against the total stockholder return of a select group of peer companies over a three-year period. For awards with performance-based or market-based vesting requirements, the number of shares that ultimately vest can vary from 0% to 200% of target depending on the level of achievement of performance criteria.

Service-based restricted stock units are expensed on a straight-line basis over the total awards' requisite service period. Performance-based restricted stock units subject to graded vesting are expensed on an accelerated attribution basis. Performance share award expense is primarily recognized in the performance period of the awards' requisite service period. Market-based restricted stock units without graded vesting features are expensed on a straight-line basis over the requisite service period. Compensation expense for stock options and stock appreciation rights is recognized on a straight-line basis over the awards' requisite service period, net of forfeitures. The Company adjusts share-based compensation expense on a quarterly basis for actual forfeitures. Unrecognized compensation expense presented excludes the effect of potential forfeitures, and will be adjusted for actual forfeitures as they occur.

As of May 5, 2018, there was \$34.4 million, \$7.5 million and \$7.2 million of total unrecognized compensation cost related to service-based, performance-based and market-based restricted stock units, respectively. The unrecognized compensation cost is expected to be recognized over a weighted-average period of 18 months, 14 months and 15 months for service-based, performance-based and market-based restricted stock units, respectively.

The actual tax benefit realized for tax deductions related to the issuance of shares associated with restricted stock unit vesting was \$3.4 million and \$2.1 million for the thirteen weeks ended May 5, 2018 and April 29, 2017, respectively.

Additional information pertaining to restricted stock units for the thirteen weeks ended May 5, 2018 and April 29, 2017 follows:

(in thousands)	May 5, 2018	April 29, 2017
Service-based restricted stock units:		
Total grant date fair value of awards granted	\$14,627	\$13,540
Total grant date fair value of awards vested	\$10,774	\$13,457
Performance-based restricted stock units:		
Total grant date fair value of awards granted	\$3,026	\$4,774
Total grant date fair value of awards vested	\$—	\$—
Market-based restricted stock units:		
Total grant date fair value of awards granted	\$4,784	\$2,793
Total grant date fair value of awards vested	\$137	\$—

The weighted-average assumptions used for market-based restricted stock units in the Monte Carlo simulation during the thirteen weeks ended May 5, 2018 and April 29, 2017 were as follows:

May 5, 2018	April 29, 2017
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Grant date market price	\$23.59	\$11.43
Fair value	\$33.69	\$11.79
Assumptions:		
Price volatility	54	% 47 %
Expected term (years)	2.9	2.9
Risk-free interest rate	2.4	% 1.5 %
Dividend yield	3.4	% 7.0 %
Average volatility of peer companies	37.4	% 35.2 %
Average correlation coefficient of peer companies	0.2709	0.2664

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## Stock Appreciation Rights

The following table summarizes stock appreciation rights activity for the thirteen weeks ended May 5, 2018:

	Number of Underlying Shares	Weighted-Average Exercise Price	Aggregate Intrinsic Value	Weighted-Average Remaining Contractual Life
Outstanding at February 3, 2018	3,010,720	\$ 49.35		
Granted	—	—		
Exercised	(41,653 )	22.24		
Forfeited or expired	(1,609,646)	54.69		
Outstanding at May 5, 2018	1,359,421	\$ 44.00	\$ 1,043,513	3.6
Stock appreciation rights exercisable at May 5, 2018	1,235,825	\$ 45.87	\$ 734,472	3.3
Stock appreciation rights expected to become exercisable in the future as of May 5, 2018	116,408	\$ 25.46	\$ 284,639	6.8

As of May 5, 2018, there was \$0.7 million of total unrecognized compensation cost related to stock appreciation rights. The unrecognized compensation cost is expected to be recognized over a weighted-average period of 6 months.

The grant date fair value of stock appreciation rights that vested during the thirteen weeks ended May 5, 2018 and April 29, 2017 was \$0.9 million and \$1.9 million, respectively.

## Stock Options

The following table summarizes stock option activity for the thirteen weeks ended May 5, 2018:

	Number of Underlying Shares	Weighted-Average Exercise Price	Aggregate Intrinsic Value	Weighted-Average Remaining Contractual Life
Outstanding at February 3, 2018	87,200	\$ 78.20		
Granted	—	—		
Exercised	—	—		
Forfeited or expired	(77,200 )	78.65		
Outstanding at May 5, 2018	10,000	\$ 74.74	\$ —	0.0
Stock options exercisable at May 5, 2018	10,000	\$ 74.74	\$ —	0.0

As of May 5, 2018, there was no unrecognized compensation cost related to currently outstanding stock options.

## 7. DERIVATIVE INSTRUMENTS

The Company is exposed to risks associated with changes in foreign currency exchange rates and uses derivative instruments, primarily forward contracts, to manage the financial impacts of these exposures. The Company does not use forward contracts to engage in currency speculation and does not enter into derivative financial instruments for trading purposes.

The Company uses derivative instruments, primarily foreign currency exchange forward contracts designated as cash flow hedges, to hedge the foreign currency exchange rate exposure associated with forecasted foreign-currency-denominated intercompany inventory sales to foreign subsidiaries and the related settlement of the foreign-currency-denominated intercompany receivables. Fluctuations in foreign currency exchange rates will either



increase or decrease the Company's intercompany equivalent cash flows and affect the Company's U.S. Dollar earnings. Gains or losses on the foreign currency exchange forward contracts that are used to hedge these exposures are expected to partially offset this variability. Foreign currency exchange forward contracts represent agreements to exchange the currency of one country for the currency of another country at an agreed upon settlement date. These foreign currency exchange forward contracts typically have a maximum term of twelve months. The sale of the inventory to the Company's customers will result in the reclassification of related derivative gains and losses that are reported in accumulated other comprehensive loss ("AOCL"). Substantially all of the unrealized gains or losses related to designated cash flow hedges as of May 5, 2018 will be recognized in cost of sales, exclusive of depreciation and amortization over the next twelve months.

The Company presents its derivative assets and derivative liabilities at their gross fair values on the Condensed Consolidated Balance Sheets. However, the Company's derivative contracts allow net settlements under certain conditions.

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As of May 5, 2018, the Company had outstanding the following foreign currency exchange forward contracts that were entered into to hedge either a portion, or all, of forecasted foreign-currency-denominated intercompany inventory sales, the resulting settlement of the foreign-currency-denominated intercompany accounts receivable, or both:

(in thousands)	Notional Amount (1)
Euro	\$ 158,613
British pound	\$ 68,633
Canadian dollar	\$ 30,812
Japanese yen	\$ 14,074

(1) Amounts reported are the U.S. Dollar notional amounts outstanding as of May 5, 2018.

The Company also uses foreign currency exchange forward contracts to hedge certain foreign-currency-denominated net monetary assets/liabilities. Examples of monetary assets/liabilities include cash balances, receivables and payables. Fluctuations in foreign currency exchange rates result in transaction gains/(losses) being recorded in earnings, as U.S. GAAP requires that monetary assets/liabilities be remeasured at the spot exchange rate at quarter-end or upon settlement. The Company has chosen not to apply hedge accounting to these instruments because there are no differences in the timing of gain or loss recognition on the hedging instruments and the hedged items.

As of May 5, 2018, the Company had outstanding the following foreign currency exchange forward contracts that were entered into to hedge foreign-currency-denominated net monetary assets/liabilities:

(in thousands)	Notional Amount (1)
Euro	\$ 14,525
Canadian dollar	\$ 4,768
Japanese yen	\$ 3,342

(1) Amounts reported are the U.S. Dollar notional amounts outstanding as of May 5, 2018.

The location and amounts of derivative fair values on the Condensed Consolidated Balance Sheets as of May 5, 2018 and February 3, 2018 were as follows:

(in thousands)	Location	May 5, 2018	February 3, 2018	Location	May 5, 2018	February 3, 2018
Derivatives designated as hedging instruments:						
Foreign currency exchange forward contracts		\$ 5,924	\$ 37		\$ 1,151	\$ 9,108
Derivatives not designated as hedging instruments:						
Foreign currency exchange forward contracts		\$ 154	\$ —		\$ 15	\$ 39
Total	Other current assets	\$ 6,078	\$ 37	Accrued expenses	\$ 1,166	\$ 9,147

Refer to Note 3, "FAIR VALUE," for further discussion of the determination of the fair value of derivative instruments.



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The location and amounts of derivative gains and losses for the thirteen weeks ended May 5, 2018 and April 29, 2017 on the Condensed Consolidated Statements of Operations and Comprehensive Loss were as follows:

(in thousands)	Location	Thirteen Weeks Ended		Thirteen Weeks Ended	
		May 5, 2018	April 29, 2017	May 5, 2018	April 29, 2017
Derivatives not designated as hedging instruments:					
Foreign currency exchange forward contracts	Other operating income, net	\$2,702	\$	28	
Derivatives in cash flow hedging relationships:					
Foreign currency exchange forward contracts	Cost of sales, exclusive of depreciation and amortization	\$8,607	\$(1,373)	Other operating income, net	\$ 1,370